

**ASSESSMENT OF THE IMPACT OF FOREIGN DIRECT
INVESTMENT ON ECONOMIC GROWTH IN TANZANIA**

**ASSESSMENT OF THE IMPACT OF FOREIGN DIRECT
INVESTMENT ON ECONOMIC GROWTH IN TANZANIA**

By

Winnie Emmanuel Moshi

**A Dissertation proposal Submitted in Partial Fulfilment of the Requirements
for the Award of the Degree of Master of Science in Accounting and Finance
(MSc-A&F) of Mzumbe University**

2015

CERTIFICATION

We, the undersigned, certify that we have read and hereby recommend for acceptance by the Mzumbe University, a dissertation/thesis entitled **Assessment of the Impact of Foreign Direct Investment on Economic Growth in Tanzania**, in partial/fulfilment of the requirements for award of the degree of Master of Science in Accounting and Finance of Mzumbe University, Tanzania.

Major Supervisor

Internal Examiner

External Examiner

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DEDICATION

The dissertation is dedicated to my parents Mr and Mrs E.Moshi, My son Elijah, and My brother Gilliad Moshi and his family, for their love, support, prayers and encouragement to persure further studies.

LIST ABBREVIATIONS

| | | |
|--------|---|--|
| B.O.T | - | Bank of Tanzania |
| FDI | - | Foreign Direct Investments |
| GDP | - | Growth Domestic Products |
| TIC | - | Tanzania Investment Center |
| UNCTAD | - | United Nations Conference on Trade and Development |

ABSTRACT

The main objective of the study was to explore the impact of Foreign Direct Investment on economic growth of Tanzania. Specifically the study was intended to ascertain the extent at which FDI inflows in Mining and Quarrying sector, manufacturing sector and Agriculture and Livestock sector influence economic growth in Tanzania. The significance of the study was built upon the need to understand if the sector matters in FDI impacts concerns. The study was to add value in the available contradicting empirical findings of the same. Time series data from 1998 to 2013 were used in multiple linear regression using the ordinary least square (OLS) method.

The findings show that Foreign Direct Investment in the studied sectors of Mining and Quarrying has a positive significant impact on economic growth while Manufacturing and Agricultural sector have positive but insignificant impact on Economic growth of Tanzania. Unlike the manufacturing sector, a comparatively lesser FDI inflow in the Agricultural sector could be the reason for insignificant effect.

The implication is that for the hosting country to benefit from FDI the hosting country needs to have FDI-specific policies. Such a policy would state clearly about the contract both parties are about to enter in consideration of issues like the types of FDIs to be attracted, how to attract including reasonable incentives, what the country should gain in terms of added value for each specific FDI that is attracted and how to sustain the potential and actual FDI benefits.

TABLE OF CONTENTS

| | |
|--|-----------|
| CERTIFICATION | i |
| DECLARATION AND COPYRIGHT..... | ii |
| ACKNOWLEDGEMENT | iii |
| DEDICATION | iv |
| LIST ABBREVIATIONS | v |
| ABSTRACT | vi |
| TABLE OF CONTENTS..... | vii |
| LIST OF TABLES..... | x |
| LIST OF FIGURES | xi |
| | |
| CHAPTER ONE..... | 1 |
| INTRODUCTION | 1 |
| 1.1 Overview of the Study | 1 |
| 1.2 Background to the problem | 1 |
| 1.3 Statement of the Problem | 6 |
| 1.4 Objectives of the study | 8 |
| 1.4.1 General objective..... | 8 |
| 1.4.2 Specific objectives..... | 8 |
| 1.5 Research Questions | 8 |
| 1.6 Significance of the study | 9 |
| 1.7 Scope of the study | 9 |
| 1.8 Delimitations of the study | 9 |
| 1.9 Limitations of the study..... | 9 |
| | |
| CHAPTER TWO..... | 11 |
| LITERATURE REVIEW..... | 11 |
| 2.1 Introduction | 11 |
| 2.2 Theoretical Literature Review | 11 |
| 2.2.1 The Historical Back Ground of Foreign Direct Investment (FDI)..... | 11 |
| 2.2.2 Definition of FDI | 11 |
| 2.2.3 Theories of Foreign Direct Investment..... | 12 |
| 2.2.4 FDI Inflows in Tanzania | 19 |

| | |
|---|-----------|
| 2.3 Empirical Literature Review | 20 |
| 2.3.1 Impacts of FDI | 20 |
| 2.3.2 FDI and Growth | 22 |
| 2.3.3 Case experience of the impact of FDI on the Tanzania's Economic Development Capital Formation | 24 |
| 2.4 Conceptual Framework and research model | 31 |
| CHAPTER THREE..... | 33 |
| RESEARCH METHODOLOGY | 33 |
| 3.1 Introduction | 33 |
| 3.2 Research Design | 33 |
| 3.3 Study Area..... | 33 |
| 3.4 Types and the Source of Data..... | 33 |
| 3.5 Data Collection Methods..... | 34 |
| 3.5.1 Secondary Data | 34 |
| 3.6 Data Analysis Method..... | 34 |
| CHAPTER FOUR..... | 36 |
| PRESENTATION OF THE FINDINGS..... | 36 |
| 4.1 Introduction | 36 |
| 4.1.1 Data Analysis | 36 |
| 4.1.2 The Model Specification..... | 37 |
| 4.1.3 Variable Description | 38 |
| 4.2 Descriptive Statistics..... | 39 |
| 4.2.1 GDP Growth..... | 39 |
| 4.2.2 Mining and Quarrying Sector..... | 39 |
| 4.2.3 Manufacturing Sector..... | 40 |
| 4.2.4 Agricultural Sector | 40 |
| 4.2.5 Labor force | 40 |
| 4.3 Econometric Results..... | 40 |
| 4.3.1 The extent at which FDI inflows in Mining and Quarrying Sector Influence Economic Growth in Tanzania | 41 |

| | |
|---|-----------|
| 4.3.2 The extent at which FDI inflows in Manufacturing Sector Influence Economic Growth in Tanzania | 42 |
| 4.3.3 The extent at which FDI inflows in Agriculture Sector Influence Economic Growth in Tanzania..... | 42 |
| 4.3.4 The extent at which labor force Influence Economic Growth in Tanzania .. | 42 |
| CHAPTER FIVE | 43 |
| DISCUSSION OF THE FINDINGS..... | 43 |
| 5.1 Introduction | 43 |
| 5.2 The extent at which FDI inflows in Mining and Quarrying Sector Influence Economic Growth in Tanzania..... | 43 |
| 5.3 The extent at which FDI inflows in Manufacturing Sector Influence Economic Growth in Tanzania | 44 |
| 5.4 The extent at which FDI inflows in Agriculture Sector Influence Economic Growth in Tanzania | 44 |
| 5.5 The extent at which labor force Influence Economic Growth in Tanzania | 45 |
| CHAPTER SIX..... | 46 |
| SUMMARY, CONCLUSIONS AND POLICY IMPLICATIONS | 46 |
| 6.1 Introduction | 46 |
| 6.2 Conclusion..... | 46 |
| 6.3 Recommendations..... | 46 |
| 6.3.1 To Policy Makers..... | 46 |
| 6.3.2 Infrastructure improvements | 47 |
| 6.3.3 The negative effects of FDIs | 47 |
| 6.3.4 Implications | 47 |
| 6.4 Suggestions on the direction for future study..... | 48 |
| REFERENCES | 49 |

LIST OF TABLES

| | |
|--|----|
| Table 1.1: Tanzania's Selected Macroeconomic Indicators, 2008-2011 | 5 |
| Table 1.2: Tanzania's Capital Flows, 2008-2011..... | 6 |
| Table 2.1: Contribution of the Privatized Firms to the Tax Revenue in Tanzania..... | 28 |
| Table 2.2: FDI and host country economic growth – results of empirical studies on various countries | 30 |
| Table 4.1: Variable Description | 38 |
| Table 4.2: Descriptive Statistics for the Variables Used in the Analysis | 39 |
| Table 4.3: Econometric Results..... | 41 |

LIST OF FIGURES

| | |
|---|----|
| Figure 1.1 Ownership of Project Registered by TIC 1990-2011..... | 7 |
| Figure 2.1: The model showing conceptual framework for analysis of growth within a country | 32 |

CHAPTER ONE

INTRODUCTION

1.1 Overview of the Study

The research intended to examine the impact of Foreign Direct Investment on economic growth of Tanzania. This chapter presents an initial introduction of the study; it contains background to the problem, statement of the problem, objectives of the study, research questions, and significance of the study also the scope of the study.

1.2 Background to the problem

Economic growth is an increase in the capacity of an economy to produce goods and services, compared from one period of time to another. Economic growth can be measured in nominal terms, which include inflation, or in real terms, which are adjusted for inflation. Economic growth also associated with technological changes. Gross Domestic Product is an estimated value of the total worth of a country's production and services, within its boundary, by its nationals and foreigners calculated over the course on one year. Gross National Product is an estimated value of the total worth of production and services, by citizens of a country, on its land or on foreign land. In this research GDP will be used as measure for economic growth, because the researcher is dealing with the impact of FDI, in order to know the results of those investments, GDP will be the right measurement in knowing the economy within the country, because it includes both nationals and foreigners.

Foreign Direct Investment is one of many other factors that contribute on Tanzania's economic growth. Foreign Direct Investment is still in its relative infancy stage in Tanzania (Ngowi, H.P, 2002). In 1963 government attract FDIs by establishing Foreign Investment Act in order to motivate FDIs in the newly independent Tanganyika, then name of mainland Tanzania before the 1964 union with the island of Zanzibar (Green, 1982).The effort was unsuccessful after Arusha Declaration in 1967, where the agreement was "socialism and self-reliance", so the government opted for socialist for economic development. There were minimal FDI activities taking place in Tanzania between 1970 and 1985. The majority of the investments

were made by the state directly or indirectly, by 1980 there were about 400 public owned corporations and companies in form of state Owned Enterprises (SOEs). The majority of these were owned by the Tanzanian government with 100% shares.

In 1990, the government set out an Investment Promotion Centre (IPC) to help attract FDIs in Tanzania, and later after seven years not much of FDIs attraction and private sector development were achieved. The level of annual FDIs value attraction was about USD 148.64 million. With such achievement called for a need to transform IPC into a more aggressive institution on attracting more FDI in Tanzania. Later Tanzania Investment Centre was established in 1997 by the Tanzania Investment Act No.26 of 1997 to be the primary agency of Governments to coordinate, encourage, promote and facilitate investments and to advise the government on investment related matters (TIC Investment Report, 2009).

TIC is the focal point for investors and first point of call for potential investors. It is also an efficient and effective investment promotion agency, a “One Stop Facilitative Centre for all investors” engaging in the business of the Government in all investment matters, TIC in charge with the following roles;

Assisting in the establishment of enterprises; obtain necessary licenses, work permits, visas, approvals, facilities or services, sort out any administrative barriers confronting both local and foreign investment activities; secure investment sites and assist investors to establish Export Processing Zones (EPZ) Projects; Grant certificates of incentives, investment guarantees and register technology agreements for all investments, which are over and above US\$ 300,000 and US\$ 100,000 for foreign and local investments respectively; provide and disseminate up to date information on existing investment opportunities, benefits or incentives available to investors; and assist all investors whether or not registered by TIC (TIC Investment Report, 2009).

In order to strengthen and expedite facilitation services, senior officers from Government or its Executive Agencies have been permanently stationed at TIC to serve investors under the general direction of the TIC Executive Director. Presently these officers are drawn from Lands Department; Land Division; Directorate of

Trade and Business Registration and Licensing Agency (BRELA), (Tanzania Investment Act, 1997).

The priority sectors for investment, as identified by TIC are; Tourism, Infrastructure Development, aviation, agriculture, construction, manufacturing and financial services. However, investment is not restricted in other sectors. TIC services are provided to local and foreign investors without discrimination, though a variety of regulatory fees are higher for foreign firms than for local firms.

Remaining obstacles to foreign investment include bureaucratic intransigence, corruption and poor infrastructure, and for the case of Zanzibar, there is Zanzibar Investment Promotion Agency (ZIPA). Like Tanzania mainland, Zanzibar aims to create a welcoming environment for foreign investors and provides similar incentives. (Mahiti, 2012).

Various scholars have associated economic growth with various factors one of them being Foreign Direct Investment (FDI). For instance Mencinger (2003) has argued that FDI is generally considered, by many international institutions, politicians and economists, as a factor which enhances host country economic growth, as well as the solution to the economic problems of developing countries. Many policy makers and academics contend that foreign direct investment (FDI) can have important positive effects on a host country's development effort (Markusen, 1995 & Caves, 1996). FDI can be a source of valuable technology and know-how while fostering linkages with local firms, which can increase momentum to the economy. Based on these arguments, industrialized and developing countries have offered incentives to encourage foreign direct investments in their economies. This research intends to explore the effects of FDI on economic growth.

FDI inflows and outflows over time, has not been equally distributed across the globe. Information from UNCTAD's World Investment Reports (WIR) for various years (www.unctad.org) reveals that there has been a strong increase in FDI in the recent past. The increase is both in absolute terms and relative to trade. FDI growth at an annual average of 23 per cent since 1986 has been twice that of trade.

“FDI flows to Tanzania rose by 39 per cent to \$1.7 billion in 2012. Just as in other African countries, a large share of FDI flows to Tanzania is directed to extractive industries.”

UNCTAD forecasts FDI in 2013 to remain close to the 2012 level, with an upper range of \$1.45 trillion. As macroeconomic conditions improve and investors regain confidence in the medium term, transnational corporations (TNCs) may convert their record levels of cash holdings into new investments. FDI flows may then climb to \$1.6 trillion in 2014 and \$1.8 trillion in 2015. However, the report warns that factors such as structural weaknesses in the global financial system, the possible deterioration of the macroeconomic environment, and significant policy uncertainty in areas crucial for investor confidence might lead to a further decline in FDI flows.

Developing countries took the lead in attracting FDI in 2012. For the first time ever, developing economies absorbed more FDI than developed countries, accounting for 52 per cent of global FDI flows. The report finds that FDI inflows to developing economies nonetheless declined slightly (by 4 per cent), to \$703 billion – the second-highest level recorded. Among developing regions, flows to Asia and to Latin America and the Caribbean remained at historically high levels, but their growth momentum weakened. Africa saw a year-on-year increase in FDI inflows in 2012. (UNCTAD press 2013).

In 2014, the global foreign direct investment (FDI) inflows declined by 8% to an estimated US\$ 1.26 trillion due to fragility of the global economy, policy uncertainty and geopolitical risks. A large divestment in the United States also lowered the global level of FDI flows. FDI flows to developed countries dropped by 14% to an estimated US\$ 511 billion, significantly affected by a large divestment in the United States. FDI flows to the European Union (EU) reached an estimated US\$ 267 billion; this represents a 13% increase on 2013, but is still only one-third of the 2007 peak.

Flows to transition economies more than halves reaching US\$ 45 billion as regional conflict, sanctions on the Russian Federation, and the negative growth prospects deterred foreign investors (especially from developed countries) from investing in the region.

Developing economic saw their FDI reaching a new high of more than US\$ 700billion, 4% higher than 2013, with a global share of 56%. At the regional level, flows to developing Asia were up; those to Africa remain flat, while FDI to Latin America decline. In 2014 china, with a model increase of 3% became the world’s largest recipient of FDI. The United states fell to the 3rd largest host country with almost a third of their 2013 level. Among the top five FDI recipients in the world, four are developing economies. Cross- border megers and acquisitions (M&As) rose by 19%, driven mainly by restructuring deals. Announced Greenfield investment projects rose by 3% in 2014. A solid FDI rise remains distant. A subdued global economies outlook, volatility in currency and commodity markets and the elevated geopolitical risks will negatively influence FDI flows. On the other hand, the strengthening of economic growth in the United States, the demand-boosting effects of lower oil prices and proactive monetary policy in the Eurozone, coupled with increased liberalization and promotion measures, will favourably affect FDI flows.

From Tanzania Investment Centre report shows how FDI trends over time also the GDP as shown below;

Table 1.1: Tanzania’s Selected Macroeconomic Indicators, 2008-2011

| Indicator | 2008 | 2009 | 2010 | 2011 |
|---------------------------------------|---------|---------|---------|---------|
| Population (Million) | 39.3 | 40.7 | 43.2 | 44.5 |
| GDP growth (%) | 7.4 | 6.0 | 7.0 | 6.4 |
| GDP per capita (USD) | 525.0 | 526.0 | 547.0 | 558.0 |
| CPI average inflation rate (%) | 10.3 | 12.1 | 7.6 | 12.6 |
| Exports of goods and services/GDP (%) | 26.9 | 23.8 | 27.6 | 30.6 |
| Imports of goods and services/GDP (%) | 41.9 | 35.0 | 39.1 | 49.9 |
| CAB/GDP (%) | -12.4 | -8.4 | -8.5 | -16.5 |
| CAB*/GDP* (%) | -15.3 | -11.4 | -11.9 | -19.0 |
| Average exchange rate (TZS/USD) | 1,196.9 | 1,306.0 | 1,395.7 | 1,557.4 |
| Official reserves (USD Million) | 2,872.6 | 3,552.5 | 3,948.0 | 3,744.6 |
| Reserves months of imports cover | 4.0 | 5.6 | 5.2 | 3.7 |

Source: Tanzania investment report, 2012

Notes: CAB = Current Account Balance, “pa” means period average, CAB* = CAB excluding official grants.

Table 1.2: Tanzania's Capital Flows, 2008-2011

| Type of investment | Capital inflows(USD Million) | | | |
|---------------------------|------------------------------|---------|---------|---------|
| | 2008 | 2009 | 2010 | 2011 |
| Capital flows and stocks | 1,555.5 | 1,023.4 | 1,812.5 | 1,330.0 |
| Foreign direct investment | 1,383.3 | 952.6 | 1,813.3 | 1,229.4 |
| Portfolio investment | 0.2 | 0.4 | -0.1 | 0.7 |
| Other investment | 172.0 | 70.4 | -0.7 | 99.9 |

Source: Tanzania investment report, 2012.

This study is worth conducting because it will enable the country to appreciate the impact that FDI has had on her economic growth since the major economic policy liberalization took place and to take necessary measures in terms of policy formulation so as to attract an even more share of FDI's inflows to the nation.

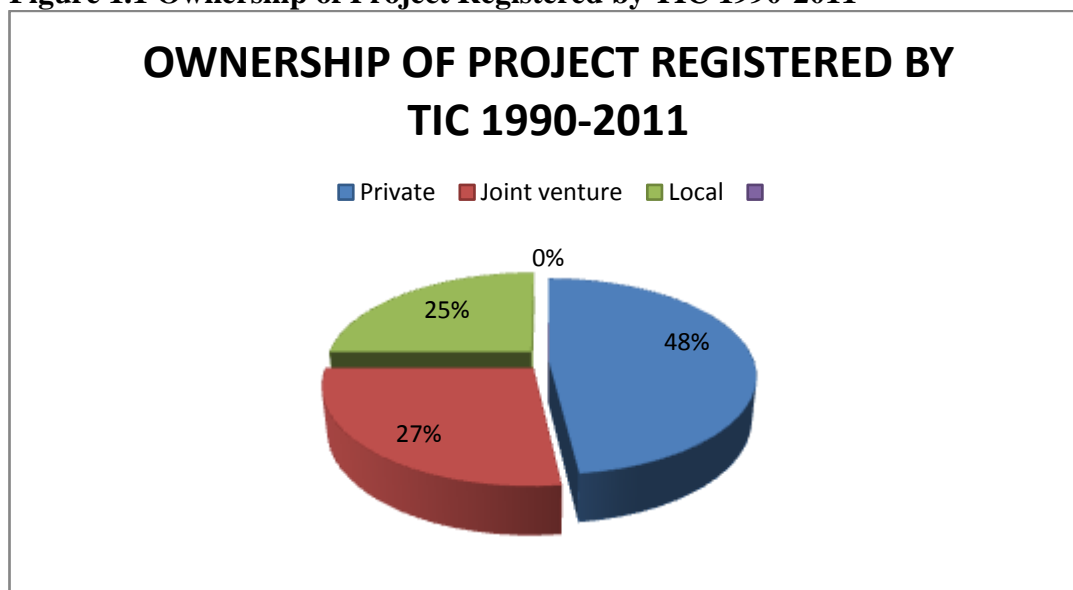
1.3 Statement of the Problem

Foreign Direct Investment is an investment made by a company or entity based in one country, into a company or entity based in another country. Foreign direct investments differ substantially from indirect investments such as portfolio flows, wherein overseas institutions invest in equities listed on a nation's stock exchange. Entities making direct investments typically have a significant degree of influence and control over the company into which the investment is made. Open economies with skilled workforces and good growth prospects tend to attract larger amounts of foreign direct investment than closed, highly regulated economies.

Foreign Direct Investment (FDI) is generally considered, by many international institutions, politicians and economists, as a factor which enhances host country economic growth, as well as the solutions to the economic problems of developing countries (Mencinger, 2003). In 2002, OECD reports that countries with weaker economies consider FDI as the only source of growth and economic modernization. For this reason, many governments, particularly in developing countries, give special treatment to foreign capital (Carkovic and Levine, 2002).

In recent years after liberalisation the private investors have captured a greater percentage of total investment in the country. This is evidenced by the greater percentage (48%) they took on the economy of this country as indicated in the chart below.

Figure 1.1 Ownership of Project Registered by TIC 1990-2011



Source; Tanzania Investment Centre, 2011

The results of a rapidly growing number of empirical studies on the relation between FDI and economic growth differ, although most studies start with the essentially the same benchmark cross-country growth model. In many studies dealing with the subset of the countries, FDI or FDI in combination with some other factor or factors is positively related to growth. Among the studies that have concluded a positive relationship between FDI and Growth are those of Blomström (1986), De Gregorio (1992), Mody and Wang(1997), Nair-Reichert and Weinhold (2001), and Lensink and Morrissey (2006). However, there is also evidence that FDI is a source of negative effects as witnessed by Haddad and Harrison (1993), Grilli and Milesi-Ferretti (1995) and Javorcik (2004). Although many studies have confirmed positive effects of FDI, some authors stress that there is still no consensus on the degree of these effects (Blomström and Kokko, 1998; Lim, 2001).Also Pessoa (2007) and Wang (2009) report that the main conclusion to be drawn from several studies is that results are ambiguous. Nair-Reichert and Weinhold (2001) emphasize that it can be

caused by potential errors in the estimation method. Wang (2009) suggests that one possible reason is the use of total FDI, rather than FDI by sector. Furthermore Edison et al. (2002) concluded that differences in the sets of the countries included, sample periods, data, and estimation techniques hamper comparisons across the studies. Due to the lack of consensus about the effects of FDI on economic growth, and as suggested by Wang (2009), the researcher considers it relevant to conduct the study of impacts of FDI (by sector) on economic growth of Tanzania. The strength of the study was built upon not only current data but also the researcher included the Agricultural sector was left by most of previous researchers.

1.4 Objectives of the study

1.4.1 General objective

The objective of the study was to explore the impact of Foreign Direct Investment on economic growth of Tanzania.

1.4.2 Specific objectives

The study was guided by the following specific objectives.

- i. To ascertain the extent at which FDI inflows in Mining and Quarrying sector influence economic growth in Tanzania.
- ii. To ascertain the extent at which FDI inflows in manufacturing sector influence economic growth in Tanzania.
- iii. To ascertain the extent at which FDI inflows in Agriculture and Livestock sector influence economic growth in Tanzania.

1.5 Research Questions

- i. To what extent do FDI inflows in Mining and Quarrying sector influence economic growth in Tanzania?
- ii. To what extent do FDI inflows in manufacturing sector influence economic growth in Tanzania?
- iii. To what extent do FDI inflows in Agriculture and Livestock sector influence economic growth in Tanzania?

1.6 Significance of the study

The study was intended to provide information as to what extent FDI (by sectors) influences the economic growth of our country. Also the study is useful to Tanzania investment authority because it is provide information on which sector performs well in FDI inflows and which one requires improvement. This will help them in reviewing their policies and regulations so as to create conducive environment for attracting more FDIs into the country. Increase of awareness to the users on impact that FDIs have on the Tanzanian economy. Lastly the study was enabled the researcher to meet the requirements to be awarded a degree of masters of Science in accounting and finance. Since there is no consensus on the degree of the effects of FDI on Economic growth the study was focused of contributing to the platform of comparing the findings with other studies as the basis of establishing conventional measures of the effects of FDI on growth.

1.7 Scope of the study

The study intends to explore the effects of FDIs on economic growth and it covers only one country in this case Tanzania. Therefore the findings and results from this study may not necessarily apply to other countries.

1.8 Delimitations of the study

The study was focus on the impact of Foreign Direct Investment (FDI) on economic growth in Tanzania. The researcher collected secondary information through content-analysis method. Content- analysis consists of analysing the contents of documentary materials such as books, magazines, newspapers and the contents of all other verbal materials which can be either spoken or printed. The researcher was employ secondary data in the analysis. Secondary data was obtained from Tanzania Investment Centre (TIC), Bank of Tanzania (BOT) and National Bureau of Statistics.

1.9 Limitations of the study

This study is was dealing with secondary data this cause or lead to inherit the errors done when those data were collected, also thee data miss contextual details because

other people where the one responsible to collect the data, the errors can diverge the results of the research, data might be not reliable.

Lack of fund, the researcher is private sponsored so was face the challenges of getting adequate finance of some research materials and bought some document like pamphlets, journals and internet bundles are expensive. They make the study completed in a difficult situation.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter is about reviewing of various literatures about FDI and economic growth. This includes Theoretical literature review, Empirical literature review and also conceptual framework.

2.2 Theoretical Literature Review

2.2.1 The Historical Back Ground of Foreign Direct Investment (FDI)

FDI is believed to begin in the late nineteenth century. The Victorian and Edwardian eras saw the creation of many of the great vertically integrated multinationals that would be recognized today as colonial plantation companies such as Lever Brothers (now Unilever) investing in West African vegetable Oil plantations, Cadbury's in Cocoa, Dunlop in rubber. The UK as the great imperial power of the time, dominated world international business with over 45% of the world's total stock of the FDI in 1914. Following the World II, the FDI leadership passed over to the US, with companies such as General Motors, Ford Chrysler, and IBM, developing manufacturing bases around the world. By 1960, US counted over 48% of the world investment. However; the significant entrant in international scene has been Japan. In 1960, Japanese firms accounted for less than 1% of the world accumulated FDI. By 1989, the Japanese share was over 12%, against 29.5% for the US and 15% for the UK. In 1990s there was a significant change in the trend of FDI. This is because FDI flowing to the developing countries surged to 30%-40% compared with just 15% and 18% in 1980s. However, the majority of the FDI went to countries of the Asia-Pacific region. Major countries namely the US, UK, and Japan, accounted for this bulk outward investment (Buckley, 2000:356).

2.2.2 Definition of FDI

Foreign direct investments are defined as investments in which a firm acquires a majority or at very least a controlling interest in a foreign firm. Foreign investments not involving a majority or controlling stake are typically referred to as a portfolio

investments. Firms making foreign direct investments (FDI) are referred to as multinational enterprises (MNE) and the two terms are used somewhat interchangeably.

A direct investment may involve creating a new foreign enterprise, often referred to as a green field investment, or acquiring an existing foreign firm (sometimes referred to as a brown field investment, though that term is much less common; acquisition is the typical label). (Kenneth A. and Ramkishen S, 2008).

Bjorvatn (2000) defines FDI as an investment made to acquire a lasting interest in a foreign enterprise with the purpose of having an effective voice in its management. The literature distinguishes between horizontal and vertical FDIs. Horizontal FDIs, as seen in Markusen (1984), Horstmann and Markusen (1992); Brainard (1993); Markusen and Venables (1996a,b, 1998) is the type of FDI undertaken to place production closer to foreign markets. In this case, production of goods and services in the host economy takes the place of exports and FDI can substitute trade.

Vertical FDIs as seen in Helpman (1984); Helpman and Krugman (1985) is undertaken to exploit lower production costs in order to serve both foreign and home market. In this case FDI can be a complementary to trade when a part of the production in the host economy is exported back to the home country, Ngowi (2012).

2.2.3 Theories of Foreign Direct Investment

The Foreign Direct Investment (FDI) theories can be classified broadly into two categories. One is at the macro level and the other is at the micro level. Again at the macro-level, we have capital market theory, Dynamic macroeconomic theory, FDI theories based on exchange rates, FDI theories based on economic geography, gravity approach to FDI and FDI theories based on institutional analysis.

At the micro-level, we have the theories like Existence of firm specific advantages (Hymer), FDI and oligopolistic markets, Theory of internalisation, and Electic FDI theory (John Dunning). Recently another type of FDI categories discussed by the economists is the development theories which combine both the micro-level and macro-level FDI theories. The development theories are Life cycle theory, Japanese

FDI theories and five stage theories (John Dunning). Questions like what are the factors that attract FDI, why the firms prefer to invest abroad and how they make entry to the foreign countries etc. have been addressed.

Macro-Level Foreign Direct Investment Theories

From a macroeconomic point of view, FDI is a particular form of capital flows from countries of origin to host countries and these capital flows are found in the balance of payments. Lipsey (2001) said that the macroeconomic theories try to explain the motivations of the investors for investment in foreign countries. The macro-level determinants that affects the host country's FDI flows are market size, economic growth rate, infrastructure, natural resources, political situation and so on (Woldemeskel, 2008). The macro-level theories are explained below:

Capital market theory is one of the oldest theories of FDI. According to this theory, FDI is determined by interest rates. Capital market theory is a part of portfolio investment (Iversen, 1935; Aliber, 1971). Boddewyn's (1985) Capital market theory talked about three positions which attract FDI to the less developed countries (LDCs). First is the undervalued exchange rate, which allows lower production costs in the host countries. Second position said that since no organised securities exist, therefore long term investments in LDCs will often be FDI rather than purchase of securities. And the third position is that since there is limited knowledge about host countries' securities that is why it favours FDI which allows control of host country assets. Another macroeconomic theory is **dynamic macroeconomic FDI theory** according to which the timing of investments depends on the changes in the macroeconomic environment (Sanjaya Lall 1997). The macroeconomic environment consists of gross domestic product, domestic investment, real exchange rate, productivity and openness which are the determinants of FDI flows.

This theory states that FDI is a long term function of multinational companies' strategies. Similar to these two theories, FDI theories based on **exchange rate** tried to show the relationship between FDI and exchange rate. The theory tries to explain how the flow of FDI affects the exchange rates. The theory describes FDI as a tool of exchange rate reduction (Cushman, 1985). Another macroeconomic FDI theory is

based on economic geography which focuses on countries and explained why internationally successful industries emerge in particular countries (Porter, 1990; Nachum 1999). These explanations were based on the differences among countries in terms of availability of natural resources, nature of labour force and local demand, infrastructure and so on, the FDI theories based on economic geography also covers the ways in which governments can affect the resources within the jurisdiction by various policy actions since economic unit of analysis is defined by political boundaries. Again the theory explains why some regions or cities within countries are economically successful (Storper 1996, 1997; Sassen 1991, 1994).

The **Gravity approach to FDI** contends that if two countries are very close geographically, economically, and culturally, then the FDI flow between the countries is the highest. The theory includes traditional gravity variables such as size, level of development, distance, common language and other institutional variables such as shareholder protection (Pagano and Volpin, 2004, La Porta et al., 1998) and openness to FDI flows (Shatz, 200) as the determinant of FDI flows. Another macroeconomic FDI theory is based on **institutional analysis**, which was developed by Saskia Wilhelms (1998) explores the importance of institutional framework on the flows of FDI. The theory said that political stability is the key factor of a healthy institutional framework. According to This theory, FDI is determined more by institutional variables viz. policies, laws, and their implementation and less by intransigent fundamentals. The four institutions contributing to FDI flows are governments, markets, education and socioculture (Wilhelms, 1998).

Micro-Level Foreign Direct Investment Theories

The Micro level FDI theories try to provide the answers of why MNCs prefer opening subsidiaries abroad rather than exporting or licensing their products, how MNCs choose their investment locations and why they invest where they do (Woldemeskel, 2008). The micro-level theories are explained below:

Existence of **Firm specific Advantage theory of FDI** was developed by Stephen Hymer (1976). According to this theory, firms invest abroad because of certain firm specific advantages such as, access to raw materials, economies of scale, and

intangible assets such as trade names, patents, superior management, and low transaction costs and so on. If markets work effectively and there are no barriers in terms of trade and competition, international trade is the only way to participate in the international market. Therefore the realisation of direct investment is determined by some certain distortions, and these distortions were first noticed by Hymer. He believes that local firms will have always been informed about local economic environment and for FDI to take place there must be some conditions. These are foreign firms must possess certain advantages that allow such investments to be viable and markets of these benefits has to be imperfect (Kindleberger, 1969).

Hymer said that market imperfections lead to divergence from perfect competition in the final product market and multinational enterprise (MNE) appears. MNEs face some adjustments costs when they make investments abroad and these are firm level costs. Hymer recognises FDI as a firm level decision rather a capital market decision. He saw FDI as a means of transforming knowledge and firm assets both tangible and tacit in order to organise production abroad (Sethi et al., 2003).

FDI and oligopolistic markets said that in a two-tier oligopoly model, there are two foreign investors—one produces intermediate products and other produces final products. The two investors decide independently whether or not they will enter a host country. The entry of either of the firms incurs some fixed costs and generates technological spill over for the local firms of the same sector and reduces the marginal cost of production (Lin and Saggi, 2010). Hoenen and Hansen (2009) said that FDI is a defensive move in oligopolistic markets. Knickerbocker argued that risk-averse firms follow their main competitors to avoid any distortions in oligopolistic equilibrium. When one firm in an oligopolistic markets moves, the other firms also reacts with countermoves at both domestic and international levels (Schenk, 1996). In oligopolistic markets, firms follow the actions of the market leader, if FDI is a move of the market leader then other firms also reacts by investing abroad and oligopolistic equilibrium sustains.

Buckley and Casson (1976) and Hennart (1982) developed the **Theory of internalisation**. Due to market imperfections, firms aspire to make use of their monopolistic advantage themselves. Buckley and Casson (1976) suggest that firms

can overcome the market imperfections by internalising their own markets. That means, internalisation involves a vertical-integration in the form of bringing new operations and activities under the governance of the firm. Earlier these activities were carried out by the intermediate firms. Initially, the theory was developed by Coase (1937) in a national context and Hymer (1976) in an international context. Hymer identified two major determinants of FDI—one is removal of competition and the other is advantages which some firms possess in a particular activity (Denisia, 2010). Dunning (1980, 1988) considered the internalisation theory as very important and used it in his **eclectic theory**.

But he argues that internalisation theory explains only part of FDI flows. He draws partly on macroeconomic theory and trade as well as microeconomic theory and firm behaviour.

The eclectic theory of John Dunning is a mix of three different theories of FDI, i.e. OLI (Denisia, 2010). From OLI theory four types of FDI derived, they are;

- a) Resource seeking FDI
- b) Market seeking FDI
- c) Efficiency seeking FDI and
- d) Strategic asset/capabilities seeking FDI.

OLI stands for ownership advantages, locational advantages and internalisation. Ownership advantages refer to intangible assets which are possessed by the firm exclusively and may be transferred within MNCs at lower costs, leading to higher incomes or reduced costs. Ownership of limited natural resources, patents, trademarks etc., is some of the examples of ownership advantages. When the first condition is fulfilled, then location advantages determine who will become the host country for the activities of MNCs. Benefits of quantitative and qualitative factors of production, resource availability, lower costs of transportation, telecommunications, and large market size, common government policies, and distance from the home country, cultural relations etc. are the location specific advantages.

I stand for internalisation. When the first two conditions are fulfilled, it must be profitable for the firm to use these advantages in collaboration with some of the factors outside the country of origin (Dunning, 1973, 1980, 1988). The eclectic paradigm of OLI shows that OLI parameters differs from company to company and it reflects the economic, political and social conditions of the host countries.

Development Theories of Foreign Direct Investment

The product life cycle theory was developed by Raymond Vernon in 1966. The theory can be used to analyse the relationship between product life cycle and possible FDI flows. Generally FDI can be seen in the maturity phase and then decline. It was developed as a response to the failure of the Heckscher-Ohlin theory of international trade.

The theory said that firm set up production facilities abroad for those products which are already standardised and matured in the home country (Sethi et al. 2003).

The theory talked about a cycle where a product is produced by the parent firm, and then to catch the world market, the firm's foreign subsidiaries produced the product and finally the product is produced in any part of the world where the cost of production of the product is the least (Vernon: 1966, 1971; Wells: 1968, 1969). Furthermore the theory explains the invention of a product, become export worked through the life cycle and ultimately becomes an import as the product is produced in the least cost countries rather than the inventing country. The key factors of the theory are technological innovation and market expansion. Technology creates and develops a new product and the market size and market structure influence the extent and type of international trade.

This theory was used to explain certain types of FDI made by US companies in the Western Europe after the World War II in the manufacturing industry. Vernon talked about four types of production cycles viz. innovation, growth, maturity and decline. According to him, in the first stage MNCs create new innovative products for local consumption and export the surplus to serve the foreign markets. The theory said that after the Second World War, Europe had increased demand for manufactured products and US companies began to export, having the advantage of technology on

international competitors. With the technological advantage, the product develops and the technologies become known. Manufacturer will standardise the product and foreign companies will imitate it. Thereby, European countries started initiating American products which are exported by the US companies to these countries. US companies were forced to set up production facilities in the local markets to maintain their market shares in those areas (Denisia, 2010).

Japanese FDI theories analysed the relationship of FDI, competitiveness and economic development based on the ideas of Michael Porter. Terumoto Ozawa was the main representative of the theory and it was initially developed in the 1970s. He identified three main phases of development when he analysed the waves of FDI flows of a country.

In the first phase of economic growth, the country is an underdeveloped one and it is targeted by foreign companies to use its potential advantages especially low labour costs. The country experiences the inflows of FDI and there is no outflow of FDI from the country. In the second phase more and more FDI inflows enter the country. The labour costs raises and the standard of living of the people goes up. As the labour costs raises, outflow of FDI takes place. In the third phase, the country face serious competition and this competition is based on innovation. The incoming and outgoing of FDI are motivated by market factors and technological factors (Kojima and Ozawa, 1985).

Five stage theories of John Dunning suggests that countries tend to go through five main stages of development and these stages can be classified according to the propensity of those countries to be outward and inward direct investors. At the first stage, the country is unable to attract inward FDI since it has no specific advantages except the possession of natural resources. Its deficiency in location bound created assets may reflect limited domestic markets. Demand levels are minimal because of its low per capita income, inappropriate government policies, inadequate infrastructure and unskilled labour force. At this stage, little outward FDI can be seen and foreign companies will prefer to export and import from the country. In the second stage, inward FDI starts rising and outward FDI remains low.

Domestic markets may grow either in size or purchasing power, and making some local productions by the foreign firms. Initially this production by foreign firms takes the form of import substitution manufacturing investments. Low labour cost and growing infrastructure and government policies able to establish export oriented firms by the foreign investors.

Outward FDI is still low in this stage as well. In the Third stage marked by declining rate of inward investments and growing outward investment which results in raising Net Outgoing Investments. Large inward investments lead to high technological capabilities and standardised products. High labour costs leads to high income and demand high quality products. In the fourth stage, the comparative advantage of low labour costs deteriorates and outward investment will be directed to the low wage countries. Outflows of investments takes place strongly and seeks advantages in the foreign countries especially low labour cost. And in the final stage, the inflows and outflows of investments come into balance and the investment decisions are completely based on the strategies of MNCs.

2.2.4 FDI Inflows in Tanzania

FDI in East Africa have been increasing over time. BOT et al (2001:9) point out that monetary value of the FDI inflow into Tanzania increased sixteen-fold from US\$ 47 million in 1990 to US\$ 768 million by 2000. This is an increase by 15.3% over a decade or an average of 1.53% annual increase. There has been an increase in FDI stocks in Tanzania from 1985 to 1990. Then there was a dramatic decline in 1995, before peaking up in 1998 and 1999. FDI in flows into Tanzania have been increasing over time.

The increase from 1996 is both in absolute terms and in relation to other countries, including Kenya. The increased inflows can be attributed to, inter alia, the far – reaching reforms that Tanzania has been undertaking and still at the midst of mainly from the mid-1980s (Ngowi, 2002).

Tanzania under Julius Nyerere attempted a socialist transformation that saw widespread nationalization of property, including the seizure of foreign assets. Foreign investment was legally and effectively banned. This was widened in the

1970s to include most Asian-owned businesses and an (unevenly enforced) expropriation of any property valued at greater than \$15,000. Capitalism and foreign capital in particular were considered UN African, whereas **Ujamaa** was considered more “authentic” and appropriate.

Recently the climate has changed considerably. Economic reforms began slowly in 1986, and accelerated after an economic crisis in the mid-1990s, substantially altering the government’s stance on foreign investment.

The privatization program, which included many nationalized firms previously owned by foreign companies, facilitated the return of foreign firms back into the country. Mining reforms in the early 1990s allowed major new investment by foreign firms, especially Ghana’s Ashanti Goldfields and South Africa’s AngloGold.

Foreign banks were allowed entry after 1993 and several large South African and British banks began operations soon thereafter. Legal changes in 1997 lifted most of the remaining sectorial restrictions on foreign investment in Tanzania Mainland (although many regulations remain in place in semi-autonomous Zanzibar). Previous demands of government equity have also been lifted for all sectors, except for petroleum (UNCTAD, 2002).

2.3 Empirical Literature Review

2.3.1 Impacts of FDI

Usiri (2014) conducted a study on The Effects of Foreign Direct Investment on Economic Growth the Case of Tanzania. The results from Econometric analysis indicate that FDI investment in manufacturing sector has no significant effect on economic growth of Tanzania while the results from the Econometric analysis indicate that FDI investment in Mining and Quarrying sector has a positive effect on economic growth of Tanzania. This variable has a positive coefficient and is statistically significant at 5 per cent

Onakoya (2012) conducted a study on Foreign Direct Investments and Economic Growth in Nigeria: A Disaggregated Sector Analysis basing on the sectors in order to give better insight into the variations inherent therein. The finding shows that FDI

has a significant impact on output of the economy but that the growth effects of FDI differ across sectors. The impact on manufacturing sector was insignificant while of the agricultural sector was positively less sensitive but significant. The paper recommends sector-specific policies, enhanced trade openness, import substitution development strategy incentives to existing investors, and potential overseas investors so as to enhance the development of the country.

Abala (2014) investigated the main drivers of real Gross Domestic Product growth in Kenya as well as those that drive the foreign direct investment (FDI) in Kenya. The findings show that FDI in the mining sector was insignificant while significant in the manufacturing sector. The reasons behind was pointed out to be the nature of FDI attraction in Kenya to be market seeking in which case the manufacturing sector was in favor compared to other sectors like mining, tourism and service sectors.

There are many benefits of FDI both to the host country and the home country, these benefits are noted by different authors. For instance, Alfaro (2003) said that in addition to the direct capital financing it supplies, FDI can serve as a source of valuable technology and know-how to the host developing countries by fostering linkages with local firms. These technological innovations by MNEs play a central role in the economy and they are some of the most important areas where MNEs as catalyst in developing countries.

MNEs have the financial strength to invest in large plants. This might be very difficult for local investors due to their lack of huge investment funds which MNEs can afford. Through FDI “scarce” capital can be made available to the developing counties. This is very crucial to economic growth. Jones (1996) notes that the transfer of capital by MNEs can supplement domestic savings and contribute to domestic capital formation for countries that are capital constrained and this can increase domestic investment.

Some investments are better off if managed under foreign control. This will put the level of government interference at its minimal. More often than not, FDI brings along solid ownership and independent management.

The secretary general of United Nations (Koffi A Annan) summarised the importance of FDI to the developing economies as follows “with the enormous potential to create jobs, raise productivity, enhance exports and transfer technology, foreign direct investment is a vital factor in the long-term economic development of the development of the developing countries” (United Nations,2003 page iii).

Despite the benefits that can be delivered from FDI, it should be noted that it can also bring about some negatives impact. For instance activities of MNEs can displace local firms that can't cope with the competition from foreign firms, thereby reducing the growth of the local firms. (Jones, 1996). Also if proper regulation is not in place in the host country, FDI can serve as a source of capital flight from the developing countries to the developed ones. For instance due to some specific risks in the host country (economic and political risks), there could be large flow of capital from the host country to the home country if there is no legislation against such practice. This can have adverse effect on the host economy especially if such capital is sourced for within the host country. Finally due to MNEs higher production capacity, FDI can cause large scale environmental damage which sometimes is not well taken care of especially in the mining sector (Bora 2002). It should be noted that the net contribute fgmon of FDI to growth can only be measured empirically.

2.3.2 FDI and Growth

Many research works have shown that the contribution of FDI to growth is positive. Using different data and methodologies, many researchers have concluded that FDI has positive impact on economic growth.

For instance, in a paper by Loungani and Razin (2001), it was reported that of the three sources of capital flow to the developing countries (FDI, portfolio investment and primary bank loans), FDI was discovered to be the most resilient during the global financial crises in the 1980s. Moss, Ramachandran and Shah (2005) had a similar conclusion in their study which focused on three countries in Africa: Kenya, Tanzania and Uganda. It was discovered that the percentage of export that is from MNEs is far more than the one from local investors. This shows that FDI contributed more to GDP than local investment in the three countries. The OECD (2002) simply

stated that FDI increases efficiency of resources and raises factor productivity in the host country, so it sees the influence of FDI on growth as positive.

Some research works agree that the FDI contribution to growth is positive but depends on some factors in the host country. Alfaro (2003) concluded that the contribution of FDI to growth depends on the sector of the economy where the FDI operates, claimed that FDI inflow to the manufacturing sector has a positive effect on the growth whereas FDI inflow to the primary sector tends to have negative effect on growth. For the service sector, the effect of FDI inflow is not so clear. However, an economy with a well-developed financial sector gains more from FDI (Alfaro et al, 2003). The impact of FDI on growth also depends on the local condition of the host country. Chowdhury and Mavrotas (2003) said FDI's contribution to growth depends on factors such as human capital base in the host country and the degree of openness in the economy, and even when FDI is contributing to the economy, its impact might not be easily noticed in the short run. Lall (2002) even said that FDI inflow affects many factors in the economy and these factors in turn affect economic growth. Therefore the impact is through its contributions to these other factors.

Countries with high growth can attract FDI better than countries where the economy is not in good shape. This confirms the fact that even though FDI contributes to growth, growth also influences the level of FDI in a country. Chowdhury and Mavrotas (2003) conducted a Toda

-Yamamoto test of causality on three countries (i.e Malaysia, Chile and Thailand) from 1969-2000 to explore the degree of causation between FDI and growth, and they discovered that it is GDP that causes FDI in Chile and not the other two countries. Kumar and Pradhan (2002) discovered that in the majority of cases, the direction of causation between growth and FDI is not pronounced. Furthermore, in poor countries the direction seemed to be running from growth to FDI in an equal number of cases as from FDI to growth.

This conclusion is similar to that of Hansen and Rand (2004), which said that foreign direct investment and growth have a positive relationship, but the direction of

causality is not clear, and knowing this direction of causality is very important for the formulation of the economic policy. Although

The contribution of FDI to growth might be positive; Ray (2005) does not think it helps to develop the local industries in the host country. Hence the multinational companies can be flourishing in the host country while the local firms are not developing. This type of contribution is not good for the economy in the long run.

It is worth noting that some research work has claimed that the contribution of the FDI to growth is not positive. In a study by Carkovic and Levine (2002), it was concluded that FDI does not have robust independent influence on growth. The study employed two models for the empirical work and used data 75 countries. Mwlima (2003) also did not see FDI as important tool for development. He claimed that the incentives have not been successful; instead it is adding to the economic problems of some of the countries. He said most African countries are competing to attract FDI to the level that each country wants to give the best incentives. This sometimes leads to the level that each country wants to give the best incentives. This sometimes lead to the situation where the incentives could be more than the gain from the foreign investment and this can leave the country worse off than it was before the investment. Zambia was mentioned as specific example. He concluded that there is no real evidence that FDI brings development, nothing that the aim of any MNE is to make profit and not to provide development.

2.3.3 Case experience of the impact of FDI on the Tanzania's Economic Development Capital Formation

In Tanzania FDI has significantly contributed to capital formation despite the fact the large share of capital formation is held by the domestic investment.

Using the official statistics, between 1999 and 2004, FDI averaged about 5 percentage of GDP. Its contribution to the Gross Fixed Capital Formation (GFCF) averaged about 25.7 during the same period.

Technology; Technology from FDI generally may take the following forms: (a) technology-embodied product such as machinery, equipment and tools; (b)

technical skills such as management and organizational expertise, marketing, quality control and other production related skills; and (c) process-related technologies such as proprietary. Note that, form (c) is very rare in Tanzania (UNCTAD, 2000).

According to the literature, there are four channels through which these packages of technology transferred by FDI can be diffused in the host country. These include: (a) FDI establishing linkages with domestic enterprises as suppliers (backward linkage) or users (forward linkage). (b) Skills transfer through training, learning by doing, learning by interacting, and job mobility, (c) demonstration effects as local firms copy or adapt new technologies, market channels and management techniques introduced by foreign investors. This can take place in activities that involve processing or manufacturing and also services (d) strategic technology partnership between a foreign investor and a domestic partner in areas such as R&D; and know-how, design and technical specifications and R&D capability.

Tanzania Breweries can provide a good example of how an FDI can transfer technology through backward linkage. For example, with backward linkage the Tanzania Breweries initiated a comprehensive programme of local sourcing. In the context of this strategic development therefore, Tanzania Breweries identified a number of inputs to the production of beer that could be sourced locally from the primary inputs (barley) to other intermediate inputs in the packaging process. It is approximated that Tanzania's Breweries sources about 30 percentage of its barley requirement from domestic sources. For this purpose it has set up malting plant in Moshi to systemize the purchase of barley from over 500 farmers in the region. In 2000, approximately US\$ 2.4million was paid to farmers for the crop, representing the single largest source of direct income for farmers in the region. In the near future, TB plans to meet the entire barley requirement from local sources (increasing from 6,000 to 26,000 tones) through further investment in research and development of the crop to improve yields and deepening of the present linkages with the farming community.

Another important backward linkage established by TB is the sourcing of locally manufactured glass beer bottles. The supplier, KIOO Glass Ltd, an MNE affiliate, has established close technical collaboration with TB so as to meet production

quality requirements. Another supplier in Tanzania for TB is Carnaud Metal Box, manufacturer of metal croen corks. This supplier is also a long established foreign affiliate and was the first supplier to enter into a technical collaboration with TB after privatisation in 1993. In addition, TB sources plastic crates and shrink to fit packaging from Simba Plastics and is currently sourcing some of its bottle label requirements from Tanzania Printers, a local printing company (labels). TB has also established strong backward links with Showerlux Ltd, manufacturer of industrial chemicals. Around 36 per cent to 50 per cent in the next 3 to 5 years (Portelli and Narula, 2004).

Demonstration effects – another channel of technology transfer – occur when local firms copy or adapt new technologies, market channels and management techniques introduced by foreign investors. This often happens to services and manufacturing companies. Companies with high market shares, such as the Tanzania Breweries, may lead to other small companies management and marketing techniques. It is noteworthy that demonstration effects are often related to competition (Blomstrom, 1986).

Skills and management; Tanzania Cigarette company (TCC) gives a good example of the importance to human resource training and development. For TCC, the human capital component was vital in the achieving various forms of upgrading and benefiting from the forms of technology transfer from the parent company. In the immediate aftermath of privatisation, staff complement downsizing was undertaken. The workforce was reduced from 1300(750 on the production floor) to 730 (300) over four years. The main downsizing was undertaken in the production floor, as a result of extensive automation of plant and equipment which led to a drastic decrease in manual jobs. There are only 3 expatriates in the company who are employed in the key executive and technical roles. Locals are employed in the key management positions (such as technical, administrative and sales and marketing positions) as a result of the extensive capabilities and host country experience they possess.

TCC has now put in place extensive internal and external training programs. TCC is one of the main employers in the host country, and seeks and retains the best young graduates in Tanzania, providing them with career advancement opportunities as well

as external training and secondments to other plants around the world. TCC initial post-privatisation training mainly focused on generic training to enhance employee awareness of organisational change, professionalism and life skills. Substantial changes to the work ethic inherited from parastatal period were required. The continuing training initiatives addressed employees individual development needs and increase effectiveness, particularly of those employees at the production floor without basic skills but who were deemed to be trainable.

Other training programs have been aimed at broadening managers' international exposure within the parent network and the training centre in St. Petersburg, Russia. For example, a system of secondment of TCC personnel to sister affiliates has picked momentum in recent years and a number of local personnel from middle management upwards have already benefited. These training programs are emphasized for the development of senior management, i.e. supervisory and technical staff.

A threshold level of capability for production floor workers was important as the company has been modernizing its plant and equipment. For example, suppliers provide training on specific machinery prior to commissioning so that when the actual machinery is installed in the Dar es Salaam plant, it can be utilised immediately without undue work stoppages. Normally, employees short term ad-hoc training courses with direct relevance to on the job specific tasks.

Revenue generation: Government revenue contribution is also very important for economic development. Table below shows the contribution of 10 privatized industries (to foreign investors) in tax revenue in Tanzania between 2001 and 2003. According to the Table the privatized companies contributed about 6.7, 9.1 and 9.2 percent of total tax revenue in 2001, 2002 and 2003 respectively. However, there have been some policy conflicts between revenue generation and FDI attraction through tax incentives. Tax incentives can cost the government lot of money. For example, if you consider the companies which have privatized in 200, such as Carnaud Metal Box, and DAHACO a three year tax holiday given to the companies could have cost the country loss of about 0.2 and 0.4 percent of total tax revenue during the year 2001-2003.

Table 2.1: Contribution of the Privatized Firms to the Tax Revenue in Tanzania

| Name of the company | Year of privatization | Year | Tax contribution (Tsh.Million) | % of Total Tax Revenue |
|-----------------------|-----------------------|------|--------------------------------|------------------------|
| TBL | 1993 | 2001 | 30,052.1 | 3.2 |
| | | 2002 | 45,065.5 | 4.3 |
| | | 2003 | 58,665.8 | 4.8 |
| TCC | 1995 | 2001 | 11,445.8 | 1.2 |
| | | 2002 | 15,781.3 | 1.5 |
| | | 2003 | 24,443.2 | 2.0 |
| CARNAUDMETALBOX | 2000 | 2001 | 412.6 | 0.0 |
| | | 2002 | 815.8 | 0.1 |
| | | 2003 | 1,210.8 | 0.1 |
| TZ PORTLAND CEMENT | 1997 | 2001 | 3,445.1 | 0.4 |
| | | 2002 | 4,083.2 | 0.4 |
| | | 2003 | 6,217.1 | 0.5 |
| DAR BREW LTD | 1997 | 2001 | 347.0 | 0.0 |
| | | 2002 | 5,537.2 | 0.5 |
| | | 2003 | 293.2 | 0.0 |
| THA | 2000 | 2001 | 5,681.6 | 0.6 |
| | | 2002 | 7,670.1 | 0.7 |
| | | 2003 | 7,415.8 | 0.6 |
| DAHACO | 2000 | 2001 | 893.6 | 0.1 |
| | | 2002 | 2,023.2 | 0.2 |
| | | 2003 | 1,060.1 | 0.1 |
| NBC(1997) LTD | 1997 | 2001 | 4,217.3 | 0.5 |
| | | 2002 | 5,797.4 | 0.6 |
| | | 2003 | 6,506.4 | 0.5 |
| TANZANIA DISTILLERIES | | 2001 | 4,163.5 | 0.4 |
| | | 2002 | 5,781.5 | 0.6 |
| | | 2003 | 3,198.8 | 0.3 |
| CRDB | 1997 | 2001 | 1,498.8 | 0.2 |
| | | 2002 | 2,201.6 | 0.2 |
| | | 2003 | 3,215.5 | 0.3 |

Spillover Effects: evidence of spillover effects (externalities) played by FDI in Tanzania can be drawn from different sectors. Mining spillover effects as mining is considered lacking linkages with the rest of the economy. To start, the Kahama Mining Corporation Ltd (KMCL) at Bulyankulu made it possible for people living around the area to reap some social and economical benefits. For example, KMCL initiated a US\$ 5.48 million housing loan scheme to construct over 800 modern houses at subsidized costs in Bulyanhulu ward.

According to KMCL, the scheme will change the bad housing situation in the area. This scheme follows a water supply project through a 47km long pipeline and a 130km extension of the national grid from Shinyanga to the mine. The mine needs only a quarter of the national grid from 150MVA per year. The rest is made available for the surrounding community's domestic and economic use. US\$ 3.4 million water project avails clean water throughout the day to over 30,000 people in the surrounding villages. According to KMCL, agricultural and small/micro business development, roads, schools and clinics have also received substantial attention and resources from the company.

The Ashanti Gold Mining Company (AGMC) has also produced some positive externalities in Tanzania. The company has used about 1.6 billion shillings for various development projects in Geita district, Mwanza region since it started operation in the area in 2000. For example it has completed upgrading a 76 kilometre road. It has financed the construction of water wells; the buildings of dispensaries, the rehabilitation of the designated district hospital, as well as building a dozen of classroom in six primary schools.

Geita Gold Mine (GGM) has produced similar externalities to AGMC in Geita District. GGM donated computers with hi-tech software to the University of Dar es Salaam's Geology Department, and supported orphans of AIDS victims. The Equal Opportunities Trust Fund has benefited from the mine's philanthropy with 16 million shillings. It has also established a micro finance credit scheme with financing base of 40 million shillings. GGM has contracted most of its jobs to local companies, with over 90 local firms regularly doing business with the company in different operation.

Table 2.2: FDI and host country economic growth – results of empirical studies on various countries

| Author | Year | Countries | Variables (*) | FDI impact on growth |
|---------------------------------|-------------|--|---|--|
| Balasubramanyam et al., 1996 | 1970 - 1985 | 46 developing countries | GDP; employment; domestic capital stock; stock of foreign capital; exports | + (with more significance in countries with export promotion policies) |
| Borensztein et al., 1998 | 1970 - 1989 | 69 developing countries | Per capita GDP growth; FDI; stock of human capital; initial GDP per capita | + (magnitude depends on the existing capital stock) |
| De Mello, 1999 | 1970 - 1990 | 15 countries from OECD and 17 non-OECD countries (Africa and America) | Total factor productivity (TFP) growth; Capital stock; FDI | + / - (positive within OECD countries but negative in other countries) |
| Campos and Kinoshita, 2002 | 1990 - 1998 | 25 countries in transition from Central and Eastern Europe and ex-Soviet Republics | Annual growth rate of GDP per capita; initial GDP per capita; enrollment ratio in primary education; government consumption as a percentage of GDP; FDI; percentage of domestic investment in GDP; population | + |
| Carkovic and Levine, 2002 | 1960 - 1995 | 72 countries | Growth rate of GDP per capita; FDI | FDI has no strong positive Impact |
| Basu et al., 2003 | 1978 - 1996 | 23 developing countries | GDP; FDI | + (and enduring) |
| Bengoa and Sanchez-Robles, 2003 | 1970 - 1999 | 18 countries of Latin America | GDP; FDI; economic freedom | + |
| Choe, 2003 | 1971 - 1995 | 80 countries | Annual growth rate of GDP per capita; percentage of FDI in GDP; percentage of domestic investment in GDP | + |
| Omran and Bolbol, 2003 | 1990 - 2000 | Arab countries | Per capita income growth rate; initial per capita income; percentage of FDI in GDP; percentage of investment in GDP; financial development | + (after economic reforms) |
| Janicki and Wunna, 2004 | 1997 | Bulgaria, Czech Republic, Estonia, | GDP; FDI; imports; the cost of labor; the country political risk | + (gains are note easily) |

| | | | | |
|-----------------------|-------------|---|--|--|
| | | Hungary, Poland, Slovakia, Slovenia, Romania; Ukraine | | achieved) |
| Li and Liu, 2005 | 1970 - 1999 | 84 countries | Investment, population growth, initial GDP per capita, initial human capital and FDI inflows byGDP | + (only from the 80's) |
| Hansen e Rand, 2006 | 1970 - 2000 | 31 developing countries: 10 from Africa; 11 from Latin America Latina; 10 from Asia | GDP; FDI | + |
| Duttaray et al., 2008 | 1970 - 1996 | 66 developing countries: 12 Asian countries, 30 Africans, 21 South America and Caribbean, and 3 other island countries | Growth rate of GDP ; exports as apercentage of GDP; ratio of FDI tothe GDP | + (but only in 29 countries - 44% of the sample; great impact in South America countries, lower impact in Asian countries) |

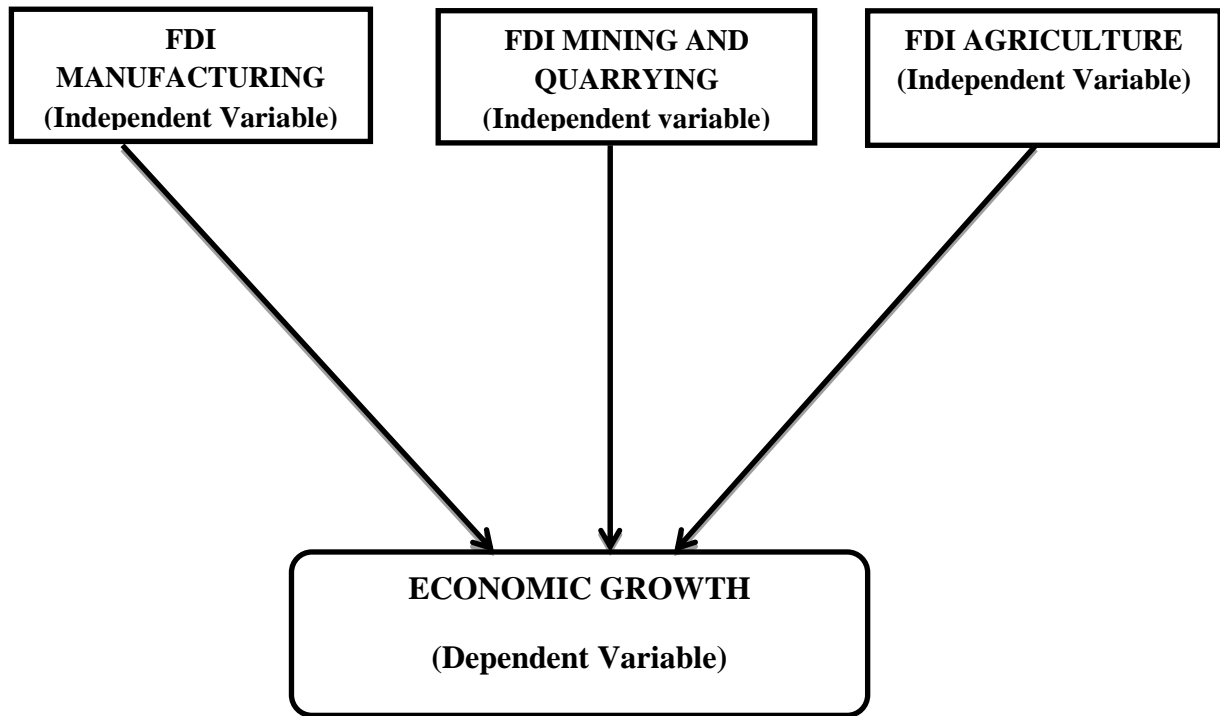
(*) The dependent variable is marked in bold.

Source: Adapted from Ozturk (2007)

2.4 Conceptual Framework and research model

For an analysis of growth within or across countries the Augmented Solow model developed by Mankiw et al (1992), is capable of incorporating factors such as trade, FDI, etc. in addition to the core variables. The growth model in this study will include FDI (by sector). The following figure illustrates the growth model, in which Growth (Economic growth measured in terms of GDP) is a dependent variable while foreign direct investment (FDI by sector); Manufacturing, Mining and Quarrying, Agriculture are Independent variables.

Figure 2.1: The model showing conceptual framework for analysis of growth within a country



CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

Research methodology is a way to systematically solve the research problem. It may be understood as a science of studying how research is done scientifically, Kothari (2003). This chapter presents the methods and techniques used to approach the research problem, which include research design, types and source of data, and methods of data collection, analysis and presentation.

3.2 Research Design

Research design is a plan that specifies the sources and the types of information relevant to the research problem as well as the approach that used for gathering and analysing the data. The proposed study is an exploratory research; survey design was employed to obtain the required information. The use of survey permit a researcher to study more variables at one time than is typically possible in laboratory or field experiments, whilst data can be collected about real world environments. Surveys also enable the researcher to obtain data about practices, situations or views at one point in time through questionnaires or interviews.

3.3 Study Area

The United Republic of Tanzania specifically its economy was used as the study area. The Tanzania Investment Centre (TIC) and Bank of Tanzania (BOT).

3.4 Types and the Source of Data

Quantitative data was employed to answer research equations in the study. The researchers gathered secondary data from World Bank, Bank of Tanzania (BOT) database.

3.5 Data Collection Methods

3.5.1 Secondary Data

The researcher collected data through content-analysis method. Content-analysis consists of analysing the contents of documentary materials such as books, magazines, newspapers and the contents of all other verbal materials which can be either spoken or printed.

3.6 Data Analysis Method

The data was analysed using STATA econometrics software. The researcher will use a time series data from 1999 to 2014 in the analysis. In line with similar studies on FDI and economic growth especially across countries, the study uses a linear regression approach in determining the influence and relationship which Foreign Direct Investment has on Tanzania's economic growth. It will look at FDI (By sector) and economic growth. The statistical methods that used include the Ordinary Least Square Method (OLS) and Unit root test.

This effect/ impact was assessed using multiple linear regression model consisting of three independent variables; FDI inflows in Manufacturing, FDI inflows in Agriculture and FDI inflows in Mining and Quarrying sectors (inflows were measured in US\$) and one dependent variable which is Growth will be measured by GDP.

From the above multiple linear regression model, the following equation summarizes the empirical model for investigating the potential impact that FDI by sector might have on Tanzania's economic growth.

$$\text{Growth} = \beta_0 + \beta_1 \text{Capital} + \beta_2 \text{Labor} + \beta_3 \text{FDI.Mf} + \beta_4 \text{FDI.Mq} \\ + \beta_5 \text{FDI.Agr} + U$$

Where Growth= Economic growth of a country measured by GDP

Capital = Gross fixed capital formation percentage of GDP

Labor = Labor force total

FDI.Mf = FDI inflows in Manufacturing Sector

$FDI.Mq$ = FDI inflows in Mining and Quarrying Sector

$FDI.Agr$ = FDI inflows in Agriculture sector

β_0 = Y Intercept, which is the value of Growth when $\beta_1, \beta_2, \beta_3, \beta_4$ and $\beta_5 = 0$

β_1 = The effect of *capital* on growth when other factors are held fixed.

β_2 = The effect of *labor* on growth when other factors are held fixed.

β_3 = The effect of $FDI.Mf$ on growth when other factors are held fixed.

$(\beta_4)'$ = The effect of $FDI.Mq$ on growth when other factors are held fixed.

β_5 = The effect of $FDI.Agr$ on growth when other factors are held fixed.

U = The Error term which accounts for other unobserved factors that may have an effect on Growth.

CHAPTER FOUR

PRESENTATION OF THE FINDINGS

4.1 Introduction

This chapter presents the analysis of findings of the study. The research intended to examine the impact of Foreign Direct Investment on economic growth of Tanzania. The study was guided by the following specific objectives:

- iv. To ascertain the extent at which FDI inflows in Mining and Quarrying sector influence economic growth in Tanzania.
- v. To ascertain the extent at which FDI inflows in manufacturing sector influence economic growth in Tanzania.
- vi. To ascertain the extent at which FDI inflows in Agriculture and Livestock sector influence economic growth in Tanzania

4.1.1 Data Analysis

STATA econometric software was used to analyse the data. Quarterly and annual data were collected provided they were within the time period of 1999 to 2013 from the Bank of Tanzania (BOT). Before multiple regressions analysis tests for the model fitness were performed including:-

Unit root test results

| Variable | Test Statistic Lag(1) | | Interpolated Dickey Fuller | | | MacKinnon approximate P value | Null hypothesi | Conclusion |
|----------|-----------------------------|------------|----------------------------|-------------------------|--------------------------|-------------------------------------|-------------------------|------------|
| | | | 1% Critical Value | 5% Critical Value | 10% Critical Value | | | |
| Growth | Z(t) | - 3.555 | -3.750 | -3.000 | -2.630 | 0.0067 | There is a unit root | Rejected |

Multicollinearity test results

Using **Klein's Rule of Thumb** if R2 for the auxiliary regression is higher than R2 for the original regression, there may be multicollinearity.

| Assumed Dependent Variable | R2 for the auxiliary regression | R2 for the original regression |
|----------------------------|---------------------------------|--------------------------------|
| Capital | 0.216 | 0.253 |
| Labor | 0.173 | 0.253 |
| FDIMq | 0.012 | 0.253 |
| FDI Mf | 0.032 | 0.253 |
| FDI Agr | 0.008 | 0.253 |

Conclusion: No multicollinearity

Autocorrelation test results

Durbin-Watson d-statistic (5, 15) = 1.855663

For n (15) and k=5; d-lower = 0.390, d-upper = 1.967.

Since the d-statistic is between the d-lower and d-upper and closer to 2 autocorrelation is in evident (zero autocorrelation)

4.1.2 The Model Specification

The specific time series regression model used is:

$$\begin{aligned} Growth = & \beta_0 + \beta_1 Capital + \beta_2 Labor + \beta_3 FDI.Mf + \beta_4 FDI.Mq \\ & + \beta_5 FDI.Agr + U \end{aligned}$$

Where Growth= Economic growth of a country measured by GDP

Capital = Gross fixed capital formation percentage of GDP

Labor = Labor force total

FDI.Mf = FDI inflows in Manufacturing Sector

FDI.Mq = FDI inflows in Mining and Quarrying Sector

FDI.Agr = FDI inflows in Agriculture sector

β_0 = Y Intercept, which is the value of Growth when $\beta_1, \beta_2, \beta_3, \beta_4$ and $\beta_5 = 0$

β_1 = The effect of *capital* on growth when other factors are held fixed.

β_2 = The effect of *labor* on growth when other factors are held fixed.

β_3 = The effect of *FDI.Mf* on growth when other factors are held fixed.

β_4 = The effect of *FDI.Mq* on growth when other factors are held fixed.

β_5 = The effect of *FDI.Agr* on growth when other factors are held fixed.

U = The Error term which accounts for other unobserved factors that may have an effect on Growth.

In the aforementioned model capital and labor are treated as control variables.

4.1.3 Variable Description

The researcher used variable measurement as used in the reviewed literature and in the previous studies.

Table 4.1: Variable Description

| S/N | Variable standard name | Description | Variable name in regression model | Expected effect on Growth |
|-----|----------------------------|------------------------------------|-----------------------------------|---------------------------|
| 1 | Growth(Dependent variable) | Economic growth measured by GDP | Growth | |
| 2 | Capital | Fixed capital formation | Capital | + |
| 3 | Labor | Labor force total | Labor | + |
| 4 | FDI in Mining & Quarrying | Investment in Mining and Quarrying | FDI _{mq} | + |
| 5 | FDI in Manufacturing | Investment in Manufacturing | FDI _{mf} | + |
| 6 | FDI in Agriculture | Investment in Agriculture | FDI _{agr} | + |

4.2 Descriptive Statistics

The table 4.2 shows the summary statistics of variables included in the regression analysis model. Statistics include mean, standard deviation, minimum and maximum.

Table 4.2: Descriptive Statistics for the Variables Used in the Analysis

| Variable | Obs | Mean | Std. Dev. | Min | Max |
|-------------------------------|-----|----------|-----------|----------|----------|
| Growth (%) | 15 | 6.659533 | .8704619 | 4.8404 | 7.8283 |
| Capital (% of GDP) | 15 | 26.41707 | 8.486963 | 16.3547 | 41.9314 |
| Labor | 15 | 19900000 | 2396032 | 16300000 | 23500000 |
| <i>FDI.mq</i> (USD Millions) | 15 | 330.236 | 297.0627 | 6.58 | 909.9 |
| <i>FDI.mf</i> (USD Millions) | 15 | 206.512 | 150.9501 | 64.21 | 563.8 |
| <i>FDI.Agr</i> (USD Millions) | 15 | 14.21333 | 6.569395 | 4.7 | 31.4 |

Source: STATA Analysed data

4.2.1 GDP Growth

From the table 4.2 above the findings show that GDP growth reveals an impressive pattern with the smaller standard deviation of 0.87 which reflects normal distribution. The range between maximum and minimum is also small where the maximum GDP growth is 7.83%. the same was attained in the year 2004. The a maximum growth can be linked to the increased FDI in all sectors under the study except for the Agricultural sector in which FDI had declined previously.

4.2.2 Mining and Querying Sector

From the table 4.2 above the findings show that the Mining and Quarrying sector recorded the highest FDI inflow of 909.9 US Million dollars in the period under review, this happened in the year 2010. The findings imply that FDI in Tanzania focuses on mining and Quarrying related activities. On the other hand the variable also shows a larger standard deviation of 297.1. This is equivalent to 297.1 US Million dollars, signified by less investments in mining and quarrying sector from

2000 to 2001 and unlike 2008-2013 where investment in the sector developed significantly.

4.2.3 Manufacturing Sector

From the table 4.2 above the findings show that the manufacturing sector recorded the highest FDI inflows of 563.8 US Million. This variable has a wide range of 150.95 US Million Dollars. The reason for such discrepancy can be traced in relation to the introduction of private ownership of industries as a result of the privatization policy introduced during the Hon. Benjamin Mkapa's era. This policy accounts for major increase in FDI inflows in this sector because it attracted investors from various parts of the world to Tanzania. However the results from Econometric analysis indicate that FDI investment in Manufacturing (*FDI.Mf*) sector has no significant effect on economic growth of Tanzania

4.2.4 Agricultural Sector

From the table 4.2 above the findings show that the Agricultural sector recorded the highest FDI inflow of 31.4 US Million dollars in the period under review, this happened in the year 2011. Also the findings show a standard deviation of 6.6 which is equivalent to 6.6 US Million dollars. The findings imply that FDI in Agricultural sector is still smaller compared to other sectors under the study. Although the sector witnessed increasing FDI inflows from 2001 to 2011, FDI inflows are declining as revealed in the period from 2012 to 2013.

4.2.5 Labor force

From the table 4.2 above the findings show that the labor force recorded the highest count of 23500000 in the period under review, this happened in the year 2013. Also the findings show a standard deviation of 2396032. The findings imply that labor force is still smaller compared to the population of the country.

4.3 Econometric Results

Multiple linear regression analysis was conducted using STATA econometric software to determine the impact of FDI inflows on the economic growth in terms of

Gross Domestic Product (GDP). The findings are summarized below in the ANOVA statement and table 4.3.

ANOVA Statement

| Source | SS | Df | MS | Number of obs = 15 |
|----------|------------|----|------------|-----------------------|
| | | | | F(5, 10) = 168.53 |
| Model | 667.922178 | 5 | 133.584436 | Prob> F = 0.0012 |
| Residual | 7.92644071 | 10 | .792644071 | R-squared = 0.253 |
| | | | | Adj R-squared = 0.161 |
| Total | 675.848619 | 15 | 45.0565746 | Root MSE = .89031 |

ANOVA statement shows that the model fits the expectation since the F statistic is less than p value of 0.05 at the 95% confidence interval. The R-squared ratio of 0.253 indicates that the independent variables included in the model explain the dependent variable (in this case economic growth by 25.3%). The multiple regression output was summarized in the table 4.3 below.

Table 4.3: Econometric Results

| Variable | Coefficient | Robust Std. Err. | t | P>t | VIF | 1/VIF |
|-----------------|-------------|------------------|-------|-------|----------------|-------|
| Capital | (0.078) | .0617921 | -1.27 | 0.234 | 3.40 | .294 |
| Labor | (0.00001) | 6.87e-08 | -6.34 | 0.000 | 2.78 | .360 |
| <i>FDI.mq</i> | 0.0002 | .0010064 | 3.16 | 0.030 | 1.99 | .503 |
| <i>FDI.mf</i> | 0.001 | .001858 | 0.24 | 0.620 | 1.88 | .531 |
| <i>FDI.Agr</i> | 0.046 | .0390973 | 0.36 | 0.263 | 1.83 | .548 |
| <i>Constant</i> | 5.744 | .6449218 | 4.32 | 0.000 | Mean VIF 2.376 | |

Source: STATA Analysed data

4.3.1 The extent at which FDI inflows in Mining and Quarrying Sector Influence Economic Growth in Tanzania

From the table above the findings show that the results from Econometric analysis indicate that FDI investment in Mining and Quarrying Sector (*FDI.Mq*) has a positive significant effect on economic growth. A unit increase in FDI investment in

Mining and Quarrying Sector (FDI_{mq}) results into 0.02% increase in the economic growth in terms of GDP.

4.3.2 The extent at which FDI inflows in Manufacturing Sector Influence Economic Growth in Tanzania

From the table above the findings show that the results from Econometric analysis indicate that FDI investment in Manufacturing (FDI_{mf}) sector has no significant effect on economic growth. A unit increase in FDI investment in manufacturing sector (FDI_{mf}) results into 0.09% increase in the economic growth in terms of GDP.

4.3.3 The extent at which FDI inflows in Agriculture Sector Influence Economic Growth in Tanzania

From the table above the findings show that the results from Econometric analysis indicate that FDI investment in Agriculture sector (FDI_{Agr}) has no significant effect on economic growth. A unit increase in FDI investment in manufacturing sector (FDI_{mf}) results into 4.61% increase in the economic growth in terms of GDP.

4.3.4 The extent at which labor force Influence Economic Growth in Tanzania

From the table above the findings show that the results from Econometric analysis indicate that labor force negative significant effect on economic growth. A unit increase in labor force results into 0.001% decline in the economic growth in terms of GDP.

CHAPTER FIVE

DISCUSSION OF THE FINDINGS

5.1 Introduction

This chapter presents the discussion of the findings with respect to each of the following research objective.

- i. To ascertain the extent at which FDI inflows in Mining and Quarrying sector influence economic growth in Tanzania.
- ii. To ascertain the extent at which FDI inflows in manufacturing sector influence economic growth in Tanzania.
- iii. To ascertain the extent at which FDI inflows in Agriculture and Livestock sector influence economic growth in Tanzania.

5.2 The extent at which FDI inflows in Mining and Quarrying Sector Influence Economic Growth in Tanzania

The findings show that FDI investment in Mining and Quarrying Sector (FDI_{Mq}) has significant effect on economic growth. A unit increase in FDI investment in Mining and Quarrying Sector (FDI_{mq}) results into 0.02% increase in the economic growth in terms of GDP. The findings are in line with Usiri (2014) who found FDI inflow in the mining and quarrying sector in Tanzania to be significant. Also the findings show that the Mining and Quarrying sector recorded the highest FDI inflow of 909.9 US Million dollars in the period under review, this happened in the year 2010. The findings imply that FDI in Tanzania focuses on mining and Quarrying related activities. On the other hand the variable also shows a larger standard deviation of 297.1. This is equivalent to 297.1 US Million dollars, signified by less investments in mining and quarrying sector from 2000 to 2001 and unlike 2008-2013 where investment in the sector developed significantly. The findings show that the results from Econometric analysis indicate that FDI investment in Mining and Quarrying Sector (FDI_{Mq}) has significant effect on economic growth. A unit increase in FDI investment in Mining and Quarrying Sector (FDI_{mq}) results into 0.02% increase in the economic growth in terms of GDP.

5.3 The extent at which FDI inflows in Manufacturing Sector Influence Economic Growth in Tanzania

The findings show that FDI investment in Manufacturing Sector ($FDI.Mf$) has no significant effect on economic growth. A unit increase in FDI investment in Manufacturing Sector (FDI_{mf}) results into 0.09% increase in the economic growth in terms of GDP. The findings are in support of Usiri (2014) and Onakoya (2012) who found the effects of FDI in manufacturing sector on economic growth to be insignificant. Also the manufacturing sector recorded the highest FDI inflows of 563.8 US Million. This variable has a wide range of 150.95 US Million Dollars. The reason for such discrepancy can be traced in relation to the introduction of private ownership of industries as a result of the privatization policy introduced during the Hon. Benjamin Mkapa's era. This policy accounts for major increase in FDI inflows in this sector because it attracted investors from various parts of the world to Tanzania. However the results from Econometric analysis indicate that FDI investment in Manufacturing ($FDI.Mf$) sector has no significant effect on economic growth of Tanzania. The findings show that the results from Econometric analysis indicate that FDI investment in Manufacturing ($FDI.Mf$) sector has no significant effect on economic growth. A unit increase in FDI investment in manufacturing sector (FDI_{mf}) results into 0.09% increase in the economic growth in terms of GDP.

5.4 The extent at which FDI inflows in Agriculture Sector Influence Economic Growth in Tanzania

The findings show that FDI investment in Agricultural Sector ($FDI.Agr$) has no significant effect on economic growth. A unit increase in FDI investment in Agricultural Sector (FDI_{Agr}) results into 0.46% increase in the economic growth in terms of GDP. The findings are contrary to Onakoya (2012) who found the effects of FDI in agricultural sector on economic growth in Kenya to be significant. Lack of or comparatively lesser inward FDI in the agricultural sector can be the cause of such insignificant effect as pointed out by (Ek, 2007). Also the findings show that the Agricultural sector recorded the highest FDI inflow of 31.4 US Million dollars in the period under review, this happened in the year 2011. Also the findings show a standard deviation of 6.6 which is equivalent to 6.6 US Million dollars. The findings

imply that FDI in Agricultural sector is still smaller compared to other sectors under the study. Although the sector witnessed an increasing FDI inflow from 2001 to 2011, FDI inflows are declining as revealed in the period from 2012 to 2013. The findings show that the results from Econometric analysis indicate that FDI investment in Agriculture sector (FDI_{Agr}) has no significant effect on economic growth. A unit increase in FDI investment in agricultural sector (FDI_{Agr}) results into 4.61% increase in the economic growth in terms of GDP.

5.5 The extent at which labor force Influence Economic Growth in Tanzania

The findings show that labor force has negative significant effect on economic growth. A unit increase in labor force results into 0.001% decline in the economic growth in terms of GDP. The labor force recorded the highest count of 23500000 in the period under review, this happened in the year 2013. Also the findings show a standard deviation of 2396032. The findings imply that labor force is still smaller compared to the population of the country.

CHAPTER SIX

SUMMARY, CONCLUSIONS AND POLICY IMPLICATIONS

6.1 Introduction

The chapter presents summary of the findings, conclusion, recommendations and suggestions for further research are presented. The main objective of the study was to explore the impact of Foreign Direct Investment on economic growth of Tanzania. Specifically the study focused on three sectors, namely Mining & Quarrying, Manufacturing and Agriculture. The proxy for economic growth was the GDP growth rate. Ordinary Least Square method was used to arrive at the findings of the study.

6.2 Conclusion

With respect to the findings in chapter four above it can be conclude that Foreign Direct Investment in the studied sectors of Mining and Quarrying has a positive significant impact on economic growth while Manufacturing and Agriculture has a positive but insignificant impact on Economic growth of Tanzania. Unlike the manufacturing sector, a comparatively lesser FDI inflow in the Agricultural sector could be the reason for insignificant effect.

6.3 Recommendations

6.3.1 To Policy Makers

Tanzania's government through Tanzania Investment Center should put more effort in improving economy and tax policies in order to attract more FDIs, as the research shows FDI has impact but not significant in manufacturing and agricultural sector, for that to be significant, the government should improve its policy for example instead of only providing tax haven to companies they should also consider inducements like lowering taxes on imported parts like machines that are specifically going to be installed in various industries and infrastructures. That will attract major international companies to also initiate operations in other economic sectors other

than Mining and Quarrying, such as manufacturing which will make a significant contribution to economic growth for this nation.

6.3.2 Infrastructure improvements

Tanzania has witnessed major discoveries of Gas and Oil deposits in Songo Songo, Lindi and Mnazi bay in Mtwara. These discoveries have attracted more exploration activities in Mkuranga, Coast region and Msijute in Mtwara as well as at the deep sea. Following the above discoveries we recommend that the government should improve the country's infrastructure like Railways, Roads, Harbours and Airports in order to make all these regions easily accessible for foreign direct investment.

6.3.3 The negative effects of FDI

We have noted that despite all the benefits that FDI bring to the host country there are also negative effects that might happen, so the government should take it in to consideration. Multinationals can transfer inappropriate technologies and the host country can also become dependent on technologies introduced by multinationals. Also FDI can result into the disappearance of local firms due to high competition with the multinationals which may also lead to the problem of unemployment and the host country economy may be affected by the difficulty of implementation of economic policies, resulting from FDI inflows. In fact, FDI inflows are sources of instability by the difficulty or even impossibility, of predicting these flows. This may destabilize the country's economic development and affects negatively the implementation of economic policies. Another harmful event to the host country economy occurs if there is a sudden and high capital inflow because it is likely to increase inflation in proportion to that inflow. Additionally, FDI can cause a decline in the local authorities 'autonomy. Large multinationals get control over assets and employment, which enables them to influence the political and economic decisions of the host country authorities.

6.3.4 Implications

A number of FDI developing issues have been outlined in the study. These issues need policy so that the hosting country can benefit out of the FDI, the hosting country need to have FDI-specific policies cannot be over emphasized. Such a policy

and its vision, mission, statement and strategies would state clearly about the contract both parties about to enter in consideration of issues like the types of FDIs to be attracted, how to attract including reasonable incentives, what should the country gain in terms of added value for each specific FDI that is attracted and how to sustain the potential and actual FDI benefits. When FDIs operate in policy vacuum environment it will be very challenging for host economies to get most out of such investments.

6.4 Suggestions on the direction for future study

The study we conducted covered only the major three sectors of FDI at the time. The study could be extended to cover other important sectors such as Accommodation, Information and Communication, Construction, Real estate activities, Professional activities, Transport and Storage as well as Education. Also they might consider capital or labour as intermediate so to know if they have influence on growth.

Also in other countries where their primary economic activities are exports and imports of goods and services, a similar study could be done but including Merchandise Trade as an independent variable and growth as a dependent variable.

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