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ARTICLE

Foreign Direct Investment and Manufacturing Export in Nigeria

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ABSTRACT

The potential impact of Foreign Direct Investment (FDI) on recipient and investing economies is of considerable policy interest (Pain and Wakelin, 1997). Important to the theory of foreign investment in Nigeria is the question whether foreign investors coming to Nigeria are market-seeking or export-driven. This finding is relevant to economic managers in the design and implementation of appropriate macroeconomic policies to attract FDI. It is also relevant to investigate whether FDI contributes to the overall capacity of developing economies to export. This study investigates the contribution of FDI to manufacturing export in Nigeria. Using firm level data collected from 232 manufacturing firms in Nigeria, probit regression analysis revealed that FDI does not significantly contribute to manufacturing exports in Nigeria. This finding supports that of Soderbom and Teal (2002) and Nunnenkamp (2002) that FDI in developing countries like Nigeria are not export-driven but are attracted by certain economic fundamentals within the economy like market size and the availability of natural resources.

KEYWORDS: Foreign direct investment, manufacturing, export, Nigeria

INTRODUCTION

Results from empirical studies show that there are diverse, and often conflicting, reasons why foreign investors seek opportunities abroad. Some of these studies include the works of Dunning (1993), Globerman and Shapiro (1999), and Shapiro and Globerman (2001) among others. These studies conclude that multinational corporations' (MNCs) FDI are attracted by strong economic fundamentals in the host economies (Blomstrom and Kokko, 2003). The most important of these economic fundamentals are market size, and the level of real income, with skill levels in the host economy, the availability of infrastructure and other resources that facilitate efficient specialisation of production, trade policies, and political and macroeconomic instability as other major determinants. The import of these conclusions is that there are diverse factors that tend to influence the

decision of foreign investors to invest in a particular economy. These studies also show that some FDI are market-seeking since they are attracted by market size and the level of real income. There are still explanations to show that where domestic markets are not so attractive perhaps due to poor income distribution or because of low population density, then foreign investors might invest due to the attractiveness of some economic fundamentals with the objective to export.

This study investigates whether FDI in Nigeria's manufacturing sector is essentially market-seeking. If its contribution to export is significant, then we will conclude that foreign investors are not essentially attracted by the availability of domestic market in Nigeria, but also by the presence of some economic fundamentals which make production cheap and they invest to exploit these production opportunities then sell abroad. The work is presented in five sections. After this introduction is the literature review. That is followed by the explanation of the methodology employed in the study. In section four, the results of the study are presented. Section five concludes the paper.

LITERATURE REVIEW

The beginning of capital investments in foreign countries is hard to trace to a specific period in history. However, international funds transfer, especially in the African continent, actually climaxed with the emergence and spread of MNCs. This is not, however, to assert that the global movement of FDI started with the phenomenon of multinational corporations. For most developing countries, the flow of FDI had started during the colonisation era when MNCs began to establish their subsidiaries in colonial territories. This flow has been rapid over the years. This view is supported by Lambo (1987:400) that, the growth of private foreign investment in the Third World has been extremely rapid. Available data show that cumulative foreign direct investment in Nigeria during the period 1970-1998, has maintained a persistent upward trend. It rose from N1.003 billion in 1970 to about N3.620 billion in 1980. By 1990, cumulative foreign direct investment in the economy was N10.436 billion, which rose to about N119.39 billion in 1995 (CBN, 1993, 1998). By 2000, net FDI inflow to Nigeria amounted to N115.952 billion (Dandi, 2009). By 2002, nominal FDI in Nigeria stood at N225 billion (Ayanwale, 2007). Thus, apart from a few declines noted in some years (mainly in the 1980s), there has been a persistent rise in net FDI inflow to Nigeria.

It is relevant to note that Nigeria is one of the largest recipients of FDI in Africa. For example, in the period 1993-1997, Nigeria topped all other African countries in the inflow of FDI with an annual average of 1, 503 million dollars for the period, far ahead of Egypt's 775 million dollars and South Africa's 755 million dollars for the same period (UNCTAD 1999; 50). This trend has continued into the 21st century. The UNCTAD World Investment Report 2006 shows that FDI inflow to

West Africa is mainly dominated by inflow to Nigeria, who received 70% of the sub-regional total and 11% of Africa's total. Out of this, Nigeria's oil sector alone received 90% of the FDI inflow (Dandi, 2009).

A review of theories on the flow of FDI across boundaries explains what opportunities foreign investors seek in recipient economies, and specifically in the sectors in which they invest. There are divergent views on the opportunities foreign investors seek to exploit in recipient economies. Whereas some theories explain that foreign investors seek investments abroad to enjoy absolute and comparative advantage in some countries, other theories explain that it is the extension of product life-cycle and the protection of monopoly that encourages firms to invest abroad (see the works of Vernon, 1966 and Teichova, 1989). Many other scholars have contested that in the 1990s most FDI is attracted by some economic fundamentals in the recipient country-market size, the level of real income, skill levels, trade policies, infrastructures etc (see the works of of Dunning, 1993; Globerman and Shapiro, 1999; Shapiro and Globerman, 2001 and Blomstrom and Kokko, 2003). Newer theories suggest that at the beginning of the 21st century, investment incentives are the most potent motivations for inward FDI in most recipient countries (see Neven and Siotis, 1993; UNCTAD, 1995, 1996 and Blomstrom and Kokko, 2003). A number of studies have indicated that market size, natural resources and liberalisation policies have served to attract foreign investments to Nigeria despite political instability (see Dandi, 2009). Both Obadan (1982) and Asiedu (2002) and Asiedu (2006) who have studied the determinants of foreign direct investment into the Nigerian economy confirmed that market-size is the determining factor of FDI inflow into Nigeria. These studies agree with those theories which suggest that FDI is attracted by strong economic fundamentals (like market size) and those that suggest investment incentives as the major attraction to FDI.

Studies have shown that FDI could improve performance of both recipient firms and even of firms that compete with FDI firms. To cite some examples, Aitken and Harrison (1999) studying Venezuelan manufacturing firms observed that case studies present mixed evidence on the role of foreign investment in generating technology transfer to domestic firms. Mansfield and Romeo (1980) however, found that only a few of the multinationals in their survey helped domestic firms acquire new technology. Yauri (2006) found that FDI increases the employment of technology by domestic firms in Nigeria's manufacturing sector. There is also some evidence to suggest that the export performance of manufacturing firms in some countries has improved due to the inflow of FDI. Pain and Wakelin (1997) argue that the potential impact of FDI on recipient and investing economies is of considerable policy interest and that FDI could contribute to exports by improving the productivity of domestic enterprises. Blake and Pain (1994) have studied the UK export performance due to foreign direct investment. Their results suggested that net inward investment into the UK had a significant effect on export performance after

allowing for the impact of relative price and non-price factors. Rhee and Belot (1989) studying a group of low income countries found that the entry of several foreign firms led to the creation of a booming, domestically owned export industry for textiles. There are no similar results from empirical studies on the contribution of foreign direct investment to export in Nigeria, especially with respect to manufacturing exports.

METHODOLOGY

The data utilised for analysis in this study was collected by the RPED Department of the World Bank in a survey research on Nigerian manufacturing firms conducted in 2001⁴. A team of World Bank specialists conducting a survey of Nigerian manufacturing firms have administered questionnaires and interview modules on a sample of 232 firms in the Nigerian manufacturing sector. This sample of 232 was drawn from 9 sub-sectors of the Nigerian manufacturing sector, specifically chemical/paints, food/beverages, metal, non-metal, paper/printing/publishing, pharmaceuticals, plastics, textiles and wood sub-sectors (see appendix I for identities of sectors as employed in the regression model).

Also, the sample firms were selected from the three major geographical regions and industrial axis of Nigeria namely, East (Region 1 in regression analysis), North (Region 2) and Lagos and South (Region 3). The Lagos and South region had the highest share of the sample with 125 firms, North 60 and East 47. Of the firms in the sample, 102 had FDI at the time of the survey (represented in the model as $\beta_7 fdisurvey_{it}$), 130 are wholly owned by domestic entrepreneurs.

Gorg and Strobl (2002) similarly utilised the World Bank RPED Survey data for Ghanaian manufacturing firms for the period 1991-1997 in their study. Gorg and Strobl (2002) observed that the data set includes among other things, data on the level of output, total expenditures on wages, the replacement value of the capital stock, the level of value added, and the level of employment. More importantly, they noted that the data collection entails an intricate questionnaire on the background of the owner, or, in the case of a corporation, the chairman of the firm. Thus, the data sets reveal whether a firm is owned by foreigners through direct investment, a firm has received some amount of foreign investment or not at all. Specifically, according to Gorg and Strobl (2002) one is able to identify whether the owner/chairman has received any explicit training by foreign firms in the past, whether their immediate previous experience was working with a foreign firm within the same industry as the industry of their current firm or in some other industry, and whether they have had any previous same industry experience in general.

For the purpose of this study, the following hypothesis is formulated:

H₁: FDI firms in Nigeria export a significantly higher proportion of their total output

To test this hypothesis, we needed data on the export performance of the manufacturing firms in the sample. Question *gen51* of the general questionnaire in the World Bank Survey of Nigerian manufacturing firms asked responding firms (both FDI and domestic firms) to indicate the percentage of their production that is directly exported. Thus, we generated a discrete parameter and we employed a probit regression to test the hypothesis. The probit regression model is expressed as follows:

$$gen51_{it} = \alpha + \beta_1 fdistartup_{it} + \beta_2 fdisurvey_{it} + \beta_3 firmage_{it} + \beta_4 sectorid_{it} + \beta_5 region_{it} + \beta_6 firmsize_{it}$$

gen51_{it} = A dependent variable which is a proxy for percentage of firm *i*'s production that is exported at time *t*.

α = an intercept

$\beta_1 fdistartup_{it}$ = firm *i* that commenced business with FDI at time *t* (1 if firm with FDI, 0 if none)

$\beta_2 fdisurvey_{it}$ = firm *i* with FDI at the time of survey *t* (1 if firm with FDI, 0 if none)

$\beta_3 firmage_{it}$ = the age of firm *i* at the time of survey *t* (years)

$\beta_4 sectorid_{it}$ = the sector of firm *i* at the time of survey (1=food and beverages sector, 0=otherwise)

$\beta_5 region_{it}$ = the region where the firm *i* is located at time *t* (1=East, 0= otherwise)

$\beta_6 firmsize_{it}$ = the size of firm *i*, whether small-medium or large at time *t* (1 if large; 0 otherwise)


RESULTS AND DISCUSSIONS

The results (see appendix II) indicate no significant relationship between FDI and export. In other words, less than a significant proportion of the output of FDI firms in Nigeria is exported to markets abroad. Both firms that commenced business with some foreign investments (*fdistartup*) and those that had FDI at the time of the World Bank Survey but which firms we cannot ascertain whether or not they started business with foreign investments (*fdisurvey*) did not possess high tendency to export. Thus, the hypothesis that FDI firms export a significant proportion of their total output is rejected. However, the results above show a positive but weak relationship between firm size and export, indicating that larger firms are slightly more likely to export than smaller firms. An interesting result is that firms in sector 8 (leather) have a higher tendency to export compared to firms in sector 1, and in all other sectors considered in the study. The findings above reveals,

first, that manufacturing in Nigeria is mainly of consumer goods and is targeted towards local consumption. Secondly, the findings show that FDI inflow in Nigeria is driven by the existence of a large consumer market. Thirdly, it confirms the traditional activities in the Nigerian leather sector which has historically remained an export commodity especially in the northern part of Nigeria.

The results are consistent with findings of other studies. Many studies have indicated that most FDI to third world countries is market-driven and is not likely to manifest export orientation. Nunnenkamp (2002) noted that in contrast to FDI in industrial countries, FDI in developing countries still is directed predominantly to accessing natural resources and national or regional markets. Majority of firms in the Nigerian manufacturing firms, therefore, produce for the local economy. Soderbom and Teal (2002) also found that a striking feature of Nigerian manufacturing firms is that not many of them export. Their survey of Nigerian manufacturing enterprises 2001 shows that only 7 percent of the sampled firms (about 176 of them) export. Excluding exporters to Africa, only 5 percent of firms export out of Africa. Thus, this study agrees with other empirical studies which have found that manufacturing firms in Nigeria produce largely for domestic consumption. In a Report on Nigerian manufacturing exports for the same period 2000-2001, Albaladejo (2003) found that manufactured exports plummeted from USD216 million in 1985 to USD88 million in 2000, making Nigeria one of the least export-oriented economies in the world.

CONCLUSION

The findings from the test of hypothesis have shown that FDI firms in Nigeria's manufacturing sector are not export-driven. It is conclusive, therefore, that foreign investors in Nigeria's manufacturing sector are mainly attracted by the availability of domestic markets for their output. Other economic fundamentals like cheap labour and raw materials (though not investigated in this study) might have explained the flow of FDI into Nigeria's manufacturing sector. Because firms in the oil sector have not been included in the sample (as shown in appendix I), this study cannot conclude on the aggregate contribution of FDI to Nigeria's total exports. 

Appendix I: Identity of Sectors of Firms in the RPED Survey

Sector identification	Name of sector
sector1	Food and beverages
sector2	Wood and furniture
sector4	Textile and garments
sector6	Metal

sector8	Paper/printing/publishing
sector9	Non-metal
sector12	Pharmaceuticals
sector13	Plastics

Appendix II: Results of Regression Analysis

Independent variables	Dependent variable=export P > z
<i>fdistartup</i>	0.1404
	1.3770
<i>fdisurvey</i>	0.9323
	1.4693
<i>firmage</i>	0.0691
	0.0682
<i>sector2</i>	8.2867
	7.9134
<i>sector4</i>	-1.8445
	1.9671
<i>sector6</i>	-1.1016
	1.5193
<i>sector7</i>	-2.0141
	3.0845
<i>sector8</i>	57.4995***
	17.9709
<i>sector9</i>	-1.9786
	1.6861
<i>sector11</i>	-0.8320
	1.6067
<i>sector12</i>	5.4128
	4.5697
<i>sector13</i>	1.6840
	3.1663
<i>Region2 (North)</i>	-5.6926
	4.3281
<i>Region3 (Lagos/South)</i>	-8.4287**
	4.2627
<i>firmsize</i>	5.2761*
	3.2252
F statistic	3.03***

R squared	0.4284
Constant	5.2033

*, **, *** significant at 10%, 5% and 1% level respectively

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True Purpose

The first necessity we face here is that of having to make a simple but vital distinction – one that is of crucial importance, not only for assuring sound technique and technology, but also for maintaining a sound civilization. We must learn to distinguish carefully between strictly technical purpose and what is ordinarily identified falsely with it, namely, personal motive.

For, technically, the purpose of a maker or a performer is to produce something that does well what it is meant to do – that answers the need properly which it is meant to answer; it is not primarily to make money and to assure the comfort, status and power that money can purchase.

Nothing could be more harmful to a culture – nothing, indeed, could more certainly degrade it into a commercialized, philistine distinction. For, once money, and therefore profit, becomes the primary objective of making or performing, the members of a culture become so obsessed by it that gradually, fatally, they begin to lose almost all sense of humane values. A product or service becomes something to be turned out with just enough quality to make it acceptable, but at as little cost and as high a sales price as possible; this, through the use of mechanical efficiency and niggardly cost accounting. It becomes interesting to the distributor as affording him a high percentage of rake-off, even it is designed to pander to wants created by advertising. And it becomes prized by its user on the basis of whether it enables him to make money or to enjoy what money can buy.

John Julian Ryan, *The Humanization of Man*, pg. 15