Foreign Direct Investment in The Sub-Saharan Africa: Unveiling The Pains and Gains of Domestic Firms

Abstract

This study aimed at unveiling the pains and gains of domestic firms towards Foreign Direct Investment (FDI) in the Sub-Saharan Africa (SSA). The objectives of the study were to ascertain the effect of inward FDI on DFs, and to establish gulfs between gains and pains of DFs in SSA relative to technology spillover, competition, environmental degradation and GVCs. The study used a systematic review. This enables the drawing of experience, ideas, and similar situations of others. Search strategy was incorporated to enable the searching of literature in database of reputable journals. It was discovered that the volume of FDI is high in SSA, and that it has greater positive effect on DFs. It was established that FDI presents gains as well as pains to DFs in SSA relative to technology spillover, competition, environmental degradation and GVCs. The study concluded that FDI is not totally inimical to DFs in SSA. Thus, the study suggested that government of various countries in SSA should revisit and review their policies, where necessary, to protect their infant firms or DFs, and should intervene in the drain experienced by DFs, and cushion the negative impact of technology spillover by providing capital support and enhancing strong institutional quality.

Keywords: Foreign Direct Investment, Technology Spillover, Competition, Environmental Degradation, Global Value Chains

Introduction

Today, the world has globalized its economy that countries have to worry less about deficits. Foreign direct investment (FDI) is at the core of globalization with nations have opportunities to transfer factors of production within regions and blocks. Pekarskiene and Susniene (2015) expressed that FDI and the operations of Multinational Corporations (MNEs) are thought to be the main broad routes for the expansion of the economic processes of globalization to nations with varied degrees of development. Foreign direct investment (FDI) into Africa increased to US$46 billion in 2018, up 11percent from the preceding year (United Nations Conference on Trade and Development [UNCTAD], 2019). The year 2020 was a challenging one for Africa. Following a decline brought on by the COVID-19 pandemic in the year 2020, the continent experienced a significant resurgence in FDI. The African nations saw the inflow of $83 billion FDI in 2021 (UNCTAD, 2022). One of the pivot activities of MNEs is inward investments in the Sub-Saharan Africa (SSA). Inward investments are inevitable because SSA has been unable to

participate in Global Value Chain (GVC) due to little foreign investment. Boly et al. (2015) posited that the largest source of inward investments is foreign capital invested by MNEs, either to increase their own footprint or to meet a specific demand of the domestic economy.

It is evident that MNEs have channeled their investment capital in domestic countries of SSA. Importantly, Domestic Firms (DFs) have adopted copy strategy in which the firms amass appropriate information, absorptive capability and technology spillover, and learn from partnership and inward investment of MNEs. Sequel to the presence of MNEs, Olayinka and Loykulnanta (2019) affirmed that DFs majorly benefit from technology spillover. Theoretically, it is believed that FDI will be crucial in aiding DFs to witness production externalities from technology spillovers (Abereijo & Ilori, 2012; Fajgelbaum et al., 2014; Lindblad, 2015). It should be highlighted that MNEs are not in the economic development game and have little interest in spreading their proprietary technologies, and that spillover effects rely on how well DFs can absorb new technologies (Dishon & Yabs, 2017).

Ample of literature has shown that FDI holds more benefits for developing countries, but it is certain that SSA has some challenges based on inward investment from MNEs. For instance, Chinese firms are presumed having ulterior motive based on the popular perception that China intends to capture Africa. Kaplinsky and Morris (2016) expressed that the China's impact on Africa has been a common issue which have often marched under the slogan "Whilst China has a strategy for Africa, Africa lacks a strategy for China." This signifies that FDI through Chinese firms is a false impression, and has more detriment than gains for SSA. American international oil & gas corporations are in SSA in their large number, tapping heavily from her natural resources which could have benefitted the DFs. Shell, Chevron and ExxonMobil are considerable examples of these MNEs that have consistently repatriated profit from Nigeria’s natural resources. These MNEs strongly rely on their business model (Li et al., 2022) without minding the possible negative consequences on DFs. Also, there is issue of Global Value Chains (GVCs) impeding on DFs in the agricultural and food sectors of the SSA nations. Agriculture and food trade has expanded overtime, with a growing reliance on international production networks to supply the food and clothing that we consume. Key determinants of GVC involvement and domestic value-chain generation include trade as well as investment policies. Agro-food GVC engagement can be favourably impacted by FDI (inward and outward).

This study is concerned with how DFs have gained from FDI in the SSA (region of the African continent that is located south of the Sahara Desert). It is certain that the operation of MNEs has some impediment for DFs in the SSA, but its benefits or gains are worth investigating. The study of Boly et al. (2015) found that FDI inflow serve as a significant catalyst for structural change in SSA. The objectives of the study were to:

i. ascertain the effect of inward FDI on DFs, and
ii. to establish gulfs between gains and pains of DFs in SSA relative to technology spillover, competition, environmental degradation and GVCs.

Literature Review

The expansion of global capital movements, particularly FDI, may be the greatest distinguishing aspect of the most contemporary globalization. Global capital flows are essential to the functioning of the world economy. According to Koepke (2018), they offer a variety of gains and concerns to host nations, and are closely correlated with financial and economic situations, and create significant policy concerns. The enormous amount of research on global capital flows reflects the significance of these movements for the world economy.

FDI reflects the investment interest of government, companies and investors of foreign countries in the business and economy of host nations. Also, it is an investment made by companies established in another nation that takes a controlling interest in a companies in another country. It also acts as a substantial development accelerator, and is essential to a free and effective global economic system. However, the benefits of FDI are not automatically and fairly dispersed among nations, industries, and local communities. National policies and the international investment architecture are crucial to attracting FDI to more developing countries and maximizing its benefits for development (Organisation for Economic Co-Operation and Development [OECD], 2002). The challenges largely affect the host countries, which must establish an open, inclusive, and supportive policy environment for investment and build the institutional and human resources required to put it into action (OECD, 2002).

Domestic FDI regulations include limitations on MNCs' ability to enter and operate in the market, access to the capital market, and FDI promotion initiatives like tax breaks and subsidized manufacturing inputs. Nations have gradually replaced FDI restrictions with FDI incentives over

the past two decades. The admittance and operations of MNCs are restricted by formalized FDI restrictions in a similar way to how capital controls, tariffs, or nontariff barriers do (Pandya, 2016). The admission and operations of foreign-owned companies are subject to some regulations. MNCs must create joint ventures with domestic companies that retain substantial ownership due to ownership restrictions. Operations and maintenance constraints include domestic content specifications, export quotas, and requirements for domestic representation on directorship boards (Pandya, 2016).

Growing numbers of nations in the SSA, rising economies, and transitioning nations now view FDI as a driver of revenue growth, employment, and economic modernization. To draw investment, nations have liberalized their FDI laws and adopted various measures. They have discussed how to implement domestic policies in a way that will maximize the advantages of having foreigners in the home economy. With an emphasis on the broad impact of FDI on macroeconomic growth and other welfare-enhancing processes as well as the pathways via which these advantages manifest, the research Foreign Direct Investment for Development aims to mainly shed some light on the second issue.

The overall benefits of FDI for developing country economies are well documented. Given the appropriate host-country policies and a basic level of development, a preponderance of studies shows that FDI triggers technology spillovers, assists human capital formation, contributes to international trade integration, helps create a more competitive business environment and enhances enterprise development. All of these contribute to higher economic growth, which is the most potent tool for alleviating poverty in SSA. Moreover, beyond the strictly economic benefits, FDI may help improve environmental and social conditions in the host country by, for example, transferring "cleaner" technologies and leading to more socially responsible corporate policies (Pandya, 2016).

The Gains of DFs from FDI

As earlier noted, Africa has become a home for many multinational corporation, and there has been consistent heavy FDI inflows for some decades now. Only 2% of all FDI stock was in Africa in 2009, and from 2009 to 2011, the region received an average net flow of 46 billions of

US dollars in FDI (Boly et al., 2015). Even if they are still small, the inflows are getting fewer and less clustered both regionally and sectorally as contrasted to former years. In reality, the five primary receiving nations amounted for almost 90% of overall inflows less than ten years ago, but in 2011 this number dropped to around 50% due to an increase in FDI directed towards non-extractive sectors like light services and manufacturing (Boly et al., 2015; UNCTAD, 2012). Table 1 shows that investment inflow has grown consistently in Africa since 2017. It dropped only in 2020. It is assumed that DFs would have gained from this investment inflow into Africa. Table 2 shows that gulfs exist with respect to inward FDI and its effects in the SSA. The table indicates that inward FDI is economically malign for SSA. It is seen that the benefits on FDI outweighs its demerits in many nations of SSA. However, the case of Uganda, Lesotho, Ghana, and Niger seems to be different as the negative effect of FDI outwits its positive effect (Boly et al., 2015). On a general note, the table 2 reveals that SSA's domestic firms derive 34.4% benefits as against 24.9% negative effect suffered by the firms in the host countries.

Table 1. Investment flows to Africa

Year	Inward ($)	Outward
2021	83 billion	-
2020	39,785 million	1,592 million
2019	47,143 million	4,930 million
2018	45,374 million	8,013 million
2017	40,176 million	11,779 million

Source: Kamer (2022)

Table 2. Effects of inward FDI on DFs by country in SSA

Country	Positive	Negative	No. effects	No. obs.
Burkina Faso	41.1	26.0	32.9	73
Burundi	35.5	27.3	37.2	121
Cameroon	37.6	27.8	34.6	133
Cape Verde	33.1	31.6	35.3	272
Ethiopia	27.4	20.2	52.4	431
Ghana	27.7	31.9	40.4	235
Kenya	25.9	19.3	54.7	316
Lesotho	7.8	39.2	52.9	102
Madagascar	50.0	20.6	29.4	102
Malawi	44.0	25.3	30.7	75
Mali	25.6	25.1	49.2 195	195
Mozambique	82.5	6.3	11.1	189
Niger	24.6	29.2	46.2	65

Nigeria	37.7	23.0	39.3	387
Rwanda	27.8	24.1	48.1	108
Senegal	42.8	23.0	34.2	152
Tanzania	32.4	24.7	42.8	299
Uganda	5.8	27.3	46.9	403
Zambia	47.3	33.5	19.2	203
Sub-Saharan Africa	34.4	24.9	40.7	3861

Source: Authors' elaboration on UNIDO Africa Investor Survey 2010

Technology Spillover and DFs in SSA

Technology spillover is malign for DFs with respect to information and data collection. "By technology spillovers, we mean (1) firms can collect the information generated by others without having to pay for it in a market transaction, and (2) the information's creators (or current owners) have no real legal remedy if other firms use the knowledge they have received in this way" (Grossman & Helpman, 1992, p.16). In cases where there is high mobility of labour, the movement of technical-know-how from MNEs to DFs becomes inevitable. Employees who have gained technical-know-how while working for MNEs may transfer that technology to DFs when they are hired by those firms. The behavior of foreign companies, such as their production processes and other business practices, can be used by DFs to acquire technology. Urata and Baek (2022) posited that these are known as horizontal spillover, and frequently occur when domestic and foreign firms are active in the same sector (linkage).

Naturally, concealing technology would have been the practice of MNEs in SSA. MNEs would not have invested in the development of technology expertise without special interest in human capital. Literarily, Osabutey and Jackson (2019) opined that it is anticipated that the presence of MNEs in emerging nations will be associated with the dissemination of managerial and technological expertise to DFs. Also, it is imperative to note that internalizing managerial and technological expertise would have become almost impossible for MNEs. This makes the externalization of advanced technology a common event to be expected in SSA.

DFs have the avenue to copy the technology that have been traced to huge success of MNEs. Researchers uncover evidence that many DFs in SSA "imitate" the foreign firms in their technology and strategic responses, primarily by creating identical products and utilizing similar marketing tactics or strategies (Boly et al., 2015). Technology spillover becomes beneficial to

DFs when the demonstration effect is substantially positive. Also, the presence of MNEs heightens the level of competition and drives DFs to upgrade their technology; leading to competitive impact. DFs in SSA become more productive today as a result of MNEs' technology spillover to them.

Competition and DFs in SSA

Many MNEs have found SSA as a potential market for massive production in mother country. From the implicit point of view, FDI inflow is driven by the motive to make SSA a dumping site. For example, the reasons for excess production in China is the utilization of available labour in their large number, and that Chinese MNEs have to crowd out the excess production from their country to strategically improve the economy of the mother country. Thus, Chinese MNEs have cheap factors of production and can afford to sell at competitive price in the SSA. This possibly culminate into price war for DFs. There is possibility that DFs heavily feel the drain due to issues around economies of scale.

DFs face unhealthy competition due to dumping and price war among others. However, competition between MNEs and DFs is imperative to drive in economic progress. In the case of Nigeria, the competition between MTN and GLO has made the telecommunication industry to witness consistent improvement. The competition between these firms was moderated by the Nigerian Communications Commission. Competition between MNEs and DFs is economically viable for countries.

It is uneconomically viable when MNEs nurture the intent to fizzle out DFs. MNEs incur marginal loss to create unhealthy competition for DFs. The MNEs have the economic capacity to sell below cost of production for a long time, and can incur marginal loss if their intent is to drive out DFs and gain monopoly. Although, it has not been empirically proven that MNEs transfer sophisticated technology to Africa to create unhealthy competition for DFs. According to a major research theme, new infrastructure technologies like the Internet and mobile phones are delivered within a regulatory framework that fosters market competition and encourages private capital (Amankwah-Amoah, 2014). The strategy behind the transfer of sophisticated technology by MNEs is that infant firms may not be able acquire the technology or copy technical-know-how based on limited economic or financial power, and there is no strict regulation to moderate the activities of MNEs in Africa. Maintaining Chinese companies' competitive edge in Africa does

not imply a need to shift technology and knowledge to indigenous partners (Osabutey & Jackson, 2019).

Environmental Degradation and FDI in SSA

The expansion of global capital movements, particularly FDI, may be the greatest distinguishing aspect of the most contemporary globalization. The popular expectation is that FDI will be instrumental to progressive economies of countries in the SSA. In addition to supplying much-needed financial resources, Dada and Akinlo (2021) posited that FDI also transfers vital technology and technical know-how which supports local investment by DFs. The irony may be that countries of the Saharan Africa are perceived a potential market for huge returns, and investments in these countries are not likely conceived with the original motive of supporting local investment by DFs.

It is no newer that the most pressing issues facing the globe today is the environmental problems. Environmental degradation has become quite severe and destructive in the Saharan Africa. This is due to the "avalanche" of developmental challenges, which also include unemployment, a decline in poverty, and an unsettling and turbulent political climate (Osabuohien et al., 2013). The impact of environmental degradation could have been minimal if MNEs are committed to Corporate Social Responsibility (CSR) in the SSA. Environmental degradation is associated with the basic fact that FDI has led to the increased production and the consumption of energy in the SSA. This is also explained by the Environmental Kuznets Curve (EKC) theory as one of the environmental degradation around the globe (Grossman & Krueger, 1993).

Some America firms have contributed to terrifying oil spillage on the reveries in the SSA. Over time, according to Iruoma (2020), oil exploration has had a detrimental effect on the physical environment of the towns that contain oil in Nigeria and has accelerated the rate of environmental degradation. Osabuohien et al. (2013) argued that there is little empirical proof that MNEs have a negative impact on environmental degradation in the SSA. Some DFs get their supplies from domestic source, particularly from the agricultural sector, but evidence abound that construction and oil multinationals have caused so much benign to the agricultural sector in the SSA. This is true because the external intrusion of MNCs have caused environmental degradation; leading to poor host communities' water quality and availability of arable land.

Global Value Chains and DFs in SSA

Global Value Chains (GVCs) have been a subject of importance in previous researches (Costinot et al., 2013; Del Prete & Rungi, 2017). GVCs, in which the various phases of the manufacturing process are distributed across many nations, are the policy framework within which trade, investment, and international production are progressively organized. Lately, trade policies' implications on the development of GVCs have been theorized and practically examined (Gereffi et al., 2021; Ruta, 2017). However, value chain issues are topical in the discussions of international trade agreements like Trans-Pacific Partnership (TPP), the African Continental Free Trade Area (AfCFTA), and the North American Free Trade Agreement (NAFTA), which raise the threat of protectionism to its highest level (Balié et al., 2018).

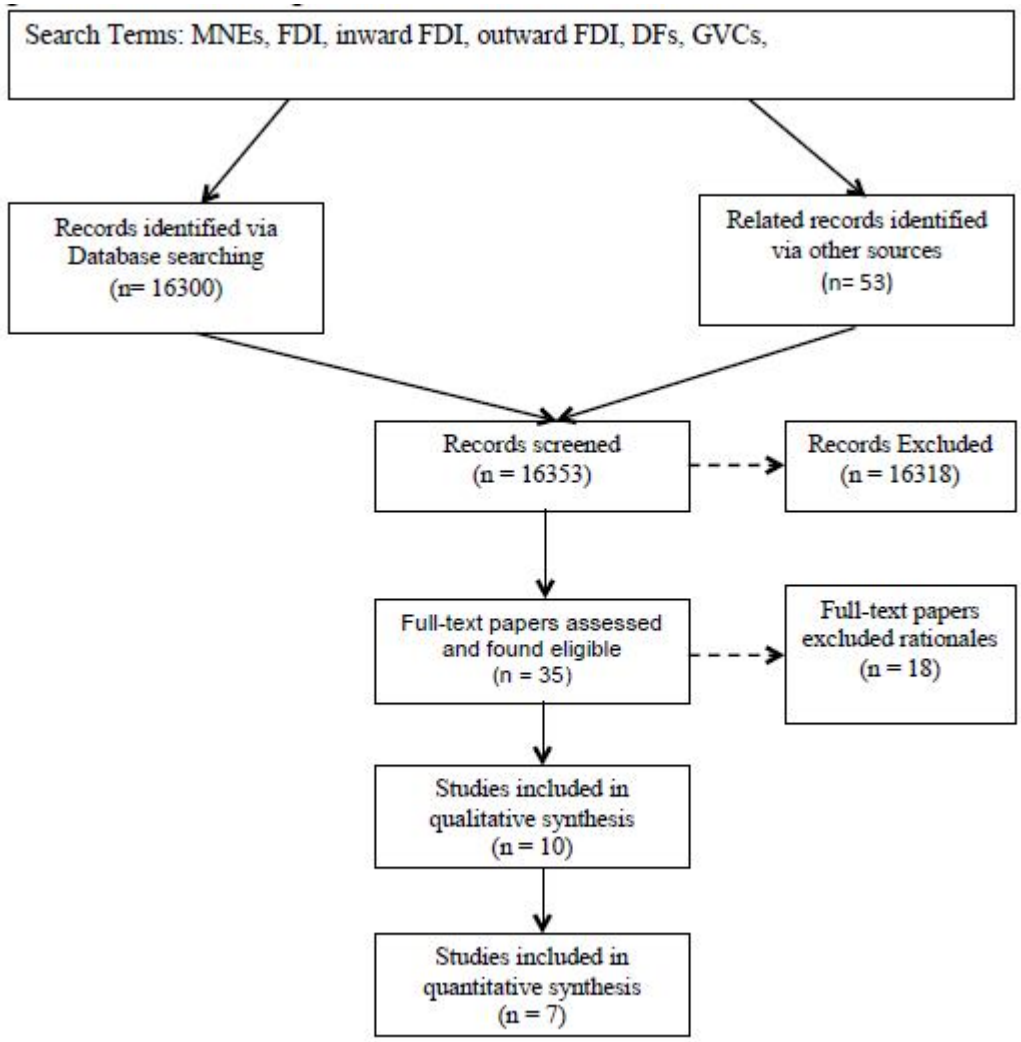
Countries in the SSA region may be questioned with respect to involvement in GVCs. According to Aggarwal (2010), only market forces cannot ensure a successful integration of DFs in the GVC. Evidence from Dollar, Ge, and Yu (2016) suggests that membership in the GVC is influenced by institutional quality. The institutional quality of SSA countries appears very low for holistic participation in GVC. The paper assesses institutional quality according to development level in African countries and concludes that weak institutions, as evaluated by the World Bank's Rule of Law index, are a problem in African countries. This helps to explain Africa's comparatively low involvement in GVCs. Instead, African countries are accustomed with extra-regional trade. SSA trails other parts of the world in terms of joining GVCs. Importantly, the percentage of foreign value-added (FVA) in SSA nations' exports is one sign of how well its economy has integrated into the world market (Copley, 2017). These nations have FVA below average (50%) among developing nations of the world

Research Method

Ample scholarly literature is available on the subject “FDI and DFs”. The study used a systematic review to acquire a thorough understanding of the topic and support relevant facts. The best strategy to draw from experience, ideas, and similar situations of others to the current study issue is to review pertinent and academic literature. The approach's fundamental goal is to make it easier to attain the research objectives. Search strategy was incorporated to enable the searching of literature in database of reputable journals. Comprehensive search was employed using google scholar, sciencedirect, sage and *Web of Science* (Arts and Humanities Citation

Index and Social Sciences Citation Index). A different technique used was forward/backward searching, which requires citing sources in publications. To ensure all pertinent qualitative research had been found, manual searches of the most pertinent journals (on FDI) and reference lists were carried out. Figure 1 shows the flow chart of the number of studies reviewed.

Figure 1: Prisma Flow-diagram of Relevant Literature Searched



Conclusion and Suggestions

There is more inward inflow of FDI compared to its outward flows in SSA. FDI is not totally inimical to DFs in SSA. Evidences have shown that the positive effects of FDI are substantial to many countries of SSA. Countries like Uganda, Lesotho, Ghana, and Niger have suffered

negative consequences of inward FDI, and/or no significant effect at all. This may be subject to poor policy framework or institutional quality.

Technology is physical and it involves technology transfer. Inward FDI has been appreciated for technology transfer which has in turn revolutionized the operations of DFs. The drain must be management by governments in the SSA to avoid unhealthy practices by MNEs. These practices may be underlined by the intent to monopolize the market. There is probably unimaginable motive of technology spillover by MNEs, but in most cases technical know-how and crucial information are concealed. The cost of acquiring advanced technology is also a considerable factor that are posing threat to infant firms due to limited scope. DFs gain from technical-know-how by attracting employees from MNEs. Technology spillover has advantage to DFs when the demonstration effect is substantially positive.

Countries in the SSA have a poor institutional quality. The poor institutional quality is also traceable to the inability of DFs to participate in GVCs. Competition could have been instrumental to the economic growth under ideal situation. Some MNEs are powerful that they have been strategic to leadership choices in SSA. This may be linked to the annulment of ideal business conditions for MNEs in SSA. Many MNEs repatriate profit and capital easily based on their political influence, and have been uninterruptedly permitted to utilize local natural resources for their production. In fact, some MNEs may be blamed for production using the available local natural resources and repatriating the outputs to home country. Government policy on competition is instrumental to the protection of DFs. Unhealthy competition can often rule out infant firms. MNEs are giants that engineer cut-throat competition. The expansion of global capital movements can be linked to the observed environmental degradation in SSA. Increasing transfer of technology by MNEs coupled with their operation has made environment very hampered. DFs in the Agricultural industry have suffered from the emission of carbon and oil spill majorly in the rural settlements. In SSA, environmental degradation has gotten pretty bad and destructive. Thus, the study suggests that:

i. Government of various countries in SSA should revisit and review their policies, where necessary, to protect their infant or DFs. The policies should incorporate production subsidy, tax incentive via tax holidays and strict regulation on the excessiveness of MNEs in SSA.

ii. Governments in SSA should intervene in the drain experienced by DFs, and cushion the negative impact of technology spillover by providing capital support and enhancing strong institutional quality. This will enable DFs to take part in the GVCs.

iii. The likelihood that DFs will holistically benefit from FDI is low. Thus, DFs' strategic reactions to FDI should be spurred by strategic thinking and action research on the ways to make substantial contribution to the economic growth and favourably compete with MNEs.

iv. Governments in SSA should wake up to the reality that MNEs will always repatriate both profit and capitals, and as such should come up with unbeatable regulations that can commit the MNEs to full environmental development. This will have positive implication on the operations of DFs, particularly those in the agricultural industry.

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