

# The Effect of Governance Quality on Foreign Direct Investment Flows into Sub-Saharan Africa

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## ABSTRACT

*We examine the relationship between quality of governance and the flow of foreign direct investment (FDI) into Sub-Saharan African (SSA) countries for the period 1996 - 2004. The study indicates that the presence of raw materials and markets account for the bulk of FDI flows into SSA. However, the quality of governance appears to be increasing in importance in attracting foreign investment to the region. This is evident in the less resource-endowed countries. Governance-FDI relationship in SSA appears consistent with the trends elsewhere, suggesting congruency in global investment requirements and underscoring the need for SSA to develop and strengthen governance mechanisms for a competitive investment environment.*

## INTRODUCTION

A major characteristic of the global economy in recent decades has been the explosive growth in foreign direct investment (FDI) flows. Unfortunately, these flows have been regionally uneven. Between 1994 and 1997 the developed countries received 58 percent of the global FDI inflows while Sub-Saharan Africa (SSA), a huge triangular region of 47 countries, home to roughly 10% of the global population, received only 2.3 percent in 1994 that dropped to 1.2 percent by 1997 (UNCTAD, 1998). Its share of global FDI plummeted below 1 percent by 1998. In perspective, the whole of Africa received \$8.3 billions in FDI compared to Korea's \$5 billions and China's \$45 billions (UNCTAD, 2003). Further, the World Bank (2000) estimates a rapid decline in Africa's share of global FDI flows.

SSA's inability to attract FDI is attributed to a myriad of factors, including fragmented small markets, low incomes, political instability, corruption and general inefficiencies (Ndikumana, 2003). These factors create a hostile investment environment leading to higher political and economic risks (UNCTAD, 2004). This fact and the vital role of FDI in economic development have prompted aid, lending agencies and other supranational organizations (e.g., the World Bank, IMF, and the UN) to pressure SSA countries to address the perceived hostile or unattractive investment climate. Several countries have responded with policies aimed at reducing political instability, corruption and endemic inefficiencies in order to create enabling environments and good governance (Morisset, 2000). The question then is: Are SSA countries perceived as well-governed, where the rule of law, established institutional structures, intolerance for corruption, effective government machinery and general stability are the norms, more likely to receive FDI than their poorly governed counterparts? We review empirical data from the region to address this question.

The link between governance and FDI flows is not new but empirical investigation is relatively recent in the business literature. A sample examination of this relationship is offered by Globermann and Shapiro (2003) who used a probabilistic model to examine the importance of governance infrastructure in determining US investment outflows. Similarly, Morisset (2000) developed an FDI "business climate" index for 29 SSA countries that he used to demonstrate an association between "openness to international trade" and FDI inflows into Mali and Mozambique. We build upon these studies to analyze the FDI/governance linkage in SSA.

The Globermann and Shapiro study appears to suggest a predisposition of potential US investors towards certain investment destinations. However, it is unclear whether such a disposition is shared by non-US investors who are likely to invest in SSA. Since non-US investors account for the bulk of FDI into SSA, we need to examine whether these investors hold similar expectations of their investment destinations as the US investors who invest elsewhere. Similarly, it is unclear whether the association between Morisset's "FDI environment" index and anecdotes of "openness to international trade" from two countries demonstrates definitive linkage between FDI and the gamut of governance

variables across SSA. Thus, we need to review the efficacy of Morisset's index and the applicability of the FDI/openness to international trade linkage noted in Mali and Mozambique to the other elements of governance throughout SSA. Therefore, our objective is to examine FDI/governance linkage in SSA by broadening data beyond Mali and Mozambique and covering a longer period for a broader range of governance variables. The rest of the paper is organized as follows: The section below provides a review of the relevant literature, followed by a definition of the elements of governance, a discussion of research methodology and results, and a conclusion.

## LITERATURE REVIEW

Early FDI theories attributed FDI to the search for factor or resource endowments. FDI flows were therefore categorized as resource-seeking, market-seeking or efficiency-seeking (Dunning, 1997). However, (Porter, 2006) has claimed that recent developments in the global economy including the growth of multinational enterprises, improvements in communication and other technological advances, as well as the increased pace of globalization have made factor or resource-endowments less relevant as drivers of investment flows. In other words, in the current global economy, hitherto salient parameters have increased in significance in directing FDI flows (Buckley, et. al, 2007; UNCTAD, 2004).

A stream of recent research (e.g., Chan, Makino, and Isobe, 2006) points to multi-dimensional competitive forces that drive multinational corporations' FDI decisions; inducing them to seek investment environment with potential externalities and prospects for efficiency gains beyond the traditional FDI stimulants. For instance, rampant outsourcing, networking, inter-organizational and technological advances appear to open investment opportunities in new areas and loosen the location-specificity of investment decisions. The indication is a shift in global FDI trends. According to UNCTAD (1999), global FDI stock data indicate a shift from manufacturing to service with the bulk of international production in the developed countries tending to the service sector while those in developing countries have shifted from extraction to manufacturing. That is, FDI in basic production is declining in the developed markets while FDI in the service sector is gaining importance even in the developing countries thereby elevating the significance of institutional parameters such as governance in FDI decisions.

The growing significance of institutional factors in FDI decisions is apparent among investors. According to Kearney (2004), 36 percent of the global investors consider global or regional trade initiatives to be the most likely factors that impact their FDI decisions while 34 percent consider government regulation or governance more important. The prominence of governance to these foreign investors and the noted shift of global FDI from basic production to service are indicators of the growing association between governance and FDI. The association can be particularly important for developing countries as Kearney's data shows that developing countries constitute about one-half of the twenty five global favorite FDI destinations. However, these FDI favorites are not the most resource-endowed among the developing countries. Apart from a large potential market, the distinguishing feature of the top four developing countries (Brazil, China, India, and Mexico) consistently favored by foreign investors since 1998 appears to be the elements of governance such as aggressive market liberalization and political/social stability (Kearney, 2004).

The prioritization of governance among investors accounts for a probable negative association between elements of poor governance and FDI. According to Habib and Zurawicki (2002), who used FDI of seven countries with varying levels of Corruption Perception Index developed from a group of 89 (developed, transition, and developing) countries for three years, corruption and political instability dampen FDI. From this probable governance/FDI association, we can conjecture that otherwise resource/market comparable SSA countries with relatively effective governments, stable institutions that are well-governed, relative political stability, rule of law, regulatory quality, and less graft, are likely to receive more FDI than their relatively poorly-governed counterparts. We develop this conjecture in the following section.

### Governance

Although governance is a broad concept, it is rooted in government and all that emanate from public institutions and policies created by governments as a framework for economic, legal and social relations (Globerman and Shapiro,

2003). Following Kaufmann, et al. (1999) broad categorizations of the rule of law, government effectiveness and graft as adopted by Globerman and Shapiro (2003), we confine ourselves to the elements of governance that are peculiar to developing countries such as found in SSA that can create a hospitable investment environment. While pragmatically efficient, this approach belies the complexity that characterizes information collection from institutions in such a data-deficient source such as SSA. For instance, some SSA countries like Somalia and Congo did not and still do not even have functioning governments—the primary source of laws and governance. Some countries like Rwanda, S. Africa, Angola, Mozambique, and Liberia just emerged from conflict/civil strife and upheavals during the data period while the rest operated under nominal governments with barely credible institutions (Maathai, 2009). Thus, the basic elements of governance adopted here only serve as useful surrogates in SSA.

We estimate the quality of governance to include: Voice of accountability (VOICE) that measures civil liberties, press and political freedoms; Political stability (PSTAB), a measure of political instability, potential for terrorism and violence; and Government effectiveness (GEFFECT) that measures the quality/efficiency of government and public administration. The other measures are: Regulatory effectiveness (REGEF) that is the extent of economic and financial regulation; Rule of law (LAW), a measure of the rule of law, enforceability of contracts; and Graft or corruption (GRAFT) measures the extent of corruption in government and private institutions.

According to Globerman and Shapiro (2003), these meta-indices provide a more precise measure of governance than individual indicators. However, they are estimates of subjective perceptions and are thus subject to measurement errors. Furthermore, high levels of correlation among these measures preclude their use in a single equation. Therefore, they suggest the necessity for creating a first principal component by aggregating the measures, that is, the Quality of Governance Index (QGI). This index possesses greater representation faithfulness than the separate governance measures.

## DATA AND METHODOLOGY

To analyze the data, we specified the following model:

$$\text{LFDI}_{it} = \alpha_0 + \beta_1 \text{GOVERNANCE}_{i,t} + \beta_2 X_{i,t} + \varepsilon_{it-1}, \quad (1)$$

where, LFDI is the natural log of FDI inflows into country  $i$  in period  $t$ ,  $\beta$  is the parameter to be estimated, GOVERNANCE is an aggregate index of governance variables,  $X$  is a vector of control variables; and  $\varepsilon$  is a normally distributed error term. The lag in the error term is attributed to the fact that investment decisions are made ex-ante.

Theoretical and empirical literature indicates a number of control variables that influence FDI flows. For instance, host country market size (SIZE) -- proxied by GDP, is known to influence FDI flows (UNCTAD, 2001; Root and Ahmed, 1979). In this study, we use the natural log of GDP per capita to control for host country market size. Similarly, openness (OPEN) to trade and investment, defined by the formula (Exports + Imports)/GDP has been found to influence investment flows (Goldberg and Gross, 1994). It is also possible that communication infrastructure (access to telephone services) has bolstered data processing/management investment decisions (Morisset, 2000). Therefore, we control for this element by the number of phones available in a country. It is possible that the number of phone and/or computer users might provide a better proxy for communication infrastructure but given SSA's technological lag, this might be likely for later data periods beyond 2004. Finally to control for natural resource endowments such as oil and mineral reserves (traditional FDI stimulants), we use a dummy variable, "1" indicating the presence of such resources in the host country or "0" to denote their absence.

We believe that a country's stock of physical and financial infrastructure generally correspond to resource-endowment (Porter, 1990) unless mitigated by poor governance as has been the case of SSA "curse of natural resources" -- endowments mired in unproductive conflict and corruption (Sachs and Warner, 2001). Thus we assume these factors are captured in the resource-endowment dummy and they are not controlled separately in the model. Other factors that can influence FDI inflows to a country include the level of privatization, generally associated with 'openness' to investors of hitherto closed markets in emerging economies. Indeed, foreign investors have been known to target former state-owned enterprises following market liberalizations. In SSA, state-owned or parastatal enterprises, normally set up to manage or market products from the natural resources, have been associated with inept management

by corrupt government officials and their cronies, resulting in general citizen dissatisfaction and occasional public uprisings. Some SSA countries have squelched such citizen discontent while others have responded by yielding the control of these enterprises to private investors, a response that corresponds to the *voice of accountability* element of the governance variable and the *openness to international trade* control. Thus, we assume the level of privatization in SSA is not a separate variable but a consequence of general civil liberty, and government accountability to its citizens leading to openness to investors as captured by the *openness to international trade* control. It is also possible that inflation played some role in SSA FDI inflows. However, since the data is compiled in the US dollar and for the same period, potential inflation effect is probably comparable across the sample countries unless confounded by a country's fiscal/monetary policies, both rubrics of the *government* and/or the *regulatory effectiveness* elements of the governance variable.

Following the discussed trends that indicate increasing importance of governance to foreign investors in the 21<sup>st</sup> century, we collect data from the close of the 20<sup>th</sup> century at the peak of globalization. We also choose alternate years between 1996 and 2004 to provide observations for five different years that represent this period. The 1996-2004 period is ideal since FDI research indicates that 1990s denote the reemergence of institutional factors as important FDI influencers in the developing world (Kearney, 2004; Cleeve, 2005; UNCTAD, 2000). "Governance" regained theoretical importance among FDI researchers leading various agencies to start assembling such data in the 1990s. Thus it is hard to obtain reliable governance data for developing countries that predate the 1990s. Furthermore, since related empirical data such as Morisset's (2000) and Gliberman and Shapiro's (2003) capture early 1990s trends, we build upon these and start with data from the 1996-1997 period. The end period (2004) is based on the latest complete data availability and the five year period corresponds to the secondary data compilation regime. We are assuming that in response to supranational agencies such as the IMF, the UN, and declining donor funding, as well as the *Asian Tigers* examples, most SSA refocused their attention on FDI and started addressing their disposition toward related factors about early 1990s. It is possible that not all sample countries started addressing governance issues at the same time, but generally, these countries tend to experience similar trends (e.g., the sixties wave of decolonization), competed and sought development funds from similar sources about the same period (UNCTAD, 2003).

We obtained data on the thirty nine SSA countries(Exhibit A) used in the study from several sources including the United Nations Conference for Trade and Development (UNCTAD), the World Bank's Development Indicators, the CIA World Fact Book, and the IMF International Financial Yearbook. The "Openness to international trade" data was obtained from Penn World Tables and we reconstructed missing data where possible by using relevant information from other sources to compute the missing data (e.g., divided host country's total GDP by its total population to obtain "GDP per capita"). Following is a discussion of the analytical procedure and the results of our analysis.

### Analytical Procedure and the Results

We used STATA 7 software to run GLS regressions on the time-series cross-sectional data on the thirty nine SSA countries. The GLS regression is ideal for managing autocorrelations (AR1) and multicollinearity problems (Hamilton, 1998). Table 1 below provides the descriptive statistics and bivariate correlations among the governance variables.

**Table 1: Descriptive Statistics and Correlation Matrix**

Variable	Mean	S. D.	1	2	3	4	5	6	7	8	9
1 Voice	-0.57	0.74									
2 Political stability	-0.59	0.96	.71***								
3 Government effectiveness	-0.62	0.64	.72***	.69***							
4 Regulatory quality	-0.49	0.7	.71***	.73***	.80***						
5 Rule of law	-0.59	0.97	.48***	.53***	.56***	.52***					
6 Graft	-0.57	0.57	.59***	.55***	.70***	.58***	.48***				
7 GDP per capita	1107.2	1424.7	.48***	.41***	.49***	.45***	.49***	.48***			
8 Openness	67.08	36.79	0.04	.20*	0.04	.03	.09	.20**	.34***		
9 Raw materials	0.28	0.45	-.23**	-.37**	-.25**	-.24**	-.14*	-.19**	.09	-.01	
10 Phone infrastructure	42.24	88.56	.41***	.29***	.44***	.33***	.41***	.42***	.45***	.14*	.06

\* $p < .05$ , \*\* $p < .01$ , \*\*\* $p < .001$

The table indicates that the bivariate correlations range from 0.48 (between the “Rule of Law” and “Voice” and between the “Rule of Law” and “Graft”) to 0.80 (between “Government effectiveness” and “Regulatory quality”). Such high correlations indicate the possible presence of collinearity, precluding the use of the variables simultaneously. Multicollinearity may lead to inflated standard errors, and subsequently make parameter estimates less efficient. However, this does not bias the parameter estimation (Cohen and Cohen, 1983). Again, since all the variables mattered in defining the concept of governance, they all had to be included.

Table 2 shows the regression models for the SSA data starting with the control variables, raw materials (e.g., oil), level of income (GDP per capita), openness of the economy, and telephone infrastructure in Model 1. This model result is consistent with the literature (UNCTAD, 2001; Root and Ahmed, 1979; Goldberg and Gross, 1994).

**Table 2: GLS Regression Results**

Variable	Model 1	Model 2	Model 3
Intercept	1.9674 (.7702)*	4.1151 (.9716)**	3.8938 (.9779)***
Raw Materials	1.3389 (.2570)***	1.65929 (.2817)***	1.7406 (.2828)***
Log of GDP per Capita	0.2276 (.1282)*	-0.0789 (-.1482)	-0.0252 -0.1496
Openness	0.0011 -0.0034	0.0051 (-.0035)	0.0025 (-.0033)
Telephone Infrastructure	0.0023 (.0014)*	0.0093 -0.0015	0.0008 (-0.0015)
Voice		-0.0669 (-.2522)	
Political Stability		-0.2479 -0.2043	
Government Effectiveness		0.3171 -0.3503	
Regulatory Quality		0.8106 (.2941)**	
Rule of Law		0.0792 -0.1467	
Graft		0.0454 -0.2813	
Governance			0.1314 (.0426)***
<i>N</i>	197	197	197
Log Likelihood	-363.47	-372.6	-367.96
Wald $\chi^2$ (4, 10, 5)	66.27	42.96	54.54
$p > \chi^2$	0	0	0

Model 1 shows statistically significant relationship between the presence of raw materials and FDI that indicates the continuing strength of raw materials in stimulating FDI in the SSA region. This model also shows a weak statistical significance between market size and communication infrastructure and FDI flows in the region—reassuring indicators of a fledgling SSA market and outsourcing potential (given the weak measure of communication infrastructure used).

To estimate their coefficients in Model 2, governance variables were introduced one by one in a stepwise fashion due to their high inter-correlation that precludes their simultaneous inclusion in one regression model. Table 2 shows that when entered separately (Model 2), the only governance variable that indicates a statistically significant impact on FDI is regulatory quality. In fact, regulatory quality appears to have a stronger impact on FDI that overshadows the modest impacts of market potential and communication infrastructure noted in Model 1 earlier. That is, it appears appropriate economic and financial policies are so critical to foreign investors that without them they would overlook market and outsourcing potential in a SSA country in preference for its neighbor that offers adequate regulatory quality albeit with a lower market or outsourcing potential.

As predicted, when the aggregated GOVERNANCE index (composite of the governance variables) is substituted, the coefficient of the index shows statistically significant impact on FDI in the full Model (3). These results appear consistent with the conjecture that developing countries from Sub-Saharan Africa that are perceived as “well governed” in terms of regulatory quality or government effectiveness are more likely to receive FDI than their similarly endowed counterparts that are perceived as poorly governed in these respects.

## DISCUSSION OF THE RESULTS AND IMPLICATIONS

The results indicate that quality of governance is an important factor in the flow of FDI into SSA. That is, at a time when investors are wary because of complexity and uncertainty about global opportunities, perceived good governance, specifically, government effectiveness and regulatory quality could serve to “sooth their nerves” to channel FDI into a SSA country away from a neighbor that promises natural resources but without the assurance of adequate governance. These findings make common sense and are (surprisingly) consistent with Globerman & Shapiro’s (2003) findings even though theirs focused on the impact of governance institutions in the U.S. on FDI outflows during the 1994 -1997 period. We did not expect our results to mirror Globerman and Shapiro’s study for a number of reasons.

First, we selected elements of governance in the context of developing countries rather than the established governance institutions in a developed country. The fact that these show similar trends, indicates that American or not, global investors seem to expect investment destinations, whether developed or developing economy, to offer certain basic effective governance institutions or they shop elsewhere for their investment. Since investors are rarely philanthropic (unless it serves their economic interests), SSA countries can ill afford to ignore this lesson under the guise of “infant economy” or “poor nation” status as their well-governed neighbors begin to offer similar endowments that investors seek. The lesson is particularly noteworthy for well-endowed but poorly governed countries like Nigeria (inadequate electric power policy, corruption, and insecurity) that has started to see investors (foreign and domestic) shift to neighboring Ghana with the discovery of oil (see Dogberi, 2009; GIPC, 2009; Ghana Business News, July 9<sup>th</sup> 2009); the Kenyan tourism industry, once the *Safari* showcase and global investor delight, yielding ground to S. Africa and Tanzania, on account of poor governance (corruption) and insecurity; and Zimbabwe’s haphazard land policy that has diverted its commercial farmers to neighboring S. Africa, Zambia, and even further Northwest to Nigeria.

Secondly, we did not expect Globerman & Shapiro’s data to be reflective of the countries in our dataset since U.S. FDI flows to Africa are known to be relatively small and concentrated on some few natural-resource-endowed SSA countries. For instance, the U.S. Department of Commerce data indicate that U.S. FDI outflows to the SSA region has been going mainly to three or four of the 39 SSA countries in our dataset: Liberia - probably a legacy of historical ties with the U.S.; Angola - the presence of oil; Nigeria – the presence of oil and a large market; and South Africa – the presence of minerals and a large market. Moreover, Globerman and Shapiro’s probabilistic model sought to determine the likelihood of U.S. FDI based on a host country’s governance institutions at a period when most developing countries in our dataset were struggling with the establishment of such very institutions. Thus, it was unclear whether a five-year time lag since Globerman and Shapiro data would be sufficient for the establishment of these institutions and the subsequent foreign investor response that can be picked up in a statistical analysis in regions where data quality is normally problematic.

The fact that the trends observed for governance and U.S. FDI outflows are applicable to developing countries, where U.S. constitute only a small percentage of total FDI, the bulk of which come from various other countries, could indicate the perverse nature of elements of the governance-FDI linkage. It informs us that regardless of their home countries, foreign investors in SSA may value basic governance (i.e., government and regulatory effectiveness) in the host countries equally. Perhaps, basic governance in a host country (developed, transitioning, or developing) is indicative of a non-negotiable conducive investment environment to foreign investors. If this is the case, then the governance/FDI question becomes an empirical quest of what particular foreign investors consider “basis governance” in particular host countries. A situation that makes our results reconcilable with the suggestion that investors merely compensate for poor governance in an otherwise attractive host country by demanding higher return for the elevated risk (Click, 2005); or that investors self-select so that those from poorly-governed (corrupt) countries invest in equally

poorly-governed host countries (e.g., Cuervo-Cazurra, 2006). Further, such subjectivism may lead certain investors to view elements of “poor governance” such as “corruption” as mere “cost of doing business” in certain host countries so that sometimes corruption enables firms to get what they want easily through bribery or lobbying. Then perhaps we can explain the high FDI flows into certain countries generally considered corrupt such as China and Nigeria.

These results are based on FDI data from all sources to a subset of developing countries that account for a small percentage of global FDI inflows, yet we can conjecture, given the consistency with earlier studies that covered the bulk of the global FDI flows, that the level of investment may not mitigate the importance of governance (as defined here) to global investors. Further, the results are consistent with the trends indicative of enduring dominance of raw materials as FDI stimuli in SSA although governance is playing an increasingly important role in differentiating not only among these countries (UNCTAD, 1999; Ndikumana, 2003) but also between these and the developed countries (Kearney, 2004). It is noteworthy, that the preferred developing countries that are favored FDI destinations are not necessarily the most naturally endowed resource wise, but rather, investors also seem to be looking for environments where the institutions of governance are perceived to work (Kearney, 2004).

In an environment where the institutions of governance work, investors have less fear of investment loss due to political instability or threats of expropriation. The existence of the rule of law in such an environment means that business contracts can be enforced by the courts, further assuaging any fears investors may have about the loss of their investments. High levels of government and regulatory effectiveness would also imply that it may be easier to navigate the labyrinthine bureaucratic structures found in developing countries. In other words, in countries with good governance, it may be easier to deal with bureaucrats, who may also be less corrupt. Also, in such environments, there may be few impediments in the way of profit repatriation. In sum, the presence of these governance variables in a country would collectively act as an additional magnet in attracting investments into a SSA country.

## CONCLUSION

### Lessons and New Directions

The traditional FDI stimulus of raw materials (mostly hydrocarbons) and potential large markets are still important in directing FDI flows into SSA. Nevertheless, the opening of other regions with similar endowments worldwide makes these insufficient in attracting FDI. The study indicates that increasingly, investors are looking for well-governed and safe environments for their investments. This implies that in addition to aggressive developing of the abundance endowments, the creation of an attractive investment environment through good governance in a region known for corruption, political instability and mismanagement can stimulate FDI flows. Sub-Saharan African countries therefore need to strive to strengthen their governance institutions to create investment enabling environments in order to compete for global investment flows commensurate with their needs.

The dynamics of global competition go beyond resource endowments to encompass efficiency in transforming the resources to output, large markets with sophisticated and demanding customers resulting from productive long durations of participating and interacting with forces emanating from externalities outside policy mandates (Porter, 1990). In such an environment, governance is just an assurance to “glue” FDI to a particular SSA host country. Thus, governance quality is an efficacious tool that SSA countries can employ to ameliorate the perennial and endemic investment capital shortages that characterize these economies and to diversify their FDI base beyond resource and market seekers. That is, to compete for the global investment capital, it is insufficient to be resource-endowed, have an open economy, a large market, physical, and telecommunication infrastructure. Rather, these are ‘survival’ factors that are necessary and a ‘must have’ for Sub-Saharan African countries, but they must also be perceived as well-governed, with enabling investment climates that offer externalities and potential efficiency gains that are comparable to the developed and transitioning economies. To this end, economic managers or policy makers in SSA countries must formulate and implement policies that reduce the level of corruption, promote government and regulatory effectiveness, ensure the rule of law and create politically stable environments. When this is done then investor assurance for competitive returns and the safety of their investments could sway them from poorly-governed relatively endowed hosts to their relatively well-governed neighbors.

A few limitations of this study are worth noting. First, a motive of the study—to address the perennial lack of empirical data on which to base understanding of SSA also became its major challenge. Based on archival data compiled through (government) agencies, the very subject of the study, from a data-challenged region of the world, lack of data on some countries became a bottle-neck and necessitated the omission of some countries from the dataset. Sometimes even the unit of analysis—country, was challenging as in the case of Somalia that disintegrated into several war-lord domains with non definable data source, or Eritrea that split from Ethiopia, all within the data period. Secondly, governance and its constituent variables were aggregated for all SSA countries. This is an oversimplification because the quality of governance varies considerably across SSA countries. Countries such as Botswana and South Africa have a relatively high quality of governance whereas others such as the Democratic Republic of Congo and the Sudan rank at the bottom of global governance measures. A third limitation is that the study covered a relatively short period of time from 1996 to 2004, resulting in only five data points. This may be inadequate for a study of institutional factors that evolve over time.

In spite of the above limitations, our study contributes to the institutional theory-FDI literature in several ways: First, to examine the relationship between FDI flows and the quality of governance, we utilize inter-temporal changes in the quality of governance in selected countries that hitherto belonged to the “black box” or the “dark continent” as far as this stream of literature is concerned. We also apply the concept of governance longitudinally to examine its effect on FDI flows. Thirdly, by using data from late 1990s to the present, we capture unique and contemporary changes in SSA, which if linked to FDI, can prove insightful to the ongoing discourse on reforming SSA into a more competitive investment destination. It is an anomaly for over 10 percent of the global population endowed with abundance natural resources to entice less than 1 percent of global FDI. To the extent that poor governance contributes to this anomaly, it behooves us to have an honest look at governance in SSA, and toward such effort is this study directed. Finally, the study contributes to the pool of data that informs our understanding of the governance-FDI relationship in various regions of the world.

We foresee future productive research in this area as deciphering specific elements of governance practices peculiar to this region and categorizing SSA countries into well-governed and poorly-governed with their respective potential for attracting specific foreign investors. Possible insights may also attend to a comparative study of this region and other developing regions, such as South America and SE Asia, to draw parallels and possible lessons for SSA that continues to lag behind the rest of the developing world in attracting FDI.

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#### Appendix A: List of countries used in study

1	Angola	21	Madagascar
2	Benin	22	Malawi
3	Botswana	23	Mali
4	Burkina Faso	24	Mauritius
5	Burundi	25	Mozambique
6	Cameroon	26	Namibia
7	Central African Rep.	27	Niger
8	Chad	28	Nigeria
9	Congo (Brazz)	29	Rwanda
10	Congo Dem. Rep.	30	Senegal
11	Cote d'Ivoire	31	Sierra Leone
12	Ethiopia	32	South Africa
13	Gabon	33	Sudan
14	Gambia	34	Swaziland
15	Ghana	35	Tanzania
16	Guinea	36	Togo
17	Guinea Bissau	37	Uganda
18	Kenya	38	Zambia
19	Lesotho	39	Zimbabwe
20	Liberia		