

## ESSA 2009.

- Enhancing the contribution of Foreign Direct Investment to economic growth in South Africa

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## Outline of presentation

- Introduction and background.
- Review of literature.
- Results from other studies
- Mathematical Model.
- Empirical Results.
- Policy implications.
- Conclusion.

## Introduction and background

- ASGISSA objective of halving poverty and unemployment by 2014 by maintaining a growth rate of at least 5% between 2004 and 2014.
- SA developmental challenges, globalisation and potential contribution of FDI.
- FDI inflows remain the largest component of net resource flows to developing countries compared to portfolio investments and loans from international financial markets (UNCTAD, 2006).

## Review of literature.

- FDI contributes to growth via capital accumulation and the transfer of knowledge (technology transfer & diffusion).
- FDI provide channels of communication that stimulate cross-border learning of production methods, product design, organizational methods and market conditions.
- These help to either employ domestic resources more efficiently or to adjust the mix of products so as to obtain more value added per unit inputs.

## Results from other studies.

- Inconclusive about the empirical relationship between FDI and growth.
- Positive but absorptive capacity important (education and human capital stock, developed financial sector or investment in R & D).
- FDI positive effect on TFP growth in developed countries and a negative effect in developing countries (but reverse for capital accumulation). (Kumar & Pradhan, 2002:10).

## Mathematical Model: Augmented Solow Production Function.

- $Y = A K_d^\alpha K_f^\lambda L^\beta H^\gamma$
- $y = a + \alpha k_d + \lambda k_f + \beta l + \gamma h$
- $y = a + \alpha k_d + \lambda k_f + \beta l + \gamma h + \varepsilon$
- $YGR = C(1) + C(2)*RFDI + C(3)*RGFCF + C(4)*RLAB + C(5)*HC$

## Data Sources.

- South African Reserve Bank (SARB) balance of payment and national accounts data bases.
- Real time series values estimated at constant 2000 were used.
- The regression analysis made use of annual data for a period 1946 to 2007.

## Empirical Results.

$$YGR = 1.6 + 0.007*RFDI + 0.235*RGFCF + 0.028*HC (-2) + 0.052*RLAB (-5)$$

Variable	Proxy notation	t-value	$\alpha$ significance.	$\alpha/2$ significance
Growth rate of foreign capital	RFDI	2.109530	2.052(97.5 %)	2.052 (95%)
Growth rate of domestic Capital	RGFCF	5.892098	3.421 (99.9 %)	3.421 (99.8 %)
Growth rate of Human capital	HC	1.050162	0.684(75%)	0.684(50%)
Total labour force	RLAB	1.584194	1.314(90%)	1.314 (80%)

## Some Policy implications.

- Positive but not too significant contribution of FDI compared to other factor inputs.
- Attract FDI into other sectors of the economy like manufacturing and agriculture that are intensive in the usage of unskilled labour
- Address internal constraints (unemployment and labour market rigidities).
- Diversification of economy and value adding processing of primary products.

## Enhancing the Contribution of FDI.

- An education and basic skills provision system will ensure a suitable atmosphere for absorbing technologies.
- Industrial policy that encourages the inflow of new technologies and capital while ensuring promoting the development of domestic entrepreneurial skills.
- Investment in the promotion to market the image of the country, identify potential investors and focus resources towards distinguishing the economy as an ideal investment location.
- Enforcement of effective competition policy to regulate the activities of foreign enterprises in order to mitigate their impact on market structure.

## Conclusion.

- FDI can play a role under appropriate conditions and if 'right kind' attracted to 'right sectors'.
- FDI is unlikely to turn around an economy, which is in dire situation, but providing the right institutional framework may be a prerequisite to channeling FDI and the activities of Multinational companies to further national development goals (Mold, 2004:93)