

Fdi inflow into sub-saharan africa



As FDI has often been involved with investing and operating outside the economy of the investor, a lot of scholars have tried to unravel its determinants, and the factors that induce MNEs to invest in one country over another. A lot of these studies were initially centred on the causing economic factors; but recently, the role of governance in determining inward FDI into a host country has grabbed the attention of researchers.

Some of the economic perspectives in the literature on reasons why the state of governance in host country matter in driving FDI inflows have been established. Government policies and institutional factors increase or decrease the cost of investing in a country which in turn influences the return on the investment (Root and Ahmed, 1978).

This is because good governance gives birth to quality institutions that improve productivity which stimulate foreign investment. Increase productivity often come from rigorous research and development system, accessible financial institutions that can fund large scientific and technology projects, a flexible labour market, loose restriction of businesses and a stable political government (Nelson, 2008; Hodgson and Stoelhorst, 2014). Good governance thus increases productivity by bringing down transaction cost.

High transaction costs are mainly from high cost of production, logistic operation, vital business information and general management cost. These costs can arise from poor property rights protection, inefficient institutional system and underdeveloped financial system (Dunning, 2004). These are the costs looked for by potential foreign investors before entering a new market,

in order to aid them not only assess the barriers, but also to better evaluate the subsidiary in the new location when business starts.

Therefore market-based governance are aimed at removing opportunistic behaviour (Fan et al., 2009) in order to stimulate foreign competition and provide multinational enterprises with an opportunity to exploit ownership advantages abroad that will reduce cost. Reduction of transaction cost will bring about an increase in trust, competition and commitment from businesses which will in turn ensure that the host country provide a stable and developed business environment (Tomassen et. al., 2012)

Efficient governance indeed brings about the protection of property rights. Government enforces property rights to preserve and maintain value. The protection is necessary for the production of goods and services (Wall et. al., 2010) Good governance attracts FDI as stated by Fab et al., (2009).

Therefore, host countries that intend attracting FDI will need to provide the needed requirements for stable political environment where market based institutions are reliable and predictable and public institutions do not inhibit MNEs from exploiting home-country advantages, increase efficiency and reduce cost (Sethi et. al., 2003).

According to literature review, governance or institutional quality has been widely represented by the 6 World Bank Governance Indicators as mentioned previously. They are associated to cross-border economic activities and hence either deter or attract FDI to a recipient country.