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EXCHANGE RATE AND FOREIGN DIRECT INVESTMENT (FDI): IMPLICATIONS FOR ECONOMIC GROWTH IN NIGERIA .

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ABSTRACT: Research reports have shown that foreign direct investment impacts on the growth and economic development of especially the developing countries like Nigeria. But the discourse issue lies in the type of impact – negative or positive. In the bid to find the impacts of FDI on the nation's" economic growth, researchers have reviewed many factors that influence FDI flow and therefore proffered solutions based on their findings. This research in literature review found that the relationship between exchange rate and FDI has been mostly ignored. And Nigeria being a developing economy in need of constant inflow of FDI is attracting little and having problem in retaining the ones attracted. Therefore the study investigates the impact of FDI on GDP, influence of exchange rate on FDI using a descriptive analysis of secondary data on exchange rate and FDI from the CBN Statistics data base. The findings of the study agrees with some other research report that Nigeria have so far attracted little of FDI and have lost much of the few it has attracted, yet there are good developmental resources to be desired which comes with FDI. The study also found a relationship between FDI, Exchange rate and Economic Growth in Nigeria and thus made recommendations for the domestic firms, government and other stakeholders.

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INTRODUCTION

The attraction of Foreign Direct Investment (FDI) have been seen in the recent time especially by developing economies as one important means of promoting economic development. This is probably because of its power of combining Capital, technology, management and marketing. FDI have been defined by several authors, Mwillima (2008) for instance, described it as an investment made in order to

acquire a lasting management interest and at least 10% of equity shares in an enterprise operating in another country other than that of the investor"s country.

According to OECD (2008) FDI is a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of establishing a lasting interest in an enterprise (the direct investment enterprise) that is resident in an economy other than that of the direct investor.

According to Asiedu (2001), the countries of the Sub-Sahara African region have had many reasons to depend on FDI for development, and some of those reasons in addition to improving investment capital have been outlined by some other researchers (Sjoholm, 1999; Obwona, 2001, 2004). To further buttress the importance of FDI to the economy of African countries, the New Partnership for Africa"s Development (NEPAD) made it one of their objectives to increase available capital to US$64 billion (Funke & Nsouli, 2003). Most of the developing economies (including in Nigeria) are experiencing the dearth of capital for investment, which is negative for their economic development. Therefore, these countries in order to arrest such situation have resorted to much investment especially as it relates to FDI, with the objective of improving the employment rate of the country as well as attracting economic growth and development. Economic development is achieved when FDI provide foreign capital as well as encourage additional domestic investment by linking the domestic economy so as to encourage employment creation (Jenkin & Thomas, 2002).

Adegbite and Ayadi (2010) opines that FDI helps in filling the gap in developing economies for domestic revenue generation, as a reaction to solving the lack of investment capital in developing countries as pointed out by other researchers (Asiedu, 2001; Funke and Nsouli, 2003; Obwona, 2004). To expatiate the benefits of FDI to the developing economies, Alfaro *et al*., (2006) asserted that there are other benefits in the form of externalities and adoption of foreign technology; such externalities as imitation, human resource development, licensing etc. Given the nature of the Nigerian economy as „developing", it is pertinent on the policy makers to channel the investment policies towards attracting foreign investments in order to benefits from its external resources of technology, managerial and marketing expertise in addition to capital boost. And given the nature and size of the Nigeria market, the country is qualified to be a major recipient of FDI in Africa. Nevertheless, Asiedu (2003) noted that the level of FDI attracted by Nigeria is mediocre when it is compared with her resource and potential need.

There are various research reports (Odozi, 1995; Oyinlola, 1995; Adelegan, 2000; Akinlo, 2004; Ayanwale, 2007) on the influence of FDI on the economic growth of Nigeria and numerous results have been presented with no clear empirical linkage between FDI and economic growth in Nigeria. Howbeit, Asiedu (2001) argued that the determinants of FDI may vary from region to region, and in same region, may vary from country to another and from one period to another in same country. But then in Nigeria, it has been observed that very few multinational companies and subsidiaries have had FDI in the country, and those investments have in most cases been lost or not retained for some reasons. Therefore, Nigeria being a developing economy in need of constant inflow of FDI, and is qualified to attract FDI, yet attracting little and having problem in retaining the ones attracted, raises questions. The questions are: have the much attracted FDI had any impact on Gross Domestic Product (GDP)? Does exchange rate have any influence on FDI? In answering these questions, this study shall be reviewing literatures in addition to a descriptive analysis of

secondary data on exchange rate and FDI sourced from the CBN Statistics data base, in order to find out the effect of exchange rate on FDI, and its impact on the economic growth of Nigeria.

FDI and Economic Growth

Ayanwale (2007) and Asiedu (2001) reported that the relationship between FDI and economic growth may be country and period specific. According to Ayanwale (2007), the relationship in Nigeria is still unclear which made them call for more studies on this relationship. It has been made clear that the problem of the developing countries in economic development is not that they are isolated from the advanced world but in their manner of relating with international system; and it has been established that FDI is one tool of joining the international economic system (Gelb, 2005). This makes it pertinent on the developing economies to formulate, implement, and maintain economic policies that will make for a comfortable economic environment such that FDI can be attracted.

However, researchers have found inflation autonomy and exchange rate variability as two important factors impacting on the inflow of FDI into the developing nations (Lahrèche and Bénassy, 2002; Gelb, 2005; Kiat, 2008). According to these research reports, inflation and exchange rate are two important anchors in monetary policy characteristics which Kiat (2008), described as presenting the impossible trinity, that unless trade-offs are done, economic stability will be difficult if not impossible. Musila and Sigue (2006) agreed that FDI is a major player for capital inflow to the developing economies, though with contest on its contribution to economic growth, yet they agreed that the benefits are higher than the cost on the economy. Some other researchers have identified that in as much as FDI is loaded with a package of potential growth enhancing attributes needed by the developing economies, that most of these economies lack the qualifying preconditions for attracting this package (Boransztain & Lee 1998; Collier & Dollar, 2001; Mc Aleese, 2004).

It is argued that FDI could be beneficial in the short term and not in the long run. In the work of Durham (2004), for example, a positive relationship between FDI and growth could not be established; rather they made suggestions that the effects of FDI are contingent on the "absorptive capability" of host countries. Obwona (2001) studied the determinants of FDI and their impact on growth in Uganda and came out with macroeconomic and political stability and policy consistency as variables that determine the flow of FDI in Uganda; then concluded that FDI have positive but insignificant effects on growth in Uganda.

Then Tsai (1991) furthering on the determinants of FDI inflow, posited that in as much as the need for FDI for the development of less developed countries (LDCs) is being appreciated, two important issues relating to FDI must be appreciated as well. Tsai's argument is that to understand and appreciate the place of FDI in the growth and development of the LDCs, firstly, its determining factors must be investigated. Secondly, the question should be looked at from the stand point of the LDCs so as to determine if there are factors that attract FDI which are within the manipulating powers of the LDCs. Or should we just agree to the argument of some researchers who posit that the LDCs play a relatively passive role in the determination of FDI"s direction and volume? That will become a difficult thing to do, noting that many research reports have been made to the importance of FDI to the development of the LDCs (Deepak, Mody & Murshid 2001; Akinlo 2004; Aremu 2005; Dauda 2007), so it leaves the LDCs to find how to tap into these capital flow.

In the views of Sjoholm (1999) confirmed by Blomstrom *et al.* (2000) and UNCTAD (2000), FDI brings technology transfer to the host

economy through their affiliates and other firms and transnational corporations which has the ability to speed up development as well as introducing new forms of human capital. Their explanation as supported by some other researchers is that this transfer of advanced technology from developed economies to the developing through FDI can come vertically as a link between affiliates and suppliers and consumers of host country (Smarzynska, 2002); as horizontal link between affiliates and domestic firms of same industry (Lim, 2001); labour turnover from affiliates to firms in the host economy (Hanson, 2001) and internationalization of R and D (Blomstrom & Kokko, 1998).

In agreement, Carkovic and Levine (2002) argued that the speed of technological change in any economy attracting FDI will then depend on the innovative and social capability of the host economy in addition to the ability of other enterprise in the country to absorb the change as it comes. Some other researchers have argued that the impact of FDI on the economy is not only on capital flow, but its direct impact on trade in goods and services (Markussen and Vernables, 1998); which is why Blomstrom and Kokko (1998) explained trade theory as expecting FDI inflows to result in improved competitiveness of host countries" exports.

FDI and Gross Domestic Investment (GDI)

Agreeing to the importance of FDI in the development of the LDCs, Jenkins and Thomas (2002) assert that this importance is not only in its contribution to economic growth by providing foreign capital but also by bringing additional domestic investment. Olaniyi (1998) studied the impact of direct foreign capital on domestic investment in order to find out its overall contribution in promoting domestic savings in Nigeria. According to their report, domestic savings is far more needed for investment growth in Nigeria than foreign capital inflows; implying that capital inflow is only meant to complement domestic savings. The argument by some research reports in favour of the link between FDI and productivity being due to foreign investors pursuing higher productivity and capital formation raises a fundamental question, which is, does FDI take place prior to higher labour productivity and capital formation? A discrepancy is observed in previous research attempt to measure spill-over effects from FDI. These researchers have failed to investigate in details the correlation between FDI and growth. Bell and Pavitt (1993) reports that FDI has generally been a consequence, and not a cause of growth in domestic investment and the industrialization of LDCs. Empirical evidence indicates that firms" desire to invest more is as a response to the expansion of sales which is a consequence of GDP growth. Saqib et al (2013) studied the impact of FDI on Economic Growth of Pakistan from 1981-2010 using GDP as the dependent variable on FDI, Total Debt Services, Gross Domestic Savings and Inflation as the independent Variables and reveals thus: there is a negative and significant relationship between FDI and GDP. They therefore, concluded based on some other facts, that GDI will be more useful to the economy especially if its dependence on FDI is limited, encouraging the government to promote domestic investments. They further opined that some other unverified variables that have to do with technology transfer and human capital may have some impact on the relationship between FDI and the host economy. Wai-Mum et al (2008) studied the relationship between FDI and Economic Growth in Malaysia. Their result shows a positive and significant relationship between FDI and Economic

Growth in Malaysia, which agrees with Antwi et al (2013) study in Ghana. Wai-Mum *et a.l* (2008) therefore

recommend that FDI should be encouraged in addition to the adoption of policies that enable domestic producers to adopt the technology transferred through FDI. In their view, corruption and foreign exchange volatility may have impacts on the relationship between FDI and Economic growth and therefore should be tackled. In agreement to the Wai-Mum et al (2008) report, Akinlo (2004) and Osinubi and Amaghionyeodiwe (2010) studied FDI and Economic growth in Nigeria and both concluded a positive relationship between the two variables. Akinlo (2004), as confirmed by Macaulay (2011) furthered that export, labour and human capitals are positively related to growth, and that capital flight has serious negative impact on FDI and should be discouraged.

Onu (2012) in their report, described FDI as "an engine of economic growth". They therefore recommended that government should fight corruption like tax evasion as a means of encouraging the inflow of FDI. From the above empirical review, it could be concluded and agreed to, that the impact of FDI on economic growth is highly dependent on the economic environment of the host country.

In as much as we have seen empirical literatures in support of the significant role of FDI in economic growth, the attack of the opponents of neoliberal policies and globalization on the exploitative nature of foreign investors, cannot be overlooked. This is seen in Gardiner (2000) who argues that as much as FDI is a potential enhancer of economic growth, the monopolistic tendencies of foreign investors is capable of crowding out domestic investment.

Gardener (2000) further argued that in order to frustrate the domestic firms who have inadequate resources, the multinational Corporations may engage in a kind of predatory pricing with the sole aim of limiting the domestic firms" access to the market which will result to greater negative externalities.

FDI in NIGERIA

Many studies on investment and growth in Nigeria have been reported with various results. Odozi (1995) studied the factors of FDI flow into Nigeria in the pre and post structural adjustment programme (SAP). They discovered that the macro policies obtainable in the pre SAP era discouraged foreign investments.

According to Aluko (1961), Brown (1962) and Obinna (1983) there is a positive link between FDI and economic growth in Nigeria. In Adelegan (2000), the seeming unrelated regression model was examined for the impact of FDI on economic growth in Nigeria, and it was discovered that FDI is pro-consumption and pro-import and therefore negatively related to gross domestic investment. Moreover, Akinlo (2004) found FDI to have small and not statistically significant effect on economic growth in Nigeria.

Nevertheless, it could be seen that the impact of FDI in the Nigerian economy is sector specific, as it is observed that the above studies that report negative significance were done on FDI with most concentration in the extractive industry; and comparing with Ayanwale and Bamire (2001) who studied firm level productivity spill over in Nigeria and report a positive spill over of foreign firms on domestic firm's productivity. Anyanwu (1998) studied the determinants of FDI in Nigeria and identified the major determinants as change in domestic investment, change in domestic output, indigenization policy, change in openness of the economy and change in market size. He further the indigenization policy which was abrogated in 1995 encouraged the inflow of FDI into Nigeria. Jerome and Ogunkola (2004) in the assessment of magnitude, direction and prospects of FDI in Nigeria, noted that in as much as there is an improvement in the FDI regime, there are deficiencies. These deficiencies they identified as the corporate and

institutional uncertainty.

Ebekozien, Ugochukwu and Okoye (2015) in their analysis of the trends of FDI inflows in the Nigerian construction sector, posited that to solve these deficiencies, the Nigerian government have established the EFCC, the ICPC and the NIPC in order to improve the corporate environment. But their study shows that in as much as the industrial sector has a positive correlation with FDI, it has attracted little FDI into the country. This points to the fact that some other factors could be responsible for the mediocre level of FDI inflow into Nigeria. Therefore, this discourse shall take a look at exchange rate and FDI for economic growth in Nigeria.

Exchange Rate and FDI in Nigeria

With the growing support for the importance of FDI to the economic growth of developing countries, many researchers have therefore, turned their attention to the factors responsible for the inflow of FDI into the LDCs. And having seen in the reviewed literatures above that Nigeria as a developing country needs much inflow of FDI and yet getting little and finding it difficult to sustain the ones already attracted, it becomes pertinent to find out the factor(s) responsible for such twist. This study takes a descriptive analysis of exchange rate as a determinant of FDI inflow into Nigeria.

Descriptive Analysis of Exchange Rate and FDI in Nigeria's Economic Growth.

From the figure 1 below, we see a steady rise in exchange rate (BDC Dollar) from year 2008 to 2016 except in 2010 which is lower than 2009. Then FDI (equity) have been so unstable as can be observed from figure 2 there was a decreasing movement between 2007 and 2010, then from 2010 it rose again till 2012. Then from 2014 till present 2016 it has kept falling. From figure 3 it is observed that the interaction between FDI – equity and exchange rate – BDC Dollar shows that whenever the exchange rate is increasing, FDI is falling. Then it could also be deduced that between 2011 and 2013 when the exchange rate seemed stable, it met with the FDI level at same point in 2012

This supports and explains the reason for the Asiedu (2003) assertion of the level of FDI attracted by Nigeria being mediocre. The analysis from figure 3 above shows that Nigeria has been losing the much attracted FDI to some other countries due to the fluctuating exchange rate. On the effect of Exchange rate volatility on FDI, researchers are of different opinions. Some agree to a positive effect; while others argue that exchange rate volatility have negative effect on FDI. In Foad (2005) the positive effect of FDI is seen in its role as an export substituting variable. That is to say that the increase in exchange rate volatility between the investing economy and the host economy induces a local production facility services from the multinationals to the host economy, rather than exports, which insulates currency risk. They further argued that given that there are a finite number of potential direct investments, economies having high degree of exchange rate volatility will lose out on FDI to economies with more stable currencies, which is in tandem with our analysis.

Osinubi and Amaghionyeodiwe (2009) investigated the effects of exchange rate volatility on FDI in Nigeria from 1970 to 2004, and came up with the report that foreign investors need not worry about exchange rate volatility. Their reason is that there is a significant positive relationship between real inward FDI and exchange rate; meaning that when the naira depreciates, real inward FDI increases, which is not far from the observations of our analysis that shows that FDI increase at same point when -

Table1. Yearly Average Exchange Rate 2007 – March 2016.

YEAR	IFEMDollar	BDCDollar	POUNDS	EURO	CFAFr
2007	125.74	127.39	247.99	169.63	0.26
2008	118.99	120.71	218.12	173.14	0.26
2009	123.06	161.64	230.75	205.39	0.31
2010	151.08	153.06	229.40	196.52	0.29
2011	155.78	159.32	242.76	212.11	0.32
2012	158.75	160.85	247.20	200.42	0.30
2013	159.27	162.46	243.97	207.05	0.31
2014	164.88	171.44	258.57	208.58	0.31
2015	195.51	222.77	295.25	214.21	0.32
2016 January	197	289.78	283.62	214.09	0.33
2016 February	197	328.83	281.79	218.55	0.33
2016 March	197	320.93	280.4	218.89	0.33

Source: CBN Statistics Data Base (Yearly Averages worked out by the researcher)

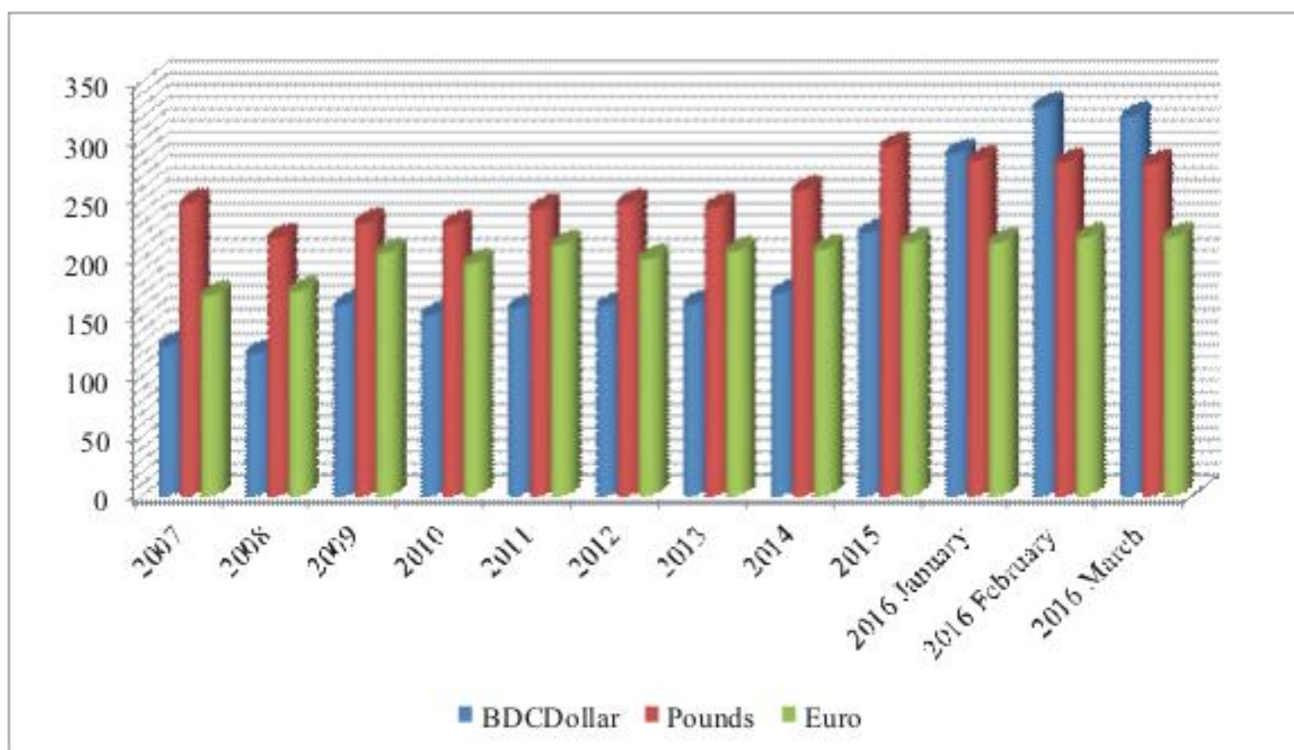

Fig. 1 Yearly Average Exchange Rate 2007 – March 2016.

Table 2: Yearly Average FDI ($US) 2007 – MARCH 2016.

Years	Descriptor	
	Foreign Direct Investment – Equity	**Foreign Direct Investment - Other Capital**
2007	353,627,917.63	3,169,758.97
2008	383,139,605.78	5,300,493.97
2009	275,473,189.88	1,726,609.73
2010	55,695,906.86	5,048,822.78
2011	124,908,916.27	21,203,274.72
2012	161,000,862.17	5,654,885.96
2013	104,224,571.89	2,394,613.72
2014	188,667,787.44	1,085,738.79
2015	120,200,232.92	350,867.30
2016 January	81,709,474.69	0.00
2016 February	72,894,236.40	0.00
2016 March	19,125,865.84	726,183.52

Source: CBN Statistics Data Base (Yearly Averages worked out by the researcher)

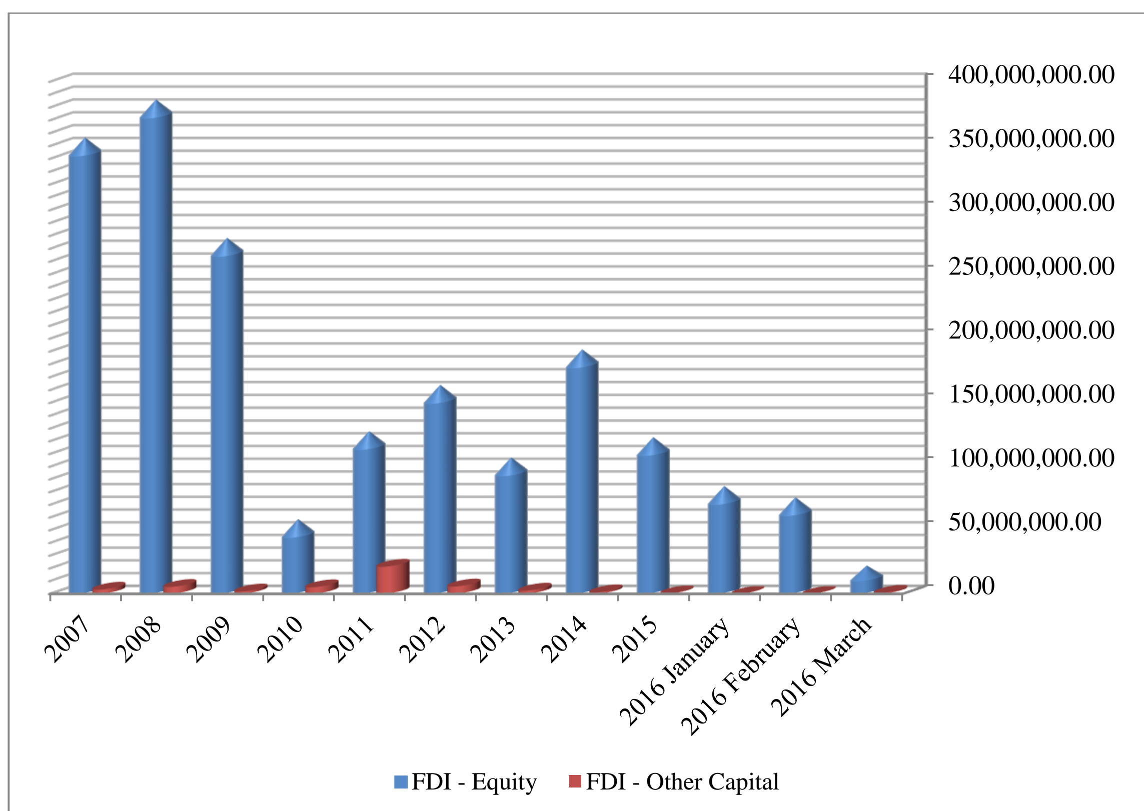

Fig. 2 Yearly Average FDI ($US) 2007 – MARCH 2016.

Exchange Rate and FDI in Nigeria – 2007 – 2016.

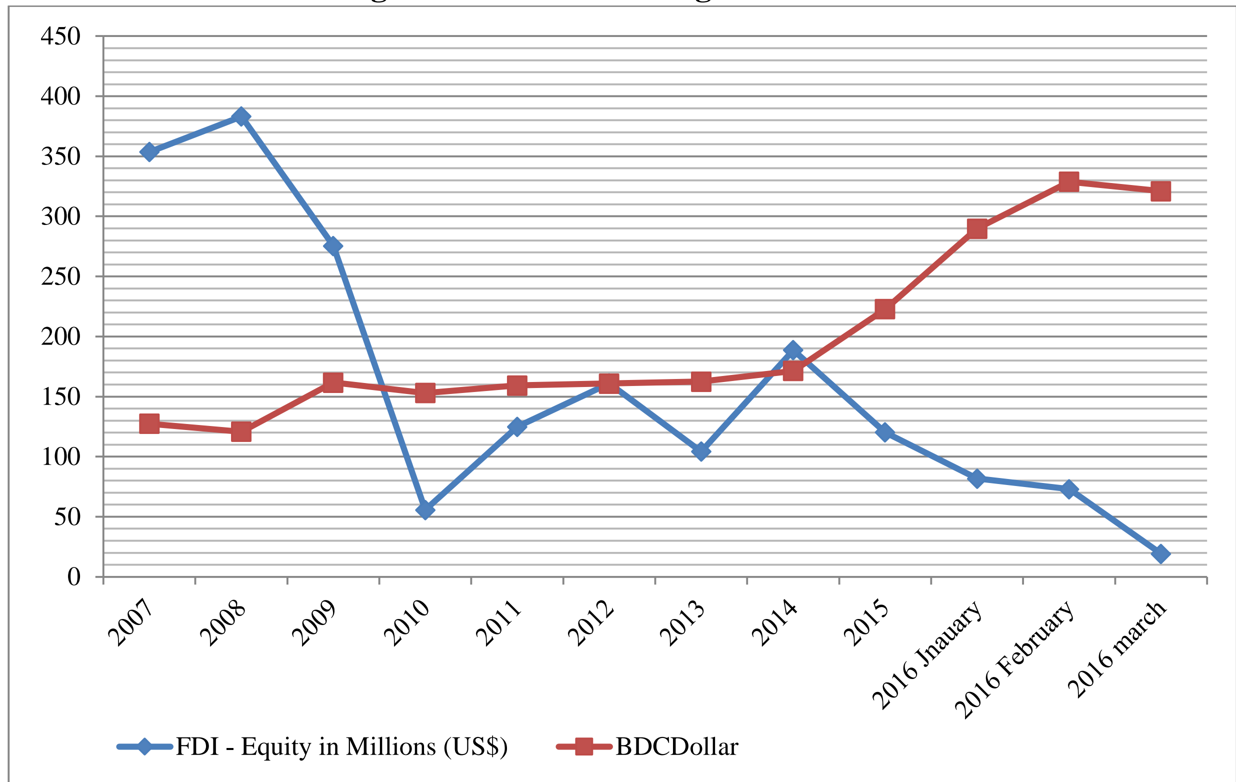

Fig. 3 Interaction between Exchange Rate and FDI

Exchange rate decreases against the naira. Alaba (2003) and Ogunleye (2008) studied exchange rate volatility and FDI in Sub Sahara African (SSA) countries, Alaba (2003) concluded for Nigeria, that the official market exchange rate volatility is not significant for FDI inflows to the manufacturing and agricultural sectors; and Ogunleye (2008) concluded in consonance with Udoh and Egwaikhide (2008) study for Nigeria, that the SSA countries does not receive the desired FDI because it is constrained by exchange rate volatility and all in consonance with the observations from the above analysis.

Conclusion

It has been discovered from various research reports that foreign direct investment has impacts on the growth and economic development of especially the developing countries like Nigeria. But the kind of impact, whether positive or negative is what has been discovered to be the issue of debate. Some researchers agree with positive significant impacts while others agree with negative impacts. In Nigeria various research report have been carried out on FDI and economic growth but majority of the literature reviewed in this discourse agree on positive impact of FDI on economic growth of Nigeria. Nevertheless, it has also been discovered that notwithstanding the much good to be derived from FDI, Nigeria have so far attracted little of it, and more so, the much that has been attracted have not so far been retained. This as a course for concern has led many research work into factors that determine FDI, and this discourse being one of them have looked at Exchange rate and FDI in economic growth of Nigeria.

In agreement with previous research reports, this study found a relationship between Exchange rate, FDI and economic growth. It is discovered that foreign direct investment brings technology and human resources upgrade

to the host economy. Therefore, if the domestic firms can tap into the resources of FDI, it will boost productivity, output, and quality products and invariably increase the GDP of the economy.

Recommendations

The paper have found FDI to be of great importance to the growth of the Nigerian economy, and that FDI have not been doing as it ought to do in Nigeria because some factors among which is exchange rate have been hindering its inflow into the country. Therefore, it thus recommends:

1. That the government in collaboration with the Central Bank and other policy making bodies in Nigeria make policies that will help the economy attain a table exchange rate regime. It is believed that this will not only attract real inward FDI but will also boost domestic production as it will help the domestic firms compete favourably with the multinationals.

2. If the above is done, it will also help the Nigerian economy to attract FDI, if the bureaucratic bottlenecks experienced by foreign investors through the customs and port authorities are minimized.

3. FDI deals with and requires ICT, therefore, the Nigerian government should work towards improving the country's ICT level. This includes electricity, road networks and other ICT infrastructures.

4. Crime and corruption especially as has to do with economic crimes, should be seen as an ill to the economy and therefore curbed to the barest minimum.

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