Research Article

Impact of Foreign Capital Inflow on a Selected Macroeconomic Variable in Nigeria 1990-2021

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Abstract: *The study examined the impact of foreign capital inflows on a selected macroeconomic variable in Nigeria from 1990 to 2021. The study used their explanatory variables (foreign direct investment, external debt and foreign portfolio investment) and one explained variable (unemployment rate). The unit root test, ARDL bound co-integration test, and error correction were all performed. According to the findings, there is a negative and substantial impact between foreign portfolio investment and Nigeria's unemployment rate, as well as a positive and significant impact between FDI, external debt, and Nigeria's unemployment rate. Based on the findings, the government should implement policies that will attract foreign investors to Nigeria and encourage them to invest more; as a result, the alarmingly high rate of unemployment will be reduced, and the government should ensure that its external debt is used to invest in critical infrastructure to create an enabling investment environment.*

Keywords: Unemployment, Foreign Direct Investment, Portfolio Investment, External Debt.

INTRODUCTION

Foreign Investment has been identified as a major driver of economic growth especially in third world countries experiencing a dearth of requisite investment to drive the strategic sectors of the economy. Various policies of the Nigerian government have been aimed primarily at promoting economic growth and development by influencing the trends of gross fixed domestic investment or indirectly by policies aimed at stimulating the inflows of foreign funds into the economy since the country gained independence in 1960.

Economists favour the flow of capital across national borders to maximize the return on capital. It is against this backdrop that multinational companies seek investment in foreign countries with reasonable risk. Issues such as inadequate governance and uncertain macroeconomic policies make Nigeria a high-risk market for investment.

The demand for foreign investment stems from Nigeria's economy's underdeveloped state, which has slowed the country's economic development. Nigeria has a monocultural economy that is overly reliant on a single sector. This is also considered to be the cause of the sub-lack regions of investment capital. Onwumere (2018) opined, "With oil as the main source of foreign exchange in Nigeria, a one-product monocultural economy must be continuously deficient in investment capital.

Nigeria has benefited from growing foreign capital inflows in the recent decade, being one of the top recipients of capital inflows from the rest of the world. However, capital inflow especially FDI is not seen to have improved the economic growth in Nigeria and Nigeria is yet to experience real inclusive economic growth despite these huge domestic and foreign resources (Akinlo, 2004; Okodua, 2009; CBN, 2010; Iwayemi, 2012; Umoh *et al.,* 2012; Ugwuegbe *et al.,* 2013; Adejumo, 2013; Aga, 2014; Adofu *et al.,* 2015; & Mohammed & Mahfuzul, 2016). In developing countries such as Nigeria, following the evolution of financial liberalization which took place in the 1980s, developing countries implemented a series of financial liberalization programmes to achieve growth and development in the financial sector. In the mid-1980s, the Nigerian economy has not recorded any figure on foreign capital inflows, or investment inflows in her balance of payments account (CBN, 2020). The zero return on the inflow column of the account was attributed to the absence of foreign private investors in Nigeria's economy. This was basically because of the non-internationalization of the country's money and capital markets, as well as the non-disclosure of information on the portfolio investments in foreign capital and money markets.

Consequently, opportunities for profitable investment increased in the 1990s as foreign capital inflows to developing countries improved from $6.2 billion in 1987 to $46.9 billion in 1993 (United Nation Development Programme (UNDP, 2013). Similarly, foreign capital inflows such as the purchase of shares,

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stocks, and depository receipts by foreign investors registered a moderate increase from 1993 through 1999 but decreased in 2000. This decrease was triggered off by the terrorist attack on the World Trade Centre in the United States of America (United Nations Economic Commission for Africa, 2013). Furthermore, a comparison analysis revealed that cumulative capital inflows fell by 49.7% to $8.6 billion between January and July 2020, compared to $17.1 billion in the same period last year, owing largely to foreign investors' risk aversion due to the pandemic, oil price shocks, and fragile economic activity (CBN, 2021).

In light of this, the study will examine the impact of foreign capital inflows on a selected macroeconomic variable in Nigeria from 1990 to 2021. As a result, the study's specific objectives are:

➢ To investigate the impact of foreign direct investment on the unemployment rate in Nigeria
➢ To look at the impact of Nigeria's external debt on the country's unemployment rate.
➢ To explore the impacts of Nigeria's foreign investment portfolio on the country's unemployment rate.

This paper is divided into five sections to fulfil these objectives, with the introduction as the first. The second section is a literature review. The methodology is examined in the third section. The fourth section focuses on the presentation and discussion of the results. The summary, findings, policy recommendations and contribution to knowledge are all covered in section five.

REVIEW OF RELATED LITERATURE

Conceptual Review

The broad and detailed objectives of this work are defined by concepts. These are foreign capital inflows (FCI) and external debt, which, as a funding vehicle, encompasses a wide range of obligations. The relevant terms are conceptualized as follows;

Concept of Foreign Capital Inflow

The 'foreign' component of my research title refers to any business, person or entity outside of the domestic economy. 'Capital' in this context is money available for investment by governments, businesses or individuals. It includes highly liquid assets like cash and credit. It also includes non-liquid assets like stocks, real estate and high-interest loans. Large financial institutions that make most investments prefer using borrowed money. 'Inflow' signifies money moving into the economy. Capital movements between residents of one country and residents of another country are referred to as foreign capital. The resident entity may be an individual, company or government. Above all, foreign capital inflow (FCI) refers to a rise in the quantity of money moving from foreign sources into a country or territory, not only to accomplish economic growth but also to improve the country's or region's overall macroeconomic performance. External debt, foreign portfolio investment and foreign direct investment are two examples of FCI proxy sources.

Concept of External Debt

The Dictionary of Banking and Finance (2005) defines external debt "as money which a company has borrowed from outside sources (such as a bank) as opposed to money raised from shareholders." This definition brings up three salient points: external debt is money needed by a person, business organization or country, which it lacks; the money (debt) must come from anywhere beyond the boundary of the borrower (for a country across national frontiers) where a capable and willing lender is located; the principal must be paid off plus interest charges in conformity with the lender's terms because the lender in this context is not a charity. External debt in this context relates to a country's indebtedness to foreign lenders.

Concept of Foreign Portfolio Investment

Onuorah & Akujuobi (2013) describe FPI as a type of foreign capital inflows that is made up of financial resources and asset transfers such as cash, tradable securities (issued or backed by the government), bond, equity shares, promissory notes, debentures and money market instruments issued in a domestic stock market by citizens of some other foreign countries with the aim of sharing profit. FPI arises when local investors buy non-controlling management and interest from an international company or buy foreign financial instruments such as shares, government bonds corporate bonds, derivatives and short-term securities.

Concept of Unemployment

According to Bakari (2012), unemployment is conceptualized as a situation whereby a worker or workers are involuntarily out of work. This means that workers are willing and able to work, but cannot find any. Classical economics commonly define unemployment as an excess supply of labor over demand for labor, which is generated by real wage adjustments. If real wages for jobs are set above the market-clearing level, the number of job applicants exceeds the number of vacancies, resulting in classical or real-wage unemployment.

THEORETICAL REVIEW
Dual-Gap Theory

Dual-gap theory was developed by Chenery & Strout (1966) to explain the usefulness of external debt in augmenting a country's domestic savings. Dual-gap theory posits that external debt is important because it fills the funding gaps occasioned by poor savings and investments, as well as low foreign exchange earnings that result from trade imbalances, thereby contributing to economic growth in borrowing jurisdictions. The dual-gap model advocates allowing a considerable flow of external money in the form of foreign loans to

account for deficits of saving or foreign currency exchange to alleviate the gaps that Nigeria is part of. In the same vein, pro-dual-gap supporters (Amassoma, 2014; & Orji *et al.,* 2014) view the efficient use of foreign finance as panacea to bridge the dual gaps.

Dependency Theory

Dependency theory was developed by Paul A. Baran in 1957. This theory describes the nature of international relations among countries of the world, stressing that developed countries influence less developed countries through their economic power. Major assumptions of the theory include that the (i) present underdeveloped state and inequality among countries are an essential aspect of these interactions; (ii) wealthy countries oppress and dominate poor countries via media control, politics, economics, education, sport, culture, banking and finance (Utomi, 2014); (iii) resources are evacuated from "periphery" of poor and underdeveloped countries to "core" of rich countries, thereby improving the economic wellbeing of the latter at the expense of the former; (iv) underdeveloped economies not only provide dumping grounds for obsolete technology, but also supply natural resources, cheap labour and markets for developed economies, enhance their living standards. Foreign help in the form of loans, aid, and investment, as well as unrestricted activities of Multinational Corporations (MNCs), are prescribed as remedial measures by proponents of the theory.

Solow Swan Growth Theory

The Solow-Swan is a long-run growth model that looks at capital accumulation, population growth, and productivity increase as technological progress (Solow-Swan, 1956; & Solow, 1999). Given these axioms, with constant technical progress, we defined production function as:

$$Y = F(K, L) \dots\dots\dots\dots\dots\dots\dots (1)$$

Y is output, K = capital, L= Labor. Given the condition of constant return to scale Y/L=F(K,1) = L. f(k) Where Y = Y/L is income per worker, k = K/L is capital-Labor ratio, and the function J(k)= J (k, 1). Thus, the production function can be expressed as;

$$y = f(k) \dots\dots\dots\dots\dots\dots\dots\dots (2)$$

N.B that, saving is a constant fraction, s, of income. So, saving per worker is sy. Since income equals output as;

$$Sy = sf(k) \dots\dots\dots\dots (3)$$

This is the amount of investment required to sustain capital per worker k, which is a function of population growth and depreciation rate, d. Meanwhile, it is assumed that the population expands at a constant rate of n and that the capital stock grows at a rate of n.k to give capital to the expanding population (Mello, 1999; Akinlo, 2004; Adeniyi *et al.,* 2012).

Empirical Review

Inekwe (2013) focused on the relationship between employment and FDI in the manufacturing and service sectors in Nigeria. This study applied the Johansen multivariate co-integration test and VECM and found that the FDI manufacturing sector is positively related to employment, while the service sector revealed that FDI and employment rate are negatively related. The study's scope is limited, and it can't be utilized to explain the economy's current state. It also ignores external debt, a key variable that influences unemployment rates as one of the indications of foreign capital intake.

Ugochukwu *et al.* (2013) in a study on the connection between FDI and economic growth in Nigeria found that there exists a positive relationship between FDI and economic growth but FDI's impact on economic growth is insignificant in Nigeria. The study concluded that FDI had little impact on economic growth, but this study would employ ARDL to determine the long and short term effects of FDI on Nigerian economic growth.

Similarly, Johnny *et al.* (2018) assessed the impact of foreign direct investment on the unemployment rate in Nigeria between 1980 and 2015. The study was carried out using the unit root test, co-integration test, and ordinary least square. For Nigeria, it was discovered that foreign direct investment and the unemployment rate have a negative and insignificant association, whereas capital formation and unemployment rate have a positive and substantial relationship. The study, therefore, suggested that government should implement policies that will attract foreign investors to Nigeria to make more investments and should also ensure that all resources for productive activities are fully employed before embarking on savings. The scope of the study is limited, used the OLS econometric method of analysis while the current study adopted ARDL and update the data to more recent years.

Babasanya (2018) examined the relationship between foreign direct investment and employment generation in Nigeria covering the period 1999 to 2016. The study considered employment rate (as a dependent variable) and gross domestic product, foreign direct investment, and exchange rate as independent variables. The ordinary least square estimation technique was used in the study and it was discovered that foreign direct investment has a positive relationship with the employment rate in Nigeria. It was therefore recommended that government should make concrete efforts in attracting foreign investors into Nigeria to increase production and thereby creates employment opportunities. The study's scope is limited, and it used the OLS econometric method of analysis, whereas the current study will use an autoregressive distributed lagged model (ARDL).

Ajayi, *et al.* (2019) investigated the impact of foreign direct investment on employment and unemployment rate in Nigeria for the period of 1980 to 2014. The study sourced data from CBN Statistical Bulletin, National Bureau of Statistics and World Bank Indicators and the data were analysed by E-view 9.5. The findings revealed that FDI has a significant role in the employment rate in Nigeria. Thus, it was recommended that policies should be implemented to exploit the impact of FDI on employment in an attempt to reduce the unemployment rate in Nigeria. The scope of the study is limited, this will use different variables and the current study will update to 2021.

Matthew *et al.* (2020) researched foreign direct investment inflow and employment in Nigeria for the period of 1985–to 2017. The study used the Fully Modified Ordinary Least Squares (FMOLS) and the Johansen co-integration econometric approach to the data, which were gathered from the World Development Indicators (WDI) and the Central Bank of Nigeria (CBN) statistical bulletin. The results obtained show that foreign direct investment is statistically significant and positively related to the employment level in Nigeria. The method for investigation is not chosen using the unit root procedure.

METHODOLOGY

Theoretical Framework and Model Specification

The study will examine the impact of foreign capital inflow on selected macroeconomic variables in Nigeria. The foundation of the model will be based on the dual-gaps theory. Also, the initial model will be adapted from the work of Okafor *et al.* (2016).

However, the model will be modified and specified to follow the study objectives and hypotheses stated in chapter one as follows;

UMP= F (FDI, FPI, EXD) ………………(1)

Explicitly, equation (1) can be written as:

$UMP_t = \beta_0 + \beta_1 FDI_t + \beta_2 FPI_t + \beta_3 EXD_t + \mu_{1t}$ …….(2)

Where:

UMP = Unemployment Rate

β_0 = Intercept term.

And β_1-β_3, are parameters known as partial regression coefficients.

A Priori Expectation

It is expected that based on a priori functional relationship between dependent and independent variables. The relationship between the coefficient of foreign direct investment, foreign portfolio investment, and external debt is expected to be negatively related to the unemployment rate.

Symbolically,

$\beta_1, \beta_2, \beta_3 < 1$

Note, that all the variables are measured in percentages annually except eternal debt.

Data Estimation Technique
Description Analysis

The ex-post facto research approach was used to examine the data's behaviour, which included the use of inferential statistics, as mentioned in the research design. The variables to determine the specific objectives are presented as follows: Dependent variable is the Unemployment Rate (UMP) while the independent variables are FDI (Foreign Direct Investment), FPI (Foreign Portfolio Investment) and EXD (External Debt). The analyses involved descriptive statistics, graph analysis, trend analysis, and regression analysis.

Unit Root Test

The test was conducted to determine the order of integration of the variables. If the test reveals that all the variables, are I (1). However, if the series is I (0) and I (1), the appropriate test will be the ARDL co-integration approach. Also, the test was conducted to ensure that none of the variables are integrated of order 2, to avoid spurious results (Ahmed, Muzib& Roy, 2013). Therefore, stationarity was achieved by applying appropriate differencing called 'order of integration'. The Augmented Dickey-Fuller tests are employed in conducting the test. Thus, the ADF test statistic was;

$$\Delta Y_t = \alpha + \beta_t + \delta Y_{t-1} + \sum_{i-1}^{m} \delta \Delta Y_{t-1} + \mu_t \dots \dots \dots \dots \dots (3)$$

Where ΔY_{t-1} equals Y_{t-1}-Y_{t-2}, ΔY_{t-2} equals Y_{t-2}-Y_{t-3}, and so on, and m is the maximum lag length on the dependent variable to ensure that U_t is the stationary random error. The null hypothesis of a unit root is rejected if the t-statistic associated with the estimated coefficient exceeds the critical values of the test.

ARDL Co-integration Test

In addition, Autoregressive Distributed Lagged (ARDL) - Bounds test procedure was used to examine the co-integration impact of foreign capital inflow on selected macroeconomic variables in Nigeria. This procedure was developed by Pesaran & Shin (1999) which was later expanded by Pesaran *et al.* (2001) and the procedure allows the researcher to use variables that are not integrated in the same order. The Autoregressive Distributed Lagged (ARDL) model that will be used to examine the impact of foreign capital inflows on a selected macroeconomic variable in Nigeria is specified as follows:

$$\Delta UMP = \alpha_0 + \sum_{g=1}^{l} \alpha_{1i} UMP_{t-1} + \sum_{h=1}^{m} \alpha_{2i} FDI_{t-i} + \sum_{i=1}^{n} \alpha_{3i} FPI_{t-i} + \sum_{j=0}^{o} \alpha_{4i} EXD_{t-i} + \sum_{g=1}^{l} \alpha_{5i} \Delta UMP_{t-1} + \sum_{h=1}^{m} \alpha_{6i} \Delta FDI_{t-i} + \sum_{i=1}^{n} \alpha_{7i} \Delta FPI_{t-i} + \sum_{j=0}^{o} \alpha_{8i} \Delta EXD_{t-i} + \varepsilon_{1t} \dots \dots \dots \dots \dots \dots \dots \dots \dots (4)$$

ARDL Error Correction Model

Also, the error correction model (ECM) was used to establish the short-run and long-run causal

relations between the variables. After estimating long-run multipliers, the final stage is to estimate short-run dynamic coefficients using an error correction model to represent the pace at which fluctuations adapt. The ECT_{t-1} is the error correction term that will be obtained from the estimated long-run equilibrium relationship and λ will be a parameter indicating the speed of adjustment to the equilibrium level. The sign of the ECT_{t-1} must be negative and significant to ensure that long-run equilibrium exists between the variables. The coefficient (λ) measures the speed of adjustment to equilibrium in the long run. This was specified as follows:

$$\Delta UMP = \alpha_0 + \sum_{g=1}^{l} \alpha_{1i} \Delta UMP_{t-1} + \sum_{h=1}^{m} \alpha_{2i} \Delta FDI_{t-i} +$$

$$\sum_{i=1}^{n} \alpha_{3i} \Delta FPI_{t-i} + \sum_{j=0}^{o} \alpha_{4i} \Delta EXD_{t-i} + \lambda ECM_{t-1} + \varepsilon_{1t} \dots \dots . (5)$$

Nature and Source of Data

The study used a secondary data collection strategy. Secondary data is research data that has been obtained by researchers or institutions other than the current user for other purposes. Our secondary data come from the Central Bank of Nigeria (CBN) and WDI. And the data spanned from 1990 to 2021, they are time series and annual data.

DATA ANALYSIS

Unit Root Test

The unit root test was carried out based on the augmented dickey fuller (ADF) test at a 5% level of significance.

Table 1. Result of Augmented Dickey-Fuller Unit Root Test

Variables	ADF Statistics	5% Critical Value	Order of Integration
UMP	-5.049162	-1.952473	I(1)
FDI	-6.077482	-1.952473	I(1)
FPI	-4.073475	-1.952066	I(0)
EXD	-5.521140	-1.952472	I(1)

Source: Author's Computation, E-views version 10.0

Based on the above result of the Augmented Dickey-Fuller unit root test, the variables are mixture 1(1) and I(0) and are significant at a 5% level. This means that the null hypothesis will not be accepted. We, therefore, conclude that the time series collected are all stationary.

ARDL Bound Test Result

Table 2. ARDL Bond Test Results

Dependent Variable: UMP
Functions: (FDI, FPI, EXD)
F-statistics: 8.397379
K 3
Critical Value Bounds

Significant	Lower Bound	Upper Bound
5%	3.47	4.45

Source: Author's Computation, E-views version 10.0

The F-statistics value of 8.40 is bigger than the I (1) bound test value of 4.45 at the 5% significant level, according to the ARDL bound test results shown above. As a result, we reject the null hypothesis of no co-integration and conclude that the variables in the model have a long-term relationship.

Results of the Short-Run and Long-Run Equations of the ARDL Model

Table 3. Short-Run and Long-Run Results of the ARDL Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(UMP (-1))	0.451211	0.191451	2.356798	0.0348
D(FDI)	5.461475	1.393419	3.919479	0.0018
D(FDI (-1))	-3.15036	1.232711	-2.55563	0.0239
D(FDI (-2))	0.349741	0.817807	0.427658	0.6759
D(FDI (-3))	1.944671	0.818468	2.375989	0.0336
D(FPI)	-0.05073	0.941321	-0.05389	0.9578
D(EXD)	0.187789	0.16633	1.129009	0.2793
D(EXD (-1))	-0.23564	0.122885	-1.91755	0.0774
D(EXD (-2))	0.093818	0.108522	0.86451	0.403
D(EXD (-3))	-0.40198	0.106505	-3.77428	0.0023

	Coefficient	Std. Error	t-Statistic	Prob.
D(@TREND ())	2.511594	0.483315	5.196595	0.0002
ECM (-1)	-0.88293	0.215395	-4.0991	0.0013
Long Run Coefficients				
Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
FDI	6.487561	2.177163	2.979823	0.0106
FPI	-1.05745	1.072947	-1.917569	0.0541
EXD	0.486368	0.141481	3.4377	0.0044
C	-65.0327	17.66656	-3.68112	0.0028
@TREND	2.844629	0.570274	4.988174	0.0002

Source: Author's Computation, E-views version 10.0

In Tables 3 the long-run coefficients of foreign direct investment and external debt have a significant positive effect on the unemployment rate in Nigeria and the foreign investment portfolio has a significant negative impact on the unemployment rate in Nigeria. The coefficient of foreign direct investment and external debt are significant at 5%. The coefficient of ECM_{t-1} is negative and statistically significant. This depicts a long-term rate of adjustment toward equilibrium. This also implies that the errors will be repaired at an 88 per cent rate.

Stability Test

Recursive least square tests (CUSUM TESTS) have been also applied for checking parameter stability for the quarterly data of the variables. The estimated values of parameters for regressand variables such as unemployment rate and explanatory factors such as foreign direct investment, foreign portfolio investment, and external debt are presented against each iteration in figure 1 The graphics depict the examination of stability from 1990 to 2021. The data appears steady during the intervals because it falls by 0.05 percent.
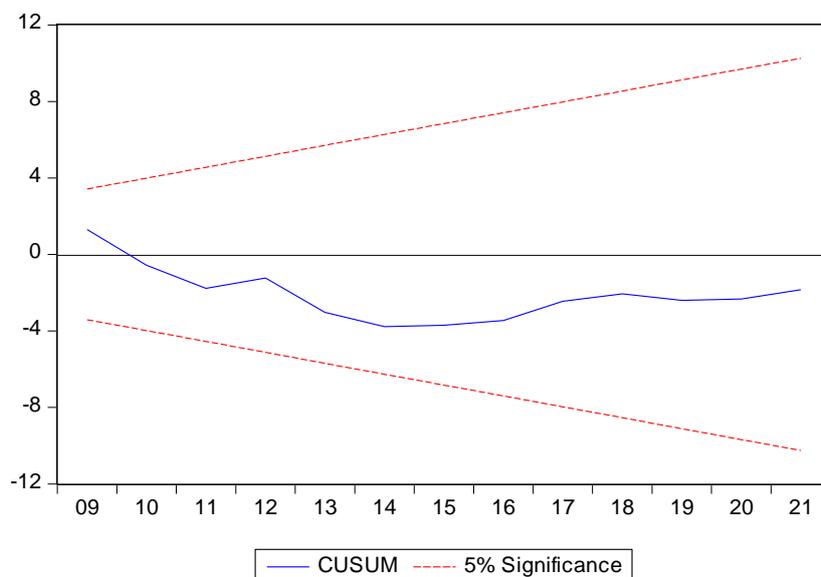

Figure 1: Stability Test
Source: Author's Computation, E-views version 10.0

DISCUSSION OF RESULTS

The result of the analyses of the bound test indicated that there is a long-run equilibrium relationship among the variables in the model. Then, the long-run coefficients of foreign direct investment and external debt have a significant positive effect on the unemployment rate in Nigeria, investment portfolio has a significant negative impact on the unemployment rate in Nigeria. The coefficient of the error correction is negative and statistically significant and this shows that the variables adjust towards equilibrium in the long run. Interestingly, recursive least square tests (CUSUM TESTS) were applied to check parameter stability for the annual data of the foreign capital inflows and unemployment rate variables. The graphs showed the stability analysis during the year 1990 to 2021. During the intervals, the data look stable because it falls by 0.05%.

SUMMARY OF FINDINGS

The work investigated the impact of foreign capital inflows on a selected macroeconomic variable in Nigeria from 1990 to 2021. Based on the findings, foreign direct investment and external debt are positively related to unemployment rates in Nigeria, while portfolio investment has a negative impact.

CONCLUSION

The study examined the impact of foreign capital inflows on a selected macroeconomic variable in Nigeria from 1990 to 2021. The variables used in the study include foreign direct investment, foreign portfolio investment and external debt as independent variables and the unemployment rate as the dependent variable. Foreign direct investment and external debt are found to impact the unemployment rate positively and significant. It means if foreign direct investment and external debt are increasing, then the unemployment rate will be increasing. This empirical finding does not follow what economic theory will have suggested. The Neo-liberal school is of the view that through foreign direct investment and external debt much of the needed economic fortune can be achieved. It can provide crucial aid in modernizing the industrial order for developing countries. As a result of this conclusion, the focus of policy and strategy should be on efforts to attract more foreign direct indirect investment into the country, and external debt should be diverted to capital projects to minimize unemployment. Portfolio investment has a negative and considerable impact on the unemployment rate. It means financial flows to a country that needs return in the long and short-run through investment in the stock and bond market leads to a low rate of unemployment. The result suggests that for a significant reduction of the unemployment rate, more focus of policy and strategy should be on financial flows into Nigeria.

Recommendations

Based on the findings of the study, the following recommendations were made;

- Government strategies should be implemented to entice foreign investors to Nigeria and encourage them to invest more; this will help to reduce the alarmingly high percentage of unemployment.
- To reduce Nigeria's unemployment rate, the government should ensure that its foreign debt is utilised to invest in key infrastructure and create an enabling investment environment.

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