THE IMPACT OF TRADE OPENNESS, FOREIGN DIRECT INVESTMENT AND ECONOMIC GROWTH IN NIGERIA

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ABSTRACT

This study explores the complex relationships between exchange openness, overseas direct funding (FDI), and financial boom in Nigeria, spanning 1990 to 2021. Using a robust econometric framework, consisting of the Johansen cointegration method and the Vector Error Correction Mechanism (VECM), the studies investigate the results of key macroeconomic variables consisting of gross home product (GDP) growth, change openness (measured as the ratio of overall change to GDP), FDI internet inflows, inflation, gross constant capital formation, and the hard work force. The findings reveal that while exchange openness exerts a slightly bad impact on Nigeria's economic growth, FDI demonstrates a statistically great adverse effect at the financial system. These results advise that notwithstanding its ability, FDI has not yet yielded the predicted boom blessings in Nigeria. Consequently, it's far imperative for Nigeria to adopt laws and rules that beautify FDI inflows, consisting of tax incentives, streamlined funding methods, and investor-friendly regulations. A strong and transparent investment environment is essential to help the sustained functioning of businesses and foster a financial boom.

INTRODUCTION

International change has lengthy been regarded as a key driver of financial improvement, enabling nations to expand their markets, create employment possibilities, and elevate dwelling standards. In an increasing number of interconnected worldwide financial system, trade has assumed even greater importance as countries pursue strategies to integrate into the global market. Many nations have followed guidelines to liberalize alternate, inspire foreign funding, and enhance their global competitiveness. According to Abubakar et al. (2018), Nigeria has emerged as one of the leading locations for FDI in Africa, often because of its considerable natural resources. Trade openness is a crucial component of Nigeria's financial framework, playing a twin position as both a catalyst for growth and a venture for macroeconomic stability. The depreciation of the naira has often made Nigeria an attractive destination for overseas buyers looking for value benefits. Crude oil, Nigeria's number one export commodity, has historically contributed significantly to the economy.

Yakubu and Akanegbu (2018) observed that change openness and FDI have had each high-quality and negative implications for Nigeria's economic development. They concluded that even as change liberalization and alternate price stability promote boom, the outcomes are contingent on effective coverage implementation and a conducive enterprise environment. Nevertheless, the capacity of FDI to stimulate monetary boom in Nigeria has been undermined by uncertainties, regulatory inefficiencies, and infrastructural demanding situations. Ugochukwu et al. (2013) referred to that no matter the giant inflow of FDI, its contribution to financial boom has been marginal, largely because of systemic issues which include corruption and weak institutional frameworks. Additionally, macroeconomic volatility, exacerbated with the aid of fluctuating oil expenses and worldwide commodity shocks, has in addition restrained Nigeria's monetary performance (World Bank, 2020).

This observes pursuits to research the impact of alternate openness and FDI on Nigeria's monetary increase, addressing two key research questions:

1. How does exchange openness affect economic increase in Nigeria?

2. What is the connection between FDI and monetary increase in Nigeria?

1.2 Statement of Research Problem

Numerous work have worked on this topic over the previous few decades. According to Wiredu et al.'s 2020 study, trade openness boosts economic development. Other research by Nwadike et. al., (2020) found no association. Several studies found it hurts economic growth (Zahonogo, 2017). Based on current data, there must be an agreement on how trade openness affects economic growth. Thus, this study examines trade liberalization's impact on Nigeria's economic growth. Second, FDI is a hot subject in economies worldwide. FDI can enter or leave a country. Foreign direct investment (FDI) is crucial to global business and may indicate a foreign investor's productive assets. Nigeria has FDI. These influxes have boosted the nation's economy. Following are the research questions of the Study; how does trade openness affect economic growth in Nigeria? And what effect does FDI have on economic growth in Nigeria?

LITERATURE REVIEW

2.2.1 Trade Openness Concept

Trade openness refers back to the degree to which a rustic reduces limitations to worldwide change, which include price lists, quotas, and different restrictive measures, that allow you to facilitate the loose trade of goods, services, and capital throughout borders. As countries open up their markets, they regularly revel in improved integration into the worldwide economic system, which may contribute to financial increase. According to Igudia (2004), as cited in Ijirshar (2019), the liberalization of exchange is an essential aspect of financial growth strategies, as it permits nations to enjoy the increasing interconnection of worldwide markets. Trade openness promotes the movement of goods, offerings, and capital, which in turn can cause extra market right of entry, extra green aid allocation, and better requirements of residing.

Proponents of trade openness argue that it permits international locations to capitalize on their comparative benefits, leading to more efficient use of sources, era transfer, and extended industrial productiveness. The classical economic theories of Smith’s Absolute Advantage and Ricardo’s Comparative Advantage highlight the importance of specialization and the blessings of accomplishing worldwide exchange. According to Smith’s principle, nations must specialize inside the manufacturing of products that they are able to produce maximum effectively, and change the ones goods with different countries. Ricardo extended this through suggesting that even supposing one USA is much less efficient in generating all items as compared to any other, it may nevertheless advantage from exchange through that specialization in the goods it produces maximum efficaciously relative to others (Keho, 2017). These theories argue that alternate opens possibilities for countries to achieve better monetary boom by utilizing their strengths and reducing inefficiencies.

However, critics of change openness warn that without proper regulation and policies, unbridled alternate can divulge growing economies to external shocks, immoderate reliance on a limited range of sources, and developing profits inequalities. Zahonogo (2016) noted that at the same time as alternate openness typically fosters a financial boom, its fulfilment is contingent on a rustic’s institutional capability and the competitiveness of its domestic industries. In precise, developing international locations can also battle to benefit absolutely from change liberalization if their industries are not sufficiently competitive or if their institutions cannot manage the volatility and dangers associated with open markets.

Concept of Foreign Direct Investment (FDI)

Foreign Direct Investment (FDI) refers to investments made by way of people, organizations, or entities from one US into commercial enterprise pursuits or assets overseas. This investment often takes the shape of buying or organizing production centers, organizing joint ventures, or acquiring enormous stakes in local businesses. FDI is visible as a key driver of monetary growth, especially for developing nations, as it includes the transfer of capital, technology, and managerial expertise. These elements can beautify productiveness, create jobs, and foster monetary development within the host.

Adeleke et al. (2014) emphasized that the fulfilment of FDI in promoting financial growth is inspired by way of the host united states's regulatory environment, hard work marketplace, and infrastructure. A nicely-functioning prison and institutional framework, access to skilled exertions, and reliable infrastructure are vital factors that determine the effectiveness of FDI in spurring development. In Nigeria, the inflow of FDI has been largely stimulated via the country's great natural useful resource endowments, especially in the oil and gas sectors, and its huge patron market. However, systemic inefficiencies, inclusive of inadequate infrastructure, corruption, and macroeconomic instability, have hindered the transformative capacity of FDI. As a result, even as FDI has contributed to job advent and some sectors of growth, its broader effect on the Nigerian economy has been confined.

Empirical Evidence

Empirical research has tested the impact of both exchange openness and FDI on Nigeria's economic boom, revealing blended findings. Nwadike et al. (2020) determined no enormous courting between trade liberalization and monetary increase in Nigeria. Their take a look at suggested that trade openness by myself is inadequate to force sizeable financial boom, and that complementary guidelines—together with infrastructural improvement, institutional reforms, and human capital funding—are important for exchange liberalization to have a meaningful effect on monetary overall performance.

On the alternative hand, Afolabi et al. (2017) observed that FDI inflows have a superb impact on productiveness inside the short term. They highlighted those overseas investments generally tend to beautify the productiveness of sure sectors, especially in phrases of era switch and activity introduction. However, the long-time period effects of FDI on economic growth in Nigeria had been constrained. Structural demanding situations, along with inadequate infrastructure, regulatory inefficiencies, and political instability, have hindered the sustained impact of FDI on the broader financial system. This aligns with the findings of Osakwe (2020), who argued that powerful governance and infrastructure development are crucial to maximizing the advantages of FDI. Without addressing these structural constraints, FDI might also fail to power long-term monetary boom and development within the United States. In summary, at the same time as each change openness and FDI are associated with fine monetary results, their full potential can simplest be realized when complemented by means of strong home rules, powerful governance, and investments in infrastructure. For Nigeria to leverage these monetary strategies effectively, it'll need to implement reforms that decorate institutional capacity, improve competitiveness, and mitigate dangers related to outside market fluctuations.

2.3 THEORETICAL REVIEW

Classical or Country-based Theories

The architects of the various theories of the classical country-based approach were primarily concerned with the notion that a nation's prosperity should take precedence. They were primarily of the opinion that economic development should be the priority. The following section discusses the principal classical theories of international commerce.

Mercantilism

In the 17th and 18th centuries, the first traditional land-based philosophy was mercantilism. A new century begins. This is one of the most discussed and debated theories. Prioritizing the wellbeing of citizens should be a nation's top concern, resulting in increased exports and decreased imports. Importing only the requisite raw materials is a necessity. Increasing precious metal reserves, according to economists, is the greatest way to preserve wealth. A nation must produce enough goods to increase exports and reduce its reliance on imports of goods and other materials for this concept to be accurate. This significantly increases exports and decreases imports. A strong commitment to mercantilist theory has historically benefited numerous nations. History demonstrates that by adhering to Mercantilism, numerous nations benefited.

Mercantilism, one of the earliest concepts of trade, persists in contemporary philosophy. Neo-mercantilist policies that discourage imports by promoting protectionist measures, restrictions, and domestic sector subsidies. Almost every nation employs a protectionist strategy to safeguard vital economic sectors. Frequently, export-oriented businesses advocate protectionist policies that benefit their industries and businesses, despite the fact that protectionism is detrimental to other businesses and consumers. Taxpayers foot the bill for export subsidies by paying higher taxes. Due to import restrictions, consumers who purchase foreign-made products and services must pay more.

2.3.1.3 Absolute cost advantage

An economist called Adam Smith criticized mercantilism and advanced the principle of absolute advantage in 1776. Smith was adamant that specialization and the division of labour were essential for the economic expansion of international trade. Specialization increases output and improves the standard of living for the general populace. He stated that specialization would be impossible on a limited market with labour division. Governments should not attempt to control international trade or impose restrictions on domestic trade, according to Smith's argument. His Theory also listed the consequences of government intervention and restrictions on unfettered commerce.

2.3.1.4 Theory of comparative cost advantage

In 1817, British economist David Ricardo presented his Theory of Comparative Advantage. Even though country A had a distinct advantage in producing goods, trade and specialization could still occur between the two countries, according to Ricardo. Theoretically, each nation should prioritize the production of products with the greatest benefits or the fewest disadvantages. As a result, a nation exports the products with the highest profit margin and imports the products with the lowest environmental impact.

METHODOLOGY

The take a look at employs annual time-collection facts from 1990 to 2021, analysed the usage of EViews 12. Econometric strategies, which include the Johansen cointegration take a look at and the Vector Error Correction Mechanism (VECM), are utilized to evaluate the relationships between the variables. Stationarity of the information is proven the usage of the Augmented Dickey-Fuller (ADF) check, whilst cointegration is confirmed through the trace statistic.

TRADE OPENNESS AND ECONOMIC GROWTH IN NIGERIA

Economic development and openness to trade in Nigeria have strong long-term connection, but a favourable short-term link (Lawal et al., 2016). Empirical study shows that rising states in Sub-Saharan Africa (SSA) must consider many policy factors to maximize trade liberalization's growth benefits. The study's econometric methodology was unspecified (Zahonogo 2016).

Iyoha and Okim (2017) explored the relationship among economic development and change in ECOWAS international locations the use of panel records from 1990 to 2013. They implemented aggregated OLS, fixed-consequences, random-effects, and dynamic panel regression models, finding that investment, forex, and exports were key predictors of an boom in in step with capita actual profits. Their look at highlighted that change, especially exports, significantly contributes to economic increase in ECOWAS member states. The use of a dynamic panel records estimator addressed issues of endogeneity. Similarly, Keho (2017) hired the Autoregressive Distributed Lag boundaries test at the side of the Toda and Yamamoto Granger causality tests to demonstrate that exchange liberalization fostered economic development in Côte d'Ivoire among 1965 and 2014.

RESULTS AND DISCUSSION

The analysis indicates a full-size bad dating among exchange openness and Nigeria's economic boom, indicating that improved alternate liberalization should have adverse outcomes with out appropriate assisting rules. Similarly, FDI inflows have a statistically sizable terrible impact on boom, emphasizing the need for structural reforms to improve capital usage performance. While these outcomes are steady with Zahonogo (2016), they evaluation with the findings of Malefane and Odhiambo (2018), who observed a positive courting between exchange openness and economic increase in different Sub-Saharan African international locations. This disparity underscores the significance of context-precise factors, such as institutional great and policy coherence.

The chart depicts the evolution of the variables GDPR, FDIGDP, LNGFCF, INFCP, LNLF, and OPEN.

Figure 4.1 Trend of Gross Domestic Product Growth Rate

Source: Researcher's Computation using Eviews 12, 2023

In Figure 4.1, the GDP growth rate has many fluctuations in the period under the study. The GDPR fell drastically from 11.8% in 1990 to 0.36% in 1991, managed to rise to 4.6% in 1992. It fell again to its all-time low in 1993 to -2.03%. The GDP growth rate increased significantly to 15.3% in 2002, which shows the increased volume of economic activity and productivity in that year. The rate fell back to 7.34719% in 2003 and remained relatively stable until 2016, when it experienced a -1.6168 growth which can be attributed to the recession that occurred in that year. A negative growth rate was also recorded in 2020 due to the reduction in productivity due to the COVID-19 pandemic.

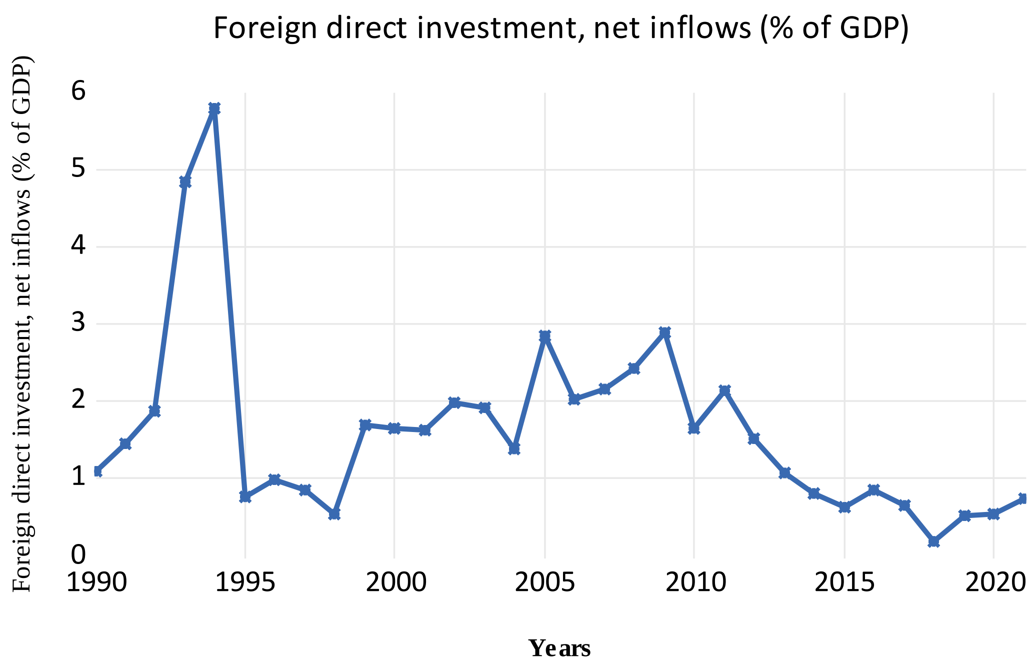

Figure 4.2: Trend of Foreign direct investment, net inflows (% of GDP)

Source: Researcher's Computation using EViews 12, 2023

In Figure 4.2, FDIGDP has many fluctuations in the period under the study. The FDIGDP increased steadily in 1990 from 1.08% to 5.79% in 1994, making it its all-time high. It then fell drastically to 0.76% in 1995. Then it increased to 1.69% in 1999 and steadily increased until 2005, when it reached 2.8%. It then decreased steadily to 2016, when the country experienced a negative growth of 0.85% which can be attributed to the recession that occurred that year. It then kept decreasing from 0.64% in 2017 to 0.18% in 2018, and it has since been increasing from 0.51% in 2019 to 0.75% in 2021.

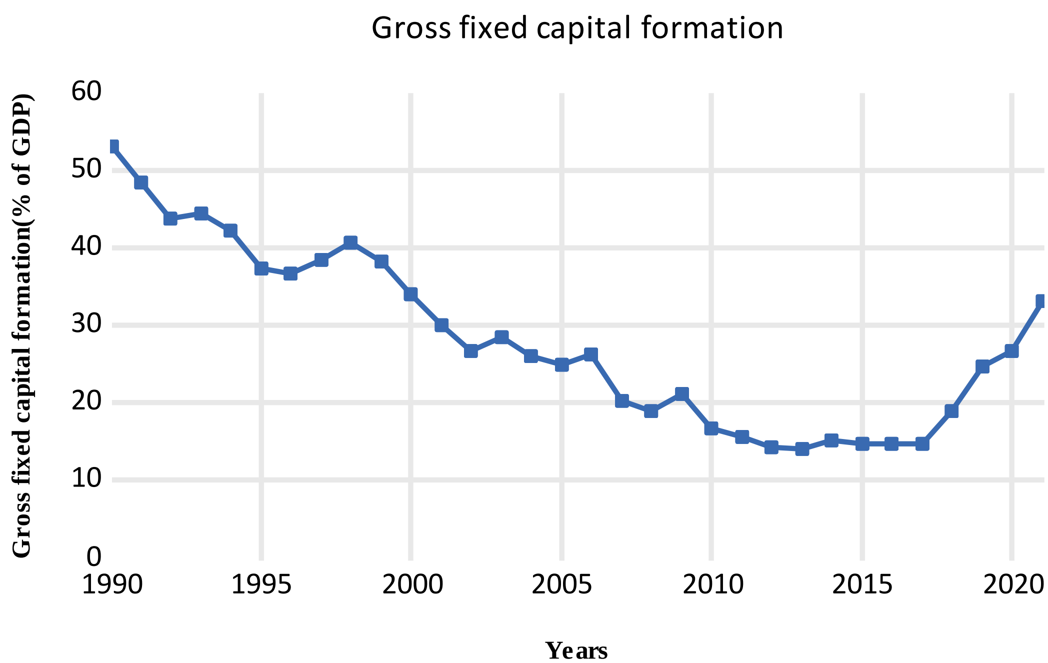

Figure 4.3: Trend of Gross fixed capital formation (% of GDP)

Source: Researcher's Computation using EViews 12, 2023

In Figure 4.3, The GFCF decreased drastically from 53.12% in 1990 to 43.7% in 1992, increased by a small margin to 44.47% in 1993, then kept on decreasing till 1998, where it rose to 40.5%. It then decreased steadily over the years, from 38.2% in 1999 to 18.8% in 2008. It increased to 21.1% in 2009 and then started decreasing steadily up until 2017, where it was 14.71%; from this point onwards, Gross fixed capital formations have been on the rise from 2018, where it was 19.01%, then 24.6% in 2019, to 26.7% in 2020. It then took a massive leap to 33.1% in 2021.

Econometric Analysis of Data

The 1990 to 2021 time series data was analyzed using E Views 12. Co-Integration test assesses the viability of the relationships while the adjustment speed was calculated using vector error Correction model.

4.3.1 Unit Root Test

Variables	Augmented Dickey Fuller (ADF) Test Statistic		Order of Integration
	Levels I(0)	First Difference I(1)	
GDPR	-3.541832	-8.881265	I(1)
	(0.0522)	(0.0000)	
FDIGDP	-3.076784	-5.881524	I(1)
	(0.1310)	(0.0002)	
LNGFCF	1.367287	-4.200745	I(1)
	(0.9999)	(0.0125)	
INFCP	-2.628297	-4.427032	I(1)
	(0.2713)	(0.0074)	
LNLF	-2.922432	-3.621698	I(1)
	(0.1700)	(0.0500)	
OPEN	-3.399720	-5.419291	I(1)
	(0.0698)	(0.0007)	

Table 4.2: Summary of Augmented Dickey Fuller Unit Root Test Results

The variables in Table 4.2 were tested for stationarity. GDPR, FDIGDP, LNGFCF, INFCP, LNLF, and OPEN are static at the first difference. At I (1), the variables from the table are constant.

4.3.2 Cointegration Test

Table 4.3: Johansen Co-integration Trace Test

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.854776	171.2327	117.7082	0.0000
At most 1 *	0.796346	113.3483	88.80380	0.0003
At most 2 *	0.635879	65.60835	63.87610	0.0355
At most 3	0.547209	35.30025	42.91525	0.2329
At most 4	0.260323	11.53049	25.87211	0.8432
At most 5	0.079472	2.484237	12.51798	0.9313

Trace test indicates 3 cointegrating eqn(s) at the 0.05 level.

*** shows rejection of the hypothesis at 0.05 level**

**** MacKinnon-Haug-Michelis (1999) p-values**

Source: Researcher's Computation using Eviews 12, 2023

Table 4.3 shows the trace statistic at least 3 cointegrating equations at a 5% significance level at the point where the trace statistic and critical value are 65.60835 and 63.87610, respectively. Therefore, we reject the null hypothesis of no cointegrating equation. It concludes that there is evidence of a long-term relationship or cointegration among the variables.

The research was carried out mainly to investigate the impact of Nigeria's trade openness, foreign direct investment, and economic growth. The results revealed a long-term relationship between the variables of interest, foreign direct investment inflow, trade openness, gross domestic product growth rate, gross domestic fixed capital formation, inflation, and labour force on economic growth. Trade openness and FDI was also described as having a negative and vital effect on Nigeria's economic growth. The study found that in the long term, significant negative relationships exist between trade openness and economic growth in Nigeria.

The finding suggests increased trade openness will lead to decreased economic growth. This finding contrasts with apriorist expectations, which expect trade openness to have a positive relationship with economic growth. Despite contrasting with apriorist expectations, the result is consistent with the findings of Nwadike et al., (2020), which concluded that trade openness significantly boosted economic growth in Nigeria. The study showed a statistically insignificant negative relationship between economic growth and trade openness. The result also contrasts with the findings of Malefane & Odhiambo (2018), who investigated the dynamic consequences of trade openness on economic growth. Their empirical findings revealed that in the long run, trade openness affects economic growth positively and significantly when the ratio of total trade to GDP is used as a proxy alone. This is consistent with apriorist expectations but not consistent with the result, which states that trade openness has a negative relationship with economic growth in the long run. These findings highlight that when a more significant foreign market is made accessible by trade openness for domestic businesses, it may lead to more sales, better revenues, and scale-related economies of scale. Exporting goods and services can benefit businesses and help the economy flourish.

The study found that in the long run, there is a significant negative relationship between FDIGDP and economic growth in Nigeria. This finding suggests that a growth in FDIGDP (Foreign direct investment, net inflows) will shrink economic growth. This finding contrasts with apriorist expectation which expects that FDIGDP should have a positive relationship with economic growth because by boosting investment levels, enhancing productivity, and generating job possibilities, this capital inflow can spur economic growth. Although despite contrasting with apriorist expectations, the result is consistent with the findings of Afolabi, Danladi, and Azeez (2017), who used GDP served as a proxy for economic growth, with the exchange rate, government spending, interest rate, FDI, export, and import serving as independent variables.

The study's findings showed that Exchange rates and foreign direct investment are negatively insignificant to GDP. The results also contrast with the findings of Osakwe (2020), who demonstrated in his findings that foreign direct investment had a positive and elastic significant impact on economic growth in Nigeria. This is consistent with apriorist expectations but not consistent with the result, which states that FDIGDP has a negative relationship with economic growth in the long run. This finding highlights the need to reduce over-dependence on import goods, both at the domestic and industrial product levels should be discouraged with the aim of embarking on an impact substitution approach to economic development in Nigeria.

RECOMMENDATIONS AND CONCLUSION

Promote Export Diversification: Nigeria need to prioritize the improvement of export-orientated industries, mainly in agriculture, manufacturing, and services. This can be executed via financial incentives, tax reliefs, and subsidies to stimulate boom in these sectors.

Enhance FDI Attractiveness: To attract and maintain Foreign Direct Investment (FDI), guidelines ought to focus on simplifying investment processes, making sure felony and regulatory transparency, and providing strong investor safety. These steps are important to growing a extra appealing funding weather.

Strengthen Institutional Frameworks: Tackling corruption, improving governance, and investing in infrastructure are essential for creating an surroundings conducive to alternate and investment. Strengthening those institutional frameworks will foster economic improvement.

Foster Technological Innovation: Investment in studies and development, coupled with partnerships with overseas firms, can facilitate generation switch and beautify productiveness. This will force technological development and improve Nigeria's competitive side within the global market.

Conclusion

While exchange openness and FDI have extensive capability to power financial increase in Nigeria, their fulfilment is surprisingly dependent on the implementation of comprehensive and cohesive policies. Addressing the structural and institutional challenges that currently obstruct their tremendous consequences is essential to unlocking Nigeria's complete monetary capacity.

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