# ECONOMIC CONVERGENCE AMONGST ECOWAS MEMBER COUNTRIES: THE ROLE OF FOREIGN DIRECT INVESTMENT

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ECONOMIC CONVERGENCE AMONGST ECOWAS MEMBER COUNTRIES:
THE ROLE OF FOREIGN DIRECT INVESTMENT

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**ABSTRACT**

The phenoma of per capita income convergence has a lot of welfare implications. FDI is identified as a principal candidate for technology transfer to developing countries. However, the distribution of FDI is observed to be highly skewed in favour of limited number of countries. Africa in general, and ECOWAS in particular, perfromed poorly in FDI attraction compared to other countries. ECOWAS is also characterized by huge within group gap both in terms of FDI and real GDP per capita. Using data spanning from 1970 – 2014, this study investigates the relationship between real GDP per capita and FDI for a sample of 15 ECOWAS countries. The study employs SURADF procedure to investigate on absolute convergence within each income group as well as convergence within ECOWAS at large. It is observed that seven economies tend to converge to the group average real GDP per capita, of which only one is a low-income. On the speed of convergence, the study reveals that relatively poor economies tend to catch up with relatively richer economies in the group at 1.10 percent, a rate considered very slow. The study further reveals that FDI plays a significant role in facilitating per capita income convergence amongst ECOWAS member states. Investigation of the role of FDI in attaining across group convergence for ECOWAS and each income group also yields results showing a sharp difference between the two income groups. Low income countries have positive and significant relationship between FDI and convergence as opposed to the case of lower middle income. The policy implications of these findings is that ECOWAS countries need to implement policies that would aid FDI attraction as well as ensure adequate absorptive capacity, which is an important condition to reap the benefits of FDI.

**Keywords**: GDP per capita, convergence, FDI, ECOWAS, SURADF

# ABSTRAK

Fenomena penumpuan pendapatan per kapita mempunyai banyak implikasi dari aspek kebajikan. FDI dikenal pasti sebagai penyumbang utama pemindahan teknologi kepada negara-negara sedang membangun. Walau bagaimanapun, pengagihan FDI didapati sangat condong ke arah beberapa buah negara tertentu sahaja. Afrika secara umumnya, dan negara-negara ECOWAS secara khususnya didapati agak lemah dalam aspek tarikan FDI berbanding negara-negara lain. ECOWAS juga dicirikan mempunyai jurang yang besar dalam kumpulan dari segi FDI dan KDNK per kapita. Dengan menggunakan data yang terangkum sejak tahun 1970 hingga tahun 2014, kajian ini menyelidik hubungan antara KDNK per kapita dan FDI bagi sampel 15 negara ECOWAS. Kajian ini menggunakan prosedur SURADF untuk menyelidik penumpuan mutlak dalam setiap kumpulan pendapatan serta penumpuan dalam ECOWAS secara amnya. Dapatan kajian mendapati terdapat tujuh ekonomi tertumpu kepada purata pendapatan KDNK per kapita sebenar, dan hanya satu didapati berpendapatan rendah. Dari segi kelajuan penumpuan, kajian ini mendapati bahawa negara berekonomi lemah cenderung untuk mengejar negara berekonomi lebih kukuh dalam kumpulannya pada kadar 1.10 peratus, yang mana dianggap sebagai sangat perlahan. Kajian ini seterusnya mendedahkan bahawa FDI memainkan peranan penting dalam memudahkan penumpuan terhadap pendapatan kapita dalam kalangan negara anggota ECOWAS. Penyelidikan terhadap peranan FDI terhadap penumpuan kepada keseluruhaan kumpulan ECOWAS dan pendapatan setiap kumpulan juga menghasilkan keputusan yang menunjukkan perbezaan yang jelas. Negara yang berpendapatan rendah mempunyai hubungan yang positif dan signifikan antara FDI dan penumpuan yang mana bertentangan dengan negara yang berpendapatan sederhana rendah. Implikasi dasar penemuan ini adalah negara ECOWAS perlu melaksanakan dasar-dasar yang dapat membantu tarikan FDI serta memastikan keupayaan penyerapan yang mencukupi memandangkan hal ini merupakan keadaan yang penting untuk meraih faedah daripada FDI.

**Kata kunci**: KDNK per kapita, penumpuan, FDI, ECOWAS, SURADF

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## LIST OF ABBREVIATIONS

| **Abbreviation** | **Full Meaning** |
|---|---|
| ADF | Augmented Dickey-Fuller |
| DCs | Developed Countries |
| ECOWAS | Economic Community of West African States |
| EEC | European Economic Community |
| EU | European Union |
| FDI | Foreign Direct Investment |
| GDP | Gross Domestic Product |
| GMM | Generalized Method of Moments |
| IPS | Im, Pesaran and Shin |
| LDCs | Less Developed Countries |
| LI | Low Income |
| LM | Lagrange Multiplier |
| LMI | Lower Middle Income |
| OECD | Organization for Economic Cooperation and Development |
| OLS | Ordinary Least Squares |
| RFDI | Real Foreign Direct Investment |
| RGDP | Real Gross Domestic Product |
| SSA | Sub-Saharan Africa |
| SURADF | Seemingly Unrelated Regression Augmented Dickey-Fuller |
| UNCTAD | United Nations Conference on Trade and Development |
| UNECE | United Nations Economic Comparison for Europe |
| USA | United States of America |
| USD | United States Dollars |
| WAC | West African Countries |
| WDI | World Development Indicators |

# CHAPTER ONE

# INTRODUCTION

## 1.1 Introduction

This chapter consists of ten sections. It serves the purpose of introducing the entire research. Section 1.2 provides background and motivation for conducting the study. While Section 1.3 consists of problem statement, Section 1.4 presents a number of research questions which are translated into objectives of the study as contained in Section 1.5. Significance of the study is provided in Section 1.6. Study area is highlighted in Section 1.7. Scope of the study is highlighted in Section 1.8. Finally, while Section 1.9 explains organization of chapters for the entire research, Section 1.0 concludes the chapter.



## 1.2 Background and Motivation of Study

Issues surrounding economic growth, its determinants and convergence[1] among countries of the world and regions have received remarkable attention of researchers (Crespo-Cuaresma, Foster & Stehrer, 2011). Beside its human welfare effects, the phenomenon of income/growth convergence is considered as an avenue to testing the validity of alternative economic growth theories (Islam, 2003). Despite the re-emergence of interest in the debate on growth convergence and its determinants, consensus among economists appears to be impossible. In the view of United Nations

[1]The term convergence refers to an economic phenomenon where poor countries tend to grow faster than the richer ones over the long run. Convergence is said to be absolute or unconditional when the gap in the output growth between richer and poor countries vanishes over time regardless of the differences in observable characteristics of the countries. On the contrast, convergence is regarded as conditional if the reduction in the gap depends on certain observable characteristics of the countries.

The contents of the thesis is for internal user only

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