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20 March 2019

Online at <https://mpra.ub.uni-muenchen.de/92873/>  
MPRA Paper No. 92873, posted 23 Mar 2019 03:37 UTC

# **Effect of foreign direct investment and exchange rate on economic growth of Nigeria**

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**March 2019**

## **ABSTRACT**

This study examined the influence of foreign direct investment and exchange rate on economic growth in Nigeria from 1971 to 2013. The study employed trend lines and percentage to analysis the influence of both FDI and exchange rate on the economic growth of the country. From the analysis, this study found that exchange rate exerts most influence on economic growth than FDI in Nigeria.

## **INTRODUCTION**

Economic growth is the continuous improvement in the capacity to satisfy the demand for goods and services, resulting from increased production scale, and improved productivity. Exchange rate refers to the price of one currency in terms of another currency. For instance, exchange rate of naira to United State dollar is the amount of naira that is needed to receive a certain amount of dollar. Foreign Direct investment (FDI) can simply be described as the cross-border transfer of capital and technological know-how from one nation to another. Also, foreign direct investment referred to as an investment made by an individual or company in another a nation with business interest which may be in form of either acquisition of business assets in other countries or establishment of business operation such as ownership or controlling interest in a foreign organization.

Notably, that a rise in exchange rate could make domestic goods more expensive which will discourage consumer and cause that to substitute less expensive foreign goods for locally made goods lead to decline in domestic production. Whereas FDI is an aspect of foreign investment that has been well researched and found to be a major mechanism for injection of capital needed to stimulate faster economic growth in developing countries.

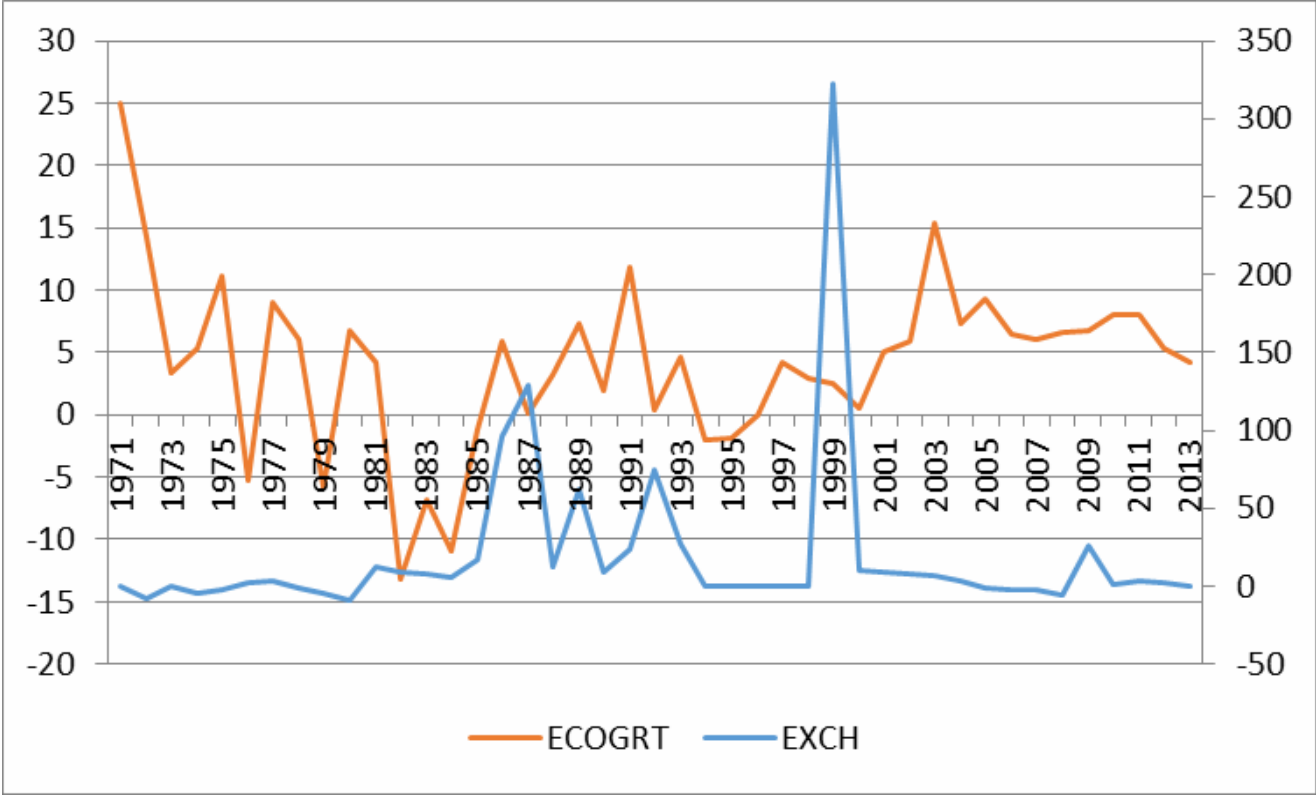
## **ANALYSIS**

### **Trend Analysis**

#### **Exchange Rate and Economic Growth rate**

Trend analysis of growth in exchange rate and economic growth of Nigeria presented in Figure 1. On the average, the exchange rate naira to US dollar appreciated by about 1.79% in 1970s but depreciated afterwards. In the 1980s, exchange rate depreciated with an average of 39.16% which depreciated further with an average of 49.6% in the 1990s. By the turn of the 21<sup>st</sup> century, the naira depreciated minimal by an average of 4.69% within 2000 to 2009 and 2.9% within 2010 to 2013 (see Table 1). The figure 1 revealed that exchange rate oscillated in most of the periods with more periods of exchange rate depreciation than appreciation. There was sharp depreciation in Nigeria's exchange rate in 1986, 1989, 1999 and 2009 with 1999 being the year with the most depreciation. In fact, the naira depreciated from ₦21.89 for US\$1 in 1998 to ₦92.34 for US\$1 in 1999. The oscillation of exchange rate revealed the currency is highly volatile suggesting its uncertainty mostly due largely on the over dependence of the economy on receipts from crude oil exports. This uncertainty of exchange rate movement is a recognized challenge facing the Nigeria economy. Instability whether positive or negative rises risk and dampens trade hence is not desirable for the economy.

The average economic growth in the 1970s was 7.03%, it fell to a negative 1.25% in 1980s, the economy improved by an average of 2.5% within the periods of 1990 to 1999. By the 21<sup>st</sup> century the average growth of the economy rose by 7.63 % within the periods of 2000 to 2009 but decline slight to average of 6.56% within 2010 to 2013. The Nigeria economy experiences the most improvement within the first decade of the 21<sup>st</sup> century. There is no correlation between the uncertain movement of exchange rate and the changes in economic growth of Nigeria.



**Figure 1: Exchange Rate and Economic Growth rate**

## Exchange Rate and Economic Growth rate

The average growth rate of FDI in the 80s was 12%, in the 90's it rose to 46%, decline to 12% in 1990s. by the turn of 21<sup>st</sup> century, FDI increase to 32% within 2000 to 2009 and decline to 8% with 2010 to 2013 (see Table 1; Figure 2). The increase in the FDI flows in the 1990s could induce improvement in the economy within 2000 to 2009. However, even with high FDI inflows in 1980s, the performance of the economy during the period was poor.

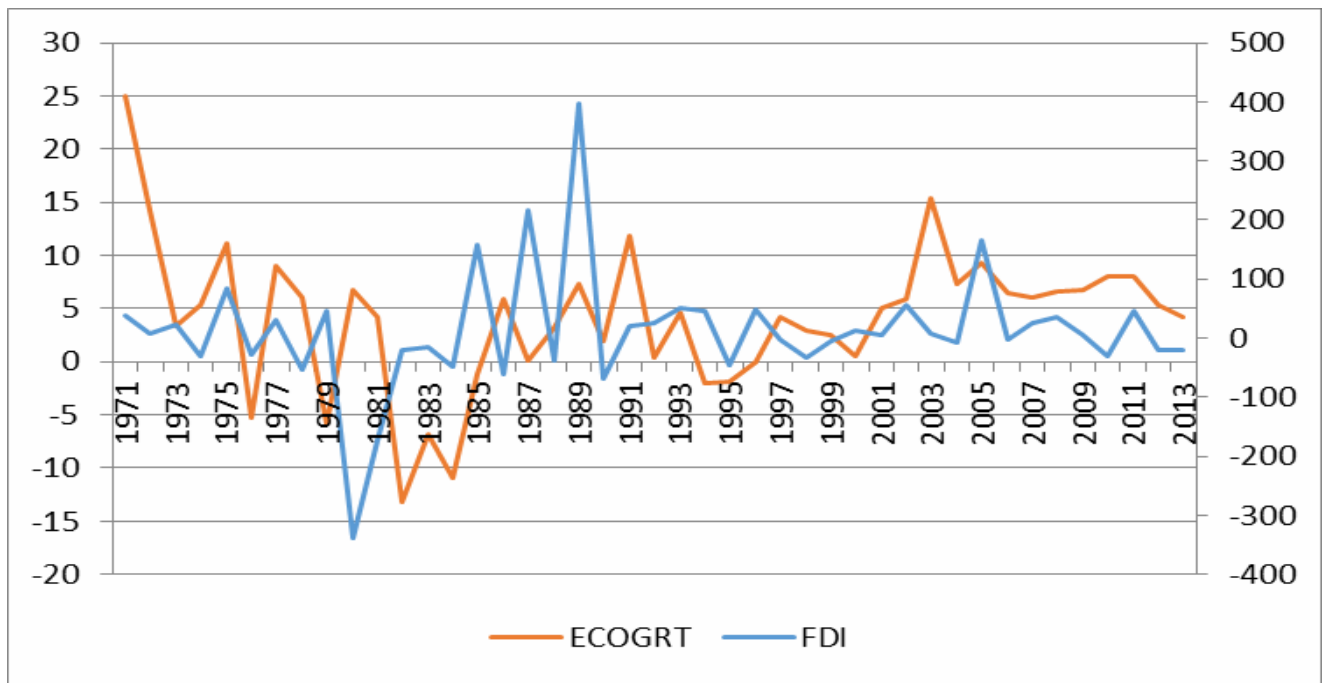


Figure 2: Exchange Rate and Economic Growth rate

**Table 1: Growth rate of FDI, Exchange rate (EXCH) and Economic Growth (ECOGRT)**

YEARS	FDI	EXCH	ECOGRT
1970-1979	12.99901	-1.79383	7.026337
1980-1989	46.07164	39.16411	-1.25089
1990-1999	11.77028	49.61003	2.506445
2000-2009	32.23157	4.688388	7.634897
2010-2013	7.773896	2.874646	6.563223

## **CONCLUSION**

The influence of exchange rate on economic performance is more crucial and visible than the flow of FDI during the period examined. The multi-dimensional effect of exchange rate and the transmission mechanism is more pronounced than FDI. most FDI are in capital intensive sectors hence, its effects if any would be felt in the economy in the long run.

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