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Specific Analysis of FDI and Economic Growth in Nigeria and Ghana

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ABSTRACT: *This study analyses the relationship between FDI and economic growth in Nigeria and Ghana and how these relationship differ between both countries. This was explored using annual time series data obtained from the World Bank WDI for the period 1970-2015. This paper adopted the Absorptive Capacity theoretical framework and using the Seemingly Unrelated Regression (SUR) technique, regressed economic growth (proxied by the growth rate of per capita real GDP) on FDI, FDI transmission channels, and five other control variables. After conducting all the necessary and sufficient statistical, economic and econometric tests, the results show that: (i) generally, FDI exerts some positive impact on economic growth in both countries; (ii) the absorptive capacity theory does not hold in both countries, (iii) there is a bi-directional causality running from FDI to economic growth and from economic growth to FDI in both countries; (iv) the relationship between economic growth and FDI does not differ between both countries.*

Keywords: *economic growth, FDI, Nigeria, Ghana.*
JEL Classification*: E22, E27*

I. INTRODUCTION

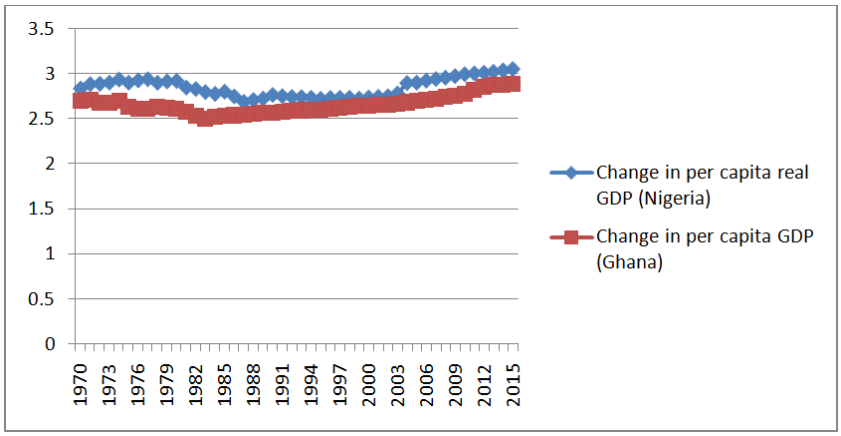
Africa has continued to experience high and continuous increase in GDP in the past decade. The average annual growth rate of real output increased from 1.8% between 1980 and 1989, to 2.6% between 1990 and 2000, and to 5.3% between 2000 and 2010. Unfortunately, this growth has not led to the development of productive capacities and structural transformation as reported by UNCTAD (2014). Also, just as the increase in growth, population has been on the increase as well hence having a kind of 'lid effect' on growth.

As reported by Umoh, Jacob and Chuku (2012), the average GDP growth rate of 3.95% achieved in Nigeria between 1970 and 2008 translates into a low growth rate of 1.49% in terms of per capita income. One of the striking features of the Nigerian economy is that it has not grown. Per capita GDP in 2006 ($847.5) is almost the same as it was in 1980 ($840.5). The growth rate of per capita GDP in Nigeria is even worse. The growth rate has hovered between 2% and 3% over the years.

The growth rate of per capita real GDP in Ghana tells the same story with that of Nigeria. Although the growth rate of GDP in Ghana is impressive, when this is compensated for inflation and population growth, it translates into a relatively poor growth.

Figure 1 shows the growth of per capita real GDP for the two countries. From the graph, it is clearly seen that the economies of Nigeria and Ghana has refused to grow. The economies of these two countries have managed to remain fairly stagnant amidst economic, social, political, and financial reforms being adopted by their various governments.

Figure 1: Growth Rate of Per Capita Real GDP: Nigeria and Ghana; 1970-2015



Source: World Bank.

Nigeria is a country which until the mid 90s was very much skeptical about FDI inflows. This can be seen from the FDI restriction policies which the country operated. The indigenization policy which started in 1972 with the Nigerian Enterprise Promotion Decree (NEPD) tightened restrictions on FDI, the NEPD was reviewed in 1979 and was further tightened to reduce foreign participation, UNCTAD (2009). With the increase in empirical and practical evidence supporting FDI as an engine of growth, Nigeria began to open up her economy to encourage more foreign participation. By 1989, the NEPD was relaxed to accommodate more foreign participation in Nigeria's economic scene. The Nigerian Investment Promotion Commission Act was enacted and it subsequently created The Nigerian Investment Promotion Commission (NIPC). The NIPC finally opened all sectors of the economy in 1995 to foreign participation except for some delicate sectors. Since then, the country has undertaken some actions as well as enacted some policies to attract more FDI and make its macroeconomic scene more FDI conducive. It is pertinent to point out at this point that the NIPC was created to attract investment in and outside Nigeria through promotional means, and as well serve as a one-stop agency and a coordinating centre that would consider and grant all industry related approvals under one roof. Some of the policies/actions undertaken by the NIPC to attract FDI are liberalizing the country's FDI enabling framework, marketing the country as preferred FDI destination, targeting investors in line with the country's developmental needs, reduced many bottle-necks and obstacles that act as disincentives to foreign investors, etc., Usman (2007). These actions were taken to achieve the three-fold vision of enhancing the image of the country (image building), generating an increased flow of investment (investments generation) and helping investors (investors servicing). All these were done to increase FDI inflow with the sole aim of achieving economic growth in line with empirical finding from studies on FDI and economic growth.

Attracting FDI has been a main feature of Ghana's Economic Recovery Program, which started in 1983 under the auspices of the World Bank and the IMF. The government of Ghana to this end has embarked on many programs to ensure continuous increase in the inflow of inward FDI into the country. The creation of the Ghana Investment Promotion Centre (GIPC) was a first step in the right direction. The GIPC was laddened with the sole responsibility of encouraging and promoting investment in Ghana as well as acting on behalf of the government to monitor and co-ordinate all investment activities within the country. The GIPC monitors investment in all sectors of the economy except for minerals and mining, oil and gas, and the Free Zone Areas. The GIPC in a bid to attract more FDI into the country has streamlined procedures and reduced delays and has also provided assistance to enable investors take advantage of relevant incentives. The government of Ghana has also embarked on many other FDI attracting policies. They include the Economic Recovery Program of 1983 (which in its second phase introduced the divestiture program and witnessed the divesting of government from many SOEs); the Vision 2020 of 1994 (which as part of its policies enacted the Investment Code), the Private Sector Development Program Strategy of 2004-2008, the Trade Sector Support Program of 2006-2010, etc., UNCTAD, (2014).

Table 1: Ranking of inward FDI stock by host country (in Billions of US$)

Country	FDI Stock	Position
South Africa	163.5	1st
Nigeria	111.4	2nd
Morocco	44.5	3rd
Mozambique	13.5	4th
Zambia	12.4	5th
Tanzania	9.2	6th
Uganda	7.7	7th
Ghana	7.1	8th
Namibia	5.8	9th

Madagascar	4.9	10th

Source: UNCTAD World Investment Report 2014

Owing to all these reforms, FDI in Nigeria and Ghana have continued to grow at a rapid pace. The World Investment Report of 2014 shows Nigeria and Ghana to be among the top ten FDI destinations in Africa. Ghana's economy particularly witnessed a remarkable increase in FDI in flows in 2006 (76.6 percent increase) and this increase has been sustained over the years.

Despite these increases in FDI inflows, the economic growth rate of Nigeria and Ghana (measured by the growth rate of real GDP per capita) is not what it ought to be. Table 2 presents the ranking of countries in Table 1 in terms of 2014 economic growth rate. The order in table 1 has not been reversed, only the position changed.

Table 2: Ranking based on 2014 economic growth rate

Country	Economic Growth rate	Position
South Africa	3.78	1st
Nigeria	3.04	4th
Morocco	3.41	3rd
Mozambique	2.73	8th
Zambia	3.01	5th
Tanzania	2.77	7th
Uganda	2.64	9th
Ghana	2.88	6th
Namibia	3.67	2nd
Madagascar	2.43	10th

Source: World Bank

The implication of Tables 1 and 2 does not augur well for Nigeria. She received the highest FDI inflow after South Africa but her economic growth rate ranks 4th. Morocco and Namibia who received lesser FDI inflow surpassed her in economic growth. Although Ghana's position improved in terms of economic growth, Namibia out-performed her in terms of economic growth. The above scenario brings to mind many provoking thoughts. Exactly how much does FDI explain economic growth? What is the nature of the relationship between FDI and economic growth? Could it be that the reason why the FDI position in table 1.1 and growth position in table 1.2 are not the same is because FDI inflow in year t explains economic growth in year t+n; where n is any positive number. This calls for an investigation into the relationship (as well as the nature of the relationship) between FDI inflows and economic growth. It is against this background that this study wants to address the following questions: (i) what is the effect of FDI on economic growth in Nigeria and Ghana? (ii) what is the causal relationship between FDI and growth in Nigeria and Ghana? (iii) how does the relationship between FDI and economic growth differ in Nigeria and Ghana? The main objective of this study is to examine the relationship between FDI and growth in Nigeria and Ghana between the periods 1970 and 2015 using the Seemingly Unrelated Regression test. In order to achieve this broad objective, the research is specifically designed: (i) to ascertain the effect of FDI on economic growth in Nigeria and Ghana? (ii) to determine the causal relationship between FDI and growth in Nigeria and Ghana? (iii) to examine how the relationship between FDI and economic growth differ between Nigeria and Ghana. The study therefore seeks to test the following null hypotheses: (i) FDI has no significant effect on economic growth in Nigeria and Ghana. (ii) there is no casual relationship between FDI and economic growth in Nigeria and Ghana. (iii) the relationship between FDI and growth in Nigeria and Ghana does not differ.

II. LITERATURE REVIEW

The Neo-Classical Theory**:** Much of what is known of FDI and growth in the neo-classical growth model was developed by Solow (1956, 1957), Nowbutsing (2009). It explains FDI through capital accumulation which is subject to diminishing returns, Because of this; it is widely held within the Neo-classical framework that FDI influences only the level of income and not long-run growth rate. As exogenous factors cause FDI to increase, the volume of capital in the host country increases too; soon however, diminishing returns on the marginal productivity of capital sets in. This counters the initial increase in capital accumulation and prevents the growth from lingering in the long-run. The point being made is that increasing the rate of savings alone (even permanently) will make output grow faster but this growth would be only temporary unless it is accompanied by technological progress (Solow 1987) and/or spillovers. Thus we end up with a model of growth

that explains everything but long-run growth, an obviously unsatisfactory situation, Barro and Salai-i-Martin (2004). This leads to the new growth theory.

Recent Endogenous Growth Models: Having seen that the Neo-classical theory which postulates that FDI as defined by capital accumulation does not guarantee permanent output growth or long-run economic growth, the new growth theory primarily focused on improving it. Seminal studies on the new growth theory done by Arrow (1962), Shell (1966), and reviewed by Romer (1986, 1990), Lucas (1988), and Grossman and Helpman (1991) focused on the role of technology and its transfer on economic growth (Nowbutsing 2009, Andinuur 2013). These growth models therefore recognize FDI as influencing economic growth through first of all influencing R&D and human capital. Although diminishing returns within the enterprise is possible, externalities outside the enterprise can sustain this growth making it to prevail even in the long-run. According to Romer (1986) quoted in Nowbutsing (2009), investment in knowledge generates natural externalities and the creation of new knowledge (e.g. technological knowledge) by one firm would have a positive external effect on other firms because knowledge cannot be perfectly patented or kept secret. With this, these models explore the role of human capital accumulation and externalities on growth and therefore see economic growth as a function of innovative technologies available in the economy. These externalities are created both directly (by the transfer of new technology and organizational form to its affiliates) and indirectly (through spillovers to other firms) by the TNFs.

Nowbutsing (2009) developed a theoretical framework which explains the impact of FDI on economic growth while controlling for host country's absorptive capacity. He sets a minimum absorptive capacity (measured by an absorptive capacity index) and defines the absorptive capacity gap as the difference between the country's minimum absorptive capacity and the country's current absorptive capacity. Borensztein et al (1998) supported the notion that FDI has an overall positive effect on economic growth but subject to the host country's level of human capital. The view of positive relationship is supported by Carkovic and Levine (2002) Alfaro (2003), Abdullahi et al (2012), Vegter (2012), Andinuur (2013), Antwi et al (2013), Aveh, Krah, and Dadzie (2013), Insah (2013) , Umoh, Jacob, and Chuku (2012)while negative relationship is buttressed by Berthelemy and Demurger (2000) and Osuji (2015)

III. MODEL

This study employs the classical linear regression model and adopts the Theory of absorptive capacity as proposed by Nowbutsing (2009). In order to capture objective 1, the model is specified as:

NG= $B_1 + B_2NFDI + B_3NGC + B_4NIO + B_5NM + B_6NCF + B_7NFRAC + U$

GG = $B_1 + B_2GFDI + B_3GGC + B_4GIO + B_5GM + B_6GCF + B_7GFRAC + U$

Where N and G before each variable denotes Nigeria or Ghana respectively, G= economic growth, FDI= Foreign Direct Investment GC= government consumption, IO= industrial output, M= broad money, CF= gross fixed capital formation, FRAC= infrastructure.

To incorporate the adopted theory, we have the following channels interacting with FDI to affect growth.

Access to credit:

NG= $B_1 + B_2NFDI + B_3NGC + B_4NIO + B_5NM + B_6NCF + B_7NFRAC + B_8NFDI * NCRED + B_9NCRED + U$ ……..2a

GG = $B_1 + B_2GFDI + B_3GGC + B_4GIO + B_5GM + B_6GCF + B_7GFRAC + B_8GFDI * GCRED + B_9GCRED + U$ ……...2b

Education level:

NG= $B_1 + B_2NFDI + B_3NGC + B_4NIO + B_5NM + B_6NCF + B_7NFRAC + B_8NFDI * NEDU + B_9NEDU + U$ ……..3a

GG = $B_1 + B_2GFDI + B_3GGC + B_4GIO + B_5GM + B_6GCF + B_7GFRAC + B_8GFDI * GEDU + B_9GEDU + U$ ……...3b

Public infrastructure:

NG= $B_1 + B_2NFDI + B_3NGC + B_4NIO + B_5NM + B_6NCF + B_7NFRAC + B_8NFDI * NFRAC + U$ ……..4a

GG = $B_1 + B_2GFDI + B_3GGC + B_4GIO + B_5GM + B_6GCF + B_7GFRAC + B_8GFDI * GFRAC + U$ ……...4b

Openness:

NG= $B_1 + B_2NFDI + B_3NGC + B_4NIO + B_5NM + B_6NCF + B_7NFRAC + B_8NFDI * NTOP + B_9NTOP + U$ ……..5a

GG = $B_1 + B_2GFDI + B_3GGC + B_4GIO + B_5GM + B_6GCF + B_7GFRAC + B_8GFDI * GTOP + B_9GTOP + U$ ……...5b

Objective 2 was attained by applying Granger causality test to check the direction of the relationship between FDI and economic growth in Nigeria and Ghana. The model is specified thus:

For Nigeria:

$NG_t = \sum_{i=1}^{p} \alpha i\ NFDI_{t-1} + \sum_{i=1}^{q} \alpha i\ NG_{t-j} + \mu_{it}$ ……...6a

$NFDI_t = \sum_{i=1}^{p} \alpha i\ NG_{t-1} + \sum_{i=1}^{q} \alpha i\ NFDI + \mu_{2t}$ ……6b

For Ghana:

$GG_t = \sum_{i=1}^{p} \alpha i\ GFDI_{t-1} + \sum_{i=1}^{q} \alpha i\ GG_{t-j} + \mu_{it}$ …….7a

$GFDI_t = \sum_{i=1}^{p} \alpha i\ GG_{t-1} + \sum_{i=1}^{q} \alpha i\ GFDI_{t-j} + \mu_{2t}$ ….....7b.

The work employed secondary time series data for Nigeria and Ghana sourced from World Bank's World Development Indicator (WDI) 2015

IV. RESULTS

Test for Unit Root: The Augmented Dickey fuller was used to test for unit root. The result is summarized in table 3 below.

Table 3: Result for Unit Root

Variable	ADF Statistic	ADF Critical Value At 5%
NG	-5.688*	-2.947
GG	-4.274*	-2.947
NFDI	-9.052*	-2.950
GFDI	-4.379	-2.947
NGC	-3.067	-2.944
GGC	-4.999*	-2.947
NIO	-6.363*	-2.947
GIO	-5.451*	-2.947
NM	-5.956*	-2.947
GM	-6.104*	-2.947
NCF	-3.907	-2.944
GCF	-7.858*	-2.947
NFRAC	-9.386*	-2.947
GFRAC	-7.205*	-2.947
NCRED	-3.053*	-2.947
GCRED	-7.629*	-2.947
NEDU	3.201	-2.944
GEDU	3.976	-2.944
NTOP	-9.048*	-2.947
GTOP	-5.902*	-2.947

Where * denotes first difference and ** denotes second difference

Co integration: This was carried out to determine the existence of long-run relationship between the variables. The result is summarized in table 4.

Table 4: Result for Co integration

Equation	ADF Test Statistic	ADF Critical Value
1	-2.961	-2.947
2	-3.473	-2.947
3	-3.542	-2.947
4	-2.545	-2.947
5	-3.705	-2.947

a) Regression Result

In equation 1 which represents our basic regression in table 5, that FDI is an important variable for explaining growth in Nigeria and Ghana. Variables like industrial output, capital formation, and infrastructure are important in explaining growth in both countries, while government consumption and money are important in explaining growth only in Ghana

Table 5: Presentation of the SUR result

Variables	Equation 1	Equation 2	Equation 3	Equation 4	Equation 5
NFDI	0.0106	-0.0178	-0.0073*	0.022	0.0582
GFDI	0.0054	0.0132	-0.005*	0.0091	0.0147

NGC	0.0002*	0.0011*	0.0072	0.0000*	0.003*
GGC	0.0172	0.0148	0.0091	0.0159	0.0169
NIO	-0.0029	-0.0016*	0.0028	-0.0028	-0.0012*
GIO	-0.0080	-0.0075	-0.0005*	-0.0093	-0.0103
NM	-0.0023*	-0.001*	0.0006*	-0.0029*	0.001*
GM	0.0058	0.0015*	0.0036	0.0061	0.0058
NCF	0.0024	0.0017*	0.003	0.0025	0.0022*
GCF	0.0039	-0.0002*	0.0001*	0.0047	0.0039*
NFRAC	-0.0047	-0.0053	-0.0033	-0.0032	-0.0049
GFRAC	0.2227	-0.0006*	-0.0005*	0.0043	0.0014*
NFDI*NCRED		-0.0005*			
NCRED		0.003*			
GFDI*GCRED		-0.0013			
GCRED		0.0195			
NFDI*NEDU			0.0001*		
NEDU			0.0069		
GFDI*GEDU			0.0002*		
GEDU			0.006		
NFDI*NFRAC				-0.0005*	
GFDI*GRAC				-0.0006*	
NFDI*NTOP					-0.001
NTOP					-0.003
GFDI*GTOP					-0.0002*
GTOP					0.0014*

Variables with * are not significant.

The R^2 of the regressions in equation 1 are 0.68 and 0.86 for Nigeria and Ghana respectively, implying that about 68% of the variations in the dependent variables in Nigeria are jointly explained by the variations in the independent variables while that of Ghana is 86%.

Equations 2 to 5 present the interactive form of the model. Each equation allows FDI interact with one FDI transmission channel, one at a time. From the table, most of these interactive terms are not significant while those that are do not conform to the theory's stipulated behavior. The interactive term for access to credit for instance is not significant in Nigeria but negative and significant in Ghana The interactive term for education is also not significant in both countries although the education variable is. The same thing is also observed with infrastructure which is not significant in both countries. Trade openness is significant in Nigeria but bears the opposite sign and in Ghana, it is not. These imply that these variables are not important channels through which FDI enhance economic growth. The results of the regression show that the Theory of Absorptive Capacity is not valid in Nigeria and Ghana.

Table 6: Presentation of the Granger Causality Test for Nigeria and Ghana.

Null Hypothesis	F-Statistic	Prob
NG does not Granger Cause NFDI	1.12691	0.3346
NFDI does not Granger Cause NG	0.52347	0.5967
GG does not Granger Cause GFDI	0.72133	0.4926
GFDI does not Granger Cause GG	0.04126	0.9596

From table 6, the probability of each null hypothesis is greater than 0.05 hence we therefore reject them and conclude that growth and FDI Granger cause each other in Nigeria and Ghana.

V. SUMMARY, CONCLUSION AND POLICY RECOMMENDATION

This work was carried out to determine the nature of the relationship between FDI and economic growth in Nigeria and Ghana, the direction of this relationship, and how this relationship differ between the two countries. It employed the seemingly unrelated regression technique and the Granger causality test to check for the relationship and the direction of causation between these variables.

The theoretical framework adopted in this study necessitated allowing FDI transmission channels to interact with FDI to effect growth. These transmission channels are access to credit (ability to invest), education level (ability to learn and create), public infrastructure (ability to move and communicate), and trade openness (ability to trade). They are ways through which FDI could be absorbed in host country so as to lead to growth. The implication of this theory is that FDI is more effective in leading to host country's economic growth in the presence of these channels. This theory was tested simultaneously for Nigeria and Ghana using the SUR technique which under this circumstance would provide a better result than OLS since both countries are alike in some ways hence we expect their error terms to be related.

The result of our basic regression shows a positive significant effect of FDI on economic growth in both Nigeria and Ghana. This supports the FDI attracting policies of the government of the two countries over the years. However, when the interactive terms are introduced, the results become interesting. We observed that most of the interactive terms were either not significant or in contrast to theoretical expectations for both countries. We can therefore conclude from these results that the theory of absorptive capacity as proposed by Nowbutsing (2009) is not applicable to Nigeria and Ghana.

The Granger causality test was carried out to determine the direction of causality between FDI and economic growth for Nigeria and Ghana. The results show a bi-directional causality running from FDI to economic growth and from economic growth to FDI. This means that FDI and economic growth Granger-cause each other in the two countries.

VI. RECOMMENDATION AND CONCLUSION

Based on the findings of this research work, FDI has a role to play in enhancing economic growth and higher economic growth attracts more FDI. To directly attract more FDI inflows, the governments of Nigeria and Ghana should implement more FDI attracting policies. The government of Ghana has increasingly made her investment climate more investor friendly with the introduction of the National Policy on Public and Private Partnership (NPPPP). The government of Nigeria has also over the years, reduced restrictions on FDI inflows into the country. Much, however, still needs to be done. The most important aim of any policy that is aimed at attracting foreign investments should be to remove impediment to investments, that is, things that make returns on investment less certain. These include inadequate power supply, corruption, restrictive trade policies, poor infrastructure, unstable regulatory environment, unreliable dispute resolution mechanisms, exchange rate volatility, insecurity, slow and ineffective judicial system, delays in the passage of announced legislative reforms, and a poor property rights system. When all these are removed, foreign investors will be more willing to invest in Nigeria and Ghana and this will increase FDI inflows and lead to economic growth.

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