FOREIGN DIRECT INVESTMENT IN NIGERIA

Omowumi Omodunni Idowu

Department Of Economics, Faculty of Social Sciences
Ekiti State University, Ado Ekiti, P.M.B 5363
Ado-Ekiti, Ekiti State, Nigeria
Email: talk2wummie@yahoo.com

Abel A.Awe

Department Of Economics, Faculty of Social Sciences
Ekiti State University, Ado Ekiti, P.M.B 5363
Ado-Ekiti, Ekiti State, Nigeria

ABSTRACT
The aim of the study was to analyze the major determinants of Foreign Direct Investment inflows in Nigeria taking Governance (Corruption, Internal Conflict, Law and Order and Socio-Economic Condition) into consideration, using data sourced from CBN Statistical Bulletin and the World Bank Development Index (2008) from 1970 – 2010. The obtained results from the analysis were made possible using the Granger Causality Test, Johansen Co-integration and the Error Correction Mechanism Estimation Test, having tested for Unit Root to avoid spuriousity. The study finds a long run relationship amongst the Foreign Direct Investment variables. It also shows that Foreign Direct Investment into Nigeria has been relatively low and not encouraging given the high Inflation rate, Lack of Openness and Poor Economic Growth caused by Frequent Political Instability Factors, Insecurity, Poor Infrastructure, Internal Conflict and Corruption.

Keywords: Foreign Direct Investment, Governance, Co-integration Test, Error Correction Mechanism.

1.0 INTRODUCTION

The growth of Foreign Investment has become more prominent in the world economy due to its contribution to the growth and development of an economy. Foreign Direct Investment as a category of international investment where resident entity in one country obtains a lasting interest in an enterprise resident in another country. FDI can be in form of equity capital, reinvested earnings and other capital (NBER, 2002). Beneficial as FDI can be, especially for developing economies through technology transfer, increasing market liquidity, increase resource absorption, its contribution can bring with it negativities in the form of loss in domestic production control, crowding out of domestic enterprise through unfair competition and

unfavorable Balance of Payment especially when production by the foreign firm still relies on importation of raw inputs.

There are several factors responsible for the poor performance of Foreign Direct Investment in Nigeria relative to the actual potential. These are internal conflicts/clashes, corruption, and its associated advance fee fraud or 419 Scams. Since 1995, the country has been ranked among the bottom five (5) nations in Transparency International Annual Corruption Perception Index (CPI). Corruption constitutes a significant barrier to entry for new investors who may not have good and sufficient navigating sense to do business in Nigeria. Efforts made to attracting FDI seem sabotaged by poor and inconsistent policy implementation, deteriorating infrastructural facilities in the area of telecommunications, water, transport and power supply. Though in recent years several positive development especially in the telecommunication sector has taken place, little or no effect have been on pulling further FDI inflow into the country. Other FDI impeding factors include social unrest, religious and ethnic strife and crime. In the oil rich Niger delta region, decades of official neglect, persistent poverty, as well as dislocations and environmental damage caused by energy project aggravated the socio-economic unrest. Sabotage and vandalisation of pipelines and expatriate kidnap of oil workers are regular occurrence. All these have contributed in one way or the other in shrinking the potentially gain derivable from foreign direct investment by Nigeria. This study therefore investigates governance as part of the major determinants of Foreign Direct Investments and its effects on Foreign Direct Investment Inflow (FDI) in Nigeria.

1.1 OBJECTIVE OF THE STUDY.

The main objective of this study is to examine the determinant of Foreign Direct Investment (FDI) in Nigeria taking into consideration four indicators of governance (in term of internal conflict, corruption, law and order and socio-economic condition). As the major limitations of studies in this area is the non consideration of governance in determining foreign flows of investment as this is one of the most important factors that determine the magnitude of flows and is most considered by investors coming to Nigeria.

2.0 BACKGROUND OF THE STUDY

2.1 ECONOMIC PERFORMANCE OF NIGERIA IN RELATION TO FOREIGN DIRECT INVESTMENT

Foreign Direct Investment contributes immensely to the growth of an economy in filling the financial gaps of savings-investment, revenue-planned expenditure, terms of trade and BOP differences, etc.

The economic performance of a country is assessed based on the examination of key economic and social indicators such as; Real GDP growth, inflation rate, real interest rate, exchange rate, infrastructure, openness (export and import divided by GDP), investment and savings, total debt, etc. as these expresses the level of achievements of set macroeconomic objectives of the country which are sustainable growth, price stability, and full employment. This section of the study intends to unravel the trend of these variables and shows how Foreign Direct Investment has been helping to fill the gaps between revenue and expenditure, investment and mobilized savings then export and import.

2.1.1 FISCAL BALANCE

The major factor in the rising fiscal deficit was the excessive growth in total expenditure which was far above the growth in revenue. The federal government was unable to reduce its spending to keep within available resources. The public expenditure increased from 21.4% to 47.4% in 1980 though not quite stable

and then decline to 5.6% in 1981. This continued for a while until 1987 when increases were experienced but fluctuating till the highest was also experienced in 2008.

Moreover, after the civil war in Nigeria, repairs of infrastructures and buildings that resulted as the aftermath of the civil war heightened the level of budget deficit as reconstruction became the priority of the then government. Also, the oil glut in the 1980 as a result of the emergence of other oil producing countries apart from OPEC which flooded the world oil market leading to a fall in the oil price. Consequently, oil revenue of Nigeria fell, while the expenditure priorities of the government were still maintained (Adofu and Abula, 2010). This resulted into fiscal deficit. In order to sustain the expenditure priorities the government in 1986 implemented the SAP and borrowing of foreign loans. Larger proportions of the loans were embezzled and were not used for intended purposes. In the 1990s, there were huge fiscal deficits because the country had to service the foreign loans with high repayment conditions. Part of the loans was paid while the other part was eventually written off during the Obasanjo's regime.

The country experienced its surplus mostly from oil at that time before the glut but a very remarkable feature of government fiscal expansion was the financing of the excess expenditures from domestic sources averaging 79.2% between 1980 – 2002, since foreign loan was difficult to obtain.Also it's the lack of diversification towards the primary sectors of Agriculture and industry.

The surplus experienced was as a result of the fiscal reform through Structural Adjustment Program (SAP) of 1986 in fiscal reforms was centered on downsizing the public expenditure to infrastructural development and human capacity building. By 1997, as a way of having foreign investment and to pursue economic liberation, the Nigerian enterprise promotion decree was abolished; all these resulted into fiscal surplus for the country.

2.1.2   INVESTMENT- SAVING GAP

The percentage of the country's total savings as a ratio of the real GDP ranges between 6% to 14%between 1970-1980 and in 1980 was 18.2%, since then it has been growing considerably. The amount of direct investment were not able to fill the investment gap experienced during these years except in 1971, due to the low interest rate that ranges between 3% to 8.5% between 1970-1980 discouraging savings but have no effect on investment as a result of other disadvantages that featured the country.Other reasons are the regulatory policy of the government on savings and investment, for example, the liberalization policy adopted, has little effect on investment than its perceived effect on savings, thereby promoting investment only in the distributive or the tertiary sector to the detriment of the production investment. This was also in support of the findings of Soyinbo (1994).

2.1.3   CURRENT ACCOUNT BALANCE

The balance on the current account of the Nigeria's balance of payment has its highest in 2005 with approximately ₦4,891,744 million and its least balance of N42.6 million naira in 1975. Between 1970 to 1989, the balance on current account as a percentage of real GDP ranges low from 0 to 10 percent except for 1974 whose value was 19.2 percent.

Foreign Private Investment has not been able to fill the gap in the current account except for in 1970, 1973, 1984, 1987 to 1989, 1992, 1993, 1999 and obviously in 2002 with a surplus of 133,808 million naira (30.8 percent). The ability of foreign direct investment to fill these gaps or imbalances in the current account is curtailed by the inadequacies in infrastructural facilities, power and energy, transportation and the presence of internal conflict and corruption in the country.

2.2   Development and Trends of Private Foreign Investment in Nigeria.

The growth of FDI in Nigeria has been unstable for quite sometimes as it is either declining or increasing. There have not been an enormous growth in the inflow of foreign direct investment (FDI) in Nigeria, especially the non oil except for 1994 which had over 700% increase with foreign private investment inflow of 55999.3 million naira from 6825.5 million naira. Other subsequent years with an encouraging performances include 1989, 1997, 2000 and between 2003 to 2010 though is unstable but encouraging. Meanwhile, there was a major decline in 1980, 1990, 2001 and 2002. According to UNCTAD Foreign Direct Investment inflow between 1970 to 1975 rose from $205m to $470m, while the positive inflow of FDI in the non oil sector were directly affected by various private sector policies adopted since early 1970s (UNCTAD, 2009).It has been made known that Nigeria receive the largest amount of FDI inflow over the course of the last decade from $1.14billion in 2001 to $2.1billion in 2004, and $11billion in 2009, making the country the 19th recipient of FDI in the world with 30% of all FDI inflow in Africa, due to its oil attractiveness.(Business, Trade and Investment Guide, 2010/2011)

The growth in foreign investment over time and the growth in real Gross Domestic Product show that apart from the inflow of foreign direct investment there are other key factors that contribute to the increases or decreases in the GDP. These include consumption, investment, government expenditure export, import e.t.c. notwithstanding, the contribution of foreign private investment can still be explored.

2.3 Foreign Investment Environment and Policy in Nigeria

2.3.1Foreign Direct Investment Environment in Nigeria

Foreign investments in Nigeria are investment that is either partly or wholly owned by foreign enterprise which according to the Central Intelligent Agency, 'the stock of FDI in Nigeria was estimated to be $67.23billion as at December 2010 and $61.23billion as of December 2009 (www.cia.gov,2011)

The Nigerian government establishes a series of incentives to attract foreign capital as foreign investment played a major role in the economy before early 1970s until 1972 when a large part of the non agricultural sector was controlled by foreign owned companies. Between 1963 and 1972, an average of 62% of total capital was in foreign hands (Biersteker, 1987). After the civil war, the government emerged with a nationalistic vigor which was embodied in the second development plan. The government pursued a policy of progressive elimination of foreign dominance in term of ownership, management and technical control through an indigenization scheme and preferential credit to nurture indigenous entrepreneur. The Nigerian enterprise Promotion Decree of 1972 was enacted limiting foreign equity participation in manufacturing and commerce sector to maximum of 60%. In 1977, a second indigenization decree was promulgated that further limited foreign equity participation in Nigerian businesses to 40%. Between 1973-1975, a new strategy was encouraged and facilitated because of the oil boom and total government revenue increased by 500% in just a year. The structural adjustment programme was under took in 1986 to restructure the economy and lay the path for self sustaining growth. This was necessitated by a balance of payment crisis as a result of glut in the world oil market in the early 1980s. In 1991, the Export Processing Zone (EPZ) scheme was adopted to allow person to establish industries and businesses within demarcated zones, principally with the objectives of exporting the goods and services manufactured and produced within the zone. Necessary infrastructure has been put in place in Calabar, as the designated primary EPZ territory. Also, one in Kano. (Ogunkola and Jerome, 2006)

In 1995, the economy was liberalized after placing a considerable restriction on FDI in most policy domain affecting business activities. The Nigerian Investment Promotion Commission Act of 1995 which laid out the framework for Nigerian investment policy. Under this act 100% foreign ownership is allowed in all

industries except for oil and gas where investment is constrained to existing joint ventures or new production sharing agreements. Also in March 2006 the (NIPC) set up a One-Stop-Investment-Centre (OSIC) on its premises in Abuja to facilitate and promote investment in Nigeria. The OSIC brings together agencies with mandates relating to investment in order to streamline the process of investing in the country. The stakeholders represented with OSIC are: Nigerian Investment Promotion Commission (NIPC), the Corporate Affairs Commission (CAC), the Central Bank of Nigeria(CBN), the National Bureau of Statistics(NBS), the Nigeria Immigration Service(NIS), the Federal Ministry of Finance, the Nigeria Custom Service and so many more. The OSIC has registered more than 2500 companies since its inception (2006). With all these the Nigerian government is committed in bringing in even more investment. In August 2009, UNCTAD and the Japan Bank for international co-operation (JBIC) presented the Nigerian government with a 15 point action plan to develop the country investment promotion structure and create more enabling investment environment so as to enable Nigeria to meet its target of becoming one of the world's top 20 economies by 2020. Among the recommendation the so called 'bluebook' calls for the installation of a computerized investment tracking system by OSIC reforms in tax system and the establishment of a presidential initiative to encourage best practices in the transfer of land rights. The book is the sixth produced by UNCTAD and JBIC for Africa with others going to Tanzania Kenya, Uganda, Ghana, Zambia.(Business, Trade and Investment Guide, 2011). Recently, the Federal Government announced its aggressive plan to also reform the oil sector. The plan propose the unbundling of the NNPC and the passing of Petroleum industry bill. This bill has been under discussion for 7 years and has faced strong lobbying from international oil companies in Nigeria. (Umueni, 2011).

However, despite all these policies and reforms Nigeria remain a high risk operating environment. Institution barriers to doing business including corruption in government are critical determinants of private sector development and prospect for sustainable growth.

2.3.2   Problems of Investment Environment in Nigeria.

Nigeria as the most perceived corrupt country not only in Africa but worldwide corruption in public and private places distorts and hamper development and the cost of doing business in the country and its international range. The continuos bombing by the Boko Haram and other peace distruption, which is believed to a have a political undertune. These thus stand as a serious impending factor in the country's capacity to diversify foreign investment inflows away from oil. Other factors include poor infrastructure, inconsistency in policy and problem of regulation, crime and other security concerns, economy mismanagement and so on.

2.3.3   Policies and Measures against the Problems of Investment Environment in Nigeria.

Economic Financial Crime Commission (EFCC) and Independent Corrupt Practices and other related Offences Commission (ICPC) and some other measures

In 2002, the government set up the EFCC and became operational in April 2003. Though since 1999, the government has determined to fight against corruption by adopting a series of anti-corruption agencies and practices among which also ICPC established by the corrupt practices and other related offences Act of 2000 whose function is to investigate and prosecute corruption cases also to correct corruption prone system and procedures of public bodies and to educate the public against corruption and enlist its support. Its main functions are prevention and investigation. By 2006 since its creation, EFCC has some concrete achievement to showcase.

Among other measures against corruption are:

-"Due process" which oversees procedures to be followed in executing government projects and activities

-EITI, under which oil companies agree to publish what they pay to the government.

-Monthly publication of revenue allocation to all three tiers of government as from January 2004.

-NEEDS, its stipulate and make sure that government is smaller and stronger and better skilled and more efficient at delivery of essential services. This is done in order to change the government from its corrupt haven to a kind of institution that spurs development and whose leaders are actually serving the people (UNCTAD, 2009). Others are

- New Partnership for Africa's Development (NEPAD); Infrastructure Concession and Regulatory Commission(ICRC); Short -Term-Action-Plan(STAP)
- Nigerian Investment Promotion Commission(NIPC)

3.0 LITERATURE REVIEW

3.1 Theoretical Review on Foreign Direct Investment

The theoretical explanation of Foreign Direct Investment starts from the traditional theories of international trade that has its root in the theory of comparative advantage that a country or region offers. The theory of comparative advantage explains why it can be beneficial for two countries to trade even when one country might not be able to produce more of both products. The Imperfect market approach consists of industrial organization theory, the theory of firm and internalization.

Among also is the Product Life Cycle theory of FDI propounded by Vernon in 1966.

The theory explains the four stages of production cycle (innovation, growth, maturity, declining) using the US experience as a case study. The US was overtime an importer of many of the goods that it had once developed, produced and exported. Vernon theory implies that overtime the main exporter may change from exporter to importer, making the low cost producers becoming exporter. Critics emphasized that Vernon theory was obsolete. It was carried out in the 60s while the trading importing and exporting has changed dramatically overtime. Vernon 's view is ethnocentric saying that new products are produced in advanced economies ,for example, Japan. Globalization implies more dispersed and simultaneous production of comparative advantage.

 The criticisms of the Product Life Cycle led to the internalization theory developed by Buckley and Casson in 1976 and then Henhart in 1982. It was initially launched by Coarse in 1937 in a national context and Hymerin an international contexts. Internalization theory postulated that TNCs organize their internal activities to develop specific advantages which then to be exploited (Denisia, 2010). This is also found in Dunning theory but Dunning emphasized that Vernon theory only explained a part of the FDI flows. In 1960, Hymerpostulated the micro level theory of FDI which was firm specific rather than country specific macro level theory, where industries is capital intensive countries invest in less capital intensive countries to maximize profit. The traditional classical macroeconomic theory hypothesized that the rate of profit tend to drop in industrialized countries mostly due to domestic competition which makes the firm to engage in FDI in underdeveloped countries. The neo-classical approach states that due to the shortage of labour and relatively high expense of labour in affluent countries they tend to transfer production facilities to poor labour intensive countries. This in both cases, capital flows from capital intensive countries to capital poor countries as firm thrive to increase overall profit.

The micro level theory of MNEs was considered necessary to replace the seemingly redundant macro level theory of FDI due to its flaws which according to Hymer include the followings: (i) the flow of capital suggested in macro level theory was one directional, from developed to underdeveloped countries.(ii) against this macro level theory, a country simultaneously received inward and engage in outward FDI. (iii) capital availability is not the only reason for FDI, otherwise there should have been variation in the amount

of outward FDI. (iv) as foreign subsidiaries were financed locally, it means that capital does not move across boarder. All these criticism indicated that the macro level theory was based on the concept of perfectly competitive market. In Hymer word, MNEs can only exist in an imperfect market where firms have non financial ownership advantages viz a vis other firms in the same industry, meaning that the drivers of MNEs lie with the individual firm instead of the country's availability of capital. After sometime, Hymer theory was brushed aside. According to Dunning and Rugman (1985), Hymer laid much emphasis on market power approach and neglect the Coarse transaction cost. Hymer theory was about why and how firm invests abroad but not on how firms operate efficiently in its mother country including its use of its advantages (Yamin, 2000; Cantwell, 2000). In 2000, Cantwell postulated the need for a theory that focuses more on a longer term orientation of MNCs away from profit associated with market power and towards profit through innovation and which must cover both micro and macro theories.

The Eclectic paradigm was considered as the general framework of analysis to be examined from various perspective in order to understand the activities of foreign owned production unlike hymer theory which was normative. Eclectic paradigm evaluates the state of existing MNEs or what is rather than what should be. It revolves around exploiting assets, categorized as ownership, location and internalization advantages which combined elements of both macro economic theory of FDI and micro theory of MNEs.

Eclectic Paradigm initially called eclectic theory of international production pioneered by John .H Dunning (1958) involves the introduction of more integrated or holistic theories of FDI and Foreign Owned Production activity. In the 80s and 90s foreign owned production variables was incorporated into international transaction model as there was a renewal of interest in FDI as a financial phenomenon and also its relationship with Foreign Portfolio Investment.

Basic Proposition of Eclectic paradigm

The idea behind the Eclectic Paradigm is to merge several isolated theories of international economics in one approach. These propositions form the bedrock of the paradigm which is the extent and pattern of international production financed by FDI and undertaken by MNEs. This paradigm asserts that at any point in time investment is determined by three forces, which are the OLI factors. The so – called OLI factors are three (3) categories of advantages namely Ownership advantage, Location advantage and internalization advantage.

The Ownership 'O' advantage talks about some competitive advantages that is unique to the country/firm and transferable to other countries/firms. The ownership advantage or Firm Specific Advantage (SFA) is usually intangible and can be transferred within the multinational enterprise at low cost, for example, technology, brand name, benefits of economies of scale (Holsapple, Ozawa and Olienyk, 2006). The advantage gives rise to higher revenues and / or lower costs that can offset the cost of operating at a distance in an abroad location.

.The greater the 'O' advantage of enterprise (that is, the net asset of any dis advantage of operating in a foreign environment), the more incentive firm have to exploit those advantages in foreign market. The Location 'L' advantage are foreign advantages which firms use in connection with its local Firm Specific Advantage (FSA) in order to earn full rents on these FSAs. Thus we can say that the location advantages of different countries are keys in determining which will become host countries for MNEs. The relative attractiveness of various location can change over time so that a host country can to some extent engineer its competitive advantage as a location for foreign private investment. The Location advantage can be due to economic differences among countries with varying forms. For example, the proximity to raw materials and other important inputs, the quantities and qualities of the factor of production, scope and size of market, transportation and communication costs. Political advantages include common and specific government

policies that influence inward FDI inflow, intra firm trade and international production. Social cultural advantage include psychic distance between the home and host country, language and cultural diversities, general attitude and the overall position towards foreigners and free enterprise. This gives the firm opportunity for it to make a defensive investment against its competitors.

Internalization 'I' advantages are advantages by own production rather than producing them through a partnership arrangement, for example licensing or joint ventures. Firm may organize the creation and exploitation of their core competencies. The greater the net benefit of internalizing cross border intermediate product market, the more likely a firm will prefer to engage in foreign production itself rather than license the right to do so.

In conclusion, despite that many researchers have explained the phenomenon, its component and effects, we cannot say that there is a generally accepted theory but everyone agrees on one point that in a world featured by perfect competition FDI cannot longer exist. As most theories especially the classical theory is based on perfect competitive market. That is, if market work effectively and no barrier in terms of trade or competition there will not be any point to trade. International trade is the only way to participate in international market and there must be some forms of distortions that determine the realization of direct investment.

3.2 Empirical Review on Foreign Direct Investment

Fuat and Ekrem (2002) examine location related factors that influence FDI into the Turkish economy. They discovered that the size of the host country's market, infrastructure (proxied by share of transportation, communication expenditure in GDP and energy) and the openness of the economy (as measured by the ratio of exports to imports) are positively related to FDI inflows. The results further revealed that both exchange rate positively related to FDI inflows. The results further revealed that both exchange rate instability and economic instability (measured by interest rate) have negative effects on FDI. A similar econometric model was used in Kenya by Elijah (2006) when he employed an econometric model to regress FDI on exogenous variables that include human capital, real exchange, annual inflation and openness of the economy. The author found that human capital affect FDI inflows positively in the short run. But inflation and real exchange rate were negatively related to FDI inflows in the short run and long run respectively. Eregba (2011) investigated on the dynamic linkages between foreign Direct Investment and Domestic Investment in ECOWAS Countries using panel co -integration. An India researcher who performed his study on Nigeria. The study revealed that foreign direct investment inflows substitutes domestic investment in ECOWAS region. Export openness were found to be positively and negatively affect respectively domestic investment accumulation in the ECOWAS region.

Dinda (2009) used co-integration technique to find out the long run relationship between FDI and resource flow time and also used Vector Error Correction model with or without exogenous factor to find the long-run relation of the variables. While investigating on the factors attracting FDI into Nigeria between 1970 to 2006 found that the market size proxied by the GDP was not significant during this period despite its important as part of the major determinants of FDI inflow in all countries. It was also discovered that the bulk of FDI inflow into a country were mostly resource seeking FDI, while natural resources, inflation and exchange rate were significant.

Nurudeen and Abu (2010) made use of OLS and ECM techniques to empirically analyze the determinant of FDI as to which of the determinant are most important and the effect of deregulation on FDI in Nigeria. The study laid emphasis on deregulation as part of the factors that encourages or discourages the inflow of FDI. However the results illustrate that openness of the economy and inflation are statistically insignificant but positively related to FDI. Similarly, the results show that infrastructural facilities have an insignificant effect

on FDI in Nigeria with the variables co-integrated and a long run relationship among the variables. Ayanwale (2007) used an augmented growth model through the OLS and 2SLS method to empirically investigate the relationship between non extractive FDI and economic growth in Nigeria. Results suggest that the determinant of FDI in Nigeria are market size, infrastructure development and stable macroeconomic policy. While openness to trade and available human capital are not inducing. It was found also that FDI in Nigeria contributes to economic growth, though all the overall effects is not significant.

Asiedu (2006), exploring the determinant of FDI into Africa deduced that inflation and efficient legal system promote FDI but corruption and political instability has a negative effect. While examining the performance, promotion and prospect of FDI in Africa it was also found that the region should pay more attention to the improvement of relation among existing investors and also offer them incentives as the features of the region contributed badly to the flow of investment into Africa. (Dupasquier and Osakwe, 2005).

Eregba (2011) discovered that FDI inflow substitute domestic investment between 1970 to 2008 in the ECOWAS region as export, import and openness contributed positively and negatively respectively to domestic investment. In a paper published by the Overseas Development Institutes (1997(3)) in low income countries, it was indicated that shortages of financial resources, technology and skills as the main obstacle to the flow of FDI in low income countries between 1970 to 1996.

Udoh and Egwaikhide (2008) through their estimation result (GARCH) indicated that exchange rate volatility, inflation, uncertainty exerted significant negative effect on FDI in Nigeria between 1970–2005 and concluded that infrastructural development, appropriate size of the government sector and international competition are crucial determinants of FDI inflow to the country. Ekpo (1997) on the other hand examined the relationship between FDI and some macro-economic variables between 1970-1994 and concluded that the political regime, real income per capital, rate of inflation, world interest rate, credit rating and debt services accounted for variance of FDI inflow to Nigeria.

Nwankwo (2006) made use of data between 1962–2003 to identify the main determinant of FDI in Nigeria and discovered that a strong market, macroeconomic stability and natural resources promote FDI in Nigeria while political instability and the transition to democratic regime has a negative effect.

Wafure and Abu (2010) laid emphasis on deregulation policy and found that there was a positive relationship between FDI inflow in Nigeria with all variables found to be significant (openness inflation, infrastructure, deregulation and market size) with R^2 of 86% and a long term relationship among the variables and that despite the political situation of the country during the period under consideration, there was a positive relationship in the previous 2 years. From political point of view found that all variables are significant with the expected approved sign except for opener. Exchange rate volatility turns out to to be a detrimental variable whose inclusion reduce the value of the R2. It was also observed that the political system in the country is very important whether stable or not as it is found out to be antithetical to FDI inflow. There was no conclusion as to whether it was the military or civilian regime attracts more FDI (Ibrahim, 2006).

4.0 METHODOLOGY

Model Specification

Foreign Direct Investment
The determinants of Foreign Domestic Investment (FDI) can be derived from the Dunning's theory of foreign direct investment.
In functional term

FDI = f (OLI advantages)-- Eqn (4.1)

Since this study talks about the inflow of FDI, that is, the determinants of the inflow of investment in the host country. Thus equation 4.1 becomes

FDI = f (location advantage)--Eqn (4.2)

The OLI advantages are the Ownership 'O' advantage, Location 'L' advantage and the Internalization 'I' advantage. These advantages are the tenets of the Eclectic Paradigm. The location advantages include the market size proxied by the Real Gross Domestic Product, the economic and political features of the country or countries involved such as the exchange rate, inflation rate, debt profile, the openness of the economy to international trade, governance in term of corruption, internal conflict, law and order and socio-economic condition.

Therefore equation (4.2) can be rewritten thus

Model 1

FDI = f (RGDP, EXCH, INF, OPN, DEBT) ---------------------------------- Eqn (4.3)

Subsequent models are with governance index (corruption, internal conflict, law and order and socio-economic condition) each one being analysed independently.

Model 2,3,4 and 5

FDI = f (RGDP, EXCH, INF, OPN, DEBT, GOV) ---------------------------------Eqn(4.4)

The multivariate specification of equation (4.3) and (4.4) for estimation are

$$FDI = \alpha_0 + \alpha_1 RGDP + \alpha_2 EXCH + \alpha_3 INFL + \alpha_4 OPN + \alpha_5 DEBT + E_t \text{--------------------Eqn (4.5)}$$
(+)   (+)   (-)   (+)   (-)

$$FDI = \alpha_0 + \alpha_1 RGDP + \alpha_2 EXCH + \alpha_3 INFL + \alpha_4 OPN + \alpha_5 DEBT + \alpha_6 GOV + E_t \text{-----------Eqn (4.6)}$$
(+)   (+)   (-)   (+)   (-)   (+/-)

Where;

FDI – Foreign Direct Investment as a percentage of the real Gross Domestic Product. It captures the total real inflow of Foreign Domestic Investment into Nigeria by its major partners.

RGDP – Real Gross Domestic Product

EXCH – Real Exchange rate

INFL – Inflation Rate

OPN – Trade Openness

DEBT – Total Debt as a percentage of real ross Domestic Product. (total debt includes both domestic and international debt)

GOV – Governance (it includes corruption, internal conflict, law and order and socio-economic condition).

E_t -Error term

Specifying in Error Correction form, we have;

$$\Delta fdi_t = \beta_0 + \sum_{i=1}^{k} \beta_{1i} \Delta fdi_{t-i} + \sum_{i=1}^{k} \beta_{2i} \Delta rgdp_{t-i} + \sum_{i=1}^{k} \beta_{3i} \Delta exch_{t-i} + \sum_{i=1}^{k} \beta_{4i} \Delta infl_{t-i} + \sum_{i=1}^{k} \beta_{5i} \Delta gov_{t-i} + \sum_{i=1}^{k} \beta_{6i} \Delta debt_{t-i} + \sum_{i=1}^{k} \beta_{7i} \Delta opn_{t-i} + \lambda \, ECM_{t-1} \text{------------------------Eqn(4.7)}$$

Where λ is the speed of adjustment parameter, ECM is the residual that is obtained from the estimated OLS co-integration model of Eqn.(4.5)

5.0 EMPIRICAL RESULTS

Error Correction Model; Results

Given the results of the co-integration test which revealed the existence of co-integration among variables in the foreign direct investment model, dynamic error correction model (ECM) is considered appropriate for the analysis. This is in line with the study of Wafure and Nurudeen (2010). This analysis on the determinants of foreign direct investment is into five models. The first model is without any of the governance indicators while the remaining four models are with governance indicators (corruption, internal conflicts, law and order and socio-economic conditions), one after the other independently. These are presented in the table above.

The result obtained from the first dynamic model indicates that the overall coefficient of determination (R^2) shows that 95.45 percent of changes in current foreign direct investment is explained by the variables in the equation. As the adjusted (R^2) tends to purge the influence of the number of included explanatory variables, the adjusted R^2 of 0.8230 shows that having removed the influence of the explanatory variables, the dependent variable is still explained by the equation with 82.30 percent. When governance variables are considered, the adjusted R^2 indicates that a reasonable amount of variation in current FDI is being explained by the models. The Durbin Watson (D.W) statistics values indicate that there is no of sign auto-correlation or serial correlation in the model specifications; hence the assumption of linearity is not violated in the entire model. While the F statistics indicates that the models are of good fit and significant. The expected Error Correction Model term (ECM) of the models have the expected negative sign and are all found to be significant.

In the first model, it was discovered that changes in previous foreign direct investment, changes in previous and current real GDP, changes in previous and current real exchange rate and changes in previous and current inflation rate, changes in previous openness and finally changes in previous and current total debt are significantly related to changes in current foreign direct investment inflow. Based on the apriori expectation, exchange rate, inflation rate and total debt negate the apriori expectation in the short run. While in the long run, changes in previous and current FDI, changes in previous inflation rate, changes in previous openness, changes in previous and current total debt, changes in real exchange rate and changes in previous real GDP(ΔGDP_{t-1}) agree the stated apriori expectation while changes in present real GDP, changes in previous and current exchange rate and changes in current inflation rate agree with the stated theory.

A unit increase in year 2 lagged of FDI leads to 0.53 percent significant changes in current FDI. While a unit increase in year 3 lagged of FDI leads to significant positive effect of 0.82 percent changes in current FDI, showing a positive relationship between past and present FDI This conforms with the findings of Fuat and Ekrem (2002) in examining the locational factor that influence FDI in Turkish economy, the market size was found to be significantly positive. Similarly, Iyaho (2001)- there exist a positive relationship between FDI and market size, proxied by GDP. This was found to be the same in all the model except for where internal conflict was used as a governance indicator. A significant negative relationship is found between past and present FDI.

At 10 percent significant level, a unit change in current real GDP decreases current FDI by 4.52 percent in model 1. While a change in year 1 lagged of real GDP leads to 1.58 percent significant positive change in current FDI. This conforms to the study of Wafure and Abu (2010) and Chakrabarti (2001), a unit increase in previous market size (GDP) increases current FDI inflows. A unit change in year 2 lagged of real GDP decreases change in current FDI by 2.22 percent. Contrarily, subsequent models indicate an insignificant relationship between real GDP and current FDI but a significant relationship exist between changes in lagged values of real GDP and current FDI.

This analysis also shows that a unit change in current exchange rate decreases current FDI by 0.06 percent and a change in year 1 lagged of real exchange rate decreases current FDI by 0.03 percent at 10 percent significant level. This is also so when governance indicators are considered, a negative relationship exists between exchange rate and FDI. This shows a negative relationship between exchange rate and FDI inflow. This conforms to the findings of Elijah (2006) in Kenya, suggesting that as changes in exchange rate tend to a rise, changes in the growth of foreign direct investment falls. Similarly, Akpan, Offiong, Ita and Esu (2011) discovered that exchange rate is a significant variable influencing FDI inflow into Nigeria. This means that a further depreciation of domestic currency (naira) induces FDI inflows, as investors take advantage of the depreciated currency. This is not so in subsequent models, an insignificant relationship is discovered between the two variables (real exchange rate and Foreign Direct Investment).

Considering inflation as part of the explanatory variables, it was discovered that a change in current inflation rate leads to 0.04 percent increase in current FDI. A unit change in year 3 lagged of inflation rate decreases change in current FDI by 0.03 percent. This conforms with the findings of Udoh and Egwakhide (2008), inflation contributed negatively to FDI inflow. With governance, a change in year 1 lagged of inflation rate has an insignificant positive relationship between inflation rate and FDI. Meanwhile, year 2 and 3 lagged of inflation rate indicate an insignificant negative relationship.

There exists an insignificant positive relationship between current degree of openness and current FDI inflows. Contrarily to this a significant positive relationship is found between the lagged values of degree of openness and current FDI, such that a unit increase in values of lagged openness increases current FDI and a negative change in openness decreases current FDI.   In support of this, Adefeso and Agboola (2012) reveals that degree of openness has a significant positive effects on FDI inflows. Contrarily, Ayanwale (2007) concluded that there was a negative tie between foreign direct investment and openness in Nigeria. A unit change in year 2,3 and 4 lagged of openness increases change in FDI by 0.01 percent in each case. This goes in line with the work of Masuku and Dlamin (2009), it is discovered that a unit increase in openness increases the stock of FDI in Swaziland.

A significant positive relationship exists between the total debt and FDI inflows. A unit change in current total debt decreases current FDI by 48.9 percent, showing a negative relationship while a change in year 1 lagged of total debt increases current FDI by 17.5 percent. At year 3 lagged of total debt a unit change decreases current FDI by 10 percent. Other models also show a significant negative relationship between total debt and FDI in Nigeria. This agrees with Anyanwu (1998), that debt contributes negatively to FDI inflow in Nigeria, as there is a unit increase in the level of the country's total debt, FDI inflows fall.

Corruption as an index for governance indicates that at 5 percent level of significant a change in corruption level in Nigeria causes a negative change of 2.71 percent in current FDI. Asiedu (2006) found that corruption has a negative effect on FDI inflow in Africa. This means that as corruption is increasing in the country the amount of FDI inflow decreases. This is evidence with so many cases of corruption even at the government level. Where Money allocated for projects are turned to personal use, thus leave the state of the country infrastructure and development battered and untouched. This impedes flows of investment into the country. For example, public holders like the former Inspector General of Police; TafaBalogun, the former speaker of representative; Honorable DimejiBankole and the rest of them who embezzled public funds. The government effort to control this menace through the establishment of Economic Financial Crime Commission (EFCC) and Independent Corrupt Practices and other related Offences Commission (ICPC) and some other measures have not yielded much result, because corruption has eaten deep into the flesh of all Nigerians and Nigeria as a whole, it is now the order of the day.

A change in current internal conflict has a significant negative effect of 0.32 percent on current FDI as a change in year 2 lagged of internal conflict ($\Delta INTCON_{t-2}$) has a significant positive effect of 0.29 percent

on current FDI. In recent time, the country has been battering with many cases of social unrest and internal conflicts where lives and properties are unsafe and unguaranteed and this scares away investors. For example, the Niger-Delta crisis of killing and kidnapping of mostly foreigners, the activities of Boko Haram who makes lives un-living for citizenry and alien through bombing and slaughtering of innocent citizen.

The inclusion of law and order as an indicator of governance shows that a change in law and order significantly reduces current FDI by 1.37 percent. This indicates that the law and order of the country (Nigeria) are not effective and that justice is expensive in the country, it favours only those who knows who. Nigeria's previous socio-economic condition has a significant positive effect on current FDI, such that a unit change in year 2 lagged of the socio-economic condition in Nigeria has a significant positive effect of 0.55 percent on current FDI inflows. This can be seen from the aspect of deregulation that took place in the communication sector, the construction of motor able and durable roads and other infrastructure just to increase the inflow of foreign investment in the country.

6.0 CONCLUSION AND POLICY RECOMMENDATION

Leaning on our research finding and extensive background to the study, we therefore conclude FDI in Nigeria have not been encouraging, as a result of major domestic flaws in the country such as high inflation, poor infrastructure, corruption and insecurity that reflect on the nominal growth of the country, low interest rate, unfavorable exchange rate and unnecessary barrier to trade and inflows of capital that manly come in the form of legal requirement, tariff barriers, duplicated tax system, etc. Also, the fear of future burden to be bore in form of higher tax and levies to redeem huge debts especially, external debts seem to deter the inflow of Foreign Private Investment in the country.

To improve on the inflow of our foreign direct investment (FDI), Government should therefore invest more in infrastructure (like power, communication, transportation and energy) and ensure the availability of other needed facilities that can attract and boost the productive capacity of direct foreign investors, so that more investors can come into the country since effective productivity of present direct investors will attract more foreign investors. With respect to the real exchange rate and FDI inflows, the government should allow naira to depreciate more since it will reduce the dollar price of some ailing indigenous companies, thus attract more foreign investment (in form of mergers and acquisition).

Improving policy and regulatory environment, tax reforms, investors tax friendly tax and legal systems, removal of capital controls are essential to FDI attraction and contribution to growth in the economy.

Loans acquired both internal and external must be use for the purpose for which they are acquired, for example, developmental projects. There is also need to weight the interest rate attached to the loan and the benefits that may likely go with the conditions/requirements, so as to see if it actually favors the recipient country rather than the donor.

Given the identified problems of internal conflicts and corruption that affect the inflows of Foreign Direct Investment (FDI) in Nigeria, this study therefore recommends that the government should fund, equip, train and retrain officers and men of internal security agencies, especially the police force who can fight and ensure the safety of life and property to eradicate internal conflicts in the country. There is need for sovereign national conference; we all coming out to fashion out on how to resolve our differences in a federal state like Nigeria. Also, the government should ensure the implementation of policies and decisions made concerning security.

Having appointed people of high integrity to head anti corruption agencies, the government should not interfere with their decision. They should act independently.

The government can also reduce corruption by establishing a body and sub bodies that evaluates the works of every ministry and public offices at national, state and local level. By so doing, it will inculcate fear in the

heart of public holders, and thereby reduce corruption. Good governance (leaders are meant to serve not to be served).

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TABLE

Table 5.1: Determinants of Foreign Direct Investment in Nigeria: Parsimonious Error Correction Model,
1974-2010.

Dependent variable: ΔFDI$_t$

Variables	*MODEL 1:* Without Governance	*MODEL 2 :* FDI with Corruption	*MODEL 3:* FDI with internal conflict	*MODEL 4:* FDI with law and order	*MODEL 5 :* FDI with socio-economic condition
Constant	0.138	-0.158	-0.242	-0.157	-0.699**
ΔFDI$_{t-1}$	0.324	0.389	-0.559***	_	_
ΔFDI$_{t-2}$	0.536**	0.918**	_	_	0.914***
ΔFDI$_{t-3}$	0.822***	0.375**	_	_	0.476**
ΔRGDP	-4.523***	1.906	_	3.730	_
ΔRGDP$_{t-1}$	1.580**	-6.082	_	_	_
ΔRGDP$_{t-2}$	-2.217**	1.007*	1.100**	8.168	1.161**
ΔRGDP$_{t-3}$	-1.268*	-8.174	_	-1.730**	-8.339
ΔEXCH	-0.061***	-0.045**	_	-0.023	-0.046**
ΔEXCH$_{t-1}$	-0.034***	0.019	_	0.013	_
ΔEXCH$_{t-2}$	-0.018	-0.014	-0.017	-0.024	-0.016
ΔEXCH$_{t-3}$	0.014	-0.008	_	0.014	_
ΔEXCH$_{t-4}$	-0.020*	_	_	_	_
ΔINFL	0.038**	_	_	0.011	_
ΔINFL$_{t-1}$	0.012	0.049**	0.058***	0.060***	0.07***
ΔINFL$_{t-2}$	_	-0.045**	-0.019	-0.037**	-0.04**
ΔINFL$_{t-3}$	-0.027*	-0.028	_	0.013	-0.04**
ΔINFL$_{t-4}$	-0.042***	_	_	_	_
ΔOPN	_	_	0.00212934	_	0.003
ΔOPN$_{t-1}$	0.001	_	_	_	0.004
ΔOPN$_{t-2}$	0.009**	0.012***	0.006*	0.012***	0.020***
ΔOPN$_{t-3}$	0.010**	_	_	_	0.009**

ΔOPN_{t-4}	0.012***	_	_	_	
$\Delta DEBT$	-48.938***	_	_	_	-4.870
$\Delta DEBT_{t-1}$	17.513***	-3.328	_	_	
$\Delta DEBT_{t-2}$	-9.741*	_	3.642	_	
$\Delta DEBT_{t-3}$	-10.017**	-6.548***	-4.312***	-5.480***	-9.106***
ΔCOR	_	-0.668	_	_	_
ΔCOR_{t-1}	_	-1.029	_	_	_
ΔCOR_{t-2}	_	1.927	_	_	_
ΔCOR_{t-3}	_	-2.708**	_	_	_
$\Delta INTCON$	_	_	-0.315**	_	_
$\Delta INTCON_{t-2}$	_	_	0.286*	_	_
ΔLAW_{t-2}	_	_	_	0.994	_
ΔLAW_{t-3}	_	_	_	-1.369**	_
$\Delta SOCECO_{t}$	_	_	_	_	-0.118
$\Delta SOCECO_{t-1}$	_	_	_	_	-0.164
$\Delta SOCECO_{t-2}$	_	_	_	_	0.554***
$\Delta SOCECO_{t-3}$	_	_	_	_	0.205
ECM_{t-1}	-1.143***	-1.535***	-0.490*	-0.873***	-0.973***
R^2	0.954	0.885	0.769	0.803	0.876
D. W	2.036	1.543	1.797	2.130	2.650
F Statistic	7.261	4.909	6.665	4.073	5.643

Source: Author Computation.

*Note : ***, ** and * represent 1%, 5% and 10% significant levels respectively.*