**Original Article**

# Impact of Private Foreign Investment on Economic Growth: A Study of Nigeria (1999-2021)

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DOI: https://doi.org/10.5281/zenodo.13789010

To facilitate economic growth, there must be an adequate level of savings and investments, and one avenue to improve the level of savings and investments is to attract private foreign capital. Therefore, this study assessed the effect of private foreign capital on economic growth in Nigeria from 1999-2021. The study proposed a model of economic growth using private foreign capital variables such as foreign direct investment (FDI), foreign portfolio investment (FPI), and remittances as predictors. The data were subjected to unit root tests and were found to be stationary in mixed order at levels and first difference justifying the choice of the Autoregressive Distributed Lag approach for data analyses. The result of the ARDL test revealed that FDI is significant and positively influences economic growth ($\beta = 2.84$, $p<0.05$). Likewise, remittances are significant but have a negative contribution to economic growth ($\beta = -0.71$ , $p<0.05$). FPI was found to not affect economic growth in Nigeria ($\beta = 0.02$, ns) in the longrun. Also, the estimated coefficients of the shortrun relationship for the model revealed that FDI and remittances are significant in impacting economic growth with FDI contributing positively ($\beta = 2.70$, $p<0.05$) and remittances contributing negatively ($\beta = -0.68$ , $p<0.05$). FPI still failed to influence economic growth in Nigeria ($\beta = -0.33$ , ns). Therefore, the study concludes that foreign direct investment and remittances are significant predictors of economic growth. The study recommended that a stable and predictable policy environment needs to be in place to build foreign investors' confidence.

**Keywords**: economic growth; foreign direct investment; foreign portfolio investment; remittances.
**JEL:** F21, F24, O40

## 1. INTRODUCTION

Economic growth in developing countries has been constrained by the inadequacy of savings and investments (Oyegoke & Aras, 2021), and one way of easing the constraints of the low level of domestic savings and investment is to attract inflows of private foreign capital (Adjei et al., 2020; Obadan, 2004). Like many other developing economies, Nigeria has long been seeking avenues for sustainable economic growth and development. In this quest, foreign capital, especially from private sources, has played a key role. Private foreign capital inflows

(PFC), which are transmitted through foreign direct investment (FDI), portfolio investment, and remittances (Obadan, 2004), constitute a crucial channel through which resources are transferred from wealthy-developed countries to poor-underdeveloped countries (Sugozu et al., 2023). According to Albulescu (2015), private foreign capital, helps to broaden and deepen the financial markets, increase liquidity, and facilitate the transfer of technology and management expertise. It can also significantly contribute to infrastructure development. Investments in sectors like energy, transportation, and telecommunication can enhance productivity, reduce costs, and improve overall economic efficiency.

Moreover, private foreign capital encourages the development of new job possibilities and accelerates economic expansion (Nguyen, 2022). Researchers and policymakers in developing economies have focused on the need to attract foreign capital, taking into account the significance of foreign capital inflows in the economic growth framework. For instance, to draw in international investment, Nigeria has launched several policies and initiatives over the years. These initiatives include the 1986 Structural Adjustment Program, the 1995 Nigerian Investment Promotion Commission aimed at improving the nation's investment environment, and the 2004 and 2009 financial sector reforms to promote private-led growth and maintain macroeconomic stability.

Despite the numerous policies and reforms, the growth trajectory is not spearheaded by the rate of private foreign capital inflows; instead, it lags. Also, the volume of private foreign capital inflows consistently falls short of the resource gap. Also, the influx of private foreign capital poses some challenges. These include the risk of capital flight during economic downturns, concerns about the exploitation of natural resources, and the possibility of increasing income inequality. These concerns have elicited interest in whether foreign capital inflows complement domestic savings and investment to stimulate growth in the real sense.

Empirically, there are mixed research findings on the role of private foreign capital in the economic growth process. Some authors (Oyegoke & Aras, 2021; Adjei et al., 2020; Lyndon & Ayaundu, 2020; Onyike et al., 2020; Otapo & Adekunle, 2020; Ezeanyeji & Ifeako, 2019; Iriobe et al., 2018) in their studies noted a positive relationship between private foreign capital and economic growth in Nigeria. In contrast, other schools of thought (Ndugbu et al., 2021; Anetor, 2019; Aisien, 2018) in their various studies noted a negative relationship between private foreign capital variables and economic growth in Nigeria.

The question then is do private foreign capital inflows complement domestic savings and investments and boost economic growth? The study answered this question by proposing a model of economic growth using private foreign capital variables such as foreign direct investment, foreign portfolio investment, and remittances as predictors using more recent data spanning 19992021.

## 2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

### Private Foreign Capital

Because of the mismatch between their capital requirements and saving capacity, domestic private investment has proven to be insufficient in the majority of economies to give the economy the necessary boost to enable it to fulfill its growth target. Therefore, private foreign money complements local resources to help the nation carry out its development programs and increase the living standards of its citizens (Nwakoby & Alajekwu, 2016). Private foreign capital is made up of Foreign Direct Investment (FDI), Foreign Portfolio Investment (FPI), and Remittances. Foreign Direct Investment involves the investment of foreign capital directly into the economy of Nigeria, typically in the form of long-term investments by multinational corporations. FDI brings with it not only financial resources but also technology transfer, managerial expertise, and access to global markets. Foreign Portfolio Investment involves the purchase of financial assets such as stocks and bonds in Nigeria by foreign investors. These investments can be more volatile and short-term compared to FDI but still contribute to capital inflows and liquidity in the financial markets. Remittances are transfers from international migrants to family members in their country of origin. It represents one of the sources of financial flows to developing countries. Remittances are different from other external capital inflow like foreign direct investment, foreign loans and aid due to their stable nature.

**Foreign Direct Investment and economic growth**

In most developing countries, Foreign Direct Investment (FDI) serves as a means of earning foreign reserves via investments, businesses, and foreign aid from advanced countries. FDI is considered a valuable source of finance and capital formation, technology transfer, and know-how, as well as a viable medium for trade among countries. The Spillover effect also allows for the transfer of innovations and inventions to the receiving countries, one of which Nigeria belongs. The requirement for accelerated growth in association with the Sustainable Development Goals is not completely clear, however, for economies to experience sustainable and inclusive development, cross-border trade is paramount (UNCTAD, 2019). Traditionally, FDI is designed to improve the recipient economies thereby enhancing economic growth and development, it is in this view that many developing countries attract foreign investors with the hope of strengthening their economy by increasing the foreign investment portfolio. However, most empirical analysis of the impact of FDI on economic growth advises otherwise, hence, a controversy.

Empirically foreign direct investment contributes significantly to the economic growth of countries where such capital flows. According to Oyegoke and Aras (2021), the developmental goal of foreign investment in developing countries is evident in Nigeria due to the improvement in the ease of doing business. In their study of the impact of FDI inflows on economic growth in Nigeria from 1970-2020, they established that FDI has a significant positive impact on the economy. Nguyen (2022) studied ASEAN-6 countries from 2002- 2019 using the threshold effect and system GMM, the results revealed a positive impact of FDI on economic growth in the region.

Similarly, Lyndon and Ayaundu (2020) examined the effect of foreign investment inflows on the economic growth of Nigeria, using multiple regression analysis techniques. The results of the analysis revealed that foreign direct investment has a significant positive influence on gross domestic product. On the other hand, Carbonell and Werner (2018) carried out a study on whether foreign direct investment generates economic growth? The study covered a period of 1984-2010 for Spain, the empirical findings suggested that foreign direct investment could not stimulate economic growth. Likewise, Anthony-Orji et al. (2018) in their study of the impact of stock market development and foreign private investment on economic growth in Nigeria found FDI to be of no effect on economic growth.

Therefore, FDI is perceived to accelerate economic growth but the magnitude and extent of its contributions still need further assessment. Moreover, the FDI inflows to Nigeria seem to be on a downward trend. For instance, the FDI growth rate was 15.33% in 2002 but declined to 3.65% in 2021 (World Bank, 2022). To investigate this phenomenon and the inconsistent research findings, this study proposes the following hypothesis:

*$H_1$: Foreign direct investment (FDI) contributes significantly to economic growth in Nigeria.* **Foreign Portfolio Investment and economic growth**

Foreign Portfolio Investment (FPI) describes the investment in financial assets, such as stocks and bonds, in a country by foreign investors. Unlike Foreign Direct Investment (FDI), which involves acquiring a significant ownership stake in a foreign company, FPI is more about Purchasing financial instruments in the open market. It helps to increase liquidity and ensure access to capital. The main distinguishing feature between FDI and foreign portfolio investment (FPI) is that FPI is the term used to describe short-term investment in shares and bonds in a host country and most of the time this is speculative in nature. Another important distinctive feature of FPI is the lack of control of the affiliate firm, because of which it is often categorized as an indirect investment (Jones & Wren, 2016).

Research findings on the relationship between FPI and economic growth produced mixed conclusions. For instance, Iriobe et al. (2018) found FPI to have a significant positive influence on the Nigerian stock market and in turn stimulate economic growth. Similarly, Ezeanyeji and Ifeako (2019) found a positive impact of FPI on economic growth in Nigeria. Another study by Otapo and Adekunle (2020) established a positive and significant impact of FPI on economic growth in Nigeria. the study argued that FPI determines long-term trends in GDP formation in Nigeria. Also, Acha and Essien (2018) established that FPI has a positive effect on GDP in Nigeria. Conversely, Onyeisi et al. (2016) implemented Granger causality test and found no causality between FDI and stock market growth in Nigeria. This implies that the contribution of FPI to stock market growth is doubtful and as such may fail to stimulate economic growth. Likewise, Ndugbu et al. (2021) studied the relationship between FPI and economic growth in Nigeria from 1986 to 2017. The study implemented VECM and Granger causality and revealed that FPI does not affect economic growth in Nigeria.

In other climes, Albulescu (2015) implemented GMM for a sample of 13 Central and Eastern European countries and found portfolio investment to influence economic growth. Ahmad et al. (2015) reported a significant relationship existing between FPI and economic growth in ASEAN5 countries after implementing Granger causality and M-Wald test. Also, Sugozu et al. (2023) interrogated the link between portfolio investment and economic growth in 18 developed and 27 developing countries. The study found portfolio investment to be positively associated with economic growth in developing countries.

Given the role of FPI in the economic growth framework and the mixed research findings, this study proposed the following hypothesis:

*$H_2$: Foreign portfolio investment stimulates economic growth in Nigeria.*

**Remittances and economic growth**

Remittances remained an important source of external financing for developing countries (Ratha, 2012). It is more stable than any other form of foreign capital. As an important source of capital, remittances can support the economic growth of the receiving countries. Information on the potential development effects of remittances is of large interest and might be especially useful for policymakers who should devise appropriate policies for transposing the economic potential of these financial resources into real economic growth. Even if remittances are not invested, remittance-based consumption can also trigger economic growth via bigger employment and production (Meyer & Shera, 2017). It is important to note that despite the perceived benefits of remittances, increased demand due to remittances may sometimes produce negative macroeconomic effects, such as inflation. Exploring the relationship between remittances and economic growth has revealed mixed conclusions. For instance, Peprah et al. (2019) examined the linkages between financial development, remittances, and economic growth in Ghana. The study implemented a dynamic heterogenous Autoregressive Distributed Lag (ARDL) model and found remittances to be significant and positive in influencing economic growth. Similarly, Bucevska (2022) empirically examined the relevance of remittances as a factor of economic growth for South-East European countries and found a significant positive impact of remittances on economic growth. Also, Goschin (2014) established a positive influence of remittances on both absolute and relative GDP growth in Central and Eastern Europe. Meyer and Shera (2017) believe that countries considered to have high remittances tend to have high growth potential as a consequence of the inflows of remittances. Contrary, Sutradhar (2020) assessed the impact of workers' remittances on the economic growth of four South Asian emerging countries by employing pooled OLS. The result confirmed a significant negative effect of remittances on economic growth. Specifically, a significant negative effect was established for Bangladesh, Pakistan, and Sri Lanka.

For Nigeria, research findings seem to be inconsistent too. Anetor (2019) implemented ARDL to assess the relationship between remittances, financial sector development, and economic growth in Nigeria. The study established a significant negative effect of remittances on economic growth. Whereas, Adjei et al. (2020) investigated the relationship between remittances and economic growth in West Africa and found a significant positive impact of remittances on economic growth for Burkina-Faso, Ghana, Guinea, Guinea-Bissau, Mali, and Nigeria. Similarly, Onyike et al. (2020) found remittances to have a significant positive effect on economic growth in Nigeria.

The role of remittances in the economic growth framework cannot be overemphasized, especially since it is an important source of capital needed to support the economic growth of the receiving countries. Thus, given the relevance of remittances and the inconsistencies of research outcomes on the role of remittances, this study proposes the following hypothesis:

*$H_3$: Remittance plays a significant role in the economic growth process in Nigeria.*

## 3. METHODOLOGY

The ex-post facto research design is used for this study and data for this research were collected from the World Bank database. The study adopted the ARDL model for data analyses and stated as follows:

GDP= $f$ (FDI, FPI, REM) ……...……………………………………(1)

Where:

GDP = Gross Domestic Product; FDI = Foreign Direct Investment; FPI = Foreign Portfolio Investment; REM = Remittances.

Incorporating the ARDL model, thus, the model for this study is restated as follows:

$$\Delta GDPy = \emptyset 0 + \theta 1 \sum pj{=}1\ \Delta GDPt{-}j + \theta 2 \sum qj{=}1\ \Delta FDIj +$$
$$\theta 3 \sum qj{=}1\ \Delta FPIj + \theta 4 \sum qj{=}1\ \Delta REMj + \gamma 0 GDPt{-}j + \gamma 2 FDIj + \gamma 3 FPIj + \gamma 4 REMj + ECT{=}1 + \varepsilon t \qquad (2)$$

## 4. RESULTS AND DISCUSSIONS

### Descriptive Statistics

The model of this study used three variables (foreign direct investment growth rate, foreign portfolio investment growth rate, and remittances growth rate) as predictors to test three hypotheses raised in the study against a dependent variable (economic growth). Table I below gives the results of the descriptive statistics/analysis of the variables employed for this study.

**Table I: Descriptive Statistics**

| | GDP | FDI | FPI | REM |
|---|---|---|---|---|
| Mean | 5.325652 | 1.470000 | 3.418696 | 4.305217 |
| Median | 5.920000 | 1.630000 | 3.090000 | 4.410000 |
| Maximum | 15.33000 | 2.900000 | 8.690000 | 8.330000 |
| Minimum | 0.580000 | 0.180000 | 1.030000 | 1.010000 |
| Std. Dev. | 3.333466 | 0.766912 | 2.167775 | 1.982370 |
| Skewness | 0.916063 | 0.137245 | 0.992430 | -0.048286 |
| Kurtosis | 4.598636 | 2.056319 | 3.060473 | 2.241459 |
| Jarque-Bera | 5.665980 | 0.925634 | 3.779022 | 0.560348 |
| Probability | 0.058837 | 0.629508 | 0.151146 | 0.755652 |
| Sum | 122.4900 | 33.81000 | 78.63000 | 99.02000 |
| Sum Sq. Dev. | 244.4640 | 12.93940 | 103.3835 | 86.45537 |
| Observations | 23 | 23 | 23 | 23 |

**Source**: Author's Eviews output, 2023.

Table I above shows the mean, median, minimum, and maximum values of each data. The mean GDP growth rate is 5.325652, the FDI growth rate is 1.470000, the FPI growth rate is 3.418696, and the REM growth rate is 4.305217. The median value of the GDP growth rate is 5.920000, the FDI growth rate is 1.630000, the FPI growth is 3.090000, and the REM growth rate is 4.410000. The maximum value of the GDP growth rate is 15.33000, the FDI growth rate is 2.900000, the FPI growth rate is 8.690000, and the REM growth rate is 8.330000, while the minimum value of the GDP growth rate is 0.580000, the FDI growth rate is 0.180000, the FPI growth rate is 1.030000 and the REM growth rate is 1.010000.

**Stationarity Test**

A unit root test was performed to ascertain the order of integration of the variables. The test revealed a mixed order of integration with GDP and FPI stationary at levels, while FDI and REM are stationary at first difference. This informed the choice of the Autoregressive Distributed Lag (ARDL) technique for analysis.

**Table II: Summary of Unit Root Test**

| Variable | ADF | P.value | Order of integration |
|---|---|---|---|
| GDP | -4.496752 | 0.0089 | I(0) |
| FDI | -7.451331 | 0.0000 | I(1) |
| FPI | -4.447347 | 0.0022 | I(0) |
| REM | 4.452960 | 0.0023 | I(1) |

**Source**: Author's Eviews output, 2023.

**ARDL Bounds Test and Estimates**

The ARDL bound test indicates that there is a co-integrating relationship between the variables because the F-statistic value (7.907456) is greater than the lower (3.23) and the upper (4.35) bound values which confirms a long-run relationship.

**Table III: ARDL Estimates**

| | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|
| **Long-run Estimates** | | | | |
| FDI | 2.834195 | 0.611660 | 4.633611 | 0.0003 |
| FPI | 0.019561 | 0.369828 | 0.052893 | 0.9585 |
| REM | -0.713586 | 0.250492 | -2.848734 | 0.0116 |
| C | 4.550837 | 1.611300 | 2.824326 | 0.0122 |
| **Short-run Estimates** | | | | |
| D(FDI) | 2.701124 | 0.855443 | 3.157574 | 0.0061 |
| D(FPI) | -0.332735 | 0.229276 | -1.451241 | 0.1660 |
| D(REM) | -0.680082 | 0.242207 | -2.807854 | 0.0126 |
| CointEq(-1) | -0.953048 | 0.203448 | -4.684490 | 0.0002 |

**Source**: Author's Eviews output, 2023.

We implemented the ARDL strategy to ascertain the effect of private foreign capital on economic growth in Nigeria. The long-run and short-run estimates are presented in Table III. The estimated coefficients of the long-run show that the FDI is significant and positively influences economic growth ($\beta = 2.84$, $p<0.05$). In the same vein, remittances are significant but have a negative contribution to economic growth ($\beta = -0.71$, $p<0.05$). FPI was found to not affect economic growth in Nigeria ($\beta = 0.02$, *ns*).

The short-run coefficient estimates show the dynamic adjustment of all variables. The estimated coefficients of the short-run relationship for the model revealed that they are all significant except for FPI. This indicates that FDI and remittances are significant in impacting economic growth with

FDI contributing positively ($\beta = 2.70$, $p<0.05$) and remittances contributing negatively ($\beta = -0.68$, $p<0.05$). FPI still failed to influence economic growth in Nigeria ($\beta = -0.33$, *ns*). The estimates of the error correction term (cointEq) measure the speed of adjustment whereby short-run dynamics converge to the long-run equilibrium path in the models. The coefficient of error correction term CointEq(-1) for the model is negative and significant at a 5% level indicating that gross domestic product, foreign direct investment, foreign portfolio investment, and remittances are cointegrated. The coefficient indicates that about 95.31 percent of the disequilibrium in the gross domestic product is corrected by the short-run adjustment in the same year.

**Diagnostic Test**

LM test for Serial Correlation test was performed to check for serial correlations and the Breusch-

Pagan-Godfrey Heteroskedasticity test was also performed to address the issue of heteroskedasticity. The results presented in Table IV and Table V respectively confirmed the absence of serial correlations and heteroskedasticity.

**Table IV: LM Test for Serial Correlation**

| | | | |
|---|---|---|---|
| F-statistic | 3.448267 | Prob. F(1,15) | 0.0831 |
| Obs*R-squared | 4.112141 | Prob. Chi-Square(1) | 0.0626 |

**Source**: Author's Eviews output, 2023.

**Table V: Heteroskedasticity Test: Breusch-Pagan-Godfrey**

| | | | |
|---|---|---|---|
| F-statistic | 1.874728 | Prob. F(5,16) | 0.1551 |
| Obs*R-squared | 8.127334 | Prob. Chi-Square(5) | 0.1494 |
| Scaled explained SS | 2.416699 | Prob. Chi-Square(5) | 0.7890 |

**Source**: Author's Eviews output, 2023.

**Test of Hypothesis**

From findings of this study the proposed *$H_1$: Foreign direct investment (FDI) contributes significantly to economic growth in Nigeria* is confirmed. Thus, foreign direct investment is an important factor in the economic growth process in Nigeria.

The findings of this study repudiate *$H_2$: Foreign portfolio investment stimulates economic growth in Nigeria*. The findings suggested that foreign portfolio investment does not affect economic growth in Nigeria.

Finally, the third hypothesis raised in this study *$H_3$: Remittance plays a significant role in the economic growth process in Nigeria* is confirmed. This means that remittances are significant in the economic growth framework in Nigeria. However, remittances are reported to hurt economic growth rather than benefit economic growth.

**Discussion of Findings**

This study implemented the ARDL strategy to find out if private foreign capital significantly influences economic growth in Nigeria. The study found foreign direct investment to significantly influence the economic growth process despite its declining growth rate. This perhaps might be due to the size of the Nigerian domestic market (Africa's most populous country). Also, Nigeria has Africa's highest GDP, important hydrocarbon resources, and high agricultural potential. The Nigerian Government's policy of economic liberalization, promoting public-private partnerships, and strategic alliances with foreign companies could also have led to this positive outcome. These findings mirrored the outcome of Oyegoke and Aras (2021) who in their work established a significant positive effect of FDI on economic growth in Nigeria. However, the finding of this study is at variance with the works of Anthony-Orji et al. (2018) who concluded that FDI does not affect economic growth.

Also, the study found that foreign portfolio investment does not influence economic growth in Nigeria. Perhaps the short-term nature of foreign portfolio investments which makes them highly volatile might have contributed to the lack of influence. That is, if the majority of investments are speculative or driven by short-term profit motives, they may not contribute to long-term economic growth. Also, portfolio investments in financial markets might not be directly linked to real economic activities. For example, investments in stocks or bonds may not translate into increased production, job creation, or other indicators of economic development. Another reason for the negative outcome could be the lack of well-developed which are subject to distortions. This will make the positive effects of portfolio investment to be limited. For instance, if the stock market is not reflective of the real economy, gains in the market may not translate to broader economic benefits.

Another factor responsible for the lack of impact might be dependency on global conditions. The performance of portfolio investments can be heavily dependent on global economic conditions. External shocks or changes in international investor sentiment can lead to rapid capital outflows, impacting the stability of the domestic economy. This study agrees with Ndugbu et al. (2021) who studied the relationship between FPI and economic growth in Nigeria from 1986 to 2017 and found that FPI does not affect economic growth in Nigeria.

Remittances, on the other hand, were found to be significant in affecting economic growth in Nigeria, however, the effect is negative. This outcome presented an interesting position and seems to contradict expectations since remittances would be expected to have a positive effect on economic growth. This outcome echoes the work of Anetor (2019) who argued that a large portion of remittances are used for consumption purposes rather than savings and investment, therefore, remittances would negatively influence economic growth. Also, remittances might negatively affect economic growth when it is invested in non-productive assets such as real estate or luxury items rather than being channeled into productive investments that contribute to economic development. The minimal level or lack of financial inclusion in some cases, could hinder the efficient integration of remittances into the formal financial system. This can limit their potential to contribute to economic growth, as funds may not be channeled into productive investments. The volatility of remittance flows can also be a concern. If remittances are inconsistent or unpredictable, it can make it challenging for households and businesses to plan for the future, potentially leading to economic instability.

## 5. CONCLUSION AND RECOMMENDATIONS

The study examined the effect of private foreign capital on economic growth in Nigeria from 1999 to 2021. Three hypotheses were developed for the study with the dependent variable measured by gross domestic product while the independent variables were measured by foreign direct investment, foreign portfolio investment, and remittances, employing the ARDL regression model for analysis; the study found that:

i. Foreign direct investment has a significant and positive impact on gross domestic product in Nigeria in the long run. ii. Foreign portfolio investment has no significant impact on gross domestic product in Nigeria in the long run.

iii. Remittances have a significant and negative impact on gross domestic product in Nigeria in the long run.

Therefore, the study concludes that foreign direct investment and remittances are significant predictors of economic growth. The study also revealed that there is a long-run relationship between the dependent variable and the independent variables. Therefore, the study established that the impact of private foreign capital on economic growth is only significant with foreign direct investment and remittances.

Based on the findings and the conclusion of this study it is recommended that a stable and predictable policy environment needs to be in place to build investor confidence. Frequent policy changes can deter foreign investors. Also, there is a need to implement reforms to simplify and streamline business regulations. Reducing bureaucratic hurdles and improving the ease of doing business can attract foreign investors.

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