

EFFECTS OF FOREIGN DIRECT INVESTMENT ON THE FINANCIAL PERFORMANCE OF THE LISTED MANUFACTURING COMPANIES IN NIGERIA

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ABSTRACT

The main objective of this study was to determine the effect of foreign direct investment and financial performance of the listed manufacturing companies in Nigeria. The study focused on the 32 listed companies randomly drawn from the 74 listed manufacturing companies in Nigeria. The secondary data extracted from the financial statement of these companies were subjected to both descriptive and inferential statistics. The result shows a significant positive relationship between the two variables. The findings also revealed that the company with the highest percentage of foreign direct investment had about twenty two percent of its assets contributed by the foreign direct investors. Therefore, efforts should be made to make the investment environment attractive in order to attract more foreign direct investment into the listed manufacturing companies in Nigeria.

Keywords: Foreign Direct Investment, Financial Performance, Internationalization, Return on Assets.

INTRODUCTION

The inflow of foreign direct investment in developing economy has generated interest in recent time not just because of the benefits to firm growth, survival and competitive position, but also because of its positive influence on a nation's economic growth and development (Mayer & Ottaviano, 2008). While foreign direct investment can be a source of growth for firms, it can also be a risky venture that can generate losses which may adversely affect the long term survival of a firm if not properly handled. Any company seeking to be an industry leader in the twenty-first century must not focus on domestic funding only, but must also focus on attracting investors and global market leadership. O'Cass and Weerawardena (2009) justified that global competition for African businesses is not an option but an economic priority.

In the developed countries, foreign direct investment has helped significantly to improve their economy. For instance, the Chinese companies have improved their management and technical skills through foreign direct investment (Lall & Albaladejo, 2004). Lower entry barriers and a more relaxed regulation of the FDI have allowed the Chinese companies to reform through foreign joint ventures with foreign companies, and the success of the Chinese open economy has also furthered the internationalisation of the Chinese companies (Andersson, Gabrielsson, & Wictor, 2006). The Chinese government has encouraged a number of Chinese companies to expand their international market through specialized foreign trade corporations, with the objective of enlarging exports and securing supplies of raw materials, and further acquiring

advanced technology and R&D capabilities through their internationalisation strategy (Child & Rodrigues, 2005).

Nigerian economy is facing contraction due to dwelling global oil price, reduced oil revenue and growing statutory expenditure, however listed manufacturing companies can leverage on FDI to improve productivity, quality and competitiveness it also increases knowledge about training the workforce, contributes to the acquisition and dissemination of new knowledge, and allows managers to learn new organizational practices to enhance return on asset through internationalisation of the goods and services (Thériault & Beckman 2008). Foreign and cheap source of funding will aid the rapid development and internationalisation of Nigerian listed manufacturing companies to advantage of the opportunities in African market (Olusegun, 2012). Therefore, this study seeks to investigate the effect of foreign direct investment on financial performance of listed manufacturing companies in Nigeria in the context of the several challenges from low demands, economic stagnation, unemployment and dwelling global oil price from a Nigerian perspective over the past ten years from 2006 to 2015.

LITERATURE REVIEW

Theoretical Review: Resource Based Theory

Resource based theory was initiated in the mid-1980s by Wernerfelt (1984), Rumelt and Lamb (1984) and Barney (1986) the Resource-Based View (RBV) has since become one of the dominant contemporary approaches to the analysis of sustained competitive advantage. The resource-based view suggests that valuable firm resources--comprising tangible and intangible elements--are usually scarce, imperfectly imitable, and lacking in direct substitutes (Brouthers & Hennart, 2007). It is about producing the most value from one's existing capabilities and resources by combining these with others' sources of advantage and, in this, ensuring complementarity is paramount (Johanson & Vahlne, 1990). The resource-based view suggests that firms develop unique resources that they can exploit in foreign markets or use foreign markets as a source for acquiring or developing new resource-based advantages (Luo, 2002). Luo (2002) suggests that firms develop resource-based advantages by developing or acquiring a set of firm-specific resources and capabilities that are valuable, rare and imperfectly imitable and for which there are no commonly available substitutes. According to Barney (1991), a firm resource must, in addition, be valuable, rare, and imperfectly imitable and substitutable in order to be source of a sustained competitive advantage. Foss (1998) states that the resource-based perspective does not escape the general problem of finding the appropriate unit of analysis. Most contributions within the RBV take the individual resource as the relevant unit of analysis to study competitive advantage. However,

Foss (1998) points out that this choice may only be legitimated if the relevant resources are sufficiently well-defined and free-standing. If, in contrast, there are strong relations of complementarity and cospecialization among resources, it is the way resources are clustered and how they interplay and fit into the system that is important to the understanding of competitive advantage. Foss (1998) recognizes that the concepts 'capabilities' and 'competences' aim perhaps at grabbing this clustering and interplay. The conceptual framework takes this problem into account by relating competitive advantage to strategy rather than to individual resources.

Barney (1991) introduced the Resource Based View (RBV) which suggests that characteristics of firm's resources may contribute to sustainable competitive advantage. However only if these resources are rare, valuable, non-substitutable and difficult to imitate the company can have a competitive edge compared to its competitors (Barney, 1991). Multinational companies have better resources as compared to local companies. Globalization has enabled these companies to reach markets overseas because of their superior marketing strategies influence by better resources. Gimeno (1999, p. 101) states that the resource-based research "has emphasized the lack of ability of imitators or rivals to erode the market position of a firm as a necessary condition for sustainability, implicitly assuming that any rival capable of eroding the position will do so, and cannot be restrained from pursuing that course of action".

Although the resource-based view (RBV) has emerged as one of the substantial theories of strategic management, it is said that it has overlooked the role of entrepreneurial strategies and entrepreneurial abilities as one of the crucial sources of the competitive advantage of a firm (Fink & Kraus, 2007). For the purpose of this study, resource based theory is found relevant as it provides theoretical foundation for explaining how companies organize resources to enhance internationalisation process and its effect on financial performance. Therefore, this theory is expected to provide theoretical basis for specific objective one to four.

Empirical Review: Foreign Direct Investment and Financial Performance

Several empirical literatures on foreign direct investment show varying results, Doukas and Lang (2003) state that foreign companies that invest in their business performed better than post-acquisition financial companies that do not diversify into fields of activities other than traditional activities. FDI can improve productivity, quality and competitiveness it also increases knowledge about training the workforce, contributes to the acquisition and dissemination of new knowledge, and allows managers to learn new organizational practices (Thériault & Beckman 2008). Many multinational enterprises have been attracted by new markets, cheap labour forces and supporting policies toward foreign direct investment (FDI) in transition economies (Cheng & Kwan, 2000; Bevan & Estrin, 2000).

Muhammad (2012) conducted a study on internationalisation speed and cost efficiency using survey data and financial statement data of German insurance groups with property-liability business for the years 2009. The study developed a resource-based perspective and argued that strategic transformation is a major factor driving insurance groups' internationalisation, whereby successful international insurance groups facilitate organizational learning from international operations to enhance home market performance. The findings of the study confirmed the notion and showed that the establishment of branch offices as well as greater internationalisation is positively correlated with company's financial performance. Chatterjee (2009) posit that the main motives for a firm to engage in foreign production are to seek natural resources, to seek market, to seek efficiency and to seek strategic asset. However, study on the factors influencing the performance of Japanese FDI in Thailand, 270 Japanese MNCs subsidiaries between year 2005-2009 were sampled and result shows that firm size is negatively associated with profitability (Hooda, 2011).

Mawugnon and Qiang (2009) investigates the effect of foreign direct investment on economic growth through internationalisation in Togo using time series data, the research found that there was a unidirectional relationship between FDI and GDP. The direction of causation ran from FDI through internationalisation to GDP enables to conclude that FDI positively influence GDP through internationalisation and not otherwise. The study therefore recommends improvement in the investment climate for foreign direct investment to enhance competitiveness and strengthen through internationalisation.

Büthe and Milner (2008) examine the influence of Foreign Direct Investment on Per Capita GDP in Nigeria using Vector Error Correction. The result shows a negative relationship between FDI and economic growth in Nigeria. Similarly, Kolstad and Wiig (2012) investigate the impact of foreign direct investment (FDI) on Economic Growth in Nigeria within the period of 1986-2011. The study employed multiple regression models to determine the impact of some external variables on the gross domestic product (GDP) proxy for economic growth in Nigeria. The study used time series data to ascertain the inflow of FDI to the Nigerian economy and its implications on economic growth. The finding revealed a positively impact on the economy though its contribution to GDP was very low within the period under review.

In addition, Head, and Ries (2008) examined the sustainability of the FDI- growth relationship in Nigeria. Using the Johansen co-integration framework and a multivariate VAR within a vector error correction model, found evidence of a long-run equilibrium relationship between economic growth and FDI inflows. The study also revealed a unidirectional causality from FDI to economic growth. Also, Kinda (2010) looking at a cross-country study on FDI and economic growth, the study used a bivariate VAR modelling technique and found evidence of a positive FDI-led growth for Nigeria, Sri Lanka, Tunisia, and Egypt; and based on weak exogeneity tests, a long-run causality between FDI and economic growth running in both directions was found for the same set of countries. Evidence from prior research on FDI and financial performance of listed companies, reveal contrary findings Damijan, Rojec, Majcen and Knell (2013) show positive effects of FDI on listed companies' financial returns, while Doytch and Uctum (2011) report negative FDI effects on profitability. Similarly, in banking sector studies, and Unite and Sullivan (2003) find negative association of FDI presence on profits of companies, while Lensink and Hermes (2004) found positive association on the same. Alguacil, Cuadros and Orts (2011) investigated the empirical relationship between FDI and economic growth in Nigeria. Using OLS technique, the study found that FDI had a positive impact on economic growth.

Mathews (2006) examine internationalisation in emerging market companies from the Asia-Pacific region, it shows that their internationalisation was very rapid and had positive influence on the financial performance of companies. Also it was different from that of the conventional western multinationals, and also from that of the erstwhile developing country multinationals in the 1960s and 1970s. Ayanwale (2007) conducted an investigation to determine whether FDI had any positive impact on the economic growth of Nigeria. The study shows that there was a positive relationship between FDI and Gross Domestic Product (GDP). The study concluded that the economy would perform better with greater inflow of FDI.

Mathews and Zander (2007) review internationalisation as practice by multinationals through FDI described it as 'accelerated internationalisation.' Newer multinationals from emerging

markets have been able to pursue rapid internationalisation owing to their distinctive ability to come up with organizational and strategic innovations compensating for their lack of financial and managerial capabilities. The resultant effect on financial performance was significantly high. The harsh environmental conditions in most emerging economies such as a weak institutional context, demanding yet price sensitive consumers, and challenging distribution networks in their home markets, instead of acting as impediments, have helped emerging market companies to develop unique competencies, to be later apply to compete successfully in foreign markets that impacted on financial returns positively

McGrew and Poku, (2007) explore the effects of internationalisation on firm performance Using a sample of 164 Japanese SMEs, finding show that higher levels of FDI are positively related to performance. Further, it also shows that exporting has a negative moderating effect on the relationship between FDI and performance, which points to the importance of the configuration of internationalisation strategies. FDI applicable to the companies through internationalisation and access to foreign markets influence performance of the companies in a positive manner (Osamor, Akinlabi & Osamor, 2013). Okpala (2012) claim that FDI flows as a bundle of resources to companies enhances SMEs' financial performance. Also FDI's effect on economic growth is thus based on its contribution to capital accumulation and total factor productivity improvements.

Khanna, Palepu and Sinha (2005) posit that the rise of companies such as Ranbaxy Laboratories from India, Samsung from Korea, and Acer from Taiwan, into powerful global giants clearly demonstrates the effect of FDI properly managed by companies to generate super high financial rewards. Gatawa, Aliyu and Musa (2013) analysed the impact of FDI on performance of manufacturing sector in Nigeria, the study employs a model that measures the exert FDI on financial performance. This study concludes that FDI have impact on financial performance. Umah (2007) states that FDI of multinational corporations distort developing nation economy, distortions include the crowding out of national firms, rising unemployment related to the use of capital-intensive technology, and a marked loss of political sovereignty.

RESEARCH METHODOLOGY

Research Design

This study will use both descriptive and quantitative research design; Orodho (2003) defines research design as the scheme outline or plan that is used to generate answers to research problems. Maxwell (2012) stated that descriptive research design is useful when the researcher objectives include determining the degree to which one variable (dependent) affect the other variable (independent). This research design will be selected for the reasons that, firstly, it helps establish the effect of foreign trade on financial performance. Secondly, it will help to achieve the main objective of this research which is focusing on effect of foreign trade on financial performance of listed manufacturing companies over a prescribed ten one-year period from January 2006 to December 2015. The quantitative portion will involve the use of multiple regressions, t test, correlation and diagnostic test.

Population

Burns and Grove (2003) describe population as all the elements that meet the criteria for inclusion in a study. A population is defined as total collection of elements about which we wish to make some inferences (Cooper & Schinder, 2011). Mcmillian and Schumacher (2010) define population as a large collection of subjects from where a sample can be drawn. In other words, population is the aggregate of all that conforms to a given specification. The population of this study is all the listed 74 manufacturing companies in Nigeria from where a sample of 32 companies were drawn. Kitchenham and Pflieger (2002) assert that a target population is the group of individuals to whom the survey applies. It is the collection of individuals about whom conclusions and inferences are made (Enarson, Kennedy & Miller, 2004).

Mugenda and Mugnda (2004) term target population as that population to which a researcher wants to generalize the results of the study. The study's target population is 74 seventy-four listed manufacturing companies in Nigeria.

Data Collection Instruments

This study will use secondary methods of data collection. The secondary data will be collected through the company's financial reports of the listed manufacturing companies in order to inquire about internationalisation and financial performance of listed manufacturing companies.

Data processing and analysis

Data analysis is the process of data to make meaningful information (Saunders, Lewis & Thornhill, 2009) defined data as mechanism for reducing and organizing data to produce findings that require interpretation by researcher. According to Hyndman (2008) data processing involves translating the answers on a questionnaire into a form that can be manipulated to produce statistics. This involves coding, editing, data entry, and monitoring the whole data processing procedure. Data collected will be analyzed by editing, coding and categorizing through the use of statistical package for social sciences (SPSS) version 20.0 computer software.

Descriptive and inferential statistics will be use to analyze and interpret the data use in this research. Specifically, descriptive statistics related to means and standard deviation. Inferential statistics included correlation and regression analysis.

Model Specification

With regression analysis, the study will assess the effects of independent variable on the dependent variable. The Univariate regression model is as laid below as the Equation shows the linear regression model of the independent variable against the dependent variable.

$$Y = \beta_0 + \beta_1(\text{FDI}_t) + e$$

Where:

Y= Financial performance this will be both ROA and

X₁= Foreign Direct Investment.

β_0 = regression output constant

β_1 = the coefficient of independent variable

e = Error Term

Data Presentation and Analysis

Descriptive Statistics

From table 4.1, it was revealed that an average manufacturing company in Nigeria had about 10% of its assets contributed by the foreign investors with the least having foreign patronage of 2% while the best was 22%. The standard deviation was about 3% indicating a moderate variation in foreign direct investment across different companies in the manufacturing sector. The result is by and large consistent with that of Kraśnicka and Głód (2013) who conducted a study on the impact of the internationalization of Polish SMEs on their performance where a mean score of 8.40% was recorded.

As touching the return on assets, the mean was 0.8466% while the minimum and maximum are 0.6% and 13.53% respectively. Although a very wide variation was observed in the reported return on assets of manufacturing companies in Nigeria, but this is not unacceptable since both large and small firms were included in the sample. The results was consistent with those of Mitton (2002) who reported a mean score of 0.68% for return on assets and Macauley and Randoy, (2013) whose mean score for return on assets was 0.99%. The results can be found in table 4.5

Table 4.1 Summary Statistics for Dependent and Independent Variables

	Mean	Std. Dev	Min.	Max.	Sum	No of Obs.
Foreign Direct Investment	10.2430	3.4247	2	22	3288	320
Return on Assets	0.8466	4.0825	0.62	13.53	271.76	320

Trend Analysis

Trend Analysis for Foreign Direct Investment

The trend analysis for foreign direct investment for the ten years under consideration was presented in figure 4.4. The trend show a gradual and consistent fall from 2005 through 2013. This implies that the inflow of foreign investment into the Nigeria economy has been on the decrease for an economically significant period of 8 years. Although, it signals a very serious danger to the local economic, it is however believed that the little rise in 2014 might indicate that efforts has been put in place by the regulatory authorities to prevent withdrawal of investment by the foreign investors.

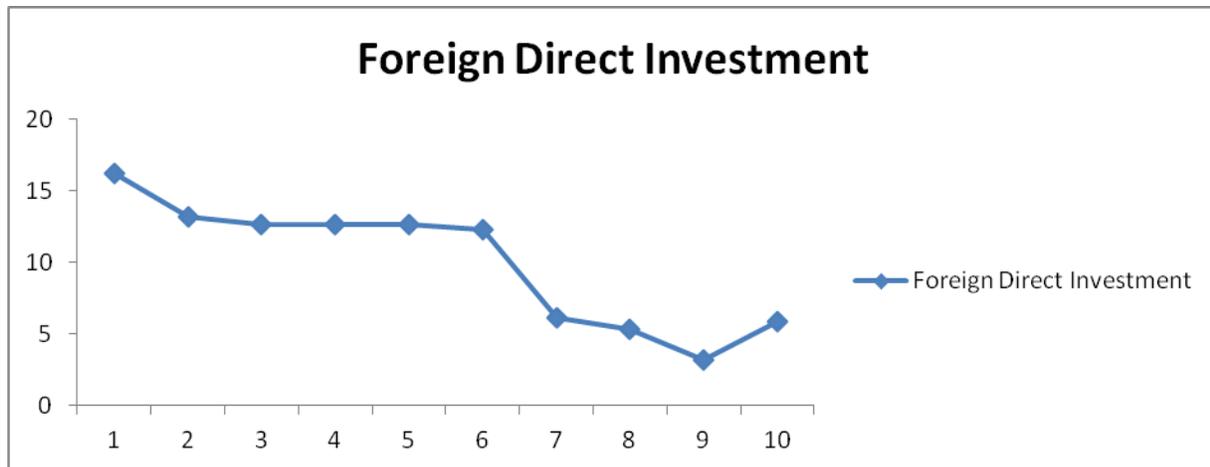


Figure 4.4: Trend Analysis for Foreign Direct Investment

Trend Analysis for Return on Assets

The results of trend analysis for return on assets witnessed a significant increase across the years under consideration except 2012 a little reduction from the previous year. For instance, return on assets was about 2% in 2005 whereas it was about 14% in 2014 indicating that management of the listed manufacturing companies in Nigeria have been efficient in the use of shareholders resources and thereby providing reasonable returns on the assets. The fall in 2012 can however be attributed to the economic reform that took place in 2011 among which was the mandatory implementation of international financial reporting standard (IFRS) which took place in 2011.

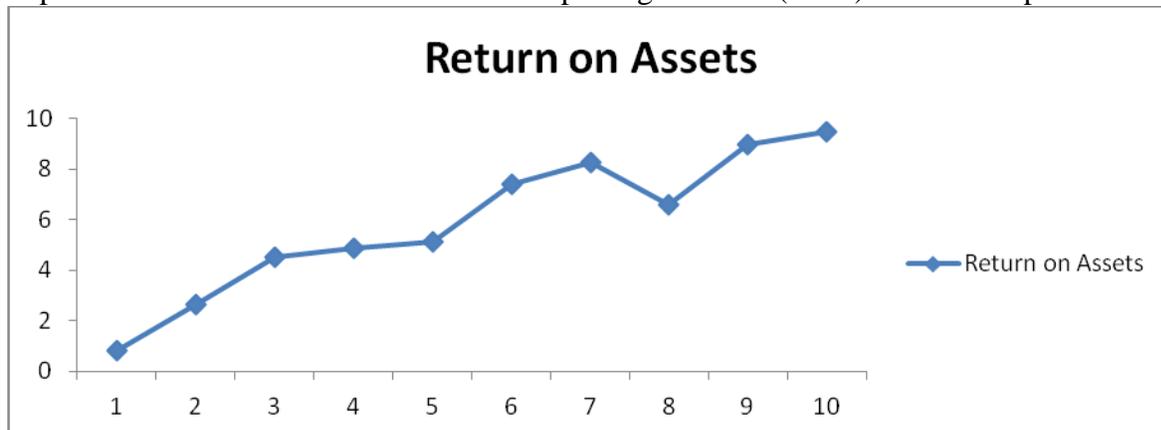


Figure 4.7: Trend Analysis for Return on Assets

Inferential Statistics

Correlation Analysis: Pearson Correlation Analysis for Foreign Direct Investment and Return on Assets

The Pearson correlation of foreign direct investment and return on assets was computed with the use of statistical package for social sciences (SPSS version 20) and the result produces a coefficient of 0.628 (p-value =0.000) indicating a strong significant and positive relationship between the two variables. The result concurs with that of Mawugnon and Qiang (2009) that investigates the effect of foreign direct investment on economic growth through

internationalization in Togo using time series data, the research found that there was a unidirectional relationship between FDI and GDP. The direction of causation ran from FDI through internationalization to GDP enables to conclude that FDI positively influence GDP through internationalization and not otherwise. The study therefore recommends improvement in the investment climate for foreign direct investment to enhance competitiveness and strengthen through internationalization. From table 4.2, it can then be concluded that there is a significant linear relationship between the foreign direct investment and financial performance on listed manufacturing companies in Nigeria since the correlation coefficient is ranging between 0.3 and +0.7 in line with Dancey and Reidy's (2004) categorization of strength of correlation coefficient.

Table 4.2: Correlation Results for Foreign Direct Investment and ROA

		ROA	FDI
ROA	Pearson Correlation	1	.628
	Sig. (2-tailed)		.000
	N	319	319
FDI	Pearson Correlation	.628	1
	Sig. (2-tailed)	.000	
	N	319	319

Regression Analysis: Univariate Regression Analysis between Foreign Direct Investment and Return on Assets

In order to establish the statistical significance of the independent variable (foreign direct investment) on the dependent variable (return on assets), regression analysis was carried out. The result of the regression analysis as presented in table 4.3 revealed that $R=0.628$ and $R^2=0.394$. This implies that 39% of the variation in financial performance can be explained by a unit change in foreign direct investment. The remaining 61% of the variation can be explained by other variables such as foreign trade, research and development and foreign funding.

Table 4.3 Model Summary for Foreign Direct Investment and ROA

R	R Square
.628 ^a	.394

a. Predictors: (Constant), Foreign Direct Investment

Furthermore, F-test was carried out to test the null hypothesis that there is no significant relationship between foreign direct investment and return on assets. The analysis of variance test in table 4.4 shows that the significance of the F-statistic 0.000 is less than the table value of 0.05 meaning that null hypothesis is rejected and can be concluded that there is a significant relationship between foreign direct investment and company's return on assets. It can also be concluded that the model $Y=0.5015+2.993X_1$ is significantly fit.

Table 4.4 ANOVA Results for Foreign Direct Investment versus ROA

	Sum Squares	of Df	Mean Square	F	Sig.
Regression	1264.842	1	1264.842	162.237	.000 ^b
Residual	2478.324	318	7.798		
Total	3743.162	319			

a. Dependent Variable: Return on Assets

b. Predictors: (Constant), Foreign Direct Investment

To test the significance of regression relationship between the foreign direct investment and return on assets, the regression coefficient (β) and the intercept (α), in the model were subjected to the t-test to test the null hypothesis that the beta is zero. The null hypothesis state that, β (beta) = 0, meaning there is no significant relationship between the foreign direct investment and financial performance as the slope β (beta) = 0 (no relationship between the two variables). The results on the beta coefficient of the resulting model in table 4.5 revealed that the constant $\alpha = 0.5015$ which is significantly different from 0, while the p- value = 0.000 which is less than 0.05. The coefficient $\beta = 2.993$ is also significantly different from 0 with a p-value=0.000 which is also less than 0.05 indicating that financial performance of listed manufacturing companies in Nigeria was significantly influenced by the foreign direct investment.

This implies that the null hypothesis $\beta_1=0$ is rejected and the alternative hypothesis $\beta_1 \neq 0$ is taken to hold implying that the model $Y=0.5015+2.993$ (Foreign Direct Investment) is significantly fit. The model Return on assets = $\alpha + \beta$ (Foreign Direct Investment) holds as suggested by the above test. This confirms that there is a significant positive linear relationship between the foreign direct investment and company's return on assets.

Table 4.5 Coefficient for Foreign Direct Investment and ROA

	Unstandardized Coefficients		Standardize d Coefficients Beta	T	Sig.
	B	Std. Error			
(Constant)	.5015	.322		1.558	.066
FDI	2.993	.187	.604	16.005	.000

a. Dependent Variable: return on assets

The results affirms those of Mawugnon and Qiang (2009) that investigates the effect of foreign direct investment on economic growth through internationalisation in Togo using time series data, the research found that there was a unidirectional relationship between FDI and GDP. The direction of causation ran from FDI through internationalisation to GDP enables to conclude that FDI positively influence GDP through internationalisation and not otherwise. The study therefore recommends improvement in the investment climate for foreign direct investment to enhance competitiveness and strengthen through internationalisation. It also contradicts that of Bütthe and Milner (2008) who examine the influence of Foreign Direct Investment on Per Capita GDP in Nigeria using Vector Error Correction. The result shows a negative relationship between FDI and economic growth in Nigeria. Similarly, Kolstad and Wiig (2012) investigate the impact of foreign direct investment (FDI) on Economic Growth in Nigeria within the period of 1986-

2011. The study employed multiple regression models to determine the impact of some external variables on the gross domestic product (GDP) proxy for economic growth in Nigeria. The study used time series data to ascertain the inflow of FDI to the Nigerian economy and its implications on economic growth. The finding revealed a positively impact on the economy though its contribution to GDP was very low within the period under review.

CONCLUSION AND RECOMMENDATION

The main objective of this study was to determine the effect of foreign direct investment on the financial performance of listed manufacturing companies in Nigeria. The study operationalized the foreign direct investment as the ratio of foreign assets to the total assets of the company. The study adopted the use of both descriptive and inferential statistics in ascertaining this relationship. The descriptive statistics adopted includes the mean, standard deviation, minimum, maximum and sum total while the inferential statistics includes correlation and regression analysis. The trend analysis was also carried out on all the variables in order to determine the behavior of those variables across the study period.

The descriptive results revealed that an average manufacturing company in Nigeria had about 10% of its assets contributed by the foreign investors with the least having foreign assets of 2% while the best was 22%. The standard deviation was about 3% indicating a moderate variation in foreign direct investment across different companies in the manufacturing sector. The correlation results on the other hand indicates that there existed a strong and significant association between foreign direct investment and financial performance ($r=0.628$, $p=0.000$). The results of ANOVA test showed that the F value is 162.237 with a significance of p value = 0.000 which is less than 0.05, meaning that null hypothesis is rejected and conclude that there is a relationship between foreign direct investment and financial performance of listed manufacturing companies in Nigeria. Furthermore, the coefficient $\beta = 2.993$ was also significantly different from 0 with a p-value=0.000 which is less than 0.05. The result implies that a unit change in foreign direct investment will result in 2.993 unit change in financial performance. This confirms that there is a significant positive linear relationship between foreign direct investment and financial performance of listed manufacturing companies in Nigeria.

The findings also revealed that the company with the highest percentage of foreign direct investment had about twenty two percent of its assets contributed by the foreign direct investors. Therefore, efforts should be made to make the investment environment attractive in order to attract more foreign direct investment into the listed manufacturing companies in Nigeria.

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