Empirical Analysis of the Relationship between Foreign Direct Investment and Economic Growth in Developing Countries- Evidence from Nigeria

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Abstract - This study examines the effect of Foreign Direct Investment (FDI) on economic growth of Nigeria. The main objective of the study is to explore and quantify the contribution of Foreign Direct inflows to economic growth in Nigeria and other macro-economic variable(s). The model built for the study proxy real gross domestic product as the endogenous variable measuring economic growth as a function of Foreign Direct Investment, Domestic capital, Government Expenditure, real exchange rate and Inflation rate as the exogenous variables in the first model while unemployment was expressed as a function of Foreign Direct Investment, Government expenditure and real GDP. Annual time series data was gathered from Central Bank of Nigeria Statistical bulletin, National Bureau of Statistics (NBS) and the World Economic Outlook spanning 1970 to 2013. The study used econometric techniques of Augmented Dickey-Fuller (ADF) unit root test, pairwise granger causality test, Johansen co-integration test and error correction model (ECM) for empirical analysis. The results of unit root revealed that, all the variables in the model were integrated at first difference while pairwise granger causality revealed a unidirectional relationship between Foreign Direct Investment (FDI) and Economic growth (GDP) in Nigeria and no causal relationship between Foreign Direct Investment and unemployment rate. The co-integration test shows that, long-run equilibrium relationship exists among the variables captured in model but model 2 revealed no hypothesized co-integrating equation. FDI had positive but not statistically significant relationship with Nigerians economy growth in both the short and long run. The findings from the error correction method show that, the distortion in will adjust itself to equilibrium at 0.3% in each period which is very slow in adjusting to equilibrium in case of any distortion. The study recommends that, the government need to aggressively initiate policies to channel the Nation's domestic savings for investment purposes and enact policies to train human capital to argument increasing FDI into the country to stimulate the economy towards rapid and sustained economic growth.

Keywords: Foreign Direct Investment, Economic Growth, Unemployment and Government Expenditure

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