INFLUENCE OF ECONOMIC GROWTH AND FINANCIAL DEVELOPMENT ON FOREIGN DIRECT INVESTMENT IN SUB- SAHARAN AFRICAN COUNTRIES

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Abstract

Most countries in the world are working hard to attract more Foreign Direct Investment (FDI). Therfore any attempt to find out the influence of FDI is promount importnant. The paper seek to look into the influence of economic growth and financial Development on Foreign Direct Investment in Sub-Sahara African Countries for the period of 2000 to 2018. The study employed panel data analysis, including the panel unit root test, panel co integration test and fully modified least square method (FMOLS). The findings reveal that, all the variables were cointegration of order one and having a long run relationship. More so the results show that financial development was positive and statistically significant in influencing FDI in the region, while Economic growth was statistically insignificant in influencing FDI in the region. The findings suggest that, the goverments of the reigon should emphasized and reconsider the important of financial reform policies, in order to have a sound financial development to attract FDI.

Keywords: Foreign Direct Investment, (FDI), Fully Modified Least Square Method (FMOLS), Emerging Sub-Saharan Africa Countries (ESSAC).

Introduction

Developing countries foreign direct investment (FDI) has increased sharply over the past two decades. Several authors have noted this 1980s (2003), and UNCTAD,(2004). Most FDI has been invested in the region by Asian companies are getting new location in other Asian countries, but investments have also been made in developed countries like the EU. Overall investment by underdeveloped countries began to increase from about (1%) of total overseas investment flows in the late 1970s to (4%) in the mid-1980s and (6%) by 1990, and stayed around (6-7%) of overall

investment in the 1990s until the Asian financial collapse. The rise went hand in hand with the downturn in the wide gap among developing and developing country growth discovered in the 1970s as well as the downturn, in several instances an inversion, of overall protection in developed and developing countries (revival of protection in developed countries; liberalization in developing countries). In addition associated with a few drop in outflow growth to developing countries, suggesting that flows in both ways were affected by the very same factors. South-South flows are projected to have increased from (5%) in 1994 to (30%) in 2000 of cumulative FDI inflows to developing countries, Aykut and Ratha (2003) (as a residual and data and method task). . GDP mean refers to Rate of economic growth is a significant measure of a country's economic performance.): GDP of a country is the annual overall Productivity or throughout in a country excluding net income from foreign investments of the country. Anyanwu and Yameogo (2015).

Moreover, Gross Domestic Product (GDP) is the final value of the goods and services produced within the geographic boundaries of a country during a specified period of time, normally a year. GDP growth rate is an important indicator of the economic performance of a country. (GDP) is a monetary measure of the market value of all the final goods and services produced in a period of time usually, often annually or quarterly. Nominal GDP estimates are commonly used to determine the economic performance of a whole country or region, and to make international comparisons. GDP (nominal) per capita does not, however, reflect differences in the cost of living and the inflation rates of the countries; therefore using a basis of GDP per capita at purchasing power parity (PPP) is arguably more useful when comparing differences in living standards between nations. In other word the OECD defines GDP as an aggregate measure of production equal to the sum of the gross values added of all resident and institutional units engaged in production plus any taxes, and minus any subsidies, on products not included in the value of their outputs, also the International Monetary Fund (IMF) in it publication states that GDP measures the monetary value of final goods and services that are bought by the final user produced in a country in a given period of time say a quarter or a year. Total GDP can also be broken down into the contribution of each industry or sector of the economy. The ratio of GDP to the total population of the region is the per capita GDP and the same is called Mean Standard of Living. GDP is considered the world's most powerful statistical indicator of national development and progress.

Literature Review

Empirical work on the number of available literatures on Edward, Paul and Donatus (2019) examines the trends in Foreign Direct Investment (FDI) inflows to Africa,

with the ultimate aim of proposing implications for policy action. The period of study is from 1990 to 2016. The findings show that, although Africa is in dire need for FDI due to scarcity of capital, it is not able to attract as much FDI compared to advanced countries and other developing regions. The little FDI that comes to Africa is concentrated sub-regionally and country-wise. Region-wise, most FDI is concentrated on Southern Africa followed by Northern Africa with East Africa and Central Africa at the bottom. Country-wise, the two main recipients of FDI in each sub-region are Angola and South Africa (Southern Africa); Egypt and Morocco (North Africa); Nigeria and Ghana (West Africa); Tanzania and Ethiopia (East Africa) and Congo and the Democratic Republic of Congo (Central Africa). The FDI that comes into the continent is further concentrated in the primary (extractive) sector. The finding concluded that, FDI is a growth point that countries can count on as a source of resources for development, however, Africa need to change the approach adopted in promoting FDI, which focuses on providing incentives to creating a domestic environment conducive to entrepreneurship and business in general. Federico et al (2019) reassesses the impact of good governance and democracy on Foreign Direct Investment (FDI) in oil-abundant countries. They used gravity equation for a dataset that covers 182 countries during 2003-2012. Their findings confirm that compliance to rule of law, lack of corruption, political stability and democracy could boost new FDI links through the extensive margin and results could not rule out the oil curse, meaning that "oil producers attract fewer new Greenfield projects than similar countries without oil. Unlike other researches , we show that the impact of institutions is not necessarily undermined by the presence of natural resources.

Dondashe and Phiri (2018) , studied the determinants of FDI by including variables such as market size, economic growth, trade balance and wage rate. Study conducted by concluded that GDP per capita, the inflation rate, government size, real interest rate variable, and terms of trade have been directly influence the FDI inflow. Likewise Hemed and Suleiman (2017) indicated that the East African countries region must remain their economies open to attract more potential investors for improving economy and to achieve the desired objectives. Abimbola and Oludiran (2018) indicated that the infrastructure development attract the FDI inflow, since the the better the infrastructure the higher the probability of attracting the multinational corporation investment. Furthermore, Suleiman et al (2015) studied the determinant of FDI inflows for the SACU countries and the results reveal that market size, natural resource availability and trade openness are positive and significant determinants of FDI for the SACU member countries.

Taking in to sector level in Ghana, Ibrahim and Abdul Azeez (2019) assessed "the determinants of foreign direct investment (FDI) by using sector level data spanning 2000-2014, results from the Ordinary Least Squares (OLS) regression analysis show that market size and labour cost have significant impact on the inflows of agriculture sector FDI. The findings also confirm trade openness and exchange rate to significantly influence services sector FDI. Unexpectedly, none of the variables are found to have significant effect on manufacturing sector FDI. Their research recommends that the government should implement strategies that will enhance the growth of Ghana's GDP, and deregulate the economy to allow more foreign investors into the country. Arawomo and Apanisile (2018) assessed the key factors driving FDI in the telecommunication sector. Using annual sector level data from 1986-2014 with the Autoregressive Distributed Lag (ARDL) approach, the findings show that market size and trade openness have positive significant effect on FDI. Inflation and real interest rate on the other hand showed a negative significant effect on telecommunication sector FDI.

Kok and Ersoy (2018) investigated the best determinants of foreign direct investment (FDI) in developing countries. They investigate whether FDI determinants affect FDI based on both a panel of data (FMOLS-fully modified OLS) and cross-section SUR (seemingly unrelated regression) for 24 developing countries, over the period 1983-2005 for FMOLS and 1976-2005 for cross-section SUR. The results reveal that, the interaction of FDI with some FDI determinants have a strong positive effect on economic progress in developing countries, while the interaction of FDI with the total debt service/GDP and inflation have a negative impact. The "most important determinant of FDI is the communication variable. Dondashe and Phiri (2018) studied the macroeconomic determinants of FDI for the South African economy using data collected between 1994 and 2016 using the ARDL model for cointegration. The specific macroeconomic determinants which are used in their study are per capita GDP, the inflation rate, government size, real interest rate variable, and terms of trade. The findings reveal that with the exception of inflation the remaining macroeconomic determinants employed in the study are positively and significantly related with FDI. While, in the short-run all variables are positively and significantly correlated with FDI.

Abdul-hadi et al (2018) examined economic determinants of sectorial foreign direct Investment to six Asian countries .The research covers over a period from 2001 to 2016, by employing static panel data model. The includes inflation, gross domestic product growth, and government expenditure on education, electric power consumption, exchange rate, trade openness and lending interest rate as economic variables. Overall results reveal that "there is a mix result in terms of key

determinants of sectorial level inward FDI which proves that FDI is not a single phenomenon and that each sector must be treated on its own terms to attract FDI into the country.

Shan et al (2018) studied the effect of natural resources, market size and five major institutional factors on Chinese foreign direct investment (FDI) in Africa. The research used regression analysis on panel data across 22 countries for the period 2008-2014. Their results reveal that, natural resources did not play a significant role in attracting Chinese investments, but market size did. Among the institutional factors, only voice and accountability had a significant and positive effect on attracting Chinese FDI; the effects of rule of law and control of corruption were not significant and political stability and regulatory quality had a significant and negative effect. Ali, Faki and Suleiman (2018) studied the determinants of Foreign Direct Investment Inflows in SADC member countries, for the period 1995–2016. Their findings revealed that infrastructure, trade openness and market size are positive and significant determinants of FDI inflows in SADC Countries. However, human capital has positive insignificant and inflation has negative significant with FDI inflows for the SADC member countries. They recommended that, SADC countries should promote trade agreements to facilitate exportation which has linked with industrial sectors, and the countries should reform investment policy to attract more foreign inflow into SADC countries in the long run. Javid and Sharif (2016) and Salahuddin et al., (2015)" are due to methodological problems like model specification and methods of estimation among others. For example, Olabode and Evan (2018) found that, bidirectional causal relationship exists among trade openness, foreign direct investment net inflows and economic growth for Gambia, Senegal and South African countries.

Large domestic markets have been found to be important, especially if foreign companies wish to sell their products in the host country. Asiedu (2002) finds that most of the FDI flows in Sub-Saharan Africa (SSA) are aimed at buyers outside the country (non-market seeking FDI). A lot of the FDI into Africa flows to natural resources, which are then exported. However, over the years there has been an increase in the amount of FDI aimed at buyers in host countries (market-seeking FDI). Youssouf (2017) investigated the robust FDI determinants in sub-Sahara Africa for the period 1985 to 2012. His empirical analysis shows the following key findings: (i) natural resources and market size are the most robust determinants; ii inflation, infrastructure, human capital and trade openness are weak robust, iii corruption and political instability are very less robust determinants in sub-Sahara African countries. Ojewumi and Akinlo, (2017) investigated the dynamic interactions among the inflow of FDI, environmental quality and economic growth

of the countries in Sub-Saharan Africa (SSA). The dynamic interaction was examined through Panel Vector Error Correction (PVEC) and Panel-Vector Autoregressive (PVAR) methodologies on a sample of 33 SSA countries. The result of panel co integration test showed the evidence of long–run association among the variables. Tuman and Shirali, (2017) applied a cross-sectional time-series data set for 66 countries for the period of 2003–2010 investigate the impact of several political and economic variables on Chinese FDI in Africa and Latin America. They result found Chinese FDI is influenced by natural resources and trade flows in host economies, including ores, metals and oil resources, also being focused on markets with lower per capita income.

Materials and Method

Even though none of the researcher applies the Fully Modified Ordinary Square (FMOLS) model in analyzing the Influence of economic growth and financial instability of Foriegn Direct Investment in sub- Saharan African countries. Therefore, in order to investigate factors affecting the influence of economic growth and financial instability of Foriegn Direct Investment in sub- Saharan African countries, the research adopt Pravin and Jadhav (2012) model with some modification. The rationale for using this model is that the FMOLS model generates dependable estimates for the small sample size and offers a robustness check for the results. Initially, the FMOLS method was incorporated and maintained by Philips and Hansen (1990) to estimate a single co-integrating relationship with a mixture of I(1) and then has a benefit over the EG methods in implementing adequate correction" to resolve the inferential problem in the EG method and therefore the t-test for long-run estimates is valid (Himansu 2007).

Therefore the method was adopted based on the objectives of the research stated earlier and the nature of data used. The models are specified as follows:

$$FDI = F(GDP, DCB) \dots \dots \dots \dots \dots 1$$

Where:

FDI = Foreign Direct Investment, net inflows

GDP= GDP per capita (constant 2010 US$) proxy for Economic Growth

DCB= Domestic credit to private sector by banks (% of GDP) proxy for Financial Development

F= functional relationship

*= multiplication symbol

Therefore, the above equations are transformed in to econometric models as follows

$$FDI_{it} = \alpha + \beta_1 GDP_{it} + \beta_2 DCB_{it} + + \varepsilon_{it} \dots \dots \dots .. 4$$

Where, the prior expectations of the parameters in equation 4 are, β_1 and $\beta_2 > 0$ and in equation 5, $\beta_1 > 0$ and $\beta_2 < 0$ respectively

Results and Discussion
Descriptive Statistics

The natural starting point of our formal analysis is the examination of the stochastic properties of the data. Therefore, descriptive statistics describe the basic features of the data used in this study. The aim of this statistics is merely to summarize a data set, rather than being used to test the hypotheses. Table 1 presents the descriptive results of the variables used in the study. The variables are FDI, GDP and DCB, where FDI is the dependent variable while GDP and DCB are indipendent variables. The table shows that, GDP and FDI have the highest mean of 1.97E+10 and 1.98E+09 follow by DCB with mean of 27.44421 respectively. In terms of median the GDP and FDI still have the highest value of 1.21E+10 and 6.71E+08 among the variables; follow by DCB with 23.14496, The maximum and minimum value of the variables under study show that FDI has the maximum of 9.89E+09 and minimum of -7.12E+09, GDP with 1.04E+11 as maximum and 256.5394 as minimum, while DCB with 78.29413 as maximum and 1.966540 as minimum respectively, also the descriptive statistics, including the indicators of skewness and kurtosis, as well as the test for normality of the variables are presented. This allows us to make some inferences about the distribution of the variables. The distributions of the dependent variable FDI and other Independent variables appear to be normally distributed, as shown by the jarque Bera LM test. The dependent variable as well as Independent variables appears to have a kurtosis of less than three (3). explain the factors determining FDI in the selected ESSAC countries.

Table 1 Descritive Statistic

	FDI	GDP	DCB
Mean	1.98E+09	1.97E+10	27.44421
Median	6.71E+08	1.21E+10	23.14496
Maximum	9.89E+09	1.04E+11	78.29413
Minimum	-7.12E+09	256.5394	1.966540
Std. Dev.	2.86E+09	2.50E+10	17.19850
Skewness	0.084489	0.096081	1.600231
Kurtosis	2.890900	2.382060	2.853288
Jarque-Bera	7.676475	5.107255	7.150661
Probability	0.721532	0.413257	0.694512

Sum	2.69E+11	2.68E+12	3732.412
Sum Sq. Dev.	1.11E+21	8.47E+22	39931.46
Observations	136	136	136

Source: Author's Computation 2019.

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Cross–Sectional Dependence Test (CD TEST)

Cross-sectional dependence test was conducted in order to examine the contagious effects of shocks within the cross-sections (Pesaran & Yamagata, 2008). Table 3 presents the cross-secectional dependence tests based on Breusch-Pagan LM and Pesaran CD tests. The results, reveal that, all the variables have no presence of common factor affecting the cross sectional units which paved way to use the first generation panel unit root test.

TABLE 2   Cross-Section Dependence Test

Test	Statistic	d.f.	Prob.
Breusch-Pagan LM	29.5862	28	0.1023
Pesaran CD	40.009508		0.2501

Source: Author's Computation 2019

Panel Unit Root Test

In order to avoid spurious regression result, various panel unit root tests were conducted for the variables of interest under study, in order to investigate the respective order of integration. It is important to note that, no variable exceeds integration of order one, that is I(1) to avoid spuious result.Therfore, in oder to achieve this, the Levin et al unit root test was conducted.The test was estimated both at level and at first difference as presented in table 3 below

Table 3 Levin et al Unit Root Test

	At Level		At First Difference	
Variables	Statistic	Prob.	Statistic	Prob.
FDI	-0.24665	0.4026	-4.01942	0.0000*
GDP	2.06281	0.9804	-2.56062	0.0275**
DCB	0.20759	0.5822	-5.5705	0.0000*

Source: Author's Computation 2019

*Note : *&** indicate significant at 1% and 5% level of significance*

Table 3 shows the levin et al unit root test both with trend and intercept. The result reveals that all the variables are not stationary at level but stationary at first

defference with different level of significant. For example FDI and DCB were statioanry at 1% statistically level of significant while, GDP was statistically significant at 5% level of significant.This means that the variables are intigrated of order one I(1).

Panel Co-integration

The first objective of this study is to examine the role of Economic growth on FDI in emerging Sub- Saharan African Countries (ESSACs).

Table 4 shows the results of the Pedroni panel co-integration for the Economic growth and FDI in the of ESSACs .The table demonstrates that, the null hypothesis of no co-integration cannot be rejected for Panel v-statistics, Panel ρ-statistics and Group ρ-statistics. However, the null hypothesis of no co-integration is rejected for Panel PP-statistics, Panel ADF-statistics, Group PP-statistics and Group ADF-statistics at 1 percent level of significance.Thus, it can be concluded that the panel co-integration tests result for the Economic growth and FDI proved that the independent variables possess co-integration in the long run for the sampled emerging ESSAC countries.Therefore table 4 present the co integration result of the varriables.

Table 4 Pedoroni Co integration test

Pedoroni					
Alternative hypothesis: common AR coefs. (within-dimension)					
				Weighted	
		Statistic	Prob.	Statistic	Prob.
Panel v-Statistic		-1.714145	0.9567	-1.036593	0.8500
Panel p-Statistic		0.749199	0.7731	0.846562	0.8014
Panel PP-Statistic		-6.909029	0.0000**	-3.713677	0.0001**
Panel ADF-Statistic		-3.912057	0.0000**	-2.893411	0.0019**
Group p-Statistic		1.664460	0.9520		
Group PP-Statistic		-4.37059	0.0000**		
Group ADF-Statistic		-2.38395	0.0086**		

Source: Author's Computation 2019

*Note : *&** indicate significant at 1% and 5% level of significance*

Estimation of the Long Run Relationship

The existence of long run relationship between FDI and independent variables for emerging Sub- saharan African countries (ESSACs) qualified this study to estimate the FMOLS regression. Table 5 represents the FMOLS regression for the factor

determinants of foriegn Direct investment in the emerging Sub- saharan African countries (ESSACs).

From Table 5 , the estimated coefficient of DCB was positive and statistically significant at 1% level of significant in determining of FDI for sampled of ESSACs, while GDP found statistically insignificant in determining FDI in the sampled study area under review. The finding of this study contradict with the finding of Chowdhury and Mavrotas (2006) for Chile, Erdal and Mahmut (2008), for developing countries and among others. The result indicates that, sound financial development results in massive attracting of FDI in the region. That is, a 1 percent increase in financial development leads to 2.7 percent increase in FDI in the study area. This findings is in line with finding of Albulescu *et al* (2010), for Central and Eastern European countries, Tsaurai (2017),for developed economics and Abu et al (2017) for developing countries. While the finding shows that GDP is statistically insignificant in determining FDI in the Emerging Sub Saharan African Countries. This means that GDP is not among the variables that determine the level of FDI inflow in to the region. This finding is contrary with the finding of Shiba (2016) for India and Pravin and Jadhav (2012) for BRICS economies among others.

Table 5 FMOLS Regression for Economic Growth and Foriegn Direct Investment in the ESSACs Dependent Variable FDI

Variable	Coefficient	Std. Error	t-Statistic	Prob.
GDP	-0.068647	0.077951	-0.880642	0.3820
DCB	2.73E+08	32543779	8.388339	0.0000*
R-squared	0.779004			
Adjusted R-squared	0.709021			

*Source: Author's Computation 2019   Note : *indicate significant at 1% level of significance*

CONCLUSION

The aim of this research is to investigate the Influence of Economic Growth and Financial Development on Foreign Direct Investment in Sub- Saharan African Countries for the period of 2000 to 2018. The properties of panel data were checked to avoid spurious results followed by co integration analysis as well as estimation of the variables using FMOLS under study. Based on the findings of the research, the studies conclude that, financial development is the major determinant factos of attracting FDI in the study area.

POLICY IMPLICATIONS

The following are some of the suggested policy options and strategic alternatives that a most of those countries and policy makers should consider:

The policy makers in ESSACs should create and foster an enabling environment. This environment should include policies that aid the development of the private sector as well as collaboration between the public and private sectors to help in the proper functioning of markets.

ESSACs leaders should also continue to deepen macro economic reforms; emphasis should be placed on the reduction of fiscal deficits, inflation, interest rates and the strengthening of their various financial systems. The setting up of efficient securities trading and settlement systems and the presence of international custodians are important elements of such a financial infrastructure (Battacharya, Montiel and Sharma 1997).

ESSACs countries should also provide conducive and well-structured institutions to support investor friendly policies. These should include well functioning legal institutions that support market transactions, protect property rights as well as laws that protect investors in times of upheavals or any sudden changes in the legal and economic environment. In view of the reasons given so far that factors affecting the patterns of attracting foreign direct investment in emerging sub- Saharan African countries it is therefore imperative that leaders in the region formulate appropriate policies to help them attract more FDI. However, developing appropriate policies and strategies alone is not enough. Governments and policy makers in the region must make sure that the policies and strategies they develop and implement are effective and investor-friendly based on specific and achievable goals.

The findings also suggest that, the goverments of the reigon should emphasized and reconsider the important of financial reform policies, especially with regards to financial development. This is because financial development has positive effect in attracting FDI in the region. Therefore, there is the need to implement policies that will enhance credit allocation and accessibility, by the government of these countries under study in order to have more FDI which in turn accelerate economic growth. Moreover, this will enable more number of people with access of capital for investment, increasing standard of living and reduce extreme poverty among various communities of these countries. The government of those countries should create enable environment which will bring sound financial development due to its role in determining of FDI

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