

# Does Foreign Portfolio Investment Affect Employment Growth in Nigeria?

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## Abstract

In the wake of rising unemployment in Nigeria, and seeming helplessness on the part of government, the need has arisen to explore even non-traditional triggers of employment growth in the quest for solution. Portfolio investment was chosen on account of its pivotal role in the development of financial market, itself a primary facilitator of employment and investment. Using single equation, reduced form specification, and employing data for the period 1980 to 2014, it was found that in the long term, portfolio investment impacts employment growth positively and significantly. This outcome supports the general view in the literature of a positive relationship between portfolio investment and economic growth, and calls attention to this variable which has hardly been considered in employment generation constructs on account of its famed volatility and risk. Closer efforts to develop the Portfolio-Flow climate were recommended, in particular the cultivation of equity-end portfolio flow and stable foreign exchange regime.

**Keywords:** Portfolio investment, employment growth, unemployment

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## Introduction

Unemployment remains a leading economic problem in Nigeria as in many countries of the world. Locally, its impact is exacerbated by peculiar features of the economy such as high dependency ratio, absent social nets, high population growth and inability truly to key-in and exploit the prospects of globalization. Its importance has not diminished in government-speaks, and through all efforts at development, the achievement of full employment has featured prominently in Nigeria's economic plan.

The magnitude of unemployment in Nigeria as put-out by the authorities is truly modest. National Bureau of statistics, for instance, estimates it at 9.9% for third quarter of 2015 (GTI 2016). This appears to be so because apart from graduates of tertiary institutions, everyone seems to be engaged in something. A great deal of this engagement, however, is quasi-employment whose magnitude is such that supplementary under-employment estimates hardly do justice to the situation. The communication sector is a case in point. A whole army of retailers is engaged in hawking recharge cards, which they promptly abandon once anything with promise shows up. Worse, perhaps, is the situation in the road transport sub-sector. It has a strong pull on youths, but checkmates their skill acquisition prospects, opening for them the unfortunate floodgate to crime via coercion, extortion and violence. Therefore the rate and impact of unemployment in Nigeria appear much worse than the figures suggest. An earlier but more realistic estimate put unemployment rate at 37% (ILO 2012). Given the features of the economy cited earlier, which further deepen the already incisive effects of unemployment on the welfare of the people, unemployment deserves all the attention it can get.

And governments have given some attention to the problem. First, the (rather unsuccessful) demand side approach entailing attempts to curtail future demand for jobs via national population policy. Then the endeavour to drive employment growth through expansion of indirect employment opportunities. This last move has become fashionable world over and entails empowerment of the private sector, encouragement of self-employment initiatives (through skills acquisition for youths and the structurally unemployed), equal gender access to economic opportunities, and micro credit facilitation. Traditional determinants of employment growth have been focused upon also with a view to driving employment generation much faster than population growth. Such traditional determinants include trade flows, investment climate, foreign direct investment, structural diversification of the economy and economic growth, achievable through a variety of sources, in particular export growth and productivity improvement via technology and human capital development. Some measure of attention has gone into all of these areas, even if half heartedly, as it sometimes seemed. Yet employment growth has remained sluggish while population growth has not begun to flag. Unemployment has therefore remained intractable. In the light of this development, it appears plausible that non-traditional triggers of employment growth also deserve to be investigated.

One potential, non-traditional trigger of employment growth is Portfolio Investment (PI). Many do not bother to look in the direction of portfolio investment because it was always perceived as both short tenured and volatile, and largely speculative, and therefore not a plausible source of enduring positive development for employment generation. Equally important, it was always deemed as not directly related to production, especially in the real economy although it is known that production and income can be created in all sectors of the economy, and any sector can lead and sustain growth. Granted that capital flows in the form of portfolio

investment can be not only volatile but had in the past led to surges and waves (IMF 2011) which did hurt economies, thereby creating unemployment, yet in the absence of economic crises, substantial levels of portfolio investment have been maintained on average in some advanced, emerging and even yet-to-emerge economies, for example the US, South Africa and Nigeria respectively. These have contributed to economic well being in those countries including employment generation which helped to roll back unemployment. In addition, except outward cross-border flow of capital via divestment, whether risk induced or in consequence of strategy change, capital flows of portfolio type can logically be traced to production. For example, government development bonds, capital market funding for private sector expansion programmes, fresh capital market listings, etc. To these must be added the equity end of portfolio flow. Ultimately these impact production, hence employment, when they flow in and are productively absorbed in the economy; in the alternative they create or exacerbate unemployment when they destabilize or worsen the crises in an economy. It is conceivable therefore that an enduring impactful relationship exists between portfolio investment, employment creation and unemployment, which could help, if understood and proactively applied in the quest to create employment, reduce unemployment and improve welfare. This study examines how portfolio investment may be related to employment growth in Nigeria and what impact it might have had on it. It is an exploratory work in the portfolio investment/employment generation nexus. The rest of the paper is structured as follows: section 2 reviews related literature while section 3 outlines methodology. Section 4 presents and discusses results. Section 5 concludes.

## 2. Brief Review of Literature

Financial liberalization facilitates capital flows, which can spur growth if inflows that are optimally absorbed, dominate; the economy can also benefit if outflows seek higher yield, and vacate lower yielding engagements. As a consequence, developing countries have been encouraged to eliminate restrictions in order to facilitate flows, which should be dominated by inflows on account of their higher marginal product of capital. Burkiewicz and Yanikkaya (2008) see rapidly growing economies as those to which important volumes of foreign capital flow.

Types of capital flows are not without significance with regard to macroeconomic outcomes. On account of tenor, volatility and risk, among others, Portfolio Investment has not been as well favoured by the receiving economy as Foreign Direct Investment, generally regarded as the most beneficial to developing countries and as such always ranked as first choice. However, the difference becomes narrower when equity-end Portfolio Investments are considered. In such flows, provided they do not supplant domestic investment, they can supplement domestic savings, thereby enlarging production possibilities and employment growth (Ajit 2004). It is even more so when FDI and FPI complement one another.

Portfolio Investments find special relevance in the development of financial markets, whose role in the growth and development of national economies is well established in the literature. It is also well known, thanks to Monetarists, that money does exert its own peculiar pressure on economic outcomes. In the same way, capital flow, in particular Portfolio Investment via financial markets, has brought about notable contributions to the growth and development of many economies, and the employment with which these outcomes are realised. However, much of all these remain uncharted or marginally so in the literature which have continued to focus predominantly on FDIs in the endeavour to tackle unemployment and other macroeconomic challenges. A few examples:

Baghebo and Apere (2014) studied foreign portfolio investment and economic growth in Nigeria from 1986 to 2011 and found that FPI has a positive long run relationship with real gross domestic product.

Using monthly data from 1995:Q4 to 2011:Q7, Sethi (2013) investigated the relationship between foreign capital inflows and economic growth in India. He found a long run equilibrium relationship between economic growth and foreign portfolio investment.

Ekeocha and others (2012) examined the long-run determinants of foreign portfolio investment in Nigeria for the period 1981 to 2010 using quarterly data and distributed lag model and found a positive long-run relationship with market capitalization and trade openness.

Rachdi and Saidi (2011) in their study of the impact of FDI and FPI on economic growth of 100 developing and developed countries over the period 1990 to 2009, found mixed results. First, portfolio investment coefficient was found to be negative and statistically not significant in developing countries, while the reverse was the case for developed countries. Even after including the random effect in a GMM procedure, the coefficient for developing countries while positive, was still not statistically significant.

While the relationship between portfolio flow and growth of the economy has attracted some attention, little has been done in the area of job growth and unemployment. This study therefore takes the exploratory step to establish what role Portfolio Flows play in employment growth in Nigeria.

### 3. Research Method.

We regress employment growth on portfolio investment, controlling for pertinent aspects of the macroeconomy, in particular, population and domestic investment. We take into account the labour practices in the country, wherein in the seemingly dominant informal private sector, a great deal of both under - and over-aged labour market participants are to be found, anchoring the case for labour force as a control for the burgeoning population. As an exploratory investigation, portfolio investment is not disaggregated although it does not appear unlikely that the disparate parts might have distinct effects on employment growth. We carry out diagnostic tests directed at the time series properties of the data and estimate the following model:

$$emplg = \beta_0 + \beta_1rgdp + \beta_2dinv + \beta_3rir + \beta_4inf + \beta_5rer + \beta_6lbfc + \beta_7pi + s$$

Where

Emplg = employment growth

Rgdp = real GDP

Dinv = domestic investment

Rir = real interest rate

Inf = inflation rate

Rer = real exchange yet

lbfc = labour force

Pi = portfolio investment.

E = stochastic error term

Our interest is in the long term effects of portfolio investment on employment growth in Nigeria, if any. Possible long run relationships were investigated using Johansen co-integration procedure, after conducting stationarity tests on all series to establish the need for such investigation. On residuals, normality and heteroscedasticity tests were carried out while specification test was employed to investigate model stability.

### 4. Results, Discussion and Policy Implication.

All series were found to be stationary, if at varying degrees of integration (Table 1). Johansen co-integration procedure revealed the existence of stable long run relationship between the variables, showing six co - integrating equations at 5% level of significance. Residuals proved to be normally distributed using Jacque Burea test, while the White no cross-term hetroscedasticity test showed them to be homoscedastic. RESET indicated the adequacy of model specification

From the long run results (Table 2), all explanatory variables were highly significant at 5% level. Most were also correctly signed. However, an important control variable, domestic investment, turned up with a negative sign. Three issues appear relevant in this connection. First is the enclave nature of the upstream oil and gas sector which, like the downstream sector, is also basically technology intensive, impacting minimally on labour and employment. This is connected with the idea that most jobs in Nigeria are created outside the areas of the greatest investment. The second is the nature of bloated public investment, which appears to rise as employment opportunities dwindle. A case in point is the power sector where in recent decades, trillions of Naira were said to have been invested alongside actual or threatened retrenchment of workers. The third issue is whether domestic investment is supplanted by foreign investment, especially foreign direct investment which we do not however consider explicitly in this study.

Our main variable of interest, portfolio investment, is highly significant as already stated and positively signed. This indicates that improvement in portfolio investment may have a real and supportive effect on growth of employment in Nigeria. To have achieved this outcome, it is implied that the bulk of portfolio investment flow would have found and funded genuine employment creating opportunities, in a non crowding-out manner with regard to domestic investment. Tentative support for this possibility may be seen in the absence of home grown asset bubbles, since the days of internally induced banking crises and consequent recapitalization/consolidation. While that may be so, the main worry with regard to portfolio investment flow, namely the prospect of a sudden stop in inflow and the possibility of a reverse flow, with the attendant challenges for the particular economy, remains the major concern that it is. This can of course be contained, as Nigeria attempted to do during the most recent global financial crises. The degree of success of such containment will depend on the relative volume of the flow as well as the nature of its components.

### 5. Conclusion

As can be tentatively concluded from this study, notwithstanding its well known challenges, namely higher risk and volatility, Portfolio Investment did show a long term positive influence on job creation, the sustenance of which will contribute towards curbing unemployment. In reality this supports the findings of several studies to the effect that Portfolio investment impacts growth positively. It will prove educative if the channel of its effect on growth is uncovered. Meanwhile, we recommend concerted effort to improve the framework for portfolio flow. Aspects requiring urgent attention include macroeconomic stability in the wake of fluctuations in global oil

prices; financial infrastructure (which facilitates capital flow) brought to a level that approximates what is tenable in emerging markets, and improved access to foreign markets via cross-listings. Emphasis should be laid on the equity end of portfolio flows and foreign exchange stability.

Table 1 Stationarity (unit root) test using ADF procedure

Variable	Level	1 <sup>st</sup> difference	Order of integration
Emplg	-0.341716	-4.515531*	I(1)
Rgdp	4.633239*	-2.600638	I(0)
Dinv	-1.509466	-3.316216**	I(1)
Rir	-3.378853**	-6.187244*	I(0)
Inf	-3.289772**	-5.752432*	I(1)
Rer	-2.781459***	-3.581109**	I(1)
Lbfc	3.084347**	-2.113049	I(0)
Pi	-0.176714	-4.006471*	I(1)
Critical	values		
1%	-3.6576	-3.6661	
5%	-2.9591	-2.9627	
10%	-2.6181	-2.6200	

\*, \*\*, \*\*\* signifies significance at 1%, 5% and 10% levels respectively

Table 2: LONG RUN REGRESSION RESULTS

Dependent variable: employment growth

Variable	Coefficient	Standard error	T statistics
Rgdp	0.000187	2.3E-05	8.1304
Dinv	-9.05E-06	1.4E-06	-6.4642
Rir	0.257860	0.03656	7.0531
Inf	-0.136936	0.02402	-5.7009
Rer	0.098063	0.00774	12.6696
Lbfc	-1.644313	0.22014	-7.4694
Pi	0.119667	0.01204	9.9391
C	57.52876		

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