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Impact of foreign direct investment on Nigerian economy

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Abstract

The study examined the impact of Foreign Direct Investment (FDI) on the growth of the Nigerian economy from 2010- Q2 2021. The aim is to investigate the impact of FDI in relation to other growth variables namely: External Debt (EXD), Domestic Investment (DI). Export (EXP) Inflation Rate (InfR) and Exchange rate (EXR) are the explanatory variables of the study on Gross Domestic Product (GDP) proxy for economic growth being the dependent variable. Data for the study were obtained from the Central Bank of Nigeria (CBN) and the National Bureau of Statistics (NBS) statistical bulletins. The data were analysed using E-view version 10.0. Results indicated that while DI, EXP and EXR have significance on GDP at a 10% level of significance, FDI, EXD and InfR showed a negative impact on GDP at the same level of significance. However, about 547 of the likely changes in GDP, growth in Nigeria is explained by a combination of the predicatory variables as indicated by the coefficient of determination $(R)^2$ value of 0.544. The study recommended among others that domestic investment and the productive capacity of the nation should be encouraged. Also, the issue of insecurity in Nigeria should be sincerely tackled.

Keywords: *Investment, Economy, Growth, Productive, Insecurity.*

Introduction

The rapid growth of the world population in this 21st century mostly in developing nations of Africa and indeed Nigeria has a lot of implications. The growth has to be matched with a more rapid increase in Gross Domestic Product (GDP) and Income per capita.

For increased GDP and income per capita, many have favoured the free flow of capital across national borders. The flow is not to seek the highest rate of return (Dorgram&Talyor, 2009). Unrestricted capital flow also offers several advantages. The advantages according to Feldstein (2000) includes (i) Integration of Capital Markets that can contribute to the spreading of best practices in corporate governance, accounting rules and legal traditions and (ii) Exponential global mobility of capital that can limit the ability f government to pursue bad policies.

In addition to these advantages, Clyton (2016) noted that the gains to list countries from the flow of capital across borders through Foreign Direct Investment (FDI) can take various forms namely (i) Technology transfer inform of new varieties of capital inputs that cannot be achieved through financial investment or trade in goods and services (ii) Promotion of competition in domestic input market (iii) Employee training for the recipient of FDI gained in the course of

operating the new businesses (iv) Human capital development in the host country and (v) increase in corporate tax revenues and employment creation in the host country.

On the growth front, the purpose of FDI is to improve the recipient economy. For developing economies like Nigeria, FDI is a vehicle for strengthening the economy as it is one of the means/sources of finance and capital formation (Dorgram& Taylor, 2009).

Generally, an increase in FDI may be associated with improved economic growth of the host country due to the influx of capital and increased tax revenue (Longman, 2010). With the influx of capital and increased tax to the government, the growth of the welfare state (free government provision in areas such as medical care, seduction, infrastructure etcetera to citizens of the host country can be guaranteed to an extent (Stutt & Morgan, 2011; Cartley&Breller, 2013).

Statement of the Problem

A nation's ability to sustain growth in its economy is a function of both internal and external factors (Balle&Nanier, 2008). Internal factors such as inflation rate, exchange rate (currency power) domestic investment (domestic capital stock), Export rate and external factors such as FDI (foreign capital inflows) and external debt rate play significant roles in economic growth.

Taglan and Neir (2014) viewed that the rate of economic growth of nations largely depends on the efficiency of the internal factors. Unfortunately in Nigeria, a gap and deficiency exist domestically available capital, foreign exchange, government revenue, skills/ technology and planned level of government revenues necessary to drive the growth target of the nation (Ormeh&Melek, 2012). The gap and the deficiencies in internal economic growth factors in Nigeria called for growth intervention of which FDI is seen as a ‘‘good’’ cholesterol to fill the gap (Erstol&Lette, 2016).

On the contrary, Omeruo (2018) viewed the cost of FDI to Nigeria and asserted that the investment has damaging effects on the nation's economy as it dwarfs the spirit of entrepreneurship of Nigerians. Further, the limited of porous Nigeria's conditions for entry, regulation of foreign capital and unguarded restrictions on the remittance of profits and capital repatriation are dysfunctional to the economic growth of the nation (Lekan &Eniola, 2018). Similarly, Galatti (2019) observed that introduction of unsuitable products and technology in Nigeria amount to exploitation and stimulating class conflict therefore a negative contribution of FDI in the country. Assessing the contribution of FDI to the growth of Nigeria's economy, Kachi&Egbu (2020) see the impact of multinational corporations (MNCs) and FDI as Oligopolistic in Nature with their investment gravitated towards countries with the highest financial returns and safety of investment of which Nigeria's business environment has fallen short of the indexes for investment.

It is in relation to these contradictory views of the contribution of the FDI in Nigeria that the study investigated the impact of this investment in the country in the last four years (2010 – Q2 2021).

Objectives of the study

The main objective of the study is to examine the impact of FDI on the growth of the Nigerian economy. However, the specific objectives are as follows:

i. To ascertain the impact of FDI on the growth of the Nigerian economy.
ii. To ascertain the impact of external debt on the Nigerian economy
iii. To ascertain the impact of domestic investment on the growth of the Nigerian economy
iv. To examine the impact of exports on the growth of the Nigerian economy.
v. To investigate the impact of inflation on the growth of the Nigerian economy.
vi. To ascertain the impact of the exchange rate on the growth of the Nigerian economy.

Hypotheses of the study

In line with the objectives, the following null hypotheses were formulated to guide the study.

$H0_1$: FDI has a significant impact on the growth of the Nigerian economy.

$H0_2$: External debt has no significant impact on the growth of the Nigerian economy.

$H0_3$: Domestic Investment has no significant impact on the growth of the Nigerian economy

$H0_4$: Exports has no significant impact on the growth of the Nigerian economy.

$H0_5$: Inflation rate has no significant impact on the Nigerian economy.

$H0_6$: Exchange rate of Nigerian currency in relation to other currencies has a significant impact on the Nigerian economy.

Literature Review

Conceptual Review

Economic Growth: It refers to the process whereby the real per capita income for a country increases over a long period of time (Jhingan, 2002). Usually measured by the Gross Domestic Product (GDP) growth rate, is growth rate measured by an increase in the number of goods and services produced in each successive time period (Glarmer&Fitzer, 2007). Thus, a nation is said to have grown economically when its productive capacity increases resulting in the production of more goods and services. It is for this growth that FDI is encouraged by economic and trade policies of many developing nations where gaps exist between the desired level of growth and internal productive capacity (Nemur & Rama, 2010).

Foreign Direct Investment (FDI): It is defined as an increase in the book value of the net worth of investment in one country held by investors of another country where investments are under the managerial control of the investor (Graham, 1995). FDI are therefore substantial investments made by a company or an investor into a concern. It is a purchase of an interest in a company by a company of an investor located outside its borders (Charles & Peter, 2013).

Generally, the term is used to describe a business decision to acquire a substantial stake in a foreign business or to buy it outright in order to expand its operations to a new region (Strautt&Rato, 2014). It is in agreement with Strautt and Rato (2014) that Mortio and Smart (2015) noted that most FDI is subsidiaries of Multi-national Corporations (MNCs) with foreign investors as parent organizations of the firms. Thus Telisman (2016) viewed that FDI flows represent the expansion of international activities of MNCs.

Empirical Review

Awe (2013) conducted a study on the impact of FDI on economic growth in Nigeria. The aim was to examine the impact of FDI on economic growth in Nigeria from 1976-2006. Data for the study were obtained from the CBN Statistical bulletin and financial review of the years. The collected data were analysed using two Stage Least Square (2SLS). Findings revealed a negative relationship between economic growth proxied by GDP growth rate and FDI.

Oyegoke, Ebunoluwa and Aras (2021) did a study on the impact of FDI on economic growth in Nigeria from 1970-2019. The aim was to determine the effect of FDI on the host country and also to evaluate the effect on the owners of the investment. Data for the study were obtained from World Bank (WB) bulletin on economic indicators. The results of simple regression analysis indicated that FDI inflows have a positive impact on the economy.

Okolie and Lambo (2018) investigated the impact of FDI in Nigeria. Data for the study were obtained from the NBS bulletin on FDI in Nigeria. Analysis of the data was done using Ordinary Least Square (OLS) regression. Findings suggested a negative impact of the investment on the Nigerian economy.

Chamberlin and Okon (2017) examined the determinants of FDI in Nigeria using the Error Correction Model (ECM): Evidence from the analysis indicated security, exchange rate and size of the market as core determinants of FDI in the nation.

Tuileh and Osadaru (2017) examined the relationship between oil exports, external borrowing and FDI between 2010 -2016 and economic growth in Nigeria. Data collected from CBN statistical bulletin were empirically analyzed using multiple regressions. Findings suggested that external borrowing and FDI negatively impacted GDP.

Onemah and Tajn (2019) did a study on determining the duty of FDI in Nigeria: It was an exploratory study that reviewed relevant literature of the subject matter. Evidence from studies reviewed suggested that the impact of FDI in Nigeria hinges on appropriate trade policies and the operating environment in Nigeria.

Omotola and Olubumi (2016) carried out a study on the role of FDI on economic growth and development in Nigeria. The aim was to examine the impact of FDI in promoting labour efficiency and productivity in Nigeria. Data from 120 employees in six (6) MNCs in Nigeria were descriptively analysed. Findings suggested that FDI has a positive impact on efficiency and productivity promotion in Nigeria.

Moledu and Odawna (2017) studied the stimulating effect of FDI on economic growth in Nigeria. Data collected from CBN and NBS bulletin were analysed using multiple regression. Results indicated that FDI negatively impacted the growth of the nation's economy.

Akiri, Vehe and Ijuo (2016) carried out a study on FDI and economic growth in Nigeria: An empirical data. Data for the study were collected from CBN annual reports from 1981-2014. The results of the Vector Error Correction Model (VECM) analysis showed a significant positive effect of FDI on economic growth in Nigeria.

Emmanuel (2016) examined the effect of FDI on economic growth in Nigeria. The aim was to investigate the relationship between FDI and economic growth. Using time series, data for the study were collected from 1981-2015. The results of the multiple regression estimation techniques showed a statistically significant relationship.

Anetor (2019) conducted a study on economic growth effects of private capital inflows: A structural VAR approach. Data obtained from 1961 Q1 – Q2 2016 were obtained from NBS. Results of the structural vector auto-regression model showed that shocks of FDI and portfolio investment inflows have a positive and significant direct relationship with economic growth in Nigeria.

Survey and Deulo (2017) examined the impact of FDI on the growth of developing nations. It was exploratory research that studied the impact of technology and knowledge transfer through FDI on the economies of developing countries. The results showed that the impact of FDI advantages depends on the openness of the markets and business climate of the recipient countries.

Diafor and Ermafla (2017) examined the extent to which economic growth in developing nations are influenced by FDI inflows. Data for the study were obtained through WB reports on developing nations from 2000 – 2016. Results of the OLS estimation technique indicated a positive relationship between FDI and the economic growth of developing nations.

Sokang (2018) carried out a study on the impact of FDI on economic growth in Cambodia: Empirical evidence. Data for the study were collected between 2006 – 2016 utilizing time series and reports of WB. The analysis of the data was done using a correlation matrix and multiple regression. The results indicated a positive relationship between FDI and economic growth in the country.

Trang, Anh and Thang (2019) examined FDI and economic growth in the short-run and long-run: Empirical evidence from developing countries. Data for the study were obtained from WB reports on developing nations from 2000 – 2014. Fully Modified OLS (FMOLS) and VECM were used to analyze both the short and long-run impact of FDI. Results indicated that FDI stimulates growth in the long run with a negative impact exhibited on economic growth in the short run.

Methodology

Data Collection Instrument

Data for the study were obtained from the Central Bank of Nigeria (CBN) annual reports and accounts publications and National Bureau of Statistics (NBS) bulletins.

Data Analysis

The analysis was done using multiple regression while E – view version 10.0 was the tool for the analysis. A further diagnostic test was carried out which include Durbin Watson and Multicollinearity tests.

Model Estimation

The a prior expectation was $\beta_1>0$, $\beta_2>0$, $\beta_3>0$, $\beta_4>0$, $\beta_5>0$, $\beta_6>0$

Model Specification

The model used for the study was adopted from the work of Morren (2007) and Dooman (2012) by including variables such as External Debts (EXD), Domestic Investment (DI) Export (EXP), Inflation Rate (InFR) and Exchange Rate (EXR). These are determinants of growth rate in developing nations apart from FDI. In the study;

$$Y = a + \beta_1 x_1 + \beta_2 x_2 - - - - - \beta_6 n x_n + \varepsilon \text{ ....equation1}$$

Economic growth is proxied by GDP growth rate (y) while x_1, x_2, x_3, x_4, x_5, and x_6 represents the explanatory /independent variables decomposed into FDI, EXD, DI, EXP, InfR, and EXR.

Substituting these in equation 1, it becomes:

$$GDP = a + \beta_1 FDI + \beta_2 EXD + \beta_3 DI + \beta_4 EXP + \beta_5 InfR + \beta_6 EXR + \varepsilon \text{....... Equation 2}$$

Where:
GDP= Gross Domestic Product (proxy for economic growth)
a= Intercept
FDI = Foreign Direct Investment
EXD = External Debt
DI = Domestic Investment
EXP = Export
InfR= Inflation Rate
EXR= Exchange Rate
ε = Error term
Therefore equation 2 was used for the analysis.

Results

Table 1: Regression Analysis using Ordinary Least Square

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	18.17266	15.53634	1.169687	0.2948
FDI	-4.886629	4.880194	-1.001319	0.3626
EXD	-0.589950	0.745027	-0.791851	0.4643
DI	0.149900	0.239924	0.624783	0.5595
EXP01	0.281312	0.427067	-0.658706	0.5392
INFR	-0.117447	0.565861	-0.207554	0.8438
EXR	5.833077	7.737570	0.753864	0.4849
R-squared	0.544367	Mean dependent var		3.299167
Adjusted R-squared	-0.002392	S.D. dependent var		3.113000
S.E. of regression	3.116721	Akaike info criterion		5.402638
Sum squared resid	48.56975	Schwarz criterion		5.685500
Log likelihood	-25.41583	Hannan-Quinn criter.		5.297912
F-statistic	0.995626	Durbin-Watson stat		2.023028
Prob(F-statistic)	0.512517			

Source: Computation using E-Views v10 (2021)

Findings and Conclusion

The results of the regression analysis indicated that about 54% of the variation in the dependent variable (GDP growth rate) are explained by the explanatory variables.

Further, on the a priori expectation, DI, Exp and EXR have positive signs indicating a direct and significant impact of the variables on GDP growth rate, Similarly, the positive signs of t-statistics results for the variables is an indication of the existence of a strong relationship between GDP growth rate and the explanatory variables at 10% level of significance with values of 0.62, 0.658 and 0.753 for DI EXP and EXR respectively. However, the negative signs of -4.886, -0.5899 and -0.117 for FDI, EXD and InfR are indications of inverse and non-impact of the variables on GDP growth rate in Nigeria. The t-statistics values of the variables showed a similar pattern with -1.00, 0.791 and -0.207 for FDI, EXD and InfR respectively. The results of the non-impact of the variables particularly that of FDI on GDP growth in Nigeria is consistent with studies (Awe, 2013, Moledu&Odawna, 2017; Tuileh&Osadam, 2017: Okolie& Lambo, 2018, Lekan &Eniola, 2018: Omeruo, 2018 Galatti, 2019 and Kadii&Egbu, 2020) that discovered FDI as a not viable investment for the growth of Nigerian economy. Similarly, continuous incurring of external debt and rising inflation in the country are not variables that can trigger economic growth a finding consistent with Tuileh&Osadaru, 2017.

Further, the F-statistics shows that the model is useful and significant at 1% with a 0.995 value. It further shows that all the explanatory variables have a measure of impact at a 1% level on GDP growth rate. The result is consistent with the regression analysis indicated by the coefficient of determination (R^2)that showed the explanatory capacity of the independent variables of the likely changes in GDP growth rate at 54% in Nigeria.

In overall, the Durbin Watson (DW) value at 2.02 indicates that there is no serial autocorrelation since the calculated value is greater than the upper value (DWu) at 1.883. This, therefore, implies the fitness of the model of the study.

Conclusion and Recommendations

That FDI has not impacted on the GDP growth rate in Nigeria does not mean that the investment impacted elsewhere on the globe. FDI has helped many nations especially the developing ones to grow their economies. The non-impact of the investment is issues of which a Myriad of factors is responsible. Key among the factors is the nature of the operating environment.

Therefore, on the basis of the findings of this study and conclusion, the following are recommended:

1. Government should encourage domestic investment by providing enabling environment especially infrastructure improvement.
2. A viable code of conduct and Nigeria's business ethics for MNCs to curb their oligopolistic and restrictive practices in order to limit their profit repatriation from the country
3. Nigeria should rigorously guide the trade liberalization policy of the World Trade Organization (WTO) for advice in areas to be resisted especially those that may be detrimental to the growth of the economy.
4. Nigeria local contentment initiative should be encouraged, production and export of Nigerian products should also be encouraged. The value of Nigeria's currency is a function of the productive capacity of the nation.
5. The issue of insecurity in Nigeria should be sincerely and properly addressed. No investment domestic or foreign can thrive in an environment tensed with insecurity.

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