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# Effect of Foreign Direct Investment on Human Welfare in Nigeria: 2000-2022

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#### Abstract

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This study examines the impact of Foreign Direct Investment on Human Welfare in Nigeria between 2000 and 2022. Human development index was used to measure human welfare while foreign direct investment inflows, exchange rate, trade openness, interest rate and inflation rate were used as the explanatory variables. The stationarity test shows that human development index and inflation rate were stationary at levels while foreign direct investment, exchange rate, trade openness and interest rate were stationary at first difference. The study utilizes the Autoregressive Distributed Lag (ARDL) modelling approach to examine the relationship between the variables. The results indicate that there is long-term significant impact of foreign direct investment on human welfare. The contegration result also shows that only the exchange rate had a short run significant impact on welfare at 5% level. The study recommend that government should formulate and implement policies that will enhance foreign direct investment into the country and should curb repatriation of profits by foreign investors through encouraging reinvestment in the host country so as to improve human welfare and grow the economy.

#### **1. Introduction**

Foreign Direct Investment has long been considered one of the essential agents of growth in developing countries, as it represents necessary capital inflows to complement domestic savings and an entry into modern technologies and managerial know-how, required for sustainable development. According to Abouelfarag & Abed, 2018, FDI inflows are needed to supplement domestic savings and provide critical accesses to advanced technologies and managerial expertise needed for modern economic development. This is the supposed-to-be conventional role of FDI in economic growth. In the instance of Nigeria, however, serious reversals have lately been observed in some of its periodical trends. The inflows, which attained \$3.31 billion in 2021, grew by 38.9% in comparison with 2020 but fell back to the all-time low of \$-0.19 billion in 2022, recording a decline of 105.64%, thus reflecting considerable instability. Evidently, such dramatic decline in conjunction with a number of unresolved issues that indicate a general feeling of insecurity across the country, uncertainty in energy supply. and unpredictability in the business climate-all operating against foreign investment and shaking economic stability.

As a part of international economic integration, FDI had provided a stable and usually long-term linkage amongst economies through encouraging technology transfer, greater trade opportunities, and the transfer of knowledge across transnational corporations and domestic firms. In this regard, FDI is also capable of making contributions to productivity growth by developing kev infrastructures, raising labor productivity, and increasing wages in host countries. FDI can become one of the drivers for economic transformation in the case of such developing economies as Nigeria, endowed with abundant natural and human resources which have not been able to harness these resources into consolidated economic growth. FDI should be seen as a driver for such economic transformation, where access to wider external markets and resources is allowed. In spite of this relatively high input of resources, however, the expected favorable contribution of FDI to socio-economic growth has not been fully realized, leaving sizeable lags in human welfare and economic stability (Nwosu & Eke, 2020).

The impact of FDI upon economic growth and human welfare is multilevel and multidimensional. While FDI theoretically generates substantial revenues, creates jobs, and thereby contributes to higher economic development and improved living standards, it is not necessarily a guaranteed benefit on the other side. In fact, its effectiveness will depend in great measure on whether or not the host country sustains an investment-friendly environment that captures the elements of stable governance, clarity in regulations, and reliable infrastructures. Fluctuating policy frameworks, poor infrastructure, and security challenges have made recent times cumulative features in Nigeria, hence making the country a less attractive destination for investment and constricting the potential of FDI in contributing to the improvement of public welfare. FDI may, therefore, be fundamental to leading economic growth at the macro level; not being as direct in its link to human welfare or social development, it would thus require further supportive policies that will guarantee conversion of economic benefits into tangible gains for citizens. Akinlo (2022) supports this view.

Conventionally, FDI has been resorted to by Nigeria not only as an avenue for muchneeded capital but also as a conduit toward productivity improving industrial and enhancing the infrastructure base of the country. Such inflow of foreign capital had contributed to the development of such strategic sectors as telecommunications, banking, and oil, each playing a key role in the economy of Nigeria. This has, in turn, contributed to the inflow of foreign capital that has created such development in sectors like telecommunications, banking, and oil-each playing a strategic role in the economy of Nigeria. At broader levels of social outcomes, the FDI contributions to poverty alleviation, employment, and quality of life are not so clear. For instance, as much as FDI in the oil sector has spurred economic growth, such growth has been confined largely to regions and sectors without trickling down in terms of improvement in the living standards of the broad economy. This therefore renders the effectiveness of FDI in realizing social development contentious, with studies calling for a balance between economic and social dimensions in FDI policies.

The ultimate macroeconomic goal aim at the improvement of human welfare. FDI is a source of revenue for an economy, which helps in economic growth through improved industrial productivity, economic indicators and human welfare in the host country by providing quality jobs with good income and access to qualitative services. However, if FDI's effect on Nigeria's economic growth does not result in a rise in employment and welfare, then social and economic development cannot be achieved. In this light, this study aims to investigate whether there is correlation between FDI and welfare in Nigeria. If FDI actually makes any significant and positive contribution to the improvement of welfare among the Nigerian populace

### 2. Literature review

## 2.1 Conceptual Review

#### 2.1.1 Concept of Foreign Direct Investment

Foreign direct investment (FDI) is the process whereby residents of one country (the source country) acquire ownership of asset for the purpose of controlling, production, distribution and other activities of a firm in another country (the host country). Foreign direct investment (FDI) can contribute in various ways to economic development in developing nations, most importantly breaking the vicious circle of poverty. The trends of the flows of foreign direct investment globally and the distribution of its attendant effect across the regions of the world have been a subject of empirical decisions over the past decades (Akinmulegun, 2012).

Foreign direct investment provides much needed resources to developing countries such as capital, technology, managerial skills, entrepreneurial ability, brand and access to markets which are essential for developing countries to industrialize, develop, create jobs and attack the poverty situation in their countries (Althukorale 2003). Likewise, Dauda (2007) sees FDI as a growth propelling force in developing countries; as it makes significant contributions the host to country's development process especially through easing of the constraints of low levels of domestic savings and investment as well as foreign exchange shortages.

Technical advancement is the eventual energy of continued economic progress (Djokoto, Agyei-Henaku, & Badu-Prah, 2022; Sharma & Gani, 2004; Solow, 1956) and has become influential in societal progress. As FDI promotes technology transmission and corporate integration between foreign and local businesses, this enhances human resources development. The benefit for developing countries lies in technology and development catch-up or convergence (Menon, 2013; Kaukab and Surwandono, 2012). Thus, the well-being of FDI recipient countries would be enhanced because of the benefits of FDI such as employment creation, skill development, generation income and technological improvements (Kaukab and Surwandono, 2012).

#### 2.1.2 Human welfare

According to the United Nations Development Programme (UNDP), human welfare is concerned with quality education, improved health and equitable income, as seen in the Human Development Index (HDI). The HDI comprises of three key welfare indicators which are long and healthy life, acquisition of knowledge and good standard of living. Human welfare relates to the wellbeing of the people in terms of good sound health, happiness, good quality of life, access to basic needs. A country will develop if the welfare of the citizens are properly taken care of. This is so because a country's progress and quality of life determines the development.

To the Welfare Economists, human welfare refers to the allocation of goods and resources for promoting social welfare. It deals with the economically efficient distribution of resources for the well being of the people. Human welfare is the satisfaction of basic needs of life which include food, water, shelter and other things that sustain life. The inadequacy or absence of these basic needs explains how healthy the citizens are in a country. Individual's objective is to continually improve its welfare by maximizing utility given certain constraints.

Poor standard of living in Nigeria is as a result of persistence increase in the price of goods and services, inequality, high rate of unemployment and underemployment and corruption which has caused many Nigerians to experience malnutrition, bad health, and poverty. The Nigerian Living Standards Survey (NLSS) of year 2020 revealed that 52% of Nigerians are living below the poverty line, which translate to over 105 million people living on less than \$1 per day. The survey conducted by the National Bureau of Statistics and the World Bank, also shows that poverty levels are higher in rural areas than in urban areas, with poverty rates of 64.2% and 40.7%, respectively. Poverty in Nigeria is worsening health standards, limiting access to education and deteriorating living standards. Nigeria's poverty rate increased from 40.1% in 2019 to 43.3% in 2021, with an estimated 87 million Nigerians living in poverty.

#### 2.2 Theoretical review

#### 2.2.1 Pareto Optimality Theory of Welfare

This theory was propounded by Vilfredo Pareto (1906). To the Welfare Economists, they seek that the economic state that will create the highest overall level of social satisfaction among its members, this microeconomic analysis leads to the condition of Pareto efficiency as an ideal in welfare economics. When the economy is in a state of Pareto efficiency, social welfare is maximized in the sense that no resources can be reallocated to make one individual better off without making at least one individual worse off. One goal of economic policy could be to try to move the economy toward a Pareto efficient state.

Pareto enunciated a very simple and straight forward criterion by saying "any change which harms no one and which makes some people better off (in their own estimation) must be considered to be an improvement. Given certain rules of distribution, any economic re-organization is said to increase social welfare, if the welfare of some persons is increased without any decrease in the welfare of others. The objective of Pareto's welfare are to (1) clarify and quantify the concept of economic welfare, (2) clarify the views of economists on matters of public policy; and (3) develop prepositions which are scientifically free from ethical judgement, but which can nevertheless serve as a basis for evaluating alternative economic policies.

Moving the economy toward Pareto efficiency might be an overall improvement in social welfare, but it does not provide a specific target as to which arrangement of economic resources across individuals and markets will actually maximize social welfare. To achieve optimal welfare, or utility, is achieved when the market is allowed to reach an equilibrium price for a given good or service—it's at this point that consumer and producer surpluses are maximized.

#### 2.3 *Empirical review*

Numerous studies analyzed have the relationship between FDI and economic growth to determine the extent to which, if any, FDI impacts economic development. The assumption common to these studies is that economic growth improves welfare. The results have been mixed, but most research finds that FDI stimulates economic growth. Hossain et al. (2019) did a study on FDI's impact on welfare in developing countries. HDI was used to measure welfare and as the dependent variable while country risk, FDI bureaucracy, trade openness, debt, governance and agglomeration as the independent variables. The study used panel data, which captured 79 countries over the span of 1998 to 2014. Fully modified OLS and dynamic OLS estimation technique was used and the study findings showed that in developing countries, there is a positive association between FDI and welfare. Nonetheless, the study failed to look at other variables, such as income inequality as a measure of welfare.

Using panel data covering the period of 1990 to 2017, Anetor et al. (2020) investigated FDI, trade, and foreign aid in the reduction of poverty in Sub-Saharan countries. The feasible generalized least square technique was used in a single model. Results displayed that both FDI and foreign aid exhibited a negative association with reducing poverty. This study suggested that FDI and foreign aid had not been transmitted accordingly, and therefore, FDI has failed to reduce poverty. This study touched on HDI but failed to touch on essential variables such as employment and income inequality.

Also. Sabuur and Ismaila (2020)investigated the relationship between foreign direct investment and economic growth in Nigeria using annual time series data from 1981 to 2020. Ordinary Least Squares was used in the investigation (OLS). According to the report, foreign direct investment (FDI) significantly boosts Nigeria's economy. Also, it was noted that over time, Nigeria's economy had benefited from the input of foreign direct investment. They suggested that the Nigerian government should concentrate on human capital development in light of their findings.

Dash (2020)examined whether remittances crowd in or crowd out domestic investment using data from 24 low income countries over the period 2004-2018. using second-generation panel methodology that accounts for endogeneity problem and crosssection dependency among countries, the study finds that remittances crowd in domestic investment in the long run. Thus, the empirical analysis in the study posits that remittances play a critical role in economic development by promoting domestic investment in the recipient countries.

Fagbemi and Osinubi (2020) in their work assessed the interconnections between FDI and human capital development in Nigeria over the period 1981-2018. The analysis was carried out with the use of both non-linear autoregressive distributed lag (NARDL) and linear ARDL bounds test approach to cointegration, and VECM Granger causality technique. Findings reveal that the effect of FDI on human capital is found to be insignificant in the long run, while it is significant in the short run. Results also indicate that there is unidirectional causality between FDI and human capital in the long run, which runs from human capital to FDI, suggesting that the quality of human capital matters for sustainable leverage and attractiveness of FDI inflows. They recommend that it is critical to adopt policy measures that could engender the sustainable development of human capital by the government, while the underlying structural

bottlenecks and protracted state of insecurity that could deter foreign investors are accorded significant attention.

Djokoto et al. (2022) examined the welfare effects of agricultural foreign direct investment in developing countries. Using an unbalanced panel data of 51 developing countries from 1990 to 2019 with a fixed-effects estimator, they found that agricultural foreign direct investment promotes welfare in developing countries. Openness to trade, population growth, human capital, and infrastructure enhanced welfare. Whilst government expenditure did not promote welfare, inflation did not affect welfare. The study recommends that whilst promoting foreign direct investment into agriculture, governments in developing countries must improve human capital, develop infrastructure, and pursue trade openness policies.

Gidiglo K. et al. (2023) in their study on the effect of foreign direct investment on welfare (human development) in Ghana employed an unbalanced panel data of 41 countries in Africa over the period of 1990 to 2019. using elasticities of the generalised estimation equations, the partial effect of foreign direct investment on welfare in Ghana was not statistically significant. The total effect of foreign direct investment on welfare in Ghana was also found to be statistically insignificant. Further, the total effect of foreign direct investment on welfare in other African countries was found to be statistically insignificant. The study recommends that Ghana and other African countries should reassess their foreign direct investment policies towards improving welfare. The interaction of policy could produce different results and can be researched subsequently.

Ganiyu (2016) observed that foreign investment creates more jobs, develops local skills, and stimulates technological progress, thereby improving welfare. However, Ranjkeshan (2021) for sub-Saharan Africa and Adegboye et al. (2021) for western sub-Saharan Africa have shown that foreign direct investment does not promote welfare. They explained that the countries in sub-Saharan Africa do not have sufficient social capabilities to absorb the benefits of foreign direct investment. Also, high levels of corruption did not allow the effect of foreign direct investment to be transmitted to the poor.

#### 3. Methodology

# 3.1 Model Specification

This study anchored on the Pareto Optimality Theory. This theory assumes that when the economy is in a state of Pareto efficiency, social welfare is maximized in the sense that no resources can be reallocated to make one individual better off without making at least one individual worse off. The model used in the study is specified, thus, in linear form

$$HDI = f(FDI, EXR, TRDO, INTR, INF)$$
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Equation (1) in econometrics form

$$\begin{split} HDI_t &= \beta_0 + \beta_1 FDI_t + \beta_2 EXR_t + \beta_3 TRDO_t + \\ & \beta_4 INTR_t + \beta_5 INF_t + e \end{split} \label{eq:HDI}$$

Where  $\beta_0$  is the constant term,  $\beta_1 - \beta_5$  is parameters to be estimated and  $e_t$  is the error term, and *t* is time. The entire variables are transformed into natural logarithm to lessen the effect of heteroscedasticity in the time series data, as presented in Equation (3)

$$InHDI_{t} = \beta_{0} + \beta_{1}InFDI_{t} + \beta_{2}InEXR_{t} + \beta_{3}InTRDO_{t} + \beta_{4}InINTR_{t} + \beta_{5}InINF_{t} + e_{t} \qquad 3$$

ARDL Model:

$$\begin{split} \Delta LHDI_t &= \beta_0 + \sum_{k=1}^n \beta_1 \Delta LFDI_{t-k} + \sum_{k=1}^n \beta_2 \Delta LEXR_{t-k} + \sum_{k=1}^n \beta_3 \Delta LTRDO_{t-k} + \sum_{k=1}^n \beta_4 \Delta LINTR_{t-k} \\ &+ \sum_{k=1}^n \beta_5 \Delta LINF_{t-k} + \mu_t \end{split}$$

where  $\beta_0$  represents drift component while  $\Delta$  shows the first difference,  $\epsilon$ t shows the white noise. The ARDL framework allows the Bounds test to swiftly determine the cointegrating relation in small sample cases (Tang, 2003). This technique is appropriate and flexible to any explanatory order of integration, either I (0) or I(1) or mutually

cointegrated while the endogenous variable is expected to be I(1).

# 4. Results and discussion of Findings

# 4.1 Unit Root Test

Augmented Dickey Fuller was used for the Unit root testing. While the ADF unit root testing of intercept was employed.

Table 1. Augmented Dickey-Fuller Test in Intercept Model

Variables	-	ADF	Critical Values	Order of
	@ Levels	@ First Difference	@ 5%	Integration
LNHDI	-4.051637	-2.342869	-3.012363	<b>I</b> (0)
LNFDI	-2.037358	-5.212873	-3.012363	<b>I</b> (1)
LNEXR	0.777792	-3.259196	-3.004861	<b>I</b> (1)
LNTRDO	-1.912874	-5.299478	-3.004861	I(1)
LNINFLR	-3.193900	-6.832076	-3.004861	<b>I</b> (0)
LNINTR	-0.850409	-4.955767	-3.004861	<b>I</b> (1)

Source: Authors' Computation (2024)

Table 1 results indicate that all the variables of interests are stationary at first difference except

for the HDI and INFLR that is stationary at level. The series are integrated in different

orders, that is, a combination of both level and first difference stationarity. Thus, cointegration test is necessary to establish a longrun relationship. Hence, the study adopts an Autoregressive Distributed Lag Model (ARDL) because none of the variables are integrated in order 2 (stationary at 2nd difference). The bound test for the cointegration is in Table 2. The bound test compares the F-value of a model at 5% level with the lower bound and the upper bound values.

Test Statistic	Value	Significance Level	Lower Bound	Upper bound
F-statistic	10.91533	10%	2.08	3.0
К	5	5%	2.39	3.38
Desigion Bula on 50/ Laval	2.5%	2.7	3.73	
Decision Rule on 5% Lever	. Кејест по	1%	3.06	4.15

**Table 2. Bound Test for Co-integration Test** 

Source: Authors' Computation (2024)

The outcome indicates that the null hypothesis was rejected, indicating that there is long term association between the explanatory variable and the dependent variable. Hence, there is long-run meaningful impact of foreign direct investment on Nigeria's welfare.

Table 3.	Short-Run	Estimates of	f Impact	of FDI o	n Human	Welfare
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Dependent Varia	ble: Human Dev	elopment Index		
Variables	Coefficient	Std. Errors	<b>T-Statistics</b>	Prob.
D(LNEXR)	-0.243742	0.041251	-5.908734	0.0001***
D(LNINFLR)	-0.002699	0.009637	-0.280123	0.7842
CointEq(-1)*	-0.123328	0.011520	-10.70565	0.0000***
Note: ***, ** and * indicates 1%, 5% and 10% levels of significance respectively				

Source: Authors' Computation (2024)

# Table 4. Long-Run Estimates of Impact of FDI on Human Welfare

Dependent Variable: Human Development Index						
Variables	Coefficient	Std. Errors	<b>T-Statistics</b>	Prob.		
LNFDI	0.252374	0.114407	2.205936	0.0476**		
LNEXR	-0.060817	0.370050	-0.164347	0.8722		
LNTRDO	-0.701639	0.448791	-1.563399	0.1439		
LNINFLR	0.308239	0.394771	0.780805	0.4500		
LNINTR	0.751991	0.597398	1.258777	0.2320		
С	7.334156	4.651751	1.576644	0.1409		
R-Squared		0.991427				
Adjusted R-Squared		0.985711				
F-Statistics		173.4615 (0.000000***)				
Durbin Watson		1.739826				

Note: \*\*\*, \*\* and \* indicates 1%, 5% and 10% levels of significance respectively Source: Authors' Computation (2024)

 $HDI = 7.334 + 0.252 lmFDI - 0.062 lnEXR - 0.702 lnTRDO + 0.308 lnINFLR + 0.752 lnINTR \\ 1$ 

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Tuble 5. Diagnosties Test	
Breusch-Godfrey Serial Correlation LM Test	0.066760 (0.8009)
Heteroskedasticity Test: Breusch-Pagan-Godfrey	1.641114 (0.2117)
Jargue-Bera Normality Test	1.371838 (0.503627)
CUSUM Test	Stabled
CUSUM Square Test	Stabled

Table 5 Diagnostics Test

From the co-integration form above, only the exchange rate had a short run significant impact on welfare, according to the co integration form above, at 5% significant levels. In the long term, 12.3% of corrections

According to equation 1, foreign direct investment has a favourable impact on Nigeria's human welfare. The serial correlation result in the table above shows probability value of 0.8009. The study concluded that there is no serial correlation in the model. Also, the heteroscedasticity test was satisfied using the Breusch-Pagan-Godfrey's heteroscedasticity test. The result shows that there exist no

to the disequilibrium can be made, according to equilibrium ARDL (ECM) the version coefficient of -0.12. As a result, in the current year, about 12% of the disequilibria from the prior year return to the long run equilibrium heteroscedasticity in the model given it chisquare value of 1.641114 and Probability value of 0.2117. Hence, it is appropriate to conclude that the model possess homoscedasticity. Furthermore, the Jarque-bera statistics of normality test shows the t-statistics of 1.371838 and the probability value 0.503627. Since the p-value is greater than 0.05, then the model residual is normally distributed.



Figure 1. Model Stability test of Cumulative Sum of Square Residuals (Long-run)



The cumulative sum test (CUSUM) and cumulative sum of square test (CUSUM of Square) plot from a recursive estimation of the model was shown in figure 1 and 2 respectively. This indicated stability in the coefficients over the sample period as the plot of the cumulative sum test and cumulative square test statistic decrease inside the critical bands of the 5% confidence interval of parameter stability. Hence, the study concluded that the model is stable and desirable. Given that the probability of the F-statistics as shown in the table above is 0.8840, we accept the null hypothesis, meaning there is no linearity in the model.

	Value	Df	Probability
T-statistic	0.252163	11	0.8056
F-statistic	0.063586	(1, 11)	0.8840

**Table 6. Ramsey Reset Test Analysis** 

Authors' computation

5. Conclusion and Policy Recommendations The findings from this study led to the conclusion that foreign direct investment has significant effect on human welfare in Nigeria. This is in tandem with some previous studies among which are Fagbemi, et al. (2020) and Subuur, et al. (2020). The stationarity test shows that human development index and inflation rate were stationary at levels while foreign direct investment, exchange rate, trade openness and interest rate were stationary at first difference. The study utilizes the Autoregressive Distributed Lag (ARDL) modelling approach to examine the

relationship between the variables. The results indicate that there is long-term significant impact of foreign direct investment on human welfare. In the short run, only the exchange rate had a significant impact on welfare at 5% level. The result implies that foreign direct investment is capable of making significant and direct contributions to sustainable development in Nigeria through their corporate social responsibility frameworks and policies. As Nigeria and order developing countries make efforts to attract foreign investment, care should be taken to ensure that investors see all reasons to invest in home's country and appreciate the unique challenges facing them and that they are expected to contribute to human welfare positively and to sustainable development in all its ramifications.

In order for foreign direct investment to promote human welfare in Nigeria, the government must formulate and implement policies that will enhance foreign direct investment into the country as the bounds test shows a significant impact of FDI on human welfare in the long run. Also, using export promotion strategy will improve the revenue generated in the country as this would be used to provide basic amenities for the populace which in turn will improve human welfare as the study shows that trade openness had a negative effect on welfare in Nigeria. Finally, government should encourage foreign investors by creating enabling environment and also curbing repatriation of profits by encouraging re-investment in the country.

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