MODERATING EFFECT OF INFLATION ON FOREIGN DIRECT INVESTMENT AND ECONOMIC GROWTH RELATIONSHIP IN NIGERIA

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ABSTRACT

Every rational economy is often poised to maintain low inflation alongside sustainable economic growth as her macroeconomic policy to ensure foreign inflows. Notably, high inflation harms economic activities while low inflation rate is advantageous. It then becomes imperative to ask, at what rate is inflation beneficial to an economy? This article estimates the impact of inflation on FDI-growth relationship for the period 1981-2017. In the results, there's a positive long-run relationship between the three variables in question. An addendum to the findings show a nonlinear relationship, such that the Nigerian economy is at its highest growth rate when inflation is less than or equal to 2.80 percent threshold level of inflation and above which it becomes harmful to growth. Further findings show that the marginal effect of FDI at less than threshold level of inflation is positive to growth while at higher than threshold level of inflation is negative to growth. In conclusion, the Nigerian government should harness, develop and stabilize her macro economy to prevent the repellence of foreign investors by maintaining its inflation at its threshold level or less.

Key words: Foreign Direct Investment, Inflation, Gross Domestic Product, linkage, threshold, long run, coefficient, relationship

1. INTRODUCTION

The importance of foreign direct investment (FDI) is very pertinent; hence its relevance cannot be overemphasized. The extent to which it matters in providing new technologies, products, management skills and competitive business environment, overtime has been a strong force for economic growth drive. The conventional way of defining foreign direct investment is that, it is an investment that requires an acquisition of a long term management interest not less than 10% in a company of a foreign country (World Bank, 1996). With this, Foreign Direct Investment has gradually turned to a crucial tool used to attract capital flows from external sources. In third world countries, foreign direct investment has immensely triggered and strengthened the growth of the economy growth (Muhammad, 2007). Foreign Direct Investment in these countries engineer a reduction in unemployment and makes them take more advantage of their natural and human resources. This also enables effective implementation of new business practices which also enhances a decline in budget deficit. Nations that are plagued with scarcity of capital and technological expertise are most likely to face slower growth rate than those that have a chunk of capital and technological expertise. Foreign direct investment could be a channel for technology and knowledge transfer (Dunning & Hamdani, 1997). The gains of FDI is seen by the New Partnership for Africa's Development (NEPAD) as a vital asset for translating into actuality, NEPAD's vision of growth and development. The reason is that Africa needs ample amount inflow

of external resources so as to bridge gaps in saving and investment as well as overtake itself to sustainable growth levels and oust the already manifesting poverty (Ajayi, 1999, 2000, 2003).

The dynamism of FDI has become even more imperative for growth in developing countries. Stefanović (2008) asserted that developing countries often consider FDI as an important asset for growth and the most desirable mode of foreign capital inflow and is relatively safe given its difficulty in withdrawing. The World Bank (2007) reported that in 2006, FDI inflows clocked a mind boggling record high of US$1.1 trillion globally and its increase into the developing economies has proven to be continuous. FDI has proven its importance over the years to both the host economy and the foreign investor. The host economy enjoys growth in business activities; boost the exportation of goods and services, clamps down unemployment and accelerates economic growth and development. FDI also triggers development financing and growth by boosting the total investments in the receiving or host country and thus enhances gains in productivity via skills in management and technology. However, the viability of FDI in host countries depends on some macroeconomic fundamental of which inflation play a major part.

Inflation no doubt plays an expedient role on influencing the level of FDI of an economy. Exploring inflation-growth relationship is of serious concern that has spurred considerable theoretical and empirical research dating back right from the onset of understanding the link as very important for effective monetary policies (Seleteng, Bittencourt, & Van Eyden, 2013). Over the years as seen in previous studies, low inflation rate has been seen to draw foreign investors to prompt growth, and with this knowledge, the various governments have made fervent efforts to keep inflation rates attractive, that is, at a relatively low rate. Whether inflation is indispensable for growth or not it is the bone of contention. Even with the variations in theoretical and empirical literatures on inflation-growth relationship, there are abundant empirical studies that confirm the negative effects of high inflation on economic growth (Fisher, 1993; Bawo, 1996; Gosh & Phillips, 1998; Khan & Sen Hadji, 2001). The fusion of a high growth rate and stable inflation – at a low rate – is the major goal of macroeconomic policies for every economy (Seleteng, Bittencourt, & Van Eyden, 2013; Vinayagathasan, 2013) because inflation at high level halts economic growth courtesy of its unwanted re-distributional and welfare effects (Eggoh & Muhammad, 2014). By fostering investment and enhancing the efficiency in the usage of productive resources, low inflation stimulates growth (Ahortor, Adenekan & Ohemeng, 2012). This calls for this question; at what level exactly does low inflation become high? With high inflation, uncertainty makes the economy more unpredictable, and the resulting effect is that sustainable growth becomes more difficult.

The Central Bank of Nigeria (CBN) revealed that FDI flows to Nigeria fell to $798.35 million in September 2017 from $1386.21 million in January 2016. Analysts attributed the decline to increased inflation in the country as well as poor infrastructure (CBN, 2017) although despite the drop, Nigeria remained the tenth greatest recipient of FDI in Africa. Thus, inflation is a major macroeconomic variable that developing nations have faced a tough time to deal with. FDI could easily be affected by inflation, but its impact on the economy cannot easily be pinpointed. Over the years FDI in Nigeria has been unstable, these fluctuations have been caused by other variables which may not necessarily be inflation.

Despite this existing debate and uncertainty in the nature of inflation-growth relationship and the environment by which inflation impacts on economic activities, Nigeria no doubt has to pursue low inflation with consistent prices to attract FDI which would drive growth. In view of this, both monetary and fiscal policies have to be put in place appropriately to stabilize a single digit inflation

target. Even though previous studies on this subject has been conducted, there hasn't been any information on the particular inflation rate that would negate the growth of FDI in the economy.

It is because of this that an empirical evaluation of the inflation-FDI-growth link in Nigeria becomes crucial and then to access the threshold link between inflation and FDI. Thus, in the light of the above issue raised, this article aims to examine and ascertain the impact FDI exerts on economic growth, the interactive effect of FDI and inflation on growth, and finally, to estimate the threshold level of inflation and above the relationship between FDI and economic growth becomes negative for a period of 1981 – 2017.

2 LITERATURE REVIEW

2.1 THEORETICAL LITERATURE

FDI is widely referred to as a crucial catalyst for transforming the economy of countries. Researchers alongside policy makers have now realized that FDI has the potential of boosting growth via a variety of channels. FDI stimulates stock of capital as well as reduce unemployment, it also enhances technological changes with the aid of technological diffusion which spills technology over for local firms within the country. Because FDI enhances technological transfer, it is considered to steer all the available share of knowledge in the recipient country. This can be by enhancing effective labour training and skills are thus acquired and distributed rightly. On the flip side FDI, there could be harmful effects that have been neglected.

It is in view of this that Srinivasan, Kalaivani & Ibrahim (2011) reported FDI to have a negative effect on growth in the host nations. The dependency theory was developed to address this negative impact, and the theorists and supporters of this school view FDI from the developed economies and conclude that it would harm the economic growth of third world nations especially in the long-term. Their supporters agree that the First World nations got their wealth from the Third World nations by extracting excessively their labour and other crude and natural resources without adequately compensating them which has led to pervasive poverty. Apart from this, Rodrik (2004) considered another facet that sees FDI as harmful on the host countries. His argument was based on the fact that FDI may bring about regrettable consequences which include pollution of the environment and exploiting labour knowing fully that the highest attainable goal of investors is profit maximization. However, Oetzel & Doh (2009) are of the opinion that FDI has the potential of contributing positively to the growth of the host country, if and only if these countries put in place suitable policies and provide institutional frameworks, legal frameworks and other incentives that will enhance the creation of benefits and advantages from FDI.

2.2 EMPIRICAL LITERATURE

Literatures on FDI and its determining factors alongside its impact on economic growth is considered valuable by many, but the empirical evidence proves to be unimpressive where facts from several researchers opine that the only few theories in existence on FDI and its determinants are available, they are still very much substantial (Lall & Narula, 2004; Blonigen 2005). With this in mind, Faeth (2009) went ahead and opined that FDI doesn't have a single theory, instead some models that are based theoretically have in the past attempted to elaborate more on FDI and the location decision of multinational firms, with the implication that any study on the determinants of FDI shouldn't hang only on one theoretical model. Nayak & Choudhury (2014) have an argument as well, even though FDI literature and its theories have been conducted occasionally, research studies on this literature examining FDI outflow from the developing nations are scanty.

2.2.1 EMPIRICAL LITERATURE ON INFLATION AND FDI

Inflation is widely considered to exert an influence in the economic growth of countries worldwide. Although, there has been diverse opinions of its impact on economic growth of countries. Li (2006) argued that one of the most significant macroeconomic debates is the inflation-growth relationship. However, there's a consensus among economists recently that barring a particular threshold that inflation does not exceed, there's going to be long-run non-linear relationship between inflation and economic growth. An addendum to this study is that of Omankhanlen (2011) who hypothesized inflation to disturb the tax system which could subsequently affect investors adversely in the long run as a result of illusion of money.

Andinuur (2013) embarked on a study to investigate the link between inflation, FDI and economic growth in Ghana. In his study, low rate of inflation internally stabilizes the host country which would in turn encourage FDI and boost its returns. Omankhanlen (2011) examined the impact exchange rate and inflation exerts on foreign direct investment in Nigeria. His study also aimed at examining FDI's influence on Nigeria's economic growth rate. They deployed time series data in the study for the period of 1980 to 2009. They went further to include control variables which are government expenditure and gross fixed capital formation. Linear regression analysis technique was deployed to examine the relationship inherent between the variables of interest – exchange rate, inflation, FDI inflows and economic growth. The study found and uncovered that inflation has no effect on FDI while the latter relates positively to the economic growth of Nigeria.

Contrary to other opinions that suggests positive relationship between inflation and FDI, Udoh & Egwaikhide (2008) were able to examine exchange volatility effect and inflation uncertainty on FDI in Nigeria over the period 1970 to 2005. GARCH model was employed to do justice to the study, and with the results suggesting that inflation is statistically significant and has a negative impact on FDI. In like manner, Djokoto (2012) didn't relent in his investigation on the effect investment promotion exerts on Foreign Direct inflow in Ghana across 1970 to 2009 and his findings suggested inflation and FDI to have a negative connection. However, Djokoto in his study used control variable to capture inflation and further employed the cointegration technique. Furthermore, Omankhanlen (2011) was of the opinion that inflation could still impact positively on FDI and growth eventually, as long as inflation is not above a particular threshold. However, the above literature shows that results of prior studies revealed that results are contradictory in some cases in terms of the linkage between inflation rate and FDI.

2.2.2 EMPIRICAL LITERATURE ON FDI AND GROWTH

Cross-country examination on the linkage between FDI and growth such as a study put forward by Balasubramanyam, Salisu, & David (1996) by sampling 46 developing countries between 1970 and 1985. The results found trade openness as a key player in the acquisition of a possible growth impact of FDI. The results also indicated that FDI affects the growth of the economy more than domestic investment does. The results further confirm the view that FDI acts as a vehicle that drives the transfer of international technology. In addition to this literature, Choe (2003) explored FDI and economic growth relationship by employing panel data to his work in eighty countries across 1971 and 1995. The findings suggested that both FDI and economic growth Granger cause each other, that is, there exists a bidirectional relationship among them.

For country-specific analysis, Adjaye (2009) study on the relationship between FDI and GDP growth in Ghana established a significant as well positive relationship between the two variables. Johansen and Juselius (1990) multivariate maximum likelihood procedure was employed across 1970 and 2007. The result of granger causality suggested bidirectional

relationship from FDI to growth. Sackey, Compah-Keyeke and Nsoah (2012) examined the impact of FDI on the economic growth of Ghana with a variety of econometric tools such as ADF tests, VAR and Johansen cointegration test using annual time series data that covers 2001 to 2010. The relationship in their finding between FDI and growth is positive and significant in the long run with uni-directional causality which runs from FDI to GDP growth. Sergius and John (2017) employed a variety of econometric tools to ascertain the relationship between FDI and economic growth in Nigeria across 1981 and 2013. In their result, the relationship is significant, positive and strong. This means that if the increase in FDI is well managed, it could be used to enhance GDP. In conclusion, FDI-growth relationship is very high, positive and significant.

2.3 GAPS IN THE LITERATURE AND VALUE ADDITION

From the aforementioned empirical literatures, no study has been able to ascertain the particular threshold of inflation and that any change above or below the threshold causes FDI impact on economic growth differently. Thus, this study adds to the already existing knowledge by estimating the threshold level of inflation and above the threshold FDI and economic growth relationship becomes negative.

3 METHODOLOGY AND DATA

3.1 THEORETICAL FRAMEWORK

We shall use time series data for our study and develop an econometric model to examine the relationship FDI has with Nigeria's economy. To analyse the exact relationship among these variables, we shall develop a model to ensure this. The AK model is the simplest endogenous model here to use that gives a constant-savings rate of endogenous growth in its special case of a Cobb–Douglas production function thus; $Y = AK^{\alpha}L^{1-\alpha}$ (1)

Where Y = Total production in an economy; A = Total factor productivity; K = Capital; L = Labour, and the parameter measures the output elasticity of capital.

For the special case in which, the production function becomes linear in capital thereby giving constant returns to scale, we have; $Y = AK$ (2)

Certainly, the extant literature has identified other channels that could impact on GDP. For example, foreign direct investment (FDI), inflation (INF). In what follows, we will rely on this growth framework to specify the model.

3.2 MODEL SPECIFICATION

Following the economic growth literature, the following baseline model is estimated to determine the impact of inflation on FDI on economic growth.

$$RGDP = \gamma + \lambda_1 FDI + \lambda_2 INF + \lambda_3 \phi + \varepsilon \quad (3)$$

Where; RGDP = Real Gross Domestic Product; FDI = Foreign Direct Investment; INF = Inflation

ϕ = control variables (such as Exchange rates, lending interest rate, broad money supply, gross capital formation and General government final consumption expenditure – constant LCU); ε = Stochastic error term; γ, λ_1, λ_2 and λ_4 are the parameters to be estimated.

Real GDP is used to proxy for economic growth. Exchange rates, lending interest rates and gross capital formation are used to measure macroeconomic stability while Government consumption expenditure, gross capital formation and broad money supply accounts for internal shocks. All variables except broad money supply, inflation and exchange rates are transformed into their natural logarithms.

The interaction term between FDI and inflation rate is included to ascertain the moderating role of inflation rate on the effect on FDI on economic growth.

$$RGDP = \gamma + \lambda_1 FDI + \lambda_2 INF + \lambda_3 (FDI * INF) + \lambda_4 \phi + \varepsilon \quad (4)$$

The marginal effects of changes in the two variables – FDI and inflation – can be captured by the partial derivatives of equation 4 with respect to FDI. This is shown below;

$$\frac{\partial RGDP}{\partial FDI} = \lambda_1 + \lambda_3 \text{INF} \quad (5)$$

The signs of the coefficients of λ_1 and λ_3 are important. If $\lambda_1 > 0$ and $\lambda_3 < 0$, it means FDI positively impacts GDP but inflation rate mitigates that positive impact. If $\lambda_1 < 0$ and $\lambda_3 > 0$, it suggests FDI has a negative impact on GDP and inflation rate adversely influences that negative impact. In the two scenarios stated above, it suggests the existence of the threshold effect that implies that the growth effect of FDI changes with inflation level. Therefore, it would be crucial to evaluate the marginal effect within the sample.

When $\lambda_1 < 0$ and $\lambda_3 < 0$, it suggests that FDI impacts negatively on GDP, and the inflation rate magnifies that negative impact. However, a positive marginal effect ($\lambda_1 + \lambda_3 \text{INF}$) implies that more FDI and inflation would enhance growth, but the opposite will be the case if the marginal effect is negative.

3.3 DATA

The data was sourced from World Development Indicators (WDI) 2018

4 RESULTS AND DISCUSSIONS ON FINDINGS

4.1 STATIONARITY TEST

VARIABLE	ADF T-STATISTIC AT LEVELS	ADF 5% CRITICAL VALUE	ADF T-STATISTIC AT 1ST DIFFERENCE	ADF 5% CRITICAL VALUE AT 1ST DIFFERENCE	ORDER OF INTEGRATION
LRGDP	1.047773	-2.945842	-4.410325	-2.948404	I(1)
LFDI	-1.021124	-2.948404	-11.38300	-2.948404	I(1)
INF	-3.443471	-2.948404			I(0)
EXR	2.248978	-2.945842	-3.297372	-2.948404	I(1)
LIR	-2.442608	-2.945842	-6.618864	-2.948404	I(1)
LGEXP	-0.333095	-2.945842	-6.175949	-2.948404	I(1)
M2	-3.423098	-2.948404			I(0)
LGCF	-0.313161	-2.954021	-3.935113	-2.954021	I(1)

The results of the stationarity test show that all the variables used in the study are stationary, but at different levels of integration. LRGDP, LFDI, EXR, LIR, LGEXP and LGCF are stationary at first difference. That is, they are integrated at order; 1(1) while INF and M2 are stationary at levels. Thus on this basis, the null hypothesis of null-stationarity is rejected and it is safe to conclude that the variables are stationary and the regression result won't be spurious.

4.2 JOHANSEN COINTEGRATION TEST RESULTS

NUMBER OF COINTEGRATING EQUATIONS	TRACE STATISTICS	5% CRITICAL VALUE	P-VALUE
None *	180.3003	159.5297	0.0022
At most 1 *	126.3416	125.6154	0.0451
At most 2	92.25329	95.75366	0.0850
At most 3	66.36285	69.81889	0.0915
At most 4	42.31702	47.85613	0.1500
At most 5	24.61632	29.79707	0.1756
At most 6	9.961947	15.49471	0.2837
At most 7	0.296136	3.841466	0.5863

The above result reveals at least two significant cointegrating equation. The presence of cointegration makes the estimation of a long-run model possible. This is in tandem with the result of the study conducted by Sackey, Compah-Keyeke and Nsoah (2012) on the impact of FDI on the economic growth of Ghana with FDI and growth indicating a positive and significant relationship in the long run.

4.3 REGRESSION RESULT

VARIABLE	COEFFICIENT	STD. ERROR	T-STATISTIC	P-VALUE
C	20.46601*	0.873733	23.42364	0.0000
LFDI	0.038950	0.063662	0.611828	0.5456
INF	-0.000316	0.002348	-0.134594	0.8939
LFDI*INF	-0.014128	0.054946	-0.257121	0.7990
EXR	0.001885*	0.000307	6.148042	0.0000
LIR	0.002801	0.003462	0.809075	0.4253
LGEXP	0.211230*	0.027590	7.655952	0.0000
M2	-0.005664*	0.002001	-2.829975	0.0085
LGCF	0.145763*	0.032960	4.422378	0.0001

R^2 = 0.986453 Adjusted R^2=0.982582 D-W stat= 1.382099 F-stat= 254.8572 Prob (f-stat) = 0.0000
Note: * denotes statistical significance at 5% significant level

LFDI stands for the log of foreign direct investment and has its coefficient as 0.038950 but is insignificant. This is in consonance with the result ofOmankhanlen (2011) who argue that FDI's effect on growth is positive but not significant and FDI was not a key instrument that enhanced the economic growth of the nation.

The coefficient (-0.000316) implies a percentage change in inflation will lead to a percentage decrease in the gross domestic product. This is consistent with previous results such as that of Vinayagathasan (2013) who reported that there exists a negative insignificant relationship between inflation and growth until it reaches a particular threshold level after which it significantly begins to slow down growth.

LFDI*INF represents the interactive effect/term of FDI and inflation on economic growth. It has a coefficient of -0.014128 which shows that a percentage change in the interactive term will have a negative effect of -1.41% on gross domestic product, holding other factors constant.

Thus, the coefficient of exchange rate (0.001885) shows that a percentage change in exchange rates leads to a percentage increase in gross domestic product by 0.2%, ceteris paribus. This is in tandem with the work by Omankhanlen (2011) when he reported that exchange rates significantly affect the growth of the Nigerian economy positively

Lending interest rate with a coefficient of 0.002801 shows that a percentage change in interest rate will lead to a percentage increase in gross domestic product by 0.3% as this conforms with the results of Akpansung & Babalola (2011) which suggested that interest rate and economic growth exerts a positive insignificant relationship in Nigeria.

Government consumption expenditure on the other hand has a coefficient of 0.211230 which means it can exert a positive and significant effect on the Nigerian economy.

Unsurprisingly, Olaleye, Edun, Bello & Taiwo (2014) in their research concluded that government consumption expenditure is positively related to growth and as well statistically significant in demonstrating changes that relate to economic growth.

The coefficient (-0.005664) of money supply demonstrates a negative relationship with economic growth. However, this is in consonance with the report given by Suleiman (2010) who suggested that money supply reflects a negative relationship with real GDP.

Here, the coefficient 0.145763 indicates the existence of a positive and significant relationship between gross capital formation and GDP in Nigeria. This result corroborates the findings of Ugwuegbe & Uruakpa (2013) as well as that of Orji & Mba (2010) and Bakare (2011) who concluded that their result showed a positive relationship that is statistically significant among the two variables.

4.4 EVALUATION OF RESEARCH HYPOTHESIS

The testing of these hypotheses below are made more concrete by the fact that the model satisfied all validity test.

H_{01}: There is no impact of FDI on economic growth in Nigeria. We fail to reject the above hypothesis (H_{01}) because the coefficient of log of foreign direct investment has a positive impact on RGDP but its impact is statistically insignificant at 5% level of significant using the P-value.

H_{02}: There is no interactive effect of FDI and Inflation on economic growth in Nigeria. As discussed earlier, equation 5 ($\frac{\partial GDP}{\partial FDI} = \lambda_1 + \lambda_3 INF$) forms the interactive term from equation 4 where λ_1 is the coefficient of FDI and λ_3, the coefficient of INF. The coefficient of FDI was found to be 3.9 while that of inflation is -1.41, with FDI (3.9) having a positive impact on GDP and inflation rate (-1.41) adversely influences that positive impact.Therefore, we reject the H_{02} because there is an interactive effect between FDI and INF on economic growth in Nigeria.

H_{03}: There is no threshold level of inflation and above the threshold the relationship between FDI and economic growth becomes negative. Having known the interactive effect of FDI and INF on economic growth in Nigeria, we find the threshold by equating equation 5 to 0 (zero).

$$\frac{\partial RGDP}{\partial FDI} = \lambda_1 + \lambda_3 INF = 0$$

3.9 + (-1.41)INF = 0

3.9 – 1.41INF = 0

3.9 = 1.41INF

INF = 2.76

INF = 2.8

Substitute INF = 2.8 into the equation, we have above;

$$\frac{\partial RGDP}{\partial FDI} = \lambda_1 + \lambda_3 INF$$

$$\frac{\partial RGDP}{\partial FDI} = 3.9 - 1.41(2.80)$$

$$\frac{\partial RGDP}{\partial FDI} = 3.9 - 3.9$$

$$\frac{\partial RGDP}{\partial FDI} = 0$$

Therefore, we reject the H_{03} and conclude that there is a threshold level of inflation which is pegged at 2.8. The question that will pop is; how do we determine the rate of growth when inflation is at its minimum and maximum? This is very easy to determine. From our descriptive statistics, the minimum inflation is found to be at 5.38% and 72.84% at its maximum.

For minimum inflation, we have;

$$\frac{\partial RGDP}{\partial FDI} = \lambda_1 + \lambda_3 \text{INF}$$

= 3.9 – 1.41(5.38)

= -3.6858

= -3.7

For maximum inflation, we have;

$$\frac{\partial RGDP}{\partial FDI} = \lambda_1 + \lambda_3 \text{INF}$$

= 3.9 – 1.41(72.84)

= -98.8044

= - 98.8

It can be observed that at the minimum level of inflation, the economy will have a negative growth of -3.7%, ceteris paribus. Now at maximum inflation, the economy will grow by -98.8 if all other factors are held constant.

4.5 SUMMARY OF RESEARCH FINDINGS

This study is poised to determine the interactive effect of FDI and inflation on economic growth, and to estimate the threshold level of inflation and above the relationship between FDI and economic growth becomes negative. From our findings, only inflation, the interactive term and broad money supply are negatively related to economic growth, but only money supply is statistically significant. On the other hand, FDI, exchange rates, lending interest rate, government expenditure and gross capital formation have a positive relationship with economic growth but with exchange rate, government expenditure and gross capital formation having a statistically significant effect on economic growth. The threshold level of inflation was found to be at 2.80% which would interact with FDI and yet ensure the economy does not experience negative growth. We were also able to find that at minimum inflation level of 5.38, the economy will have a negative growth rate of -3.7%. On the other hand, the economy will grow at an abysmal -98.8% at maximum inflation rate of 72.84%. Another major finding of this paper is that the threshold level of inflation was found to be 2.8%. This threshold level of inflation should be the highest mark of inflation in order to maintain a positive economic growth rate. Unfortunately, the minimum level of inflation in Nigeria is above the threshold level, suggesting that the negative effect of inflation outweighs the positive effect of FDI. And this has hindered the capacity of FDI to effectively enhance economic growth in Nigeria. Finally, the result also suggests a long-run relationship among the variables that makes the long-run model estimation possible

5 POLICY RECOMMENDATIONS

a) This first policy recommendation requires the government to maintain a relatively low and consistent price of goods and services produced. You could also put, inflation rate should be at most, moderate. From the analysis, the coefficient of FDI is positive and inflation is negative, the interactive effects explains that FDI has a positive impact on GDP and the inflation rate adversely influences the positive impact. Therefore, if at least a positive economic growth is to be maintained, the rate of inflation should at least be at the threshold level if not, there will be a negative economic growth. With the relevance of inflation in this study, the government should be very proactive in enacting policies to ensure moderate inflation rate that would drag foreign investors and pin down the already established ones.

b) An inflation rate as low as 2.8% is likely going to be unattainable for a developing country like Nigeria. On that note, it has become necessary for the government to tilt her attention to the area of capital formation if she must drive towards economic prosperity as capital formation is

revealed in our findings as an important factor that drives positively the growth of the Nigerian economy. If a proportion of present income is not consumed but saved and used to invest so as to augment any form of output or income in the future, it will help acquire new factories with the appropriate productive capital goods to improve economic infrastructure that can pull foreign investments constantly to become significant in affecting the economic activities that would bring about sustainable growth in the economy.

c) To further ease off the pressure mounted on inflationary rate, the government should adequately regulate her broad money supply because from our findings, it has the tendency to greatly affect the economy negatively because of its statistical significance.

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