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**PhD. Thesis**

**Impact of Governance Structures and Tax Incentives on  
Foreign Direct Investment: Evidence from Africa**

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Doctor of Philosophy

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Dedicated to my family...

I thank Almighty God for bringing me this far, and I dedicate this dissertation to my lovely mum Gifty Afia Fofie for her encouragement, prayers, and support. I also dedicate this to my entire family; especially Mr. Seth Nana Appiah Kubi, Mr. Felix Otto Fofie, Helena Wiredu, Mary Owusu Bempah, Mrs. Henrietta Opoku Mensah, Ben Agyei-Mensah, and my lovely wife Sandra Boatemaa Kutin, whose encouragement, patience, and support made this effort possible.

**Declaration**

I now declare that I have worked on my Ph.D. thesis titled " The impact of Governance Structures and Tax incentives on Foreign Direct Investment: Evidence from Africa" out of my effort, and I have used only the sources mentioned at the end of the thesis. As the author of the Ph.D. thesis, I declare that the thesis does not break any copyright.

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## **Abstract**

Foreign Direct Investment (FDI) has become a common goal for developing economies as it is not only a source of financing but also an important source of employment and technology. Given the role that foreign direct investments play in the economic development process, African countries have faced competition in attracting foreign direct investments. African economies are significant since they are large and quickly rising economies that have pursued foreign direct investment strategies. This has been backed up by effective governance structures and other incentives, although these initiatives have been in place for more than fifty years, their effectiveness is still controversial.

Given several factors that work against the business climate for foreign speculations, a few efforts have proved futile. The impact of nation-level governance frameworks and tax incentives on foreign direct investment inflows into African countries from 2000 to 2020 was examined in this study to refute this common belief. In order to meet the goals of the research, the study gathered all the data on governance systems, tax incentives, foreign direct investment, and other macroeconomic variables during the last twenty-one years. The study used annual panel sampling data from 45 African countries, as well as the System Generalized Method Moments (GMM) as an estimation technique in the empirical analysis, to obtain reliable estimates of the impact of governance structures and tax incentives on foreign direct investment inflows into Africa.

Unobserved country-specific time variants effects, endogeneity controls, time-series variations in the data, autocorrelations, heterogeneity, and other biases that may characterize panel estimate methods were all considered. The empirical findings of the System Generalized Method Moments (GMM) estimation technique reveal a positive association between government effectiveness, previous foreign direct investment, political stability, regulatory quality, voice and accountability and foreign direct investment inflows into African countries. Furthermore, African economies with longer tax holidays, greater tax withholdings, tax concession, exchange rate, gross domestic product, trade openness, and physical infrastructure levels attract foreign direct investment to African economies. Furthermore, the empirical findings suggest that during the era, corruption and corporation tax rates had a significant negative influence on foreign direct investment. Furthermore, the rule of law and inflation had no impact on the inflows of foreign direct investment in Africa.

The study recommends that African governments and policymakers should adopt comprehensive and efficient measures by strengthening their institutional policies, particularly in the areas of corruption control, effective governance, regulatory quality, and political stability, to remain competitive in attracting foreign investments. In this light of this, African leaders are recommended to develop a continent-wide plan to help the region become more appealing to foreign capital flows. In addition to the foregoing, policymakers should focus on ensuring that tax incentives are properly restructured to address policy lapses by African governments, which would support the achievement of some fundamental goals such as poverty eradication, sustainable growth and development, African integration into the global economy, and women empowerment. As a result, Africa would be a favourable destination for foreign direct investment due to its robust and business-friendly climate.

**JEL Classification:** F24, F22

**Keywords:** foreign direct investment, tax incentives political stability, government effectiveness, regulatory quality, corporate tax rate, tax holidays, generalized method of moments, Africa

## Abstrakt

Vliv správní struktury a daňových pobídek na přímé zahraniční investice: Případová studie Afriky

Přímé zahraniční investice (PZI) se pro rozvojové ekonomiky staly "posvátným pojmem", neboť jsou nejen zdrojem financování, ale také důležitým zdrojem zaměstnanosti a technologií. Vzhledem k roli, kterou přímé zahraniční investice hrají v procesu hospodářského rozvoje, čelí africké země konkurenci a některým problémům při získávání přímých zahraničních investic. Řada rozvíjejících se ekonomik nabízí iniciativy na podporu mezinárodních investorů, jako jsou silné institucionální systémy a daňové pobídky, i když údaje se různí. Mnozí se domnívají, že jsou životně důležité, zatímco jiní se domnívají, že nemají žádný vliv na umístění přímých zahraničních investic. Africké ekonomiky jsou důležité, protože se jedná o velké a rychle rostoucí ekonomiky, které uplatňují strategii příznivou pro PZI. Ta je podpořena programem dobré správy věcí veřejných a dalšími pobídkami, ale přestože tyto iniciativy fungují již více než padesát let, jejich účinnost stále není známa a jsou stále kontroverzní.

Vzhledem k několika faktorům, které působí proti podnikatelskému prostředí pro zahraniční spekulace, se několik snah ukázalo jako marných. V této studii byl zkoumán vliv rámce správy na národní úrovni a daňových pobídek na příliv přímých zahraničních investic do afrických zemí v letech 2000 až 2020, aby se vyvrátila tato zažitá představa. Pro splnění cílů výzkumu jsem shromáždil veškeré údaje o systémech vládnutí, daňových pobídkách, přímých zahraničních investicích a dalších makroekonomických proměnných za posledních jednadvacet let. Studie použila roční panelové výběrové údaje ze 45 afrických zemí a také systém zobecněné metody momentů (GMM) jako techniku odhadu v empirické analýze s cílem získat spolehlivé odhady dopadu struktur vládnutí a daňových pobídek na příliv přímých zahraničních investic do Afriky.

Byly zohledněny nepozorované efekty časových variant specifických pro danou zemi, kontroly endogenity, odchylky v časové řadě dat, autokorelace, heterogenita a další zkreslení, která mohou charakterizovat metody panelového odhadu. Empirická zjištění techniky odhadu systémové zobecněné metody momentů (GMM) odhalují pozitivní souvislost mezi efektivností vlády, předchozími přímými zahraničními investicemi, politickou stabilitou, kvalitou regulace, hlasem a odpovědností a přílivem přímých zahraničních investic do afrických zemí. Kromě toho africké ekonomiky s delšími daňovými prázdninami, většími daňovými srážkami, daňovými úlevami, směnným kurzem, hrubým domácím produktem, otevřeností obchodu a úrovní fyzické infrastruktury přitahují přímé zahraniční investice do afrických ekonomik. Empirická zjištění dále naznačují, že v daném období měly korupce a sazby daně z příjmu právnických osob významný negativní vliv na přímé zahraniční investice. Kromě toho právní stát a inflace neměly na příliv přímých zahraničních investic v Africe žádný vliv.

Studie nabádá africké vlády a tvůrce politik, aby přijali komplexní a účinná opatření posílením svých institucionálních politik, zejména v oblasti kontroly korupce, efektivní správy věcí veřejných, kvality právních předpisů a politické stability, a zůstali tak konkurenceschopní při získávání zahraničních investic. V tomto světle musí afričtí představitelé vypracovat celokontinentální plán, který pomůže regionu stát se atraktivnějším pro příliv zahraničního kapitálu. Kromě výše uvedeného by se tvůrci politik měli zaměřit na zajištění řádné restrukturalizace daňových pobídek, aby se odstranily politické nedostatky afrických vlád, což by podpořilo dosažení některých základních cílů, jako je vymýcení chudoby, udržitelný růst a

rozvoj, integrace Afriky do globální ekonomiky a posílení postavení žen. V důsledku toho by se Afrika stala příznivou destinací pro přímé zahraniční investice díky svému pevnému a podnikatelsky příznivému klimatu.

**Klasifikace JEL:** F24, F22

**Klíčová slova:** přímé zahraniční investice, daňové pobídky, politická stabilita, efektivita vlády, kvalita regulace, sazba daně z příjmu právnických osob, zobecněná metoda momentů, Afrika.



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## **Abbreviations**

<b>FDI</b>	-	Foreign Direct Investment
<b>GOVEF</b>	-	Governance Effectiveness
<b>POS</b>	-	Political Stability
<b>REQ</b>	-	Regulatory Quality
<b>CORR</b>	-	Control of Corruption
<b>ROL</b>	-	Rule of Law
<b>VOA</b>	-	Voice and Accountability
<b>TAXH</b>	-	Tax Holiday
<b>TAXW</b>	-	Tax Withholding
<b>TAXC</b>	-	Tax Concession
<b>CTR</b>	-	Corporate Tax rate
<b>EXCHR</b>	-	Exchange Rate
<b>INFL</b>	-	Inflation
<b>GMM</b>	-	Generalized Method of Moments
<b>IMF</b>	-	International Monetary Fund
<b>OECD</b>	-	Organisation of Economic Co-operation and Development
<b>OLS</b>	-	Ordinary Least Squares
<b>UNCTAD</b>	-	United Nations Conference on Trade and Development
<b>WDI</b>	-	World Development Indicators
<b>GMM</b>	-	Generalised Method of Moments
<b>WEF</b>	-	World Economic Forum
<b>WGI</b>	-	World Governance Indicators
<b>OECD</b>	-	Organisation for Economic Co-operation and Development
<b>ADI</b>	-	African Development Indicators
<b>MDGs</b>	-	Millennium Development Goals
<b>GDP</b>	-	Gross Domestic Product

# INTRODUCTION

## Background of the Study

What are the inspirational components that influence direct foreign interests in a country? There are broad monetary benefits for quite a long-time global area inside Africa, which is not a particular case. These nations have controlled the overall financing pool and upgraded their expectations for everyday comforts. As various nations put masses of drawn-out task structures in force, the seriousness of foreign direct ventures will increase. Based on this, the foreign direct investment choice is a consistently standard investigations premium.

Foreign direct investment (FDI) is the most sought-after supply of governments in growing economies, including Africa. Unlike foreign aid, which is related to situations and possible reimbursement, FDI gives itself a first-rate opportunity to fill any hole in economic improvement (Tsikata, 2005). In addition, as per Ayanwale (2007) and Connor (2018), foreign direct investment also serves as an aid for technology transfer, the creation of jobs, and ways of improving the standard of living and international market, thereby driving economic increase and improvement. Proof from quick developing economies alongside China, India, and Brazil underscores the meaning of foreign direct financing. For example, in 2018, China represented 10% of the field's total abroad direct financing inflow (UNCTAD, 2019). Foreign direct investment is one of the economic activities with the quickest growth rate as the global economy has grown more interconnected (Ramzan et al., 2019). There are new prospects for developing nations due to the fast rise of foreign direct investment. Numerous studies indicate that, in a broad sense, capital and human labor are the primary determinants of this long-term process, as economic growth leads to an increase in production capacity and technological advancement (Baejowski et al., 2016; Gedek et al., 2017; Zelazny, 2017; Dykas et al., 2018).

Therefore, the growing shift closer to overseas direct investment coverage in the current long time is no surprise. The worldwide inflow of foreign direct investment has accelerated considerably over the last few years. However, global foreign direct investment inflows for the 1970s were fantastically low, averaging \$ 23.8 billion (UNCTAD, 2019). This time, the path was controlled through distinguished colleges of concept: capitalist and socialist. The capitalists saw foreign direct investment as an essential issue of domestic improvement - their method became extra liberal and opened (Okafor et al., 2017). FDI influx and economic growth are primary subjects at the moment, both nationally and internationally (Abdouli & Hammami, 2017; Adams et al., 2018). According to Adams et al., foreign direct investment may be seen as a reaction to and a driver of globalization and economic progress. Foreign direct investment

has improved over the past three decades, going from \$55 billion in 1980 to \$1,800 billion in 2017. (Ramzan et al., 2019). The advantages of economic growth are not concentrated in a single area of the economy but spread out throughout several industries, which may raise a nation's quality of living provided money is distributed fairly. New technology investment is encouraged as additional tax revenues rise and unemployment rates decline.

The experience of Africa with foreign direct investment inflows in recent years is just like the worldwide fashion (Table 1). The vicinity is making constant development concerning the foreign ventures it draws. As Table 1 suggests, foreign direct investment flows to the area within the Nineteen Seventies barely exceeded \$ 1 billion on average (representing 0.56% of GDP). Anti-change policy became dominant throughout this era, given that maximum African international locations had just conquered the subordination of their colonial masters. The fee doubled throughout the Eighties and using of the Nineties; while most African international locations had adopted liberal exchange policies, the place had tripled to \$ 6.6 billion. The fantastic form endured, with the vicinity benefiting from an astonishing USD 31 billion in foreign direct investment inflow between 2000 and 2009, and foreign direct investment inflows had the most significant proportion of GDP on common over the same length (2.63%). These periods were also the saturation levels that made the study focus on this phenomenon in this research. After that, the vicinity saw a mild increase in overseas direct investment inflows to \$ 49 billion, which is 2.18% of GDP on average for 2010-2020.

Nonetheless, the majority of foreign direct investment inflows to the region are unevenly distributed between sub-regions. To summarize, North Africa was the region's largest recipient of foreign direct investment inflows in millions of US dollars from 2000 to 2019. (WDI, 2019). Nonetheless, the sub-regions have a higher gross domestic product share. Foreign direct investment inflows averaged less than 3%, or 2.32%, throughout the same period (See Figure 1). Foreign direct investment inflows reached 5% of the gross domestic product in 2006, the highest level ever. Despite this, the sub-region had its lowest foreign direct investment inflows in terms of value in seven years in 2011, as well as the lowest share of gross domestic product in more than a decade, at 1.1%. According to Makdisi (2017), this was mostly owing to the political protests that swept through the sub-countries. Since then, the sub-region has recovered and is once again at the vanguard of attracting FDI.

**Table 1: Average FDI inflows (1970-2020) and World share (2000-2020)**

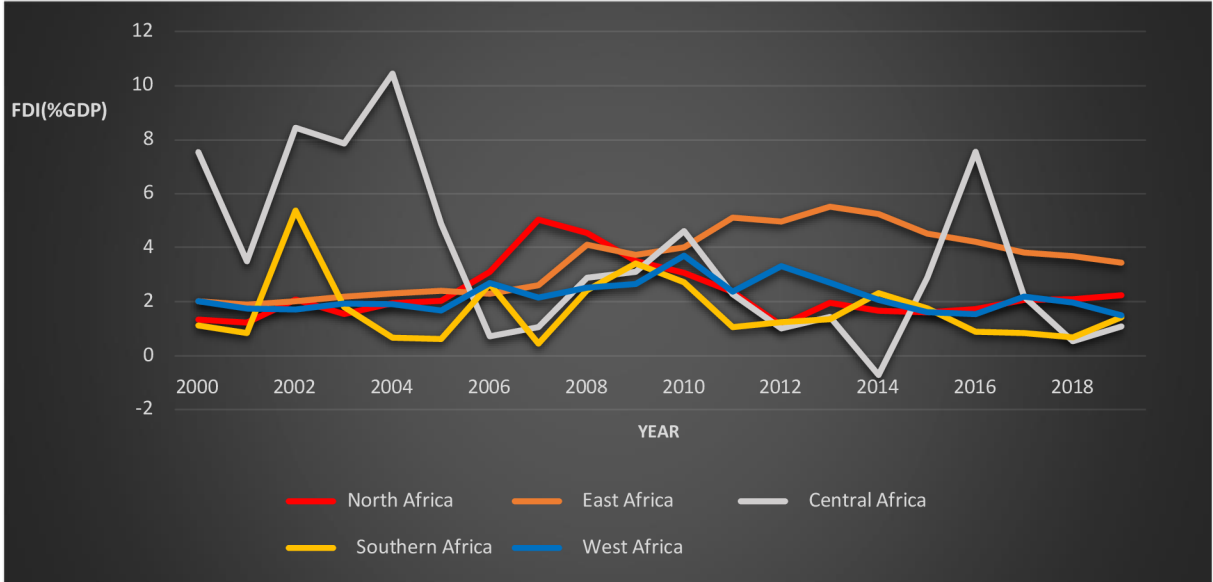
Average FDI Inflows in millions of US\$ (% GDP)					
	1970-1979	1980-1989	1990-1999	2000-2009	2010-2020
World	23800 (-)	92931 (0.62)	397497 (1.33)	1085732 (2.33)	1548023 (2.04)
Developed economies	18045 (0.41)	72435 (0.61)	282794 (1.33)	748995 (2.33)	874396 (2.04)
Developing economies	5755 (0.57)	20496 (0.7)	114703 (1.92)	336737 (2.88)	673627 (2.39)
Latin America & Caribbean	2654 (0.74)	6365 (0.79)	37636 (1.97)	81571 (2.9)	166404 (2.97)
Asia	1902 (-)	11779 (-)	70165 (1.06)	223255 (1.89)	455926 (1.86)
Africa	1124 (0.56)	2202 (0.44)	6636 (1.11)	31007 (2.36)	49304 (2.18)

Source: Researcher's computations from the World Bank World Development Indicators (WDI), Global Competitiveness Index Report (GCI) (2000–2020).

Central Africa, on the other hand, got the least foreign direct investment flows on average from 2000 to 2019 but the most as a proportion of gross domestic product (WDI, 2019). Foreign direct investment in the sub-region has been mostly sporadic (Figure 1). Between 2000 and 2019, Central Africa was the only sub-region to have a negative foreign direct investment influx in 2013, accounting for -0.7% of the gross domestic product (Figure 1). Two years later, the sub-region drew over 30% of Africa's foreign direct investment inflows in 2015, making it the greatest receiver of foreign direct investment inflows in both value and proportion of the gross domestic product. Similarly, an uneven trend can be seen in the Southern Africa sub-region, which has the lowest average foreign direct investment inflow as a proportion of gross domestic product in Africa. In comparison to Southern and Central Africa, the trajectory of foreign direct investment flows to East Africa has been generally upward in terms of value (WDI, 2019) and proportion of gross domestic product (Figure 1). From 2000 to 2019, average foreign direct investment inflows accounted for 3.5% of gross domestic investment in the sub-region, ranking second only to Central Africa.

From 2000 to 2019, the sub-region of interest, West Africa, garnered the second highest foreign direct investment influx to Africa on average, accounting for 2.2% of GDP (WDI, 2019). According to Figure 1, between 2000 and 2004, foreign direct investment as a proportion of GDP was reasonably consistent, hovering around 2%, but thereafter became irregular, albeit still above pre-2005 levels, until 2011, when the sub-region had its greatest foreign direct investment influx to date. However, as indicated in Figure 1, foreign direct investment inflows have been steadily declining since then. However, in years of consecutive decline, the subregion recorded the bottom influx of foreign direct investment.

**Figure 1: Africa sub-regional foreign direct investment net inflows from 2000-2020 (% of GDP)**

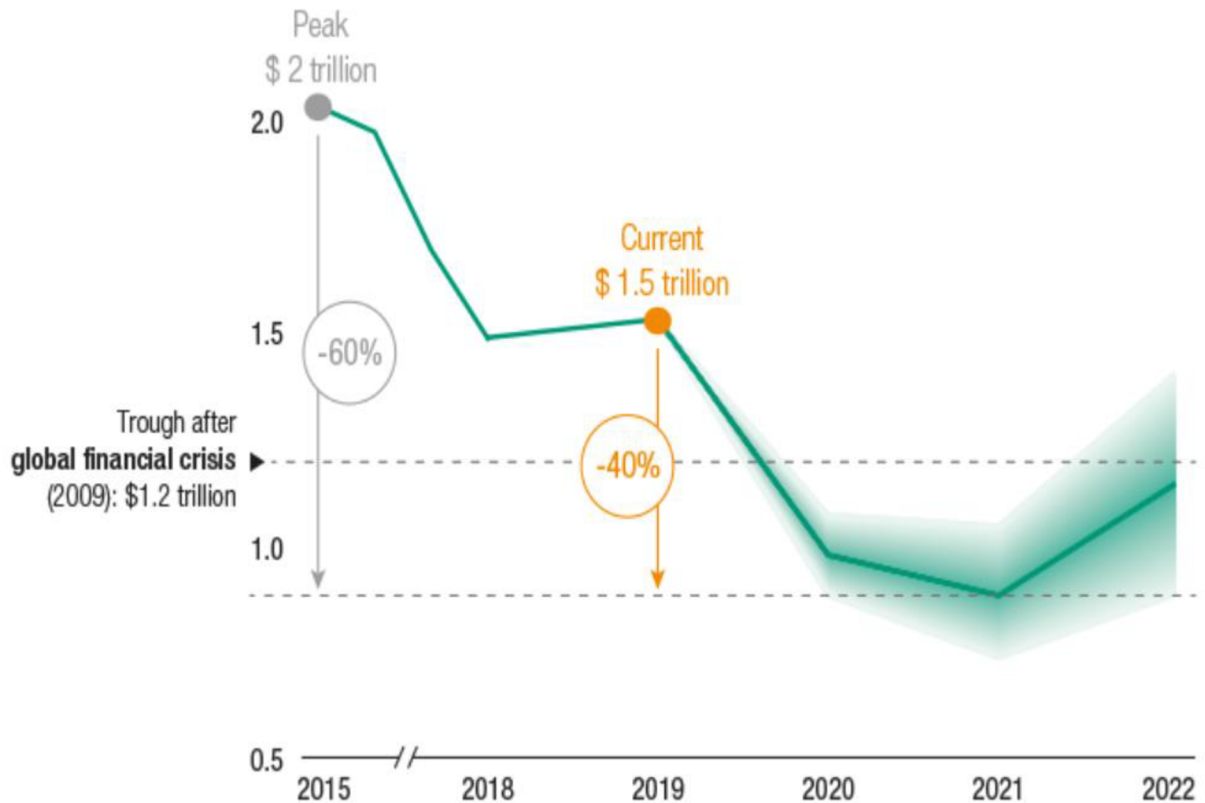


Source: Researcher’s computation via data from World Bank World Development Indicators from 2021.

The UNCTAD world investment report predicts that in 2022, foreign direct investment flows to Africa would decline by 25 to 40 percent (Figure 2). Low commodity prices will exacerbate the negative trend. In 2019, FDI flowed to Africa already declined by 10 percent to \$45 billion (UNCTAD, 2019). African international locations have been characterized by poor macroeconomic factors, terrible infrastructure, unemployment, low financial savings, and many others. foreign direct investment can be a giant alternative to reinforce the economic productivity of these countries, thereby improving monetary increase and sustainability (Anyawu, 2013; Miletkov, 2014; Saini & Singhanian, 2018). Overall, this competitiveness leads to a challenging project for African economies.



**Figure 2: Africa foreign direct investment projected to fall by 40% in 2022**



Source: UNCTAD, World Investment Report, 2021

Governance structures may be a valuable benchmark for measuring a country's business climate (World Development Indicators, 2019). Poor governance and institutions have been argued to poison a country's potential to attract FDI (Largade, 2017). According to Asiedu (2006), the number one factor limiting FDI to Africa in each poll is governance structures and institutions. According to Figure 4, the trend of governance structures and institutions in Africa have been poor. This may seem odd considering that the continent is rich in natural and mineral resources, which are important inducers of FDI; similarly, governance systems and tax incentives are important inducers of FDI (Asiedu, 2006; Anyawu, 2013; Miletkov, 2014; Peters & Kiabel, 2015; Halil, 2016; Fahad & Ahmed, 2016; Okafor et al., 2017; Luu et al., 2018). Since the global economic crisis, which has led to an almost complete stagnation of aid and made it difficult to raise private capital for smaller and poorer countries, the need to mobilize local revenues for development has become even more urgent. For the most part, this crisis has made it urgent to address the structural problems hindering social and economic growth in Africa and to find workable solutions at the local level. The focus is on an approach to development that

seeks to place full power over the development agenda in the hands of African governments themselves. African governments can reduce their dependence on ODA by making local tax revenues available as a source of development financing.

This would allow African governments to freely choose their own development goals and allocate funds according to those priorities without appeasing donors who often set limits on development aid that serve the interests of the donor rather than the recipient. The host country's tax policy is one of the elements influencing foreign direct investment decisions (Aseidu, 2004). The majority of African nations use the supply of financial and in-kind tools to gauge their effectiveness in luring these overseas investments. However, this is contingent on the host nation's government's competence and desire. According to Shala (2013), the corporate income tax rate, tax holidays, tax withholding and tax concession of the host nation is the most often utilized tool. The highest corporate tax rate in African countries is 35 percent and the lowest rate is 15 (Figure 5). Based on the figure 3 below, Liberia recorded the highest growth of FDI with corporate tax rate of 30. Although corporate income tax rates have decreased, and there are favourable tax incentives such as tax holidays, tax withholding and tax concession in place throughout Africa (see Appendix), the area still has trouble luring substantial FDI. This is a result of FDI oscillations and the African region's lack of investor appeal (Asiedu, 2002).

Like any organization, every nation aims to gain economic and financial improvement. As such, nations undertake projects to drive monetary improvement. According to a record through the United Nations Economic Commission for Africa (UNECA, 2016), industrialization is a way to enhance development in Africa. Economies that might be characterized by vulnerable governance establishments, negative tax systems, erroneous duty structures, inefficient allocation of capital, foregone sales, and inadequate protection of buyers dispose of foreigners from investing cash in their company corporations (Babajede, 2013; Peters & Kiabel, 2015; Agyemang et al., 2016). Consequently, foreign traders tend to make investments inside the firms of economies that can be regarded as sturdy and robust governance institutions and strong tax incentives guidelines, which might assist in assuring accountability, transparency, the protection of traders, and many different benefits (Bokpin et al., 2017; Appiah-Kubi et al., 2020).

Despite the restrictions, Africa can position itself to attract more foreign direct investment (FDI). Since the early and middle 1980s, more economic reforms have been implemented in most nations to enhance Africa's position in economic growth (Agosin & Machado, 2005). Among these measures, the Financial Sector Adjustment Program (FSAP), Economic Recovery Program (ERP), and Structural Adjustment Program (SAP) are noteworthy. Again, most

nations endorsed both the New Partnership for Africa's Development (NEPAD) and the African Growth and Opportunity Act (AGOA), both sponsored by the United States in 2000. All of them aim to increase access to markets across the continent (Choe, 2003).

Recent polls of Investment Promotion Agencies (IPAs), International Investment Location Experts, and Transnational Corporations support the likelihood that Africa will draw the necessary FDI (UNCTAD, 2004). According to the report, there are promising long-term prospects for FDI flows into the region. According to the studies, South Africa, Egypt, Morocco, Nigeria, and Algeria have the best prospects for foreign direct investment (FDI) within the area. Because of the relative improvement in their economic policies over the past several years, nations like Mozambique, Uganda, Tanzania, Namibia, Mauritius, and Botswana are also expected to see an increase in FDI flows (Dupasquier & Osakwe, 2005). Additionally, according to the IPAs' poll, greenfield investments rather than mergers and acquisitions by industrialized nations are the preferred method of investing in Africa.

Once again, most nations who were reluctant to liberalize trade after gaining independence have since done so. Restrictions on non-residents' ability to remit dividends, interest income, and sales profits have been eliminated. Additionally, several have signed bilateral agreements that double tax, all to draw in foreign investment. Although some African governments prefer to keep a tight grip on some strategically essential industries, they have reduced their restrictions on foreigners' capacity to participate in domestic investment. Last, because most stock markets are now computerized, recent market changes and structures have ultimately made it possible for non-residents to acquire equities and government assets.

A desirable variety of research has been related to the FDI flows in Africa, which much concentration on the nation base and regions (Globberman et al., 2006; Anyawu, 2013; Miletkov, 2014; Peters & Kiabel, 2015; Halil, 2016; Agyemang et al., 2016; Bokpin et al., 2017; Appiah-Kubi et al., 2021). Nevertheless, evaluations range in phrases of the essential drivers that impact the FDI inflows. Most research on FDI has been on the impact of macroeconomic variables such as change rate, inflation, and GDP and concentrated on foreign or country base (Coleman and Agyire-Tettey (2008) tried to find the effect of substitute charge unpredictability on FDI in Sub-Saharan Africa, involving Ghana as a case look). Many studies did not consider the governance systems, institutions, and tax incentives variables on the FDI in Africa. Considering the new context, analyzing the impact of governance structures and tax incentives on foreign direct investment in Africa would be of great interest. It is important to note that although FDI grows in value, most of it now goes in a different direction. More lately, transitional, and emerging economies have surpassed industrialized ones in attracting FDI.

However, when it comes to becoming a destination for investments by international firms, Africa continues to lag the rest of the globe. Africa can still draw significant sums of FDI if the proper procedures exist.

## **Purpose and Objectives**

The primary purpose of this dissertation is to explain the impact of governance structures and tax incentives on the inflows of foreign direct investment in Africa for the period 2000-2020. The study aims to fill the gaps in this area of research by investigating how these variables influence FDI flows. The wide array of governance structures factors affecting the influx of FDI includes government effectiveness, political stability, corruption, regulatory quality, the rule of law, and voice and accountability. Typically, tax incentives factors are associated with the corporate tax rate, tax holiday, withholding tax, and tax concession, while macro factors are related to the gross domestic product, exchange rate, trade openness, physical infrastructure, and human development index. The purpose was achieved through a series of objectives, which, in a nutshell, relate to answering the following main research questions:

The specific objectives of this study seek to:

- I. To examine the impact of governance structures on the inflow of FDI in Africa.
- II. To examine the impact of tax incentives on the inflow of FDI in Africa.
- III. To empirically and theoretically determine social-economic and political variables that contribute to the inflows of FDI in Africa.

The following main research questions will guild the study:

1. To what extent do governance structures influence the foreign direct investment decision-making process in Africa?
2. Do tax incentives have an impact on the inflows of foreign direct investment in Africa?
3. What are the social-economic and political variables that contribute to the inflows of foreign direct investment in Africa?

## **The significance of the study**

The findings from the study will be of immense benefit to the following:

- a) Policy Makers and Government: There is no doubt that this research will be of great benefit to the government and policymakers. If FDI is to be understood as having a definitive effect on financial growth, policymakers and government would like to understand FDI

governance structures and past tax incentives, as the relationship can be a crucial element in their formula the politics. Monetary. Once again, African countries continue to take advantage of financial instability (IMF, 2019). This review will provide feedback on the full impact of FDI on Africa's financial growth.

b) Foreign Investors: All Investors are concerned about the factors that could have an unfavourable effect on their investment. Since uncertainty affects investment, traders might additionally like to understand the regions in which the impact of uncertainty is real via empirical studies. These studies will essentially explore the volatility in governance systems, institutions, tax incentives, and macroeconomic variables and how they affect overseas investment in element and to be able to be of terrific benefit to many transnational agencies of their ability funding, portfolio diversification opportunities, and investment alternatives in Africa.

c) Researchers: This research will open a brand-new bankruptcy on the FDI relationship with African governance systems and tax guidelines. It will open, in addition, discussions into the FDI relationships nexus.

## **Structure of the dissertation**

The dissertation is organized into four chapters. Chapter One is the introduction and covers the research's historical past, the problem's statement, the study's goals, the research questions, the justification of the research, and the arrangement of the research. Chapter Two contains the theoretical literature; on how foreign direct investment affects monetary increase and empirical literature. Chapter three gives the method and deals with developing theoretical models and methodologies used to analyse the data. The models which were used for the research are also discussed. The main point of Chapter Four is a discussion of outcomes at the same time as the very last chapter appears at the precise foremost findings, conclusions, and recommendations of the research.

# LITERATURE REVIEW

## Theoretical Review of the study

Foreign direct investment (FDI) is considered to have dominated economic literature in recent decades, particularly in the field of development economics. With the globalization of the international economy in the 1990s, the importance of FDI grew even more, and many economists regarded it as one of the primary reasons for its domination (Massoud, 2003). According to the literature on FDI, the benefits connected with it significantly influence the host country's economic development (Hanson, 2001). According to Hanson, these include the development of new jobs, technical transfer, and know-how, and enhanced trade integration with the rest of the globe. As a result, countries worldwide, particularly emerging economies, have turned to FDI to meet their investment and development demands. Increased integration into the global economy, which FDI is thought to provide, leads to potential economic growth (Massoud, 2003). According to Hartman (1984), FDI can take various forms, and while it is commonly thought of as new foreign entrants investing in a country, the majority of FDI occurs within established foreign affiliates. According to Hartman, the transfer of cash abroad by a parent firm, either as loans to or equity investments in subsidiaries, is the most explicit, and the retention of earnings abroad by foreign subsidiaries also enhances the parent firm's subsidiary ownership in a similar way. However, FDI is a complicated topic in general. The reasons for FDI's existence and what motivate it have long been debated, and there has never been a cohesive theoretical explanation for FDI (Denisia, 2010).

Governments have always overseen providing infrastructure services to their nations. Governments in developing nations realized the private sector was a viable option to supply these infrastructure services more affordably and effectively in the 1980s due to insufficient investments, poor service, and unacceptable budgets by their governments (Sader, 2000). Investors in multinational corporations cannot abruptly remove cash if the host country's economic, political, or social climate changes since FDI is a long-term commitment that involves investors signing commitments to the host country for several decades (Meyer, 2003). Investors anticipate that the expected return rate will outweigh any potential dangers after thoroughly researching the host nation. Two types of foreign direct investment are possible. The first category is focused on financial control over enterprises and can be connected to the capital and other resources (Sooreea-Bhemul & Sooreea, 2012). Various titles, possessions, and legal and contractual rights are included in the second category of FDI. An FDI inflow, sometimes called inward FDI, is the foreign direct investment invested in the host economy

(Shih et al., 2009). Host governments promote FDI from outside through low borrowing rates, incentives, and tax benefits. The government typically supports outbound FDI to mitigate all risks (Contessa & Weinberger, 2009). According to published research, inward foreign direct investment (FDI) generally benefits economic growth and productivity in the host nation, whereas outbound FDI often has the reverse effect (Kokko, 2006; Azman-Saini et al., 2010). By supplying technological and administrative know-how to services like communications networks, waste treatment facilities, water treatment plants, and airport terminals, large overseas multinational corporations help developing countries attract FDI (Sader, 2000). When the host nation has a business opportunity but cannot take advantage of it on its own due to a lack of resources (money, technology, or capital), FDI happens (Azzimonti & Sarte, 2007). The global company can take advantage of the investment opportunity because it has the needed cash, management skills, and technology. The market size and location, the country's natural resources, human resources, and infrastructure may influence foreign direct investment.

### **Foreign Direct Investment**

There is a vast literature on foreign trade and investment dating back to the Smithian era (1776). While the mercantile system propagated hoarding and a closed economy, Adam Smith was a proponent of free trade and an open market system with the "famous" 'invisible hand.' The neo-classicalists equally hold the view that free trade and investment enhance the accumulation of capital stock. Views have been expressed about the limitations to financing opportunities, especially in the face of capital rationing and increasing the cost of capital (Jenkins & Thomas, 2002). Joint ventures between a foreign corporation and a local business constitute FDI (Hsiao & Gastanaga, 2001). Cooperative operation enterprises are the second type of FDI, and they are based on a contractual arrangement for payment between a foreign corporation and a local business. The third type of FDI is a foreign-owned entity, in which a foreign corporation buys a local business and becomes its sole owner. The fifth type of FDI is typically utilized when oil exploration is involved in cooperative development, while the fourth form of FDI is a foreign investment enterprise. This highly controlled legal framework permits a foreign corporation to participate in the local country—roughly \$138.3 billion between 1990 and 1998. Through private multinational companies, developing nations received FDI inflows of cash (Sader, 2000). Intense privatization caused more than half of this sum, or \$78.7 billion, to go to Latin America. All regions of the world, except Latin America, were severely impacted by the Asian crisis in 1998 regarding FDI influx.

Both sides gain from investments made by international corporations in developing nations. Investors benefit from a high rate of return on investment, access to new markets, and physical resources and technology that will boost the firms' trade surplus and global competitiveness (Cheng & Chung, 2012). The rise in capital benefits emerging nations by improving capital flow, managerial capabilities, employment, exports, and technology. Research on how FDI affects activities in developing and developed countries has focused on how FDI by multinational corporations is seen as a crucial instrument for developing countries to achieve economic progress (Denisia, 2010). Scholars are interested in learning how FDI impacts a nation's economic development, the extent to which multinational corporations are regulated when entering foreign markets, and how FDI affects a nation's fiscal policy (Ayanwale, 2007). Because various sectors have varied effects, policymakers are interested in learning how multinational corporations will affect the operations of local businesses and what impact, if any, they will have on the economic development and well-being of the host nation (Meyer, 2004; Lejour & Rojas-Romagosa, 2006). FDI has been defined as the investment undertaken by an entity resident of one economy in an enterprise resident in a different economy.

The investment is made to obtain and sustain a lasting interest in the enterprise and to exercise a significant level in its management (Awan, Ahmed, Shahid & Hassan, 2014). Froot (1993) defines it as the acquisition by a firm in one country of control over business activity in a second country. Acquisition of control may or may not be associated with a change in the location of manufacture, but it is necessarily allied to a change in which the firm controls production in that location. Markusen, the first scientist to do original research on the FDI horizontal model, proposed two sorts of foreign direct investment (1984). Multinational corporations who wish to enter new markets and set up and copy industrial facilities in other nations are interested in horizontal FDI (Alfaro & Charlton, 2009; Hyun & Hur, 2013). The scale of the market, the host nations' macro-organizational and macroeconomic policies, the enterprises' competitiveness, the accessibility of trained labor, and the standard of local infrastructure are essential factors that attract horizontal FDI. The primary benefit of horizontal FDI is a decrease in trade costs, as FDI may be defined by the size of the host country's market and the trade costs (Barassi & Zhou, 2012).

Vertical FDI happens when multinational companies divide supply chain and manufacturing operations among many sites (Alfaro & Charlton, 2009; Hyun & Hur, 2013). When host country governments eliminate barriers and encourage expansion, this is done to take advantage of the cost variations across international boundaries. Economic clusters,



investment incentives, economic freedoms, cost of production, efforts for new investments, entrepreneurship, and possibilities are essential factors that attract vertical FDI. Cost differences in labor and manufacturing may be the deciding reasons for FDI (Barassi & Zhou, 2012). Even though multinational corporations can mix both tactics as a knowledge-capital model, most FDI has been horizontal (Jang, 2011; Hyun & Hur, 2013). In the past, both vertical and horizontal FDI have been linked to investments between industrialized and developing nations (Herger et al., 2016).

### **Reasons for Foreign Direct Investment**

Substantial increases in domestic market share rarely come without some geographic expansion, first of sales and service operations, and later production facilities. However, the initial success drives the expansion through lower costs associated with the learning curve and through increased access to and, thus, lower cost of financial capital. The over-arching motive because firms engaging in FDI is to advance their competitive position. Increasing competitive advantage has become particularly important in the current hyper-competitive global environment. A firm's competitive position is primarily advanced by various motives shown via three main activities, according to Dunning (1993) (Luiz & Charalambous, 2009). This division finds a basis in the presumed interest of the investors and how they seek to take advantage of any economy to create a return on their investments. In other words, whatever foreign investors aim to get out of the economy affects what they put in. The aim suggests that the types of investments behave differently and that, when aggregated, some of the effects of independent variables may be muddled or concealed. (Samford & Gomez, 2014). Reasons for investment essentially elucidate the types of FDI and include:

i.           Resource Seeking

'Resource-seeking' investment is made to maximize the presence of primary goods in the recipient country that are not extracted by domestic ventures. Such investors pursue reliable stocks of materials that are either unavailable or not present in their country of origin. Typically, this includes extracting oil and gas and mining metallic and non-metallic minerals (Samford & Gomez, 2014). Resource-seeking investment is characteristically relatively immobile and location-bound because it frequently involves the construction of the infrastructure necessary for extracting primary goods (Samford & Gomez, 2014; Demirham & Mascra, 2008).

ii.           Market Seeking

They are also called horizontal FDI because it often embraces the replication of business structures and production facilities in their host countries and targets primarily local and

regional markets (Demiharm & Mascara, 2008). The aim of 'market-seeking' foreign investment is to provide non-tradable goods and services to consumers in the target country or avoid cost-raising barriers to trade by establishing local production of tradable goods. For tradable goods, this means establishing the capacity to produce and sell competitively within the domestic market of the target country, whether by avoiding a trade barrier or being located within the target market. For non-tradable goods and services (banking, telecommunications, and many others), the intention is to compete with local providers for domestic clients. This type of investment tends to produce goods and services sold within the target country rather than exported; hence, tariff jumping, or export-substituting, is viewed as a variant of this type. Samford & Gomez (2014) argue that market-seeking investment is mainly affected by government policy, both investment incentives and trade barriers; on the other hand, it is encouraged by obstacles to entering local markets, such as tariffs and transport costs (Demiharm & Mascara, 2008).

### iii. Efficiency Seeking

'Efficiency-seeking' investment takes place when it benefits from the shared governance of geographically distributed operations in the context of economies of scale and scope (Demirhan & Mascara, 2008). Investments in middle-income and developing countries are made to lower production and marketing costs by taking advantage of differentials in the costs of inputs and relying on the relative openness of cross-border markets. This type of investment often is based on vertically integrated supply chains, where a single portion of the production process is outsourced to take advantage of lower labor costs. Efficiency-seeking foreign investment is most common in high-value-added manufacturing with low transport costs (e.g., textiles, electronics, computers, machinery). (Samford & Gomez, 2014).

There are two opposing viewpoints regarding the impact of foreign direct investment on domestic investment. One is that foreign direct investment promotes domestic investment by creating new markets, input demand, and technology with a positive economic impact. Labour is movable and frequently moves from multinational corporations to domestic businesses; more skilled labour may leave a multinational corporation to find a start-up. Some think foreign direct investment can help boost competition, making markets (including financial markets) more effective. Investments in new sectors can also spark new industries and product growth. The opposing argument is that because FDI is a monopolistic competitor, it drives away domestic investment. In terms of their advertising clout, ability to control the market, and use of predatory pricing to bar entry, domestic businesses cannot compete with foreign ones. Some think that FDI discourages domestic investment by increasing credit demand and raising interest rates.

One is the technological gap or difference between domestic and foreign technology levels. Economic literature suggests that the potential for technology imitation, which fosters economic growth, increases with the size of the technology gap between the home economy and the host economy, according to Blomstrom and Kokko (2003). According to Blomstrom and Kokko (2003), spillovers might not happen if there is a significant technological gap between foreign and domestic businesses. This can be explained by the possibility that technologies created in more developed nations may not be as well suited for use in less developed nations due to the high cost of implementation. The values of the underlying technology, market competition, etc., are additional factors. FDI affects a host country's economy in several ways, including growth. Theoretically, FDI can stimulate economic growth through several channels, particularly in the host economy. The most significant one is probably spillovers and technology transfer. Economic growth literature has established the significance of technological advancement in economic development.

FDI frequently results in the transfer of technology to local affiliates of multinational corporations. MNCs' interactions with domestic suppliers and customers can result in spillovers, such as employee mobility. In light of this, FDI may affect income. Hermes and Lensink (2000) recognize and categorize various types of spillovers. The following channels have been identified as potential routes for FDI spillovers: demonstration, imitation, competition, links, and training are listed in that order. Spillovers through the demonstration channel highlight that domestic firms use less-advanced technologies than foreign firms and that they may imitate the newer technologies, increasing their productivity. The same might apply to management techniques adopted by foreign businesses. The demonstration effect can occur through direct or indirect business interactions or the transfer of workers from foreign to domestic employers. The more domestic firms may profit from stealing and copying these technologies, the more technologically backward the host nation is in comparison to the level used by the foreign firms. This seems to be an example of the idea of technological skill convergence. The competition channel emphasizes the entry of foreign companies exacerbates competition in the domestic market. This forces domestic businesses to operate more efficiently, which could result in the creation of new technologies, the imitation of existing ones, and the upgrading of current technology. The linkage channel of spillovers emphasizes how MNCs may trade with domestic firms to transfer new technology to them. For instance, such transactions might involve purchasing raw materials or intermediate goods. This might result in close buyer-seller relationships with local businesses in the host nation, and as part of those relationships, foreign businesses might train and offer technical assistance to local linkage

businesses. Additionally, selling to foreign companies may inspire domestic businesses to improve their production methods by following the technical and quality standards required by foreign clients, thereby boosting productivity. The training channel also emphasizes the need for an improvement in the domestic human resource base in order to encourage the adoption of new technologies and domestic firms' imitation of them. Only when the workforce is competent enough to use them will domestic companies be able to adopt these new technologies. Therefore, when foreign companies enter the market, local businesses may be encouraged to train their employees. This stimulus might be based on one of the previously mentioned three channels. Thus, perceived opportunities to copy recently introduced technologies, increased competition in home markets, and/or the existence or development of links between foreign and home firms may cause domestic firms to increase their training efforts. The latter point also makes it clear that it will be challenging to distinguish between the four spill over channels in practice. Most African nations are unable to access FDI, and the majority of those in the region are unable to raise money on global capital markets. As a result, the majority of the outside funding required for alleviation must come from FDI (Asiedu, 2003).

### **Theories of Foreign Direct Investment**

Overall, many countries in the sector are installing regions to attract FDI, and the significance of FDI to monetary growth cannot be overlooked. The key unanswered question, however, is the extent to which foreign direct investment drives monetary growth in various countries. While monetary theories that explain the foreign direct investment and economic growth predict a strong relationship, empirical data on the subject have mixed results. Some studies show a positive relationship, while others show a negative one. A contextual overview of theories that explain the foreign direct investment phenomenon is necessary to comprehend the financial mechanism, how economic retailers think thoroughly, and the give-up impact of FDI. The idea of proper rationalization of the foreign direct investment may be traced back to the 1960s when scholars attempted to include the activities of Multinational Corporations (MNCs) in their theories considering their expanding role in international investment (Choudhury & Nayak, 2014). However, FDI is a complicated topic in general. The reasons for FDI's existence and what motivate it have long been debated, and there has never been a cohesive theoretical explanation for FDI (Denisia, 2010). The Production Cycle Theory, developed by Raymond Vernon in 1966, examines the relationship between the product life cycle and possible FDI flows; the Theory of Exchange Rates on Imperfect Capital Markets, developed by Cushman in 1985, examines the relationship between FDI flows, and exchange

rate changes; the Internalization Theory, developed by Buckley and Casson in 1976, which aims to answer the question of why firms do not FDI, neoclassical boom theory, the Harrod-Domar boom model, the OLI theory is a combination of three different FDI theories that examine an investing firm's decisions based on ownership (O), localization (L), and internalization (I) advantages (I). Internalization Theory and Eclectic Paradigm Theory were deemed the most relevant to the subject matter of this study by the author. The summary is based on Denisia's work (2010). The following theories are examined:

### **Internalisation theory of FDI**

This hypothesis aims to explain why companies do not just sign contracts with a subcontractor in a foreign country instead of investing in that country. According to Denisia (2010), international corporations organize their internal activities to build distinct advantages they may use later. The fundamental issue with this argument is that contracting out is dangerous since it entails moving stock outside the company and revealing private information. This can cause problems for the firm, particularly if the outsourced agent decides to terminate the contract and use the technology to compete with the mother company or if the agent harms the firm's brand recognition through its activities. The corporation could have felt more comfortable partaking in the production process in a foreign country as a consequence. By acknowledging the existence of market failures, this theory attempts to explain the expansion of international corporations and their incentives for gaining foreign investment. This research intends to analyze the impact of governance structures and tax incentives on foreign direct investment in African economies, and the versed in this concept is significant. The idea of the four stages in international development states that FDI activities take place when a company has acquired a certain level of market knowledge through its early international activities, and the company can increase its market commitment abroad as a result of the increased market knowledge (Liu, 2009). This market expertise is crucial to the process of internationalization. Some studies, like Luostarinen (1979), provided empirical support for the model's four stages, but others, like Millington and Bayliss (1990) and Turnbull (1993), did not (1987). It was also criticized for being deterministic and unable to explain why a company chooses to establish a subsidiary in a foreign country rather than exporting to that country when beginning its internationalization (Liu, 2009). Additionally, research using this model has only identified one reason for FDI, which is the market's desire for FDI. Although the study by Buckley and Casson (1976) helped explain FDI through its systematic theory of FDI, the theoretical framework they developed did not apply in the short run or to smaller businesses that were only operating in

one or two countries. Additionally, the theory failed to adequately explain the various forms of FDI (Agarwal, 1980). They also noted the exposure to government risks in the host nation, but they overlooked the possibility that the level of risk might vary among the different companies. Due to the social consideration that forces businesses to balance social and private objectives, industries like power generation and telecommunication are likely to be at a high risk of government intervention (Nayak & Choudhury, 2014).

### **The Eclectic paradigm theory of FDI**

Denisia (2010) defines the Eclectic Theory as a combination of three different theories of foreign direct investments that analyze FDI based on ownership benefits (O), localization advantages (L), and internalization advantages (I). It is referred to as the OLI theory as a result. As summarized below, Denisia gives the basis of each of the three components. Ownership advantages (O) hypothesizes that certain firms possess firm-specific intangible resources (such as human resources, patent rights, brand image, innovations, and many others) which can be reproduced at minimal cost in various countries and thus yield higher earnings at lower costs, thus the incentive for Overseas investment into other countries. Nevertheless, because the investing company may incur extra costs, the company must possess certain traits to enter an international market successfully. These features, as per Denisia, could take the form of autocratic benefits, innovation to regulate creativity, and other variables like economies of scale and increased relation to finance capital. The theory's Location (L) component asserts that various countries' location advantages are significant determinants of host nations' FDI from multinational businesses (TNCs). Economic advantages such as production factors, cost of transportation, telecommunication services, and market growth; ideological factors such as government policies on FDI inflow; and social aspects such as an appreciation for multiculturalism and attitude toward strangers are all examples of country-specific advantages. However, it is essential to note that investing in corporations' capacity to use different location advantages is influenced by their unique qualities. Three different ownership benefits exist. The first type entails a collection of assets that produce income for the company and enable it to increase productivity, efficiency, and market dominance in a foreign firm. These assets include property rights and intangible ones like organizational systems, human capital, inventive capacity, technology, information, and many others (Zang, 2013). The advantages that the multinational may have over "de novo" firms (newly established firms) that are producing in a foreign company are the second type of ownership advantage. These benefits might result from the firm's size, improved resource capacity, and monopoly power. For example, with an

established company, certain resource benefits, such as market knowledge and administrative experiences, may be accessed from the parent company at a lower cost, whereas a "de novo" company may have to pay the total cost to acquire those resources (Zang, 2013). The company's multinationalism, which provides access to and better knowledge of the international markets, is the source of the third ownership advantage. This makes it possible for businesses to benefit from geographic variations in the factor markets and lowers the exchange- or political risk associated with producing in a host country (Dunning, 1977; Dunning, 1988; Zang, 2013). In terms of the internalization advantages, this arises when multinationals or firms produce internally. This makes production profitable since transactions are from within the firm, and the firms also maximize their gains rather than being dependent on external markets (Zang, 2013). Foreign firms' incentives for internalizing the market are to exploit the advantages of market failure or avoid the disadvantage of market failure. The market failure that multinationals avoid is mainly in three forms. The first is when both the buyer and seller do not have complete information about the market.

As a result, unique geographical benefits may have different values for different firms, and as a result, diverse firms' geographical choices are modified correspondingly, i.e., they could be similar throughout all Transnational corporations. On the other hand, the Eclectic Theory's internalization (I) component analyzes how the firm might utilize its resources. It states that even if the advantages of cross-border market internalization are more significant, the company would prefer to engage in global expansion rather than leasing or licensing. What is worth remembering about the Eclectic Paradigm Theory is that OLIs vary from firm to firm, are context-dependent, and represent the host nation's economic, economic, and social elements. As a result, business aims and objectives, as well as the size and structure of output, will be influenced by difficulties and opportunities offered by other nations. Nonetheless, Kusluvan (1998) concludes that the OLI theory is a better framework for investigating the inspiration for companies to go overseas, the explanations for distinct kinds of investments abroad, and why firms investing abroad can excel and that it can form a single grand theory of Multinational enterprises because it has characteristics that encapsulate all the other hypotheses as well as the — as measured for investigating the ambition for companies to go oversea, the causes for varying kinds of investments oversea, or why firms investing international can be. Expanding a multinational company's markets through exports, either to the host country's or neighbouring nations' markets, may also serve as an incentive for FDI. This is referred to as an FDI market-seeking motive. The size and growth of the domestic market, the quality of the infrastructure, the cost and availability of labour, the macroeconomic policies of the host

governments, the presence and competition of related companies, and many other factors influence the market expansion of multinational corporations (Franco et al., 2008; Sakr & Jordaan, 2016; Michalowski, 2012). Multinational corporations move their production operations to a lower cost market in the case of efficiency-seeking FDI in order to increase their cost effectiveness. The production costs of multinational corporations, the existence of agglomerative economies, investment incentives, and human resource development are prioritized with this type of motive (Sakr & Jordaan, 2016). All of the components underpinning the OLI concept are thus relevant factors to analyze in assessing whether African economies have drawn FDI as a result of the governance structures and tax incentives granted or as a result of other causes, which is the goal of this study as stated above.

### **Investment Development Theory**

Despite Dunning's innovation, the eclectic OLI paradigm has come under fire for ignoring the dynamic process of FDI that results from the interaction between businesses in various countries and for testing his theory with many variables. The Investment Development Cycle or Path (IDP) theory was developed as a result of this, and it proposed a connection between a nation's international investment positions (net outflow of FDI stock per capita) and its level of economic development, as indicated by GDP per capita (Dunning, 1982; Nayak & Choudhury, 2014). Dunning proposed four stages of the development path in 1982, and a fifth stage was added in 1986. The first stage discussed the time before industrialization when there was little FDI and little wealth. The host nation's natural resources are its sole geographic advantage. Some location advantages are lacking, which may be brought on by a small market, poor infrastructure, unfavourable government regulations, and other factors. Most FDI inflows to the host nation occur in the primary goods sector, and the nation lacks sufficient ownership advantages to get around barriers to the foreign production of goods and services. Agricultural and labour-intensive craft industries are typically the source of FDI outflows for asset-seeking purposes. The government is currently working on using the right policies to improve infrastructure and human capital (Dunning, 1993; Dunning, 2001; Zang, 2013). The second stage explains the increase in governmental economic interventions that led to location advantages and the rise of FDI inflows. The increase in the cost of education, public utilities, communications, and transportation increases the benefits of the location. The expanding market size encourages foreign companies to take advantage of scale economies in the nation. The development of ownership advantages, along with the improvement of location advantages, causes FDI to shift from the labour-intensive consumer goods sector to one that is capital-



intensive and standardized. A more significant growth rate is seen in the inflow of FDI than in the outflow of FDI. Currently, the government encourages local businesses to create and purchase cutting-edge technology to increase their ownership advantages (Dunning, 1988; Dunning, 1993; Dunning & Narula, 1996; Dunning, 2001; Zang, 2013). In the third stage, local businesses can gain ownership advantages over particular assets like skilled labour, managerial abilities, and innovation potential that draw in foreign businesses. The ownership advantages of local businesses are upgraded by the host country's location advantages, the presence of multinational corporations, and good government policies. As a result, FDI inflows decline while FDI outflows increase. The government then aims to encourage FDI outflow in the sectors with solid location advantages but weak ownership advantages while also attracting FDI in the sectors with weak location advantages but substantial ownership advantages (Dunning & Narula, 1996). It enters the fourth stage when a country experiences more FDI outflows than inflows or a net outward investor. The advantages of ownership grow more robust, and businesses can enter foreign markets through FDI. Then, businesses relocate their operations from nations on a slower development trajectory, maintaining their competitive advantages while looking for new markets and resources. At this point, the host country's industrial structure and income level are comparable to those of a developed country. The amount of FDI that a local company engages in abroad exceeds that of a foreign company in the host country. The government then contributes by lowering the cost of economic transactions to maintain a competitive market and efficient resource allocation (Dunning, 1993; Dunning, 2001). In the final stage, the FDI stocks in most nations, particularly the developed nations, converge and balance. It is the most advanced stage of development where foreign direct investment (FDI) inflow comes from nations in the lower stages of the development path in search of markets and assets. At this stage, the firm's ownership advantages are based on its capacity to coordinate various ownership advantages, update current technologies, and add assets. High-value service sectors experience both FDI inflow and outflow. Additionally, ownership and location advantages can be transferred across national boundaries, which promotes greater national convergence. According to Dunning and Narula (1996), the IDP theory's central tenet was that as nations develop gradually, the conditions that domestic and foreign businesses must contend with change over time. As a result, the government can help maintain efficient markets, cut costs, and overcome market failures. This has an effect on the flow of FDI both internally and externally, which affects the economy of the host nation. As a result, the country's level of economic development and its international investment positions are dynamically interrelated (Nayak & Choudhury, 2014).

## **Neo Classical Theory**

Early neoclassical approaches to international capital movements assumed that capital flows between countries differed depending on the rate of return. This approach is associated with the MacDougall model, which is based on perfect competition, the absence of risk, and other common simplifying assumptions. MacDougall's contribution focuses on the welfare effects of foreign investment rather than the factors that influence investment. Positive welfare effects for both capital exporting and capital importing countries are associated with capital movement between countries under unrestricted capital mobility. MacDougall examines the effects on welfare when one or more assumptions are relaxed in comparison to the basic model. The model's main components are factor endowment, expected profit/rates of information asymmetries, taxation, and government incentives. The neoclassical growth theory was one of the first theoretical approaches to understanding investment. Tasi (1994) attempted to translate a growth model into a simple production function and to investigate key variables that could provide consistent growth rates. He captures variables influencing investment in growth rates in his model. In contrast, according to endogenous growth theory, investment flows can contribute to an economy's economic growth either directly or indirectly. Wang and Swin (1994) distinguish the effects of investment activity into direct positive home-country effects, such as increased production and knowledge transfer to local suppliers, and indirect effects, such as improved workforce quality. Investment is regarded as the primary source of economic growth in less developed countries (Balasubramanyam et al., 1996), with some similarities observed in the European Union (EU). Indeed, investment inflows have contributed to EU economic growth because foreign affiliates have a higher propensity to spend on research and development (R&D) and are more productive when investing in the EU than in their home market (Barrell & Pain, 1997). Endogenous growth theory (Barro & Sala-Martin, 1996; Romer, 1990) has enabled research into the channels through which investment can be expected to promote long-run growth. Furthermore, in an analogy to Newton's law of motion, neoclassical theory was originally used to explain bilateral trade flows between countries (Breuss & Egger, 1997). This theory goes on to say that trade between two countries is determined by the size of their economies, as measured by GDP and population, as well as the distance between the two countries geographically and some preferential trade considerations. According to Zang and Chin (1996), investment should flow from the investing country, which has a comparatively disadvantaged industry, to the host country. The neoclassical assumptions of no market failure and given resource endowments are insufficient to explain trade in intermediate products based on product differentiation and the need to exploit economies of scale. It also cannot account for

other manifestations of market failure. The neoclassical approach is primarily a flexible-accelerator type of investment theory (Lucas, 1993). Lucas' theoretical approach is laid out by sketching out a simple model of capital requirements for profit-maximizing multiple product monopolists. Given a degree of monopoly in its product markets, the multinational firm is assumed to determine the profit-maximizing level of production and, as a result, the capital requirement in each host country. The basic model is expanded by incorporating elements of risk, expectations, and location interdependence. The paradigm shifts to the mode of economic organization rather than the distribution of factor endowments. Given line-specific and location advantages, foreign firms internalize operations in other countries to benefit from advantages such as scale economies and transfer pricing, as well as to overcome market imperfections caused by informational deficiencies.

### **Currency Area Hypothesis**

Aliber (1970) established a hypothesis on foreign investment based on currency strength to explain FDI placement decisions. According to his idea, a corporation belonging to a country with a strong currency would be more ready to invest in a foreign country, while enterprises belonging to a country with a weaker national currency would refrain from doing so. This was due to currency exchange rate disparities between the FDI source and host countries. FDI is more likely to flow into nations with a negative impact on the economy than countries with stronger currencies. When Aliber's concept could explain the trajectory of US FDI outflow into Europe in the 1950s and 1960s, it garnered much attention. When the US dollar depreciated in the mid-1980s, Froot and Stein (1991) tested this idea. This idea explained the increase in FDI inflows to the United States. Aliber (1970) also investigated his idea in the United States, the United Kingdom (UK), and Canada, finding that his findings were accurate and compatible with his concept. Most empirical studies that evaluated the theory found that currency depreciation stimulates FDI inflows while discouraging FDI outflows (Agarwal, 1980). Despite Aliber's (1970) prediction, his theory was not applied to less developed countries with undeveloped or non-existent capital markets and strictly regulated exchange rates (Agarwal, 1980). Furthermore, the hypothesis could not adequately explain investment between developed countries with similar currency strength and investments by multinational companies from developing countries in developed nations (such as investment in the US and UK by Indian firms).

## **A new trade of FDI**

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Despite Aliber's (1970) prediction, his theory was not applied to less developed countries with undeveloped or non-existent capital markets and strictly regulated exchange rates (Agarwal, 1980). Furthermore, the hypothesis could not adequately explain investment between developed countries with similar currency strength and investments by multinational companies from developing countries in developed nations (such as investment in the US and UK by Indian firms). Concepts of foreign direct investment are based on factors such as perfect competition, imperfect markets, currency strength, and connections to global commerce (Gupta & Singh, 2017). Their findings support the endogenous growth models, dependency school theory, and neoclassical growth models as models of how FDI contributes to productivity expansion. In endogenous growth models, FDI boosts research and innovation, management abilities, and wealth creation. According to the dependency school theory findings, first-world economies exploit emerging economies for their labor and raw materials and pay them insufficient wages. This style of capitalism has a detrimental effect on long-term economic success.

## **Assignment theory of FDI**

According to Stephen Hymer's 1960 Ph.D. thesis, the fundamental purposes of FDI were to take advantage of dominant benefits, disperse risks, and prevent market structural flaws (Oehler, 2011). Other writers regarded him as the founding father of the philosophy of the corporate giant. Hymer's FDI theory established ideologies on the study of FDI through money

planning and on the analysis of FDI through strategic management. Firm-Specific Advantages (FSA) and Country-Specific Advantages were the two categories into which the independent components were split in early research of FDI (CSA). The FSA study focuses on factors that affect global companies when they provide FDI. Hymer distinguished between direct investment, which comes with control over the operational business, and portfolio equity, which does not influence the running company (Rayome & Baker, 1995). In an environment of imperfect competition, Kindleberger and Hymer (1969) put out the hypothesis that multinational corporations can make use of their control over assets to generate additional profits.

According to Kindleberger, there are four unfavorable circumstances for FDI. These included deviations from perfect competition in the market for commodities, deviations from perfect competition in the market for factors, internal and external economies of scale, and restrictions placed on production or entrance by the government. There were some serious flaws in the Hymer-Kindleberger FDI hypothesis. The benefits that foreign enterprises would obtain were the sole driving forces (Rayome & Baker, 1995). According to Buckley and Casson (1976), effective FDI does not require any planning, investment, management, required experience, acquisition costs, or innovation transmission. Compared to Hymer and Kindleberger, Richard Caves' (1971) amendment to the FDI theory included more significant restrictions on the kinds of institutions and industries that may profit from FDI. According to Caves, small businesses would be involved in exporting or licensing, who predicted that FDI would mainly occur in more prominent corporations in industrialized nations (Rayome & Baker, 1995). A global corporation should begin exporting its products before using a subsidiary for manufacturing products domestically in a global market. Caves thought this technique would make the community more receptive to the business and its offerings, and the manufacturing cost would decrease.

Nocke and Yeaple (2004) established an "assignment theory of FDI" to explain MNCs' mode of entrance decision order to explain FDI mode of entry. They looked at two types of FDI modalities in their research: greenfield FDI and cross-border mergers and acquisitions. These modes of FDI are considered in both horizontal and vertical FDI. Cross-border mergers and acquisitions (often referred to as brownfield FDI) is the purchase or lease of a firm's assets and processes to combine them as a new entity or take advantage of complementarities. Greenfield FDI is the establishment of a new business in a foreign market, whereas brownfield FDI is the purchase or lease of a firm's assets and processes to combine them as a new entity or take advantage of complementarities. They projected that those disparities in factor prices across

nations would lead to greenfield FDI (from a high-cost to a low-cost country) and cross-border M&A (between countries), while differences in entrepreneurial ability between countries would lead to cross-border M&A. Furthermore, their model indicated that greenfield FDI is more efficient on average than cross-border M&A, and their empirical findings backed up this prediction (Nayak & Choudhury, 2014).

### **Endogenous Growth Model**

In response to the flaws and limitations in the Solow-Swan model, Romer (1990) proposed this approach. The neoclassical growth theory describes the long-run price of a financial system's boom with a heavy emphasis on endogenous causes. The model places a premium on technical progress, which is determined by the amount of finance available, the stock of human capital, and the size of the capital inventory. By emphasizing FDI as one of the long-term factors of the boom, the endogenous growth theory has tempered the ambiguity in the research. It emphasizes that variables like rising returns brought by technological changes and economies of scale within the industrial process are the primary drivers of economic growth. Various articles attempted to explain the relationship between FDI and monetary growth. For example, in an attempt to explain this link, Romer (1990) and Grossman and Helpman (1991) contributed by generating growth patterns consistent with the endogenous boom concept. Their trends are based on the premise that technological advancement significantly impacts an economy's growth. According to them, introducing and transitioning technological competence is a priority, and innovation is considered a necessary means of achieving financial growth. With this analysis, they discovered that the extent to which developing economies absorb and exploit new technologies from highly developed economies is critical in determining developing nations' development rates.

Foreign direct investment, they claimed, is how advanced technology is made available to emerging nations. Because developing nations cannot produce and generate new technology, they resort to using generation invested from established economies through the route of FDI, according to their theory. In addition, Borensztein et al. (1995) further contribute to endogenous growth theory by claiming that technical advancement, as propounded by endogenous growth theorists, occurs through the capital-deepening process, mainly through the formation of new capital items. New types of capital are provided through FDI. The endogenous growth model implicitly anticipates a positive link between FDI and monetary growth, particularly in developing nations with lower human and aggregate capital levels. This forecast is based

entirely on the importance of human capital and technological advancements in the growth process and the fact that FDI depends on physical capital, technology, and talent transfer. Even though the endogenous growth idea is designed to address the shortcomings of the new classical growth concept, Fisher (1993) criticizes the principle for its reliance on the manufacturing characteristic and the average country's best. Olson et al. (2000) also criticize the theory for overlooking the importance of institutions and putting too much focus on the role of human capital. In conclusion, the boundary between physical and human capital is not always clear among the various forms of the theory. Capital goods, for example, are critical to monetary growth under Romer's view. He believes that when human capital accumulates, it becomes a driving force when it is fully embodied in body capital. On the other hand, he fails to specify who is using force.

### **The Solow's Growth Model**

Most increase analyses in economics start with this foundation. It is a sequel to Solow's (1956) and Swan's (1957) works (1956). The model is based on the neoclassical production characteristic, which states that the amount of output and growth in an economy is determined by the quantity of labor (L), capital (K), and knowledge, as well as the efficiency of labor (A). These inputs are combined to produce output via a feature of the shape  $Y(t) = F [K(t), A(t), L(t)]$ , where Y is the output and t is the time that enters the function via capital, labor, and technology (Romer, 2012). When it comes to long-run growth rates and returns, the Solow Model predicts that countries with low GDP per capita due to low capital accumulation will likely enjoy higher rates and returns (Salai-i-Martin, 2004; Salai-i-Martin and Barro, 1995).

According to the Solow growth model, FDI enters the production function through capital inventory (K) and promotes monetary growth in the recipient country. This is because FDI includes the natural movement of capital into the host country, such as bodily capital. Which tends to feature as much as the host nation's current combination capital stock? (Solow, 1956). The usual neoclassical growth model is rendered theoretically inefficient in developing with the long-run determinants of increase when considering the underlying assumptions of diminishing returns to capital and then the prediction of the neoclassical version that boom is due to exogenous factors such as technological development, population boom, and steady savings price (Salai & Martin, 2004). This is because, in the long run, growth is determined by endogenous factors like investment and the stock of human and physical capital rather than exogenous factors. On the other hand, the inability to provide the study with the long-run causes of the boom prompted the development of the endogenous growth model, which proposes that

the boom is attributable to endogenous factors. One of the most significant flaws in this concept is that it completely ignores the issue of capital stock composition and considers capital to be a homogeneous entity, which is impossible.

Furthermore, the idea disregards technological advancement. Technological advancement is critical in a boom system, but it goes unrecognized in the Solow boom version (Romer, 1990). The difficulty of encouraging technical advancement through expertise acquisition, investment, and capital formation is also overlooked (Mankiw et al., 1992). Finally, the idea is based on the erroneous premise that capital is homogeneous. However, capital objects are no longer homogeneous, which could lead to an accumulating problem. In a word, concluding that there is a regular growth route when there are several capital items in the marketplace is highly challenging. De Mello (1997) conducted research to assess the effects of FDI influx as forms of knowledge transfers and the accumulation of technology and capital on the economic growth of developing nations, which strengthened the neoclassical growth model. According to De Mello, FDI would substantially affect economic growth in emerging nations with more sophisticated technology and less of an influence in developing nations with less advanced technology. In agreement with De Mello, Rebelo (1991) and Iamsiraroj (2016) pointed out that the neoclassical model predicted that economic growth would rise with stable and positive technical advancement.

### **The Push Theory**

According to this hypothesis, forces outside of the home country are to blame for FDI. Slow economic development and low-interest rates in industrialized nations are among the push factors, and they have been given significant significance (Calvo & Reinhart, 1998). Additionally, investors' growing desire for global diversification might drive capital toward developing economies (Calvo et al., 1996). Empirically, researchers like Calvo et al. (1993) and Fernandez-Arias (1994) linked the drop in the US interest rate to the rise in capital inflows from developing nations in the 1990s. The authors also point to the increase in multinational firms' tax rates as a significant push factor. Although a large body of research claims that recessions in industrialized nations cause the capital flow to developing nations, a different perspective has occasionally been offered for wealthy nations. According to Jeanneau and Micu (2002), strong economic growth in industrialized nations is essential in explaining emerging nations' portfolio inflows. The contagion effect is a different collection of household elements in literature. Since the Asian crises of 1997–1999, the topic of contagion has received much attention in the literature. In general, it explains the relationships between groupings of nations.



Three methods of contagion transmission are listed by Masson (1999). They are the shift or pure contagion, the spillover effects, and the monsoonal impact.

It is thought that several nations, particularly those in the same region or with comparable economic conditions, are concurrently impacted by the monsoon effect (such as accurate interest rates of large, industrialized countries). The consequences of spillover are often brought about via trade and financial channels. While financial channels are a product of PI, trade channels involve market rivalry and fluctuations in import prices. Therefore, if both nations are connected through commercial operations, a decline in competitiveness for country "A," for example, might result in a decline in country "B's" currency. However, a simultaneous crisis caused by the abovementioned reasons is known as pure contagion or shift contagion (Masson, 1999; Forbes & Rigobon, 2002). For example, a shift in investor attitude might result in fund reversals and financial crises. Forbes, Rigobon, Kleimeier, and Sander (2002) and Kleimeier and Sander (2003) evaluated the Masson contagion variables (1999). They offered proof that the first two of Masson's elements may be transmission routes for external shocks and that only the third factor might represent contagion. This idea has significant consequences for the formulation of policies aimed at African FDI inflows that are sustainable. For instance, if it turns out that lower interest rates help developing countries attract FDI, higher interest rates can make it harder for these countries to continue the inflow. Whether the domestic reaction is likely to evaluate the prospect of reversal effectively poses a crucial concern for policymakers in the host nations.

### **The Pull Factor theory**

According to the pull factor argument, the receiving nation's domestic fundamentals caused the money to move there. These internal variables include a nation's creditworthiness, fiscal and monetary policy progress, and neighborhood externalities (interest rate and host country price-earnings ratio) (Calvo et al., 1996). Haque, Mathieson, and Sharma (1997) also cited growth in domestic output and domestic money demand as pull factors. The performance of macroeconomic indicators, including capital accumulation, inflation, GDP growth rate, current account balance, and gross domestic investment, are also considered to be domestic factors. As a result, assessing the extent of solid economic policies, the longevity of capital outflows, the investment climate, technology, and institutional quality is essential. Several academics have highlighted pull factors as the key elements that explain the capital inflows of developing economies in the 1990s (Chuhan et al., 1994; Ul-Haque, Kamar, Mark, & Mathieson, 1996). The authors contend that financial liberalization has enhanced the credit

quality of developing nations, resulting in increased international capital mobility, along with other factors such as the privatization of state enterprises and an improvement in macroeconomic conditions. Basu and Srinivasan (2002) also present evidence from Africa that these nations have attracted FDI due to well-structured economic reforms, political and macroeconomic stability, and natural resources. Similarly, Asiedu (2002) discovered that weak policy and trade barriers impede capital flows to African nations. According to Asiedu (2002), these elements are crucial for explaining the share of foreign capital inflows to African nations.

### **Differential Rate of Return Theory**

This hypothesis evolved from traditional investment theory, which assumes that firms maximize profits and equates the expected marginal benefit of capital to the marginal cost of capital. The hypothesis assumed that the main reason for multinational corporations to transfer capital from one country to another was the difference in interest rates between countries. It goes on to say that when there is no risk or uncertainty in the markets, capital flows into the region or country will produce the highest return. The hypothesis gained popularity in the 1950s when American firms located in Western Europe outperformed those in the United States (Hufbauer, 1975). In the 1960s, American firms' investments in Europe suffered a setback, and returns earned by US firms in their home country outperformed those earned in Europe. However, American firms' FDI growth in Europe increased, and the differential rate of return was unable to explain the situation. Attempts by researchers to statistically test the differential rate of return hypothesis (Popkin, 1965 as cited in Agarwal, 1980; Blais, 1975 as cited in Agarwal, 1980) failed to produce conclusive results. Furthermore, Hymer (1976) exposed the flaws in this hypothesis, claiming that it was inconsistent with several aspects of international investment. This was due to the assumption that capital would flow from a low rate of return country to a high rate of return country.

### **Market Size Theory**

The market size hypothesis emphasizes that the amount of FDI inflows into a country is determined by the host country's market size. It is based on the neoclassical theories of domestic investment and the assumption of a perfect market. Most empirical studies measure market size as the host country's Gross Domestic Product (GDP) or Gross National Product (GNP). The logic behind this hypothesis is that domestic firms increase their investments in response to sales, and the country's domestic investment rises as GDP rises (Agarwal, 1980). The

connection between FDI inflows and market size has been supported by empirical studies like Moosa (2002) and Okafor (2014), which show that FDI flows to nations with larger markets or higher purchasing power, allowing foreign investors to earn a higher return on their investments. There aren't many negatives despite the link between FDI and market size. The first is that the neoclassical theories of domestic investment, which are based on irrational assumptions, are the foundation for the market size hypothesis. Additionally, the size of the domestic market in the host nation may have an effect on the creation of quality, but not on FDI exports. Furthermore, a strong correlation between FDI and GDP reveals little about their structural connection (Agarwal, 1980). Studies in imperfect markets came into being as a result of the shortcomings of the hypotheses under the assumptions of perfect markets. Variations in the goods and resources that different nations have to lead to some kind of market distortion that prevents FDI from being realized in the ideal market. This is because it is unclear how much capital will be coming in, how much it will cost to gather information, and how much risk and uncertainty there will be. Hymer (1976) first brought this up in his doctoral thesis, which laid the groundwork for market imperfections.

### **Monopolistic Approach Theory**

Kindleberger (as cited in Liu, 2009) expanded on the work of Hymer (1976), emphasizing monopolistic power in imperfect markets. He emphasized that multinational corporations benefit from patents, superior technology, and other things. These benefits drive MNCs to invest abroad to fully utilize the resources of the host nation rather than splitting them with potential rivals in the host market. Most businesses will be encouraged to invest in the host country when there is a high likelihood that these multinationals will enjoy monopoly profits. Kindleberger's analysis was unable to explain the advantages that the monopolistic firm must prioritize, despite the numerous advantages it enjoys in a foreign country. Additionally, monopolistic advantages or power are only granted to a company when the laws or policies of the government of the host country permit it (Liu, 2009).

### **Product Life Cycle Theory**

Vernon (1966) created the product life cycle theory, which was the most pertinent traditional theory related to the study of industrial location, in an effort to justify when and where FDI should occur. Hirsch was the first researcher to evaluate the product life cycle in relation to the need for labour and technology (1965). Hirsch argued that capital-intensive

processing technology matures from its initial and research developing stage to a mass production and distribution stage using a case study of the electronic industry in the United States (US) in 1960. Hirsch claimed in his analysis that electronic devices are initially produced in batches. Engineers are employed in the production of new products. As a result, manufacturers strive to maintain their investments as fixed assets. Additionally, mass production and distribution are introduced as the products move into their growth phase. Production becomes more capital-intensive, management skills become more crucial, and the labor-to-capital ratio declines. Product specifications are standardized at this stage, and the price of unskilled labour is what matters most (Hirsch, 1965). His research found that, during the early stages of industrial development in the electronic industry, when extremely highly skilled labour was needed for production, the US had the most competitive location stage. As the industry develops beyond its infancy, other nations that provide lower costs and lower wages for labour engaged in mass production overtake the United States in terms of competitiveness.

Vernon (1966) approached the process of internationalization using Hirsch's (1965) existing theory, which is almost identical to Hirsch's (1965) analysis. His research proposed the Product Life Cycle Theory as a way to explain the changes in global trade and investment (PLC). The PLC theory, which was based on the regional preferences of US producers, made the assumption that businesses in developed economies were similar and had access to knowledge. He argued that any location theory for MNCs that leaves out the importance of economies of scale, uncertainty, and ignorance, in addition to innovation, is insufficient. He treated trade and FDI as being a part of the same process of exploiting the markets of foreign countries, replacing the trade in his model with how FDI is perceived (Liu, 2009). According to his theory, MNCs' location decisions were influenced by a variety of factors, including market demand, effective and quick communication, and production flexibility, all of which were essential for the formation and growth of markets. According to Vernon's PLC theory from 1966, firms in developing nations were passive recipients of technology and expertise during the product life cycle's maturity stages. MNCs were derived from three potential sources as a result of this. The first source was the availability of highly developed technologies, whose production stages had been abandoned by developed companies but were still underdeveloped in less industrialized nations. The second source dealt with the benefits of downscaling technologies, which increase labour intensity in production. The third source, which is the last, addresses the cost advantages that result from wage reductions. Vernon (1979) expanded on his research on the product life cycle theory and proposed that producers should place less emphasis on labour and capital costs in the early stages of production. This was brought on by the

significant disparities in firm production and the early-stage monopoly power of production. He added that early locational choices made by businesses were largely based on elements that aided in the effectiveness of product development. The elements include efficient communication channels and the availability of essential managerial and technical skills (Liu, 2009). However, the firm's capital and labour cost is a primary concern when product standardization and business competition increase. This was one of Vernon's problems with the PLC theory (1979). The idea that mass production had become obsolete by the late 20th century and that specialization was now the preferred method of production was another criticism of his theory (Taylor & Thrift, 1982). Additionally, not all forms of FDI were explained by the PLC theory, and some of the presumptions were no longer valid (Agarwal, 1980).

### **Oligopolistic Theory**

Knickerbocker's Oligopolistic reaction theory was developed in an effort to explain FDI (1973). His theory was predicated on the idea that there existed an imperfectly competitive market. He identified three reasons a business might choose to invest in or establish itself in a nation. The initial driver was the desire of businesses to gain more access to the nation where they make investments. The abundance of resources in the host country was the second motivation for businesses to invest there, and a third reason was to counteract strategic moves by competitors (Head, Ries & Mayer, 2002). According to Knickerbocker's (1973) oligopolistic theory of FDI, businesses copy each other's location choices. For instance, if firm A makes an investment in a host nation, firm B will imitate firm A and make an investment in the same nation. This is a result of the unpredictability surrounding the cost of production in the host nation. Additionally, businesses are able to avoid being underpriced when they copy one another (Altomonte & Pennings, 2003). Because there are fewer firms in an oligopolistic market, it is possible to determine how a firm's actions affect its competitors (Gwynne, 1979). He calculated an entry concentration index for his study, which used manufacturing FDI data from 187 MNCs in the US to demonstrate how American companies' forays into foreign markets tend to cluster over time. His analysis revealed a strong correlation between his entry concentration index and the US industrial concentration index (Agarwal, 1980). Additionally, he discovered a negative relationship between product diversity and FDI. Based on his research, he came to the conclusion that firms' oligopolistic responses rise with entry-level concentration and fall with product diversification. When there are cost uncertainties in the host country, the oligopolistic reaction follows Knickerbocker's (1973) hypothesis. As a result, oligopolistic

businesses that are sufficiently risk averse and unsure about making investments abroad are more likely to establish themselves there if one or more of their competitors make an investment there. However, when the cost of investing abroad is known, businesses are less likely to decide to do so when one of their competitors invests abroad (Nayak & Choudhury, 2014). The theory also leaves open the question of why the leading firm chose to invest in a foreign nation.

### **Modernization Theory**

The 1950s and 1960s saw the introduction of this theory, which has since developed (up until the late 1990s). Although it has no particular proponent, American social scientists in the early 1950s are thought to be the originators. Its definition widened as it developed, and new variations emerged. The most widely accepted definition of modernization is a theory that explains how a nation transforms from a traditional way of life or society to a modern one. Marxist, capitalist, western, and many other theories have been theorized as variations of the leading theory. This study uses a different interpretation of modernization theory. The early versions of the theory can be divided into three main categories: national identity, literacy development, and economic modernization. The unpopular version of the theory—economic modernization—is used in the study. This theory examines developments in technology and society that can promote growth. The Diffusion of Innovations theory, which essentially explains why innovation spreads and measures the rate at which it can spread, is one of the sub-theories under the economic modernization theory.

On the other hand, the Economic modernization theory asserts that Foreign direct investment is essential for a nation's economy to advance. As was already mentioned, this theory challenges the dependency theory's point of view. In actuality, the critics of the dependency theory's assumptions led to the development of this theory. These systematic economic postulates serve as the foundation for dependency theorists' beliefs that significant capital investments are necessary for an economy to grow from a capitalist point of view. Foreign direct investment attracts capital investments to the nation. It is challenging to obtain these capital investments through other channels (in such quantities and favourable terms). Through Foreign direct investment, an economy can access substantial capital investments. Therefore, encouraging Foreign direct investment in the country makes sense to nations looking to grow its economy. Based on this, Foreign direct investment promotes or may promote economic growth by supplying the necessary capital investments. Neoclassical and endogenous growth thinking are the antecedents of this theory. They believe the foreign direct investment is crucial for economic growth, particularly in developing nations, because it brings in the

capital investment, innovation, and knowledge the nation sorely needs but cannot produce on its own. The human capital, infrastructure, political and social stability, technology, and innovation required to create and support growth are lacking in developing countries. In addition to providing the necessary capital, Foreign direct investment enables the transfer of knowledge and skills. This study supports the modernization theory in that Foreign direct investment is necessary for developing economies to have the resources necessary for economic growth. Foreign direct investment is necessary to achieve economic development and close the gap quickly. Here, technology flow is particularly crucial. Both direct (capital investment) and indirect investments are made in the nation (investments other than capital). Infrastructure development, novel human skills, managerial and marketing procedures or techniques, and other nuances that improve capital investment are examples of indirect investments that may enter the country. It is not unusual to see new roads built to connect a mining site to a processing facility, employees being trained in new skills, or cutting-edge equipment being imported to replace antiquated ones. The mining company will not be the only winner from this new road. It has a knock-on effect on the economy because it would encourage businesses to have simple access, boosting output and supporting economic growth.

### **The Dependency Theory**

The dependency theory was one of the first theories to explain how investments in technology spread. It began to take off in the early 1970s. The world has a capitalist economy, foreign investments always flow from developed economies to developing ones, and developed nations take resources out of developing nations are all predicated on dependency theory. According to the dependency theorist, FDI does not ultimately result in economic growth. They contend that developed nations deprive developing nations of the natural resources they need to develop by attracting foreign investment. To put it another way, proponents of dependency theory contend that FDI has both long- and short-term effects on economic growth. Arguments include that developing nations increasingly depend on foreign businesses for economic development. However, these foreign companies are only interested in making money. As a result, they develop monopolies and unfair competition in local markets (Adams, 2009). Market imperfections occur, which stifles economic expansion. According to Sylwester (2005), dependency theorists believe that FDI has a crowding-out effect that affects domestic investment by driving up investment costs and creating market distortions that harm economic growth and development.

## **The Rational Choice Theory**

According to the rational choice theory, rational decisions made by people may explain human behavior and social interactions in general. People are thought to cooperate in social interactions, including political discussions, provided the expected benefits outweigh the anticipated costs of the contact (Sato, 2013). According to Ogu (2013), citing Becker (1976), "Gary Becker, a 1992 Nobel Memorial Prize laureate in Economics Science, who was one of the protagonists in applying a wider application of the rational actor, popularized the rational choice theory first." When he said that "when presented with alternative courses of action, people often chose what they feel is predicted to have the best overall effect," Elster (1989) captured the core of the rational choice theory. The rational choice theory's definition of "rationality" is more precise and constrained. It may be summed up as "individual behaves as if calculating costs against benefits to arrive at an action that maximizes personal advantage.

The idea assumes that people are actors who always act like self-aware, logical entities. Self-centered and concerned only with oneself. According to the assumptions, these people decide what to do based on their preferences and any possibilities or limitations they may have. This implies that people make the best decisions they can, given the circumstances as they view them. An additional supposition is that the rules and regulations that govern behavior are just particular applications of the rational choice theory. The person's actions are solely focused on ensuring his welfare. People tend to act in ways that would be more advantageous to them; individuals are more likely to choose the options they believe to be best for them. Individuals manage corporations. People on the Board of Directors plan the decisions that the organizations make. As a result, this theory bases the option to invest on an individual's preferences. People who make up the government have the power to decide whether or not it should have a robust corporate governance framework.

## **The Stakeholder Theory**

Stakeholder theory was progressively developed by Edward Freeman and entrenched in the management discipline in 1970. Stakeholder theory is "any group or individual that can impact or is affected by the fulfilment of the organization's objectives," according to Freeman (1984). In contrast to agency theory, which emphasizes that managers serve stakeholders first and foremost, proponents of the stakeholder theory contend that managers in businesses must also serve a network of connections that includes customers, partners in business, and workers (Freeman, Harrison, Wicks & De Colle, 2010). In contrast to other theories focusing on



shareholders, this one considers a more extensive range of stakeholders. Stakeholders are people or organizations whose interests are impacted by business decisions, who gain from them, or whose rights are defended or promoted. The concept of a stakeholder is a generalization of the idea that shareholders have certain rights concerning the company (Freeman et al., 2010). According to Freeman et al. (2010), a "limited definition" of stakeholders covers those organizations that are essential to the success and survival of the company. Any group or person that can impact or is affected by the company is included in the "comprehensive definition."

Given that one might impact the other in terms of rights and obligations, as well as advantages and damages, the stakes for each are reciprocal. The elements included by the limited definition are essential to the firm's existence and success. Although there will undoubtedly be one stakeholder group that benefits at the expense of others, the stakeholder theory does not prioritize one stakeholder group above another (Freeman, 1987). Focusing on shareholders raises the possibility that the preservation or growth of shareholder wealth will take precedence. At the same time, the core shareholder value becomes less obvious when a wider stakeholder group is considered, including workers, suppliers, lenders, consumers, the government, and the local community (Abdulla & Valentine, 2009).

However, many businesses do work to increase shareholder value while also attempting to consider the interests of a larger stakeholder group. Since they get the remaining free cash flow, shareholders are essentially given preference over other stakeholders. This implies that the shareholders have a stake in ensuring that resources are used as effectively as possible, which should ultimately benefit society (Yusuff & Alhaji, 2012). Because it serves the greater good or because of property rights, maximizing shareholder welfare is constrained by moral or social principles (Mallin, 2004). This approach effectively conveys the obligation a firm has to stakeholders besides shareholders. Multinational firms, in this argument, even if they are foreign, nonetheless need to consider the other firm stakeholders in the host country. Additionally, domestic businesses must view foreign investment as a shareholder. The theory's primary focus is the normative prescription of moral and social obligation to the stakeholders. The prescription is seen in directors' tasks as they oversee corporate matters. The abovementioned obligations are based on common law and serve as guidelines in Commonwealth nations when they are not codified.

### **The Growth Theory**

The middle decades of the 1980s saw the emergence of new growth theories. Unlike the dependence and industrialization models, these models use a growth theory framework to

investigate how FDI affects growth. The Solow growth model or the conventional new classical model is valid here. The following are its underlying tenets: capital flows from surplus (developed areas) units to deficit units, technical development is exogenous rather than endogenous in the industrialization model, and declining returns to physical capital (developing regions). In that it implies that nations with identical capital-labor ratios and factor prices would have convergent long-run equilibrium, the growth model is comparable to the dependence theory (Fan, 2002). New growth theories have strengthened the alleged shortcomings of the neoclassical growth model. The neoclassical model has flaws, including growth measured by capital accumulation and technical advancement measured as an external quantity. The new growth paradigm emphasizes technology and its diffusion as economic development catalysts. Studies along this line of thinking have examined the impact of research and development (R&D), human capital, and its transfer through commerce on growth.

## **Governance Structures**

The term "governance structure" describes a group of rule-based procedures for laws, regulations, and accountability that control the interaction between an organization's stockholders and its management (Foo & Witkowska, 2011). Gutierrez-Urtiaga (2004) defines *governance* as the set of institutions that determines how the residual claims are distributed between those who have participated in generating profits. According to Arun & Turner (2009) for Organization for Economic Co-operation and Development (OECD) economies, governance controls and manages business corporations. Governance structures practices as a system specify how stakeholders' rights and responsibilities are distributed. They shape rules and procedures for the decision process and provide an outline for the determination of the objectives of a company. Shleifer and Vishny (1996) contend that governance structures ensure that stakeholders obtain a return on their investment. However, Arun & Turner (2009) attempt to reconcile all the previous concepts, which they regard as mutually exclusive. Therefore, corporate governance is the available system of institutions or mechanisms that induce incentives in listed business firms to distribute benefits between stakeholders, restricting discretion on such distribution. The authors focus on institutions and mechanisms that are structured to solve conflicts of interest, and if this process is successful, the risk faced by investors and creditors of the firm will be lower. The governance structure is founded on the traditional realization of the privileges allowed to the company under incorporation. It is often based upon two arguments about how these devices serve the public good. Lucas (1990), who

addresses the issue of why capital flows from rich to developing countries do not occur in the global economy until capital-to-labour ratios and, consequently, wages and capital returns are equalized, has indirectly made a case for the potential relevance of governance to explaining FDI flows across countries. He examines various hypotheses and disproves several well-known ones on conceptual grounds, including the idea that technological advancements have made capital significantly more productive in developed nations.

The efforts of the host country governments to appropriate economic rents associated with incoming foreign direct investment through instruments like heavy taxation are one explanation that he finds pretty plausible. In light of the significant factor price differences between developed and developing countries, he suggests this as a potential explanation for the relatively low rates of capital formation in developed countries. While other government policies that discourage domestic capital investment may also influence inter-country differences in economic performance, Lucas identifies explicit policies targeted at foreign investors. He emphasizes that capital flows cannot be predicted solely by considering labour and capital scarcity. The characteristics of locations that attract or repel foreign investors are the subject of the relatively large empirical literature. All other things being equal, it makes sense that FDI will be drawn to areas with better governance infrastructures, but most pertinent literature has concentrated on economic factors that influence FDI inflows. Of course, country-specific political risk has been acknowledged as necessary in the literature on international business. In order to account for inter-country variations in the general political environment, empirical analyses of FDI now frequently include some variables, though with somewhat mixed results. The premise is that sustainable development in Africa necessitates good governance. A practical and transparent public administration, a predictable regulatory system, and an independent judiciary are necessary for development and growth. However, while the state must work to create an environment that fosters growth and development, it should be understood that achieving good governance is a process (Hamdok, 2001). In a broad sense, governance infrastructure refers to the institutions and regulations governments establish as a foundation for social and economic interactions. The governance infrastructure components that have the potential to influence MNCs' investment choices are our main areas of concern. Consequently, a "positive" governance infrastructure would consist of a legal system that is effective, fair, and transparent in protecting private property and individual rights; public institutions that are dependable, trustworthy, and sincere; and public policies that support free and open markets. These conditions promote FDI and, presumably, private domestic investment by preventing arbitrary direct or indirect appropriation of privately held assets. Similarly, the same

circumstances encourage MNCs to invest in sunk costs that support effective operations in host countries. When conceived in this way, governance infrastructure can be compared to physical infrastructure and human capital. Traditionally, it has been assumed that investments in the creation and upkeep of utility, transportation, and communications networks constitute physical infrastructure. Less obvious investments in people, primarily in health and education, are reflected in human capital. Human capital can be viewed as human infrastructure to the extent that it is supported by public policy and provided by the government.

The first argument is that incorporation is a public concession by the state in return for benefits, and the second is that there is a valid contract that entitles a company to exist as a private entity and so should, in a liberal democracy, be defended by the law. The central assumption is often labeled the 'concession' view because it regards the company as an existence granted by the state as a benefit to its members, which in return has to be justified by the performance of public welfare functions such as the creation of wealth. The state is entitled to intervene to define and ensure compliance with corporate objectives. However, this argument has been increasingly undermined by the proliferation of companies and other wealth-creating organizations (Warren, 2000). The goals of FDI may not always coincide with the goals of host nations. The use of locally produced inputs by multinational companies, the ease of mobility of skilled workers and the presence of competition are just some of the factors that should be considered to maximize the positive effects on FDI. Failure to address these issues may result in job losses. Therefore, the government must intervene to lessen the negative effects of foreign capital flows by creating policies that are designed to help local businesses catch up with multinational corporations, prevent local businesses from failing, promote vertical integration, and attract foreign investors whose objectives are similar to their own. A nation must develop policies that prioritize workforce training, ensure the availability of high-quality infrastructure, maintain a stable political environment, and reduce administrative red tape in order to draw the best foreign investors and advance industrialization. Some local businesses operating in the same sector will experience losses as a result of lower profits and higher fixed costs brought on by competition effects brought on by the entry of multinational corporations into a domestic economy. Authorities are anticipated to step in to stop productivity from declining further. The government can take direct action by fostering better education systems, encouraging research and development, and enhancing transportation infrastructure. In his theory of "big push industrialization," Rosenstein-Rodan (1943) mentions this direct involvement of the government in industrialization. He suggests that governments should take a more active role in investment project coordination and provide skilled and unskilled workers with the necessary

training. These programs have long-term advantages because they boost literacy and complement industries. More robust government policies are promoted by Murphy, Shleifer, and Vishny (1989) through enhanced infrastructure (such as railroads and airports), financial assistance for businesses engaged in manufacturing, and the availability of inexpensive capital for undertaking projects.

Today, it is widely acknowledged that good governance is necessary for a country's markets to operate smoothly and, as a result, for favourable investment conditions and the sustainable allocation of capital. Many multilateral organizations have considered what constitutes good governance and how it relates to development investment. These organizations' perceptions of what makes for good governance vary as much as their cultures and experience levels. Some of the critical aspects of governance are government effectiveness, the rule of law, voice and accountability, control of corruption, regulatory quality, and political stability (Kaufmann et al., 2003). Additionally, sound democratic principles in a nation's political life are part of good governance, as are procedures for consultation with the private sector and other civil society members to ensure that laws are compatible with the requirements and potential of businesses and the economy as a whole. Regardless of each nation's unique historic-cultural context, a dysfunctional governance system can be easily detected by several signs, including corruption, the waste of environmental resources, a decline in public confidence in the government, and a lack of respect for constitutional rights, and many others. This typically results in less than ideal-use of the nation's financial and human resources. Given the relative irreversibility of FDI, unwarranted doubts about legislative action, regulations, and enforcement are significant roadblocks to increasing risk premiums generally and apprehensions about discriminatory treatment. A hostile business environment in the host nation drives up information costs, directs corporate efforts toward rent-seeking activities, and may even encourage outright criminal activity like corruption. While this hurts the entire host country's business sector, it may serve as a more significant deterrent to visitors who lack access to local knowledge. On an equal footing, all businesses, domestic and foreign, should be able to understand the environment in which they operate and adequately brace themselves for impending changes.

Transparency is arguably the most significant component of the enabling environment that policies can affect. Numerous studies indicate that if businesses can obtain a reasonable level of clarity about the environment in which they will be operating, they may be willing to invest in nations with legal and regulatory frameworks that would not otherwise be regarded as "investor friendly." On the other hand, it seems that there are some transparency thresholds

below which the business conditions become so opaque that almost no investor is willing to participate, regardless of the size of the inducement. Because it promotes governmental accountability, participation, and outcome predictability, transparency in governmental decision-making and implementing public policies is crucial. Clear and enforceable rules and procedures are necessary to achieve transparency; these are preferred to those that give government officials discretionary authority or are open to various interpretations. To make sure that rules are followed, accountability is required. Similarly, without legal frameworks that strike a balance between the right to disclosure and the right to privacy, as well as without institutions that accept responsibility, transparency and information openness cannot be guaranteed.

## **Mapping out Governance Structures and Foreign Direct Investment**

Due to considerable information asymmetry and uncertainty in most emerging nations, financial indicators of potential domestic investors are often inaccurate or even deceptive. While studies show that investors utilize corporate governance standards to assess the quality of enterprises in uncertain local markets, the question of whether the same applies to cross-national investment remains unanswered. Luo and Chung (2009) look at several foreign businesses' Joint Venture (JV) partners to see how corporate governance policies affect foreign investment in developing nations. The promise of recruiting strategic assets from local partners, obtaining indigenous knowledge, and gaining a gateway into local social networks makes forming JVs with local enterprises an appealing entrance mode for foreign companies.

Luo and Chung (2009) look at three ways corporate governance principles influence how international businesses choose local partners. The first option is based on agency theory, which holds that a set of the most dynamic management parameters exists. Foreign investors would use these factors to select local partners to reduce monitoring costs. Another complication is that multinational enterprises are eager to conform to host-country practices since institutional alignment can improve performance in local contexts. Because of their affinity with local institutions, multiple national corporate governance systems may be equally effective, according to a comparative governance structure study. Local adaptability is also essential, according to international business studies. As a result, foreign investors can choose partners who follow the local model. The similarities between the reasons of buyers and MNCs, according to Kinotsha and Campos (2003), can be categorized into several types of FDI.

- ❖ Natural aid – looking for funding to exploit raw materials for manufacturing and flow to international locations that are well-endowed with herbal assets.

- ❖ Market – Seeking investment to access markets due to the period, relevant profit generating abilities, and boom possibilities.

- ❖ Efficiency – Looking for investment opportunities that take advantage of a country's unique capabilities, such as having access to a skilled workforce, low-cost labor, and infrastructure development.

- ❖ Strategic asset – Investing in the styles of access to specialized statistics (patents), product brands, and marketplace percent of modern-day corporations is a strategic asset.

- ❖ The eclectic paradigm (OLI) was devised by Dunning (1998) as a framework for grouping and analysing MNC investment overseas into three sorts of benefits:

- ❖ Ownership (assets rights, patents and intangibles which is capable of take advantage of, get right of entry to and export herbal assets).

- ❖ Location (labour benefits, institutional frameworks, alternate obstacles, and alternate fees).

Internalization exploitation of market imperfections/arbitrage in outside markets, which include trade quotes, tariffs and subsidies, and production of products and offerings in place of licensing.

According to Markusen and Maskus (1999), foreign direct investment flows to higher-income developing countries such as China and Brazil due to MNCs' ability to exploit the superiority of skilled labor and installed infrastructure, as well as the potential to export this lower back to the MNC determine. As a result, economies of scale and manufacturing costs are important factors when investing in these countries with large local markets to serve. FDI can be described as the acquisition of a long-term managerial stake in a firm based in a foreign country by a legitimate investor from one country, and it refers to the purchase as well as all subsequent transactions (The World Bank, 2000; IMF & OECD, 2003). It usually refers to the purchase of more than ten percent of ordinary shares or vote-casting rights. Direct purchasers take a strong involvement in the organization via management and decision-making, distinguishing FDI from other investment forms. FDI also differs from other types of investment in governance and ownership. Because the decision is taken in conjunction with the long-term rights status quo in a foreign funding firm, FDI is far less volatile than other funding sources.

According to studies, multinational corporations advance technology, produce money, and generate jobs (Ofori-Brobby et al., 2010). However, other research demonstrates that multinational corporations have the power to exploit whole nations, exert disproportionate political influence over host country governments, and worsen the job situation at home (Contessa & Weinberger, 2009). Governments in host nations frequently commit to FDI for years or decades, which can put multinational corporations in financial problems if unforeseen social and political instability occurs (Meyer, 2003). However, the anticipated high return on investment will outweigh any potential hazards. Due to supply, demand, and political considerations, multinational corporations participate in FDI (Jones, 2010). The supply elements that multinational corporations desire are reduced manufacturing costs, more favorable locations, cheaper distribution costs, natural resources, and more straightforward access to technology. Improved marketing management, brand monitoring, and brand protection are demand drivers. Some political aspects are avoiding trade barriers and providing economic and fiscal advantages. Understanding the factors that influence FDI is crucial since doing so may make developing nations more alluring to FDI.

## **The Concept of Tax**

Taxes are classified as leakages in the National Income Accounting framework. Increased taxes lower consumption and investment, which are components of the national income accounting model; therefore, a rise in tax revenue is regarded as a drop in production or national income. Solow was the first to examine how taxes affect growth (1956). Solow's neoclassical growth model assumes that tax policy does not affect steady-state growth. In other words, tax policy, as distortive as it may be, does not affect long-term economic growth rates, even if it lowers long-term economic production. This is true in the context of taxation and national income accounting. The "old" endogenous growth theory developed growth models in which government spending and tax policies might have long-term or permanent economic impacts, in contrast to the "new" endogenous growth theory that was pioneered by Romer (1986). Countries have widely distinct taxation ideologies and revenue collection strategies. Different uses of total government expenditure affect growth differently, according to Castles and Dowrick (1990), Agell, Lindh, and Ohlsson (1997), and similar reasoning applies to how tax income is collected. Some nations have drastically increased taxes over the last few decades, while others have kept tax rates about the same.



Three main theoretical explanations exist for the causal relationship between government spending and revenue. The first is the fiscal synchronization theory, which states that government expenditure and revenue are set at the same time. According to Vamvoukas (1997), this indicates that expenditure and revenue have a feedback causal connection. According to this idea, the public determines government expenditure and taxation levels by comparing the advantages of government services against their costs. Meltzer and Richard (1991) have provided reasons supporting this view for the United States of America. The tax-and-spend hypothesis is the name given to the second theory. This strategy highlights the requirement that any budget for expenditures must be expanded proportionately to taxation and that expenditures must thus come after revenues. As a result, the amount of available tax revenue will influence the level of government spending. It is thought that tax increases will result in higher government spending. According to Friedman (1982), tax cuts are an excellent way to deal with budget deficits since taxes positively affect government spending. According to Friedman, tax cuts result in more significant deficits, which should compel the government to slash spending.

According to Buchanan and Wagner (1978), taxes indeed lead to government spending, but the causal link is negative. They argue that by lowering taxes, the public would believe that the cost of government programs has decreased. As a result, they will demand more government initiatives, which, if implemented, will result in more government spending. As a result, more budget deficits will be recognized as tax income declines and government expenditure rises. As a result, raising taxes is their solution to budget problems. Darrat (1998) discovered that in the case of Turkey, the tax-and-spend theory exists. According to the findings, a negative causal link exists between taxes and spending, as Buchanan and Wagner expected (1978). The third hypothesis proposes that government expenditure precedes revenue. This viewpoint, advanced by Peacock and Wiseman (1961) and others such as Barro (1979), is based on the notion that substantial exogenous defect predictions such as wars and other volatile political conditions, as well as natural disasters, cause an expansionary fiscal policy and thus an increase in tax revenues. The answer to the budget deficit problem is to cut government expenditures. Jones and Joulfani conducted empirical research in the United States of America (USA) to support this idea (1991). They look at this link between 1792 and 1860. Their findings corroborate the spend-and-tax theory in the short term and show that taxes and spending have a bi-directional causal relationship in the long run. In the example of Greece, Vamvoukas (1997) finds that the spend-and-tax theory exists in the short term, but his research appears to support the fiscal synchronization hypothesis in the long run.

Other academics have argued that government spending and revenue have no causal link. Hoover and Sheffrin (1991) researched the United States and found that spending and revenue are decided separately. Musgrave (1969) identifies four basic techniques for evaluating a country's tax performance: the "capacity to give up approach," ii) the "resource-efficient strategy," The "stochastic method" includes iii) the "ability to gather approach" and iv) the "comparison with an average performance approach." He believes that comparing a country's fiscal performance to the average performance of other countries is preferable to assessing a country's absolute performance. This is thought to be the most successful strategy. When taxpayers use tax benefits provided by another state while residing in their state, this raises two opposing issues (Oscheni, 2018). The source state tax incentive may be in opposition to the residence state's tax laws. For instance, if the residence state has a capital export neutrality policy, the source state tax incentive might undermine that policy if it benefits the taxpayer in the residence state (Peters & Kiabel, 2015). Compared to the tax burden of a comparable investment made in the state of residence, the tax advantages will often lower the overall tax cost of the taxpayer's investment in the source state. Due to this, the source state investment is now economically viable (Okafor, 2015).

Furthermore, income generated and taxed in the source nation frequently has additional tax repercussions in the country of residence. As a result, the intended impact of the source state tax incentive may be negated by interactions between the two countries tax systems (Rendon, 2016). Dividends paid to the country of residence are subject to two fundamental tax treatment options: exemptions and foreign tax credits. The effective taxation back of the incentives does not happen while using the exemption technique since there is no additional tax on the repatriated earnings. The foreign tax credit approach, however, clearly has detrimental effects on tax incentives (Obeng, 2014). When adopting the foreign tax credit technique, the resident nation applies its tax rules to the income when it is repatriated, But it also allows you to deduct any foreign taxes you've paid as long as they don't exceed the amount of income tax you'd pay in your home country (Klemm & Parys, 2012). Therefore, the benefit provided is taxed back when the income is repatriated to the resident nation if the incentives result in a tax obligation that is lower than the tax burden that would be imposed in the place of residence. Simply put, tax revenue is transferred from the source country's treasury to the residence country's treasury (Khukai & Ahmenti, 2016). Tax breaks offered by developing nations to investors from developed nations are subsidies given by developing nations to developed nations rather than incentives for international investment. Some States use tax sparing in international tax practice to encourage foreign investment and avoid international tax policy from negating advantages

provided in other countries. When tax sparing is used, the residence nation considers the remitted income as though it had not received the tax incentive and had been fully taxed. Tax breaks guarantees that investors receive the full advantage of the tax benefits (Kransdoff, 2010).

To achieve their developmental objectives, governments utilize a variety of levies and tax rates. Levies on tax are done to redistribute resources among people or groups of the population engaged in taxable activities, like business, or to divide the tax burden among those persons or classes. In the past, taxes on the poor were used to support the aristocracy; now, social security systems are designed to assist the underprivileged, the disabled, and retirees through taxes on those still in the workforce. Additionally, taxes are levied to finance military and foreign aid projects and affect the country's macroeconomic performance. A country's tax structure frequently reflects its societal ideals or the values of the ruling class. A country must decide who will pay taxes, how much they will pay, and how the funds raised through collecting taxes will be used before establishing a taxation system. These decisions reflect the kind of society the people and government desire to build in democratic nations where the general populace elects individuals in charge of designing the tax system. It may reflect the ideals of people in power in nations where the public does not have a big say in the taxation system. The amount that the government may utilize is never equal to the amount taxed from the general populace.

The difference is known as compliance cost, which might include labor costs and other costs related to adhering to tax laws and regulations. Hypothecation is collecting a tax to use the proceeds for a particular purpose, such as collecting an alcohol tax to fund treatment facilities for alcoholism directly. Finance ministers frequently object to this approach because it limits their flexibility. Since money is fungible in reality, some economists view the theory as being intellectually dishonest. Additionally, it frequently occurs that taxes or excises that were first imposed to support specific government initiatives are eventually transferred to the general treasury of the government. In other instances, such taxes—like highway tolls, for instance—are collected inefficiently. Some economists, particularly those who adhere to the neo-classical school of thought, contend that all taxes lead to market distortion and economic inefficiency. As a result, they have tried to determine what form of tax structure will reduce this distortion. Additionally, it is regarded as economically practical for the government to recover the increased value for public purposes because managing possession and use of property in the territory it has sovereign authority over is one of every government's most essential responsibilities.

The decision between direct and indirect taxation, and more specifically, the question of when differentiated commodity taxes are not a part of the ideal tax system, is one of the most

divisive issues in tax theory. The early research concentrated on the efficiency function of commodity taxes, asking when the Ramsey tax system would be applied to a particular family and whether it would include a uniform tax on commodities or, in its place, an income tax. That was resolved by the renowned Corlett and Hague (1953) Theorem. Differential commodity taxes should not be utilized for leisure if all items are "equally substitutable." Otherwise, more excellent commodities tax rates should be applied to products more complimentary to leisure. According to Sandmo (1976), this condition is satisfied by a utility function that is homothetic in goods and in which goods and leisure are separable. Although this conclusion represents a significant analytical advance, it has limited policy implications since it ignores the tax system's function as a means of redistribution. When should differential commodity taxes be used with a progressive income tax as part of a redistributive tax system? Atkinson and Stiglitz presented this topic in their landmark 1976 paper, which has since produced a sizable body of work. The A-S Theorem roughly asserts that differential commodity taxes should not be employed if household utility functions can be divided into leisure and goods. Optimal taxation has been studied in the literature, with a particular focus on the situations in which it is broken and what that means for the design of commodities taxes. It's interesting that the Corlett-Hague Theorem analog still holds, but for different reasons. Higher tax rates should be applied to items that are comparatively more complimentary with leisure if weak separability is breached, as demonstrated by Edwards et al. (1994) and Nava et al. (1996).

The use of government expenditure and revenue collection to influence the economy is known as fiscal policy. Fiscal policy contrasts with monetary policy, the other major type of macroeconomic policy that attempts to stabilize the economy by controlling interest rates and the money supply. Government spending and taxation are the two primary fiscal policy instruments. Changes in the level and composition of taxation and government spending, on the other hand, can have an impact on the following economic variables: aggregate demand and the level of economic activity; the pattern of resource allocation; and the distribution of income. Fiscal policy uses the government budget to influence economic activity, fiscal policy effects, and fiscal straitjacket. The three fiscal policy stances are neutral, expansionary, and contractionary. In most countries, government spending is entirely funded through taxation, and thus the overall budget outcome does not affect economic activity. An expansionary fiscal policy is one in which government spending exceeds tax revenue. When government spending exceeds tax revenue, fiscal policy is said to be contractionary. However, these definitions can be misleading because cyclical economic fluctuations can result in tax revenue fluctuations even if no spending changes or tax laws are made. As a result, "government spending"

"cyclically adjusted government spending", and "cyclically adjusted tax revenue" are commonly used in place of "cyclically adjusted tax revenue." for the above definitions. A government budget that is balanced throughout the business cycle, for example, is thought to represent a fiscally neutral stance. Governments spend money on various things, including the military and police, as well as services such as education and healthcare. This expenditure can be funded in various ways, including borrowing money from the population or from abroad, using fiscal reserves and selling fixed assets (e.g., land), profiting from printing money, and many others. Except for taxation, all of these are forms of deficit financing. Borrowing or fiscal deficits are frequently funded by the issuance of bonds such as treasury bills, consuls, and gilt-edged securities. These pay interest for a set period of time or indefinitely. If interest and capital repayments are excessively high, a country may default on its debts, usually to foreign creditors. Prior surpluses are consumed; a fiscal surplus is frequently saved for future use and may be invested in local (same currency) financial instruments until needed. During an economic downturn, when income from taxes or other sources falls, reserves allow spending to continue at the same rate without incurring additional debt.

Thus, the economic effects of fiscal policy can be seen when Fiscal policy is used by governments to have an impact on the level of aggregate demand in the economy in order to achieve price stability, full employment, and economic growth. However, Keynesian economics suggests that the best ways to stimulate aggregate demand are to increase government spending and lower tax rates. It is typically used during a recession or a period of low economic activity as a critical tool for laying the groundwork for strong economic growth and achieving full employment. A budget surplus can be used by governments to do two things: slow the pace of strong economic growth and stabilize prices when inflation is excessively high. According to the Keynesian theorist, removing spending from the economy will reduce aggregate demand and contract the economy, thereby stabilizing prices. Economists argue about the efficacy of fiscal stimulus. The main point of contention is crowding out, a phenomenon in which government borrowing leads to higher interest rates, which cancel out spending's stimulative effect. When the government runs a budget deficit, funds are depleted must be raised through public borrowing (the issuance of government bonds), foreign borrowing, or debt monetization. However, when governments fund a deficit by issuing government bonds, interest rates in the market can rise because government borrowing increases the demand for credit in the financial markets. This has the unintended consequence of lowering aggregate demand for goods and services. While Neoclassical economists tend to emphasize crowding out, Fiscal policy, according to Keynesians, can still be effective,

particularly in a liquidity trap where crowding out is minimal. Most classical and neoclassical economists have argued that crowding out completely negates any fiscal stimulus "Treasury View," which Keynesian economics has rejected. This Treasury View refers to the theoretical positions of British Treasury classical economists who opposed Keynes' call for fiscal stimulus in the 1930s. According to classicalists, the expansionary fiscal policy reduces net exports, which reduces national output and income. When interest rates rise as a result of increased government borrowing, foreign capital is attracted.

This is possible because, all else being equal, bonds issued by a country pursuing expansionary fiscal policy now provide a higher rate of return. As a result, companies seeking to finance projects must compete for capital with their government, offering higher rates of return. To purchase bonds issued by a specific country, foreign investors must first obtain that country's currency. As a result, when foreign capital flows into a country that is experiencing fiscal expansion, demand for that country's currency rises. The increased demand causes the currency of that country to appreciate. When a country's currency appreciates, goods from that country become more expensive to foreigners, while foreign goods become less expensive. As a result, exports fall while imports rise. Other potential issues with fiscal stimulus include the time lag between policy implementation and detectable effects in the economy, as well as inflationary effects caused by increased demand. In theory, fiscal stimulus does not cause inflation because it uses otherwise idle resources. For example, if a fiscal stimulus employs a worker who would otherwise be unemployed, there is no inflationary effect; however, if the stimulus employed a worker who would otherwise have a job, the stimulus increases labour demand while keeping labour supply fixed, resulting in wage inflation and thus price inflation.

## **Tax Policy and Foreign Direct Investment**

For countries with a high level of FDI penetration, the revenue received by FDI taxation can account for a significant portion of overall tax revenue. However, because the value of FDI is negatively affected by taxing, host countries should weigh the sales gains (if any) of increased revenue against the financial cost of discouraging FDI. A study by Shah and Slemrod (1990) discovered that in Mexico, FDI is extremely sensitive to changes in local tax rates compared to those of the destination country. The authors did, however, point out that, in addition to taxation, regulatory structures and the general financial and political atmosphere in Mexico significantly impact FDI transfers and reinvestments. For the most part, modern scholarship has found that FDI demand is primarily a commercial agency problem (Shah, 1990). The complex character

of the statutory tax fee on corporate income, the volume of tax credit awarded, and the definition of the tax base, including the process of depreciation and how gross earnings and deductions are divided among nations, is the powerful tax charge on corporate revenue from FDI.

According to Shah (2000), there are two ways to assess the impact of the high tax rate on new funding. The gap between the pre-tax return and the after-tax rate of return is a measure of the tax-related disincentive to invest. A different method would be to determine the annual tax ratio using a few income indicators independent of the definition of taxable earnings. This method may also capture some of the functions of the tax legislation and other aspects (such as inflation) that are not captured by the analytical approach. Another aspect that could impact the high tax rate is whether the tax is levied on a territorial or worldwide basis. A territorial device protects the home nations. It imposes no personal tax on earnings from overseas sources. The corporations' home nations assert the right to tax their revenues regardless of where they are created under the global device. To avoid two levels of taxation, some countries provide their multinationals with a limited credit line against the local tax liability for certain taxes paid to foreign governments. The tax liability (and credit) associated with a subsidiary's foreign source income is often postponed until dividends are repatriated to the parent company.

The degree of pre-tax return required for a model funding to provide an inevitable after-tax return is computed using the analytical technique. The gap between the pre-tax return and the after-tax rate of return is a measure of the tax-related disincentive to invest. A different method would be to determine the annual tax ratio using a few income metrics independent of the definition of taxable earnings. This method may also capture some of the functions of the tax legislation and other aspects (such as inflation) that are not captured by the analytical approach. Another aspect that could impact the high tax rate is whether the tax is levied on a territorial or worldwide basis. The tax liability (and credit) associated with a subsidiary's foreign source income is often postponed until dividends are repatriated to the parent company. In macroeconomics, the most critical question is how changes in tax policy affect economic development. Theoretically, taxes are thought to have a negative relationship with financial growth. As a result, higher tax rates result in reduced financial system boom charges. This can be explained by the fact that more outstanding taxes cause economic distortions, leading to poor performance. As a result, higher taxes push people to change their habits. This is because, regardless of how taxpayers choose to deal with taxes, they will be worse off than those who live in a world without them.

Other macroeconomic indexes use a country's tax system as a determining factor. There is a link between tax policy and the level of financial growth and improvement in both rising

and improving economies. Indeed, it has been contested whether a country's level of economic growth and development significantly impacts its tax structure (Hinricks, 1966; Musgrave, 1969) and whether tax policy objectives vary with levels of development (Hinricks, 1966; Musgrave, 1969). According to endogenous boom theory, tax policy can influence both the level and the rate of increase in production consistent with per capita. Barro (1990) and Barro & Martin (2000) provide a detailed example of the mechanism through which tax policy affects economic growth (1992, 1995). To demonstrate the positive impact of effective government spending, the authors hire a Cobb – Douglas -Type manufacturing function with the government providing products and services as input. Furthermore, under the endogenous rise model, the long-term regular nation is determined by the accumulation of replicable capital. As a result, any tax policy that distorts the incentives to amass physical and human capital will reduce the boom fee in the long run. Taxes on capital and capital accumulation, such as corporation and profit taxes, are expected to have unfavorable boom consequences. However, not all taxes are equally distorting, so the tax mix becomes a significant growth factor. If labor supply is exceptionally inelastic, neither consumption taxes nor a flat tax on labor wages may further skew a person's inter-temporal consumption preferences, leaving capital accumulation and development unchanged (Rebelo, 1990).

As per Massoud (2003), the general popularity of FDI policy principles has enhanced both the lure and stress on nations to completely liberalize FDI tyrannies, resulting in rapid changes in FDI governments in favor of a new of luring more Flow of FDI and therefore provides a wide variety of incentives to influence the number and quality of FDI. Emerging economies have seemed to have paid particular attention to FDI Inflow, owing to its low domestic savings and ineffective financial intermediaries, which also obstruct strategic initiatives and therefore necessarily require additional funds; and the hazardous concerns associated with private investment, which have become apparent during in the Asian financial crisis of 1997-98. (Massoud, 2003). Governments have incentivized foreign enterprises, particularly multinational companies, to encourage overseas investment. Partial or complete exemptions from corporation taxes, import levies, and the creation of special zones for exporting enterprises are the most typical forms of these subsidies. Nevertheless, the efficiency of policies favoring foreign direct investment, particularly for the host nation, has been a point of contention, and the research on the effectiveness of taxes on foreign direct investment has remained mostly equivocal as a result (Panagiota, 2010).

Even though it is widely acknowledged that fiscal policies can impact the FDI flows and there are significant advantages for the host nation, this capacity has been tried to argue against



assuming that all other factors are equal. Notwithstanding, states have different regulatory requirements and other corporate policies, levels of skilled workforce, facilities, and market growth, so this has been argued to be a flaw. As a result, while some economists believe that supplying opportunities to invest overall, and tax rebates specific, to prospective international investors plays a crucial role in the choice procedure of the location for their investor, others argue that other primary considerations play a more significant role (Well et al., 2001). Two main arguments made against investment opportunities, according to Wells et al. (2001), are that benefits have minimal if there are any, effect on total foreign money invested globally. Thus, in the accumulation, rewards create a net transfer from taxpayers (or indirect subsidies such as shipping protection from customers of the company's product) to shareholders. This transfer is primarily from a poor to a more affluent country in the case of foreign investment in developing nations. The second statement advanced by Wells et al. is that although benefits raise total investment globally, the economic costs of these advantages to the public outweigh any extra benefits generated by the investment. By their very nature, investment incentives are government interference in business. These regulations may have an impact on world commerce. For instance, export tax advantages may artificially increase host states' exports, compromising the interests of comparable trade states (Scarpetta et al., 2000).

Additionally, by impacting the flow of foreign investment, one country's investment incentives may harm the interests of other countries (Appiah-Kubi et al., 2021). Furthermore, when two or more governments compete with one another to win a particular investment project, "investment incentives become most distortive" (Rohwer, 2009). Many governments are worried about the impact of investment incentives' distortions on global commerce and investment; some international work has been done on this subject (Berden et al., 2012). For instance, the Organization for Economic Co-operation and Development (OECD) started talks on this topic in 1976. Specific clauses in the General Agreement on Tariff and Trade address investment incentives and were modified as part of the Uruguay Round. The Treaty of Rome, which established the European Community, also contains clauses relating to FDI investment incentives (Ocheni, 2018).

## **Empirical Literature Studies**

To discover the factors influencing FDI inflows in developing countries in comparison to Saudi Arabia, Kadi (2018) discovered that infrastructures, exchange openness, market growth, the rate of returns, gross domestic product (GDP), inflation rate, the greatness of human capital,

and the relationships that exist among nations are all factors that influence the level of FDI inflows in developing countries. The author evaluated seven publications from the Google Scholar database to determine the study's goal. The efficacy and success of FDI can be increased or decreased by local government regulations since foreign enterprises cannot control local power structures, roles, or policies (Lu et al., 2012). There were six indices of governance in Bannaga et al. (2013) 's research of 18 Arab nations: voice and accountability, political stability and absence of violence, the effectiveness of the government, standard of regulation, the rule of law, and control of corruption. Developing nations seek to have effective governance since FDI may be quickly reversed; this will help them maintain the flow of FDI. Economic growth and an open economy strongly correlate positively (Darku &Yeboah, 2018). An economy can specialize in its comparative advantage thanks to open commerce. When expertise takes place, meager income is distributed effectively, leading to higher output, increased salary, higher living standards, a larger market, more competition, and a way to facilitate the transfer of managerial and technical know-how from emerging economies.Dondashe and Phiri (2018) investigate the determinants that influence FDI, focusing on macroeconomic variables such as capita GDP, inflation price, authority size, real interest fee variable, and change phrases. The investigation occurred in South Africa, with data ranging from 1994 to 2016. The cointegration regressive-Distributed Lag (ARDL) version shows that the capita GDP, government size, the real interest rate variable, and trade terms influence FDI influx in the South African economy. Even though the 50 African nations included in Gangi and Abdulrazak's (2012) analysis concurred that solid governance is necessary to encourage FDI, only three factors reached statistical significance: voice and accountability, government effectiveness, and the rule of law. They said that African nations needed to implement institutional and economic changes to enhance governance, foster their investment climate, and draw in more FDI. The empirical analysis by Abdouli and Hammami (2017) of FDI inflows in 17 Middle Eastern and North African nations showed that higher FDI inflows result in higher economic development. However, Borda Reyes et al. (2019) research that examined 11 Latin American nations revealed that the relationship between FDI and economic development is not as clear-cut as it would first appear. The writers argued that recent national movements, which supported nationalism and raised protectionist measures, undermine globalization.

Okafor (2015) concluded that the provision of crude oil and natural fuel, infrastructure development, market size, and overall quotes in primary education are elements that US investors look for before investing in a country, based on data collected from 23 Sub-Saharan African countries between 1996 and 2010. In recent years, international purchasers have

analyzed the macroeconomic surroundings before making investment decisions and taken into account the governance structure of an economic system. According to 2002 research by Harms and Ursprung, economic development and good governance are positively correlated. The authors argued that nations that respect civil and political freedom appeal more to multinational corporations. Foreign investors face more significant risks when investing in authoritarian governments since their policies constantly change to win over the people. Kang and Lee (2011) use a generalized method of moments (approach) to look into the problems and causes of de-industrialization with a focus on OECD nations. Their model gives FDI much attention. They can demonstrate that an increase in FDI leads to an increase in the manufacturing sector's employment rate. Additionally, their study can refute earlier claims about FDI and de-industrialization. They demonstrate the importance of FDI outflows in researching de-industrialization. De-industrialization begins with a capital outflow (FDI outflow), which lowers employment in the domestic manufacturing sector. According to Phung (2017), the large migration of foreign purchasers to developing international locations can be explained by improvements in these nations' governance and institutional systems, which provide attractive trading environments. According to Julio and York (2016), foreign funding decreases significantly during election seasons but increases afterward. This indicates that foreign investors are sensitive to political unrest. As a result, foreign purchasers are more likely to invest in countries with stable political environments and vice versa. Studies from other areas have shown that bad governance is a significant factor in FDI, while Subasat and Bellos' (2013) analysis of Latin American nations demonstrated the opposite. In contrast to other regions, Cheng and Chung (2012) and Williams (2015) found that excellent governance, infrastructure, or government debt had little to no impact on FDI inflows in Latin America and the Caribbean. Latin American and Caribbean nations' natural riches and favorable policies were to blame for the FDI flood (Agosin & Machado, 2007). Data from 1972 to 2000 were used by Barrios, Gorg, and Strobl (2005) to analyze how FDI affected the growth of regional industrial firms in the Republic of Ireland. The employment in foreign-owned factories divided by the total employment in the industry was calculated in the model they used to approximate the effect of FDI on the entry of new firms. According to their findings, FDI can contribute to the growth of local firms; therefore, the more capital inflows there are, the more influential the local firms will be. Similar outcomes are presented by Blomstrom (1986) using data from 1965 to 1970. According to the study, an increase in FDI levels in a host economy will result in more businesses operating there.

Firms operate in unstable contexts; according to Dorozynski et al. (2019), thus, most international purchasers rely on the overall performance of institutions as an intelligent way to make investment decisions. The control of corruption, political balance, voice and duty, the rule of thumb of law, regulatory quality, and the effectiveness of authorities are some institutional and governance elements traders look for (Agyemang et al., 2016; Appiah-Kubi et al., 2021). Despite the importance of these institutional elements in determining the superiority of foreign traders in a country, they have received little attention in the quest to understand the drivers of international investment, particularly in Africa. Alfaro and Rodriguez-Claire (2004) use firm-level data to examine the effects of spillovers brought on by the entry of multinational corporations focusing on Brazil, Chile, and Venezuela. The authors did not find the effects of horizontal spillovers brought on by an increase in FDI statistically significant. However, they discovered proof that suggested backward linkages. Rodriguez-Claire (1996) investigated how FDI affected employment in the economy. According to his research, there may be backward and forward linkages depending on how multinational corporations use many local goods to produce their finished goods. Other research, like Anyanwu (2013) and Bayar (2016), show that governance explains the differences in boom tiers worldwide. The concept of governance structure encompasses adequate and sound governmental institutions and the judiciary's independence (Afolabi, 2019). The concept of governance has been expanded in recent literature to control the availability of foreign buyers in a country. The premise that a country with good governance attracts more foreign investment than a country with lousy governance is tested in this study. As a result, the effectiveness of governance significantly impacts the influx of foreign investors. Pajunen (2008) sought to clarify the causal relationship between FDI flows and institutional factors using a fuzzy set analysis. 47 host countries were included in the data set used for the study. Both developing and developed nations made up these nations. Overall, his findings supported the idea that institutional factors played a significant role in persuading multinational enterprises (MNEs) to offer long-term investments. Kobrin (1976) examined 59 developing nations cross-sectionally. The study's objective was to determine how capital flows affect institutions as a whole. His research demonstrates that FDI strengthens the link between industrialization and institutions and acts as a direct and ongoing agent of manufacturing sector growth.

Globerman and Shapiro (2002) investigated the impact of governance quality on foreign possession inflows using the six (6) governance signs identified by Kaufmann et al. (1991). From 1995 to 1997, data were collected from each superior and developing country. The findings show that a country with excellent governance attracts foreign investment. As a result,

the quality of governance is a significant predictor of international ownership. From 1997 to 1999, Stein (2001) used a gravity model to examine the effect of exceptional governance on the supremacy of foreign holdings in Latin American countries. The data confirm that host country governance impacts the superiority of foreign ownership in Latin American countries. Even though studies reveal both good and negative consequences on economies, governments of developing nations are eager to use an infusion of FDI to achieve economic growth. FDI inflows have had favorable effects on economic growth, including increases in employment, salaries, the balance of payments, economic growth, technological advancements, improved productivity, and living standards (Cambazoglu & Karaalp, 2014). There is a link between FDI influx and economic growth, according to studies by Borensztein et al. (1998), Bosworth and Collins (1999), Choe (2003), Li and Liu (2005), and Chakraborty and Nunnenkamp (2008). According to Borensztein et al., FDI benefits economic growth more when people, or human capital, are engaged. Bosworth and Collins concurred with Borensztein et al. that weak economic growth results from weak human capital. Choe (2003) concurred that there is a significant positive association between FDI inflows and economic development, but he stated that there is a chance that this economic growth may also be influenced significantly by a country's gross domestic product. According to Li and Liu's 2005 analysis of 84 nations, an influx of FDI may promote economic growth, which draws additional FDI to the nation. Similar findings were found in Chakraborty and Nunnenkamp's (2008) analysis of FDI in India, which demonstrated a causal relationship between FDI influx and economic growth, which drew more FDI to the nation. India's resolve to be open to commerce improved and deepened the connection between international and domestic businesses. Zhang (2001), Adams (2009), and Azman-Saini et al. (2010) conducted studies on 11 countries in East Asia and Latin America and found that occasionally an influx of FDI can be more beneficial in some areas than others. Nevertheless, the ability of such nations to absorb FDI advantages for economic growth was hampered by their worsening infrastructure, financial systems, infrastructure, trade openness, and government corruption.

Using a dynamic panel generalizing approach of moments, Saini and Singhanian (2015) analyzed the factors influencing the amount of FDI for both developed and developing countries (GMM). The study discovered that in developed international locations, determinants are more policy-related, whereas in developing countries, determinants are mostly economic variables. The generalized Method of Moments was also used by Addison and Heshmati (2003) to assess the impact of organization pleasant on FDI inflows in Vietnam. The findings show that institutional quality impacts the amount of FDI, although the effect varies by region. From 2000

to 2014, Appiah-Kubi et al. (2019) used a dynamic panel generalizing method of moments (GMM) of 13 (thirteen) nations to investigate the impact of macroeconomic variables on the influx of foreign direct investment in the least developed West African international locations. According to the authors, infrastructure improvement has a positive impact on the influx of FDI into the least developed West African countries. According to Guidiby and Renard's (2015) analysis of the contribution FDI made to the industrialization of 47 African nations, there was little correlation between FDI and industrialization. In their study, they used a workable least square regression on a set of data spanning the years 1980 and 2009. Their results marked a significant departure from earlier studies, which typically found either a positive or negative relationship. They attribute this outcome to African governments' ineffective policies for luring FDI-seeking manufacturers. Agosin and Machado (2005) used a business survey across 40 administrative districts and one-stage and two-stage instrumental variable estimation methodologies to explore the impact of weak governance quality on FDI in Russia. The authors discovered that a higher frequency of unlawful payments and increased pressure from regulating businesses, enforcement agencies, and criminals have significantly adverse effects on FDI. The research also confirmed that changing from mediocre to excellent governance across Russian regions more than doubles the FDI inventory. Barrel and Nahhas (2018) used the generalized technique of moments (GMM) estimator to a gravity version of bilateral FDI stocks to examine the factors affecting bilateral Foreign Direct Investment (FDI) stocks from 14 high-profit countries to 31 OECD countries over the period 1995-2015. Their findings suggested that EU membership has a significant impact on FDI stocks and that European integration significantly impacts FDI stocks. According to Da Rin and Hellman (2002), robust legal frameworks that encourage bank establishment can catalyze industrialization. This would give local manufacturing companies credit. Bjorvatn and Coniglio (2012) find that developing countries require government interventions in industrialization more than developed countries do. This is according to their analysis of the impact of government policies on industrialization. In their analyses of the industrialization of Asian nations, Dahlman (2009), Rodrik (1996), and Rodrik (1995) note that improved intellectual property laws, tax cuts, tariff protection, and government policies were crucial to the industrialization of the region.

According to Aziz and Mishra (2016) and Carril-Caccia et al. (2019), an economy's government instability implies uncertainty about its political and economic tenets and has a detrimental impact on foreign direct investment (FDI). Aziz and Mishra argued in their study of FDI determinants in 16 Arab economies that there is an additional investment cost when substantial government corruption hinders the influx of FDI. Foreign investors believe that the

stability of the government is essential for them to make investments in oil-producing countries, according to Carril-Caccia et al. According to Okafor et al. (2017), there is a much more significant positive impact on FDI inflows when government corruption is reduced. The authors made the case that the low level of FDI in this region may be due to the notion that Africa is corrupt among international investors, which they said may have a detrimental effect on investors. According to Anghel (2005), countries with administrations that are relatively graded per several indices of establishment quality fare better in attracting foreign direct investment. The author finds that unique elements of a country's great institutions (corruption, asset rights protection, policies related to starting and maintaining a business, and many others.) are almost always tremendous in attracting FDI in an empirical analysis of move-segment statistics using estimation techniques of regular least squares and instrumental variables. The findings of this study demonstrate that FDI is not always a need for economic success in a nation. Other underlying factors, including social, economic, and political events, may also positively or negatively influence economic growth. According to a panel data analysis study of 15 East Asian countries with varying income levels,

In countries with favorable conditions, FDI has a beneficial influence on economic growth, such as high levels of education, well-established financial systems, well-established infrastructure, high levels of trade openness, and low levels of government corruption (Kotrajaras et al., 2011). Other research has demonstrated that there might be a conflicting or no relationship between FDI and economic growth. Vu et al. (2008) used a regression-based case study to investigate the effects of FDI on economic development in China and Vietnam by various economic sectors. The authors analyzed data from 1990 to 2004 divided into various sectors to see which nations' economies were most affected by FDI. The study demonstrated that FDI has a favorable and statistically significant impact on economic growth but is not uniform across the various industry sectors. As a result, while FDI would stimulate the manufacturing sector's economy, its effects on other industries would be statistically negligible or even harmful. Corruption control, the increased rule of law, political balance, and improved media freedom of speech are indicators of good governance and institutional nice, according to Bissoon (2001). From 1996 to 2005, the author's research empirically investigated the impact of institutional quality on FDI in forty-five developing African, Latin American, and Asian countries. The results of the OLS estimation suggest that the quality of a few institutions inside the host countries considerably impacts inward FDI. Even though extraordinary signals of institutional pleasure are complementary, their combined impact increases the amount of FDI

inflows to the host country. According to Solomon and Ruiz (2012), the impact of political change as a primary feature of universal macro corporate governance indicators is inconclusive.

Wheeler and Mody (1992) discovered that robust human rights and political stability influenced FDI in the United States. Biswas (2002) concluded that political danger indicators discouraged FDI inflows to the places where they were observed to be ubiquitous. Research by Aitken and Harrison (1999) and Carkovic and Levine (1999) demonstrates a negative link between FDI and economic growth (2002). According to Li et al. (2013), FDI can lead to inaccurate resource allocation. This depends on the trade policies and other institutional aspects that are specifically related to a specific nation and can potentially stifle economic progress, such as social, political, and environmental hazards. Economic growth can be negatively impacted by cultural changes, reliance on foreign technology, and investment that reduces autonomy drops in tax income, pollution, environmental problems, and monetary problems (Cambazoglu & Karaalp, 2014). Busse and Hefeker (2007) investigated the effect of political change and institutions on FDI flows using a panel record fixed results model and a famous technique moments (GMM) estimator (including government balance, rule of regulation, and lack of battle). They discovered an enormous and high-quality relationship between five governance elements (government stability, the absence of internal war and ethnic tensions, advancing democratic rights, and ensuring law and order) and the level of FDI inflows into these countries when they looked at FDI flows for 83 developing countries from 1984 to 2003. Using data from 1975 to 2017, Abeille et al. (2020) attempt to understand the role of fiscal incentives in influencing foreign direct investment inflows into Ghana. The distributed lag (ARDL) bounds test approach demonstrated that corporation tax rates negatively influenced FDI inflows into the Ghanaian economy over time. They suggested that the Ghana Revenue Service revamp the country's business tax administration to prevent policy lapses. In his analysis, Fawowe (2013) used created indexes to see if fiscal incentives have stimulated investment in Nigeria since 1970. His research found a significant negative link between fiscal incentives and foreign direct investment in Nigeria. According to the findings, Nigeria should focus on reducing obstacles that could deter international investment, such as insufficient infrastructure, low-quality institutions, and lax laws. Tuomi (2011) also looked into the role of the investment climate and tax incentives in foreign companies' investment decisions in South Africa. The study discovered that monetary incentives have a minor role in most international companies' decisions. Klemm and Van Parys (2012) studied the effects of tax incentives in over 40 Latin American and Caribbean nations from 1985 to 2004 using spatial econometrics methodologies. Despite significant antagonism over the corporate income tax (CIT) rate, they



discovered that there is proof of critical communication in tax holidays. There was also proof that lower CIT rates and extended tax breaks could help Latin America and the Caribbean attract FDI. Peters and Kiabel (2015) used static error correction modelling (ECM) to examine the influence of tax incentives on foreign investors' decision to locate in Nigeria, using data from the Central Bank of Nigeria's yearly measurement bulletin and the World Bank World Development Indicators Database. Their findings revealed that FDI response to tax incentives is negative. They also proposed reducing reliance on taxes and paying greater attention to alternative incentive strategies, such as financial stability and the political climate.

Using the ARDL, Lodhi (2017) examined the impact of tax incentives on investment in Pakistan from 1990 to 2014. The reliable variables were FDI and domestic investment, while the unbiased variables were corporate tax rates and levy costs. The findings revealed that the corporation tax rate is inextricably linked to both short and long-term domestic investment and FDI inflows in Pakistan. As a result, it was urged that Pakistan's government decrease corporate tax rates and levies to encourage investment in the country. In order to distinguish the determinants of FDI inflows into the South African economy, Majavu and Kapingura (2016) used the VEC model to examine a variety of factors, including exchange rate, inflation, market openness, and corporate tax, as well as using foreign direct investment as the dependent variable. The experiment results revealed that these characteristics are essential drivers of FDI inflows into the South African financial system, with corporate tax having a measurable negative influence both short and long-term. Agbloyor, Gyeke-Dako, Kuipo, and Abor (2016) used the generalised method of moments technique to examine whether FDI is more effectively used in countries with better institutions to boost economic growth. Between 1996 and 2010, the authors used sub-Saharan countries as a sample. They discover that institutions benefit economic growth in nations with limited natural resources and little financial development. Walid (2010) utilized a multiple linear regression model to examine the monetary factors and risks of FDI on a large scale from 1997 to 2007, revealing a vital and positive relationship between FDI and the monetary factors studied. Taking all the factors into account, the study recommended that FDI be promoted through tax incentives to attract new investment. Obeng (2004) used the Johansen cointegration quarterly data from 1986 to 2012 to examine the influence of corporate tax on direct regional investment in Ghana, namely in the mining, assembly, and administration sectors. The actual corporation tax rate, exchange rate, net exports, inflation, and investments in various areas were all used in the analysis. The study found that corporate taxes impact FDI inflows into those regions. As a result, the report recommends that government officials maintain a low tax rate to attract more FDI into the

country. When evaluating if a country is famous for FDI, geography plays a role. The physical state of local distribution routes, natural resources, logistical networks, communication, political environment, and local government are examined as part of strategic planning and market research into new markets (Zhang, 2019). Remote host nations may become less desirable due to increased transportation costs for goods, resources, and operational management. For foreign investors, a higher population might represent a larger potential market and workforce (Decrease & Maarek, 2015). Politically tense nations are less desirable hosts than those with close diplomatic connections to the home nation (Pandya, 2016). Aziz and Mishra's research shows that natural resources draw FDI the most.

Global corporations have the resources and know-how necessary to extract and refine oil, foreign direct investment (FDI) and oil supply are positively and significantly correlated, which is essential for the Arab world. Aziz and Mishra (2016) and Carril-Caccia et al. (2019) both conducted studies on oil-producing countries, but Carril-Caccia et al. (2019) discovered that oil-producing countries attracted less foreign investment than those in the region that did not produce oil. However, the overall amount of FDI in the area stays primarily steady. Although natural resources might initially spur economic growth, a study of 31 nations in the sub-Saharan African, Middle Eastern, and North African areas revealed that ongoing operations result in lower cash flows (Okafor et al., 2017). According to the authors, further exploitation of natural resources would eventually result in economic uncertainty and a decrease in FDI influx. Esha (1983) discovered that the actual quantity of tax income received depended on a number of other factors in addition to the taxation capacity of the particular nations, the taxation objectives established by the authorities, and the ability of governments in practice to collect taxes. More precisely, the research listed below reveals a few factors that influence tax income. In a 19-year analysis, Etim et al. (2019) examined the impact of cost-focused and benefit-fixed tax techniques on FDI in Nigeria. Multiple regression algorithms were used to achieve this using secondary data gathered from the CBN and World Bank data sets. The findings revealed that, compared to benefit-focused tax strategy incentives, expense-focused tax strategy incentives had a significant impact on FDI; however, there was no significant link between cost-focused vs. benefit-based tax strategy incentives and FDI in Nigeria. In order to attract FDI inflows into Nigeria, it was proposed that the government explore nontax incentive mediations as a crucial complement to the tax plan incentives. According to Musgrave (1969), the absence of "tax handles" may prevent revenue collection at low-income levels, but these restrictions should lessen as the economy grows. According to Tanzi (1987), as mentioned in, economic growth is

thought to result in both an increased demand for public spending and a greater supply of taxing capacity to satisfy those needs (Musgrave, 1969).

Due to the country's geography's influence on capital flows and the integration of multinational corporations, FDI depends on it (Dunning, 2009). Geographical factors are connected to the precise location of nations that receive FDI. Marshall (1998) first proposed that related sectors in a given area attract investment (Jordaan, 2005). Labor market pooling specialized local inputs, and informational spill overs that might result in establishing local knowledge- and idea-sharing networks are advantages of this group of sectors. Geographical concentration was found as a favorable driver for FDI in this study on the industrial sectors in Mexico. Geographical distances have been a barrier to the influx of FDI for many developing nations, particularly those in the Pacific Islands, whose primary markets are in remote areas (Feeny et al., 2014). Leuthold (1991) found that the share of trade had a beneficial influence, whereas the percentage of agriculture had a negative one. In related research, Stotsky and WoldeMariam (1997) discover that while export share and per capita income have a favorable impact, both agricultural and mining share have a negative relationship with the tax ratio. They also discover a strong yet shaky connection between tax sharing and IMF programs. Tang and Zhang (2016) examined the capacities for absorption and advantages of inward FDI in China over 8 years. After rejecting all of the assumptions for the pooled OLS and the random effects model, they used a fixed effects model. Their study's findings demonstrate that FDI policy had a significant positive impact on manufacturing export capacity. Papaioannou (2009) also examined the impact of cross-border borrowing using panel data and cross-sectional data techniques. Their findings demonstrated how significant increases in international financing for economic development followed changes in government policies. According to studies, what draws FDI is location, which is made more desirable by economic policy (Dunning, 2009). According to Dunning, multinational corporations believe that places with the economic and institutional resources that best use their strong points will provide them a strategic advantage. FDI is good for the economy of many developing nations. According to Azman-Saini et al. (2010), foreign investment has been linked to superior technology, brand names, management and marketing tactics, trade secrets, and patents. According to Borensztein et al. (1998), multinational corporations are responsible for a large portion of worldwide research and development due to their technical superiority. Teera (2002) examined the factors influencing Uganda's tax revenue share using time series data on that nation. He found that there is a correlation between per capita income and both total tax revenue and income taxes using the Augmented Dickey-Fuller (ADF) and the Error Correction Model (ECM). The study revealed

the theory that tax bases expand in excess of an economy's revenue growth as nations progress. Biglaiser and Staats (2010) look into how political institutions impact FDI. Their research focuses on 138 developing nations over the years 1976 to 2004. Their findings demonstrate that among all the various institutional indicators employed, the enforcement of property rights, the maintenance of the rule of law or the absence of lawlessness, and highly effective and efficient court systems were the most significant in attracting FDI. However, institutional indicators, such as respect for human rights that were not directly related to investment risk, were less significant.

When assembly lines and shipping methods are created, multinational companies assist local businesses in gaining access to markets abroad. Not all studies support the flow of FDI to developing nations. According to research, there are drawbacks to the economic freedom that FDI brings, including links, asset bubbles, foreign entities' domination, economic instability, and an influx of foreign workers (Azman-Saini et al., 2010). The authors suggested that because foreign investors have the financial edge, they may pounce during an economic crisis and buy local enterprises with the technology they want. Due to the lack of growth-capable local markets, local businesses may also sell to foreign investors, encouraging FDI rather than wealth creation. According to Stiglitz, 2000; Stehrer & Woerz, 2009, this may result in the emerging nation's eviction of local businesses, excessive investment, and economic instability. According to Ghura (1998), the tax ratio increases with income and degree of openness while decreasing with the GDP percentage of agriculture. He also discovers that other elements like corruption, structural changes, and the growth of human capital have an impact on the tax ratio. Although structural changes and an increase in the level of human capital are connected to an increase in the tax ratio, a rise in corruption is linked to a fall in the tax ratio. A positive impact on the attraction of FDI is provided by dynamic institutions that offer checks and balances on the actions of leaders chosen by stakeholders (North & Weingast, 1989). The risk of policy reversal is also decreased by institutional quality, which tends to reduce arbitrary government regulations that stifle normal business processes. According to Lothian (2006), nations with higher-calibre institutions appeal more to foreign investors. His findings contribute to understanding why most FDI does not go from rich to developing countries. Alfaro, Kalemli-Ozcan, and Volosovych (2008) also examined the Lucas paradox and found that institutional quality is the primary cause of this paradox. Investors prefer less democratic governments and better institutions when doing business in non-resource exporting nations, according to Asiedu and Lien (2011).

Numerous studies show that both small and large financial incentives are not significant drivers of internal FDI. In any case, when incentives successfully attract foreign direct investment, the costs can outweigh the benefits. Most African countries have experienced economic growth and development because of foreign investment. As a result, the goal of this research was to see if the decision of international merchants to invest in Africa is influenced in a significant way by national governance systems and tax incentives, in addition to monetary concerns.

# **METHODOLOGY**

## **Impact of Governance Structures and Tax incentives on FDI in Africa**

### **Study Population and Sample Size**

Any research population comprises all potential factors of interest. The population for this study was primarily made up of African countries. A study pattern is a group of individuals or objects chosen from a broader population to represent that population (Mason et al., 1999). The sample size of this study comprised forty-five (45) African countries. The sampled African nations for this examination encompass Algeria, Angola, Benin, Botswana, Burkina Faso, Burundi, Cape Verde, Cameroon, Central African Republic, Congo Democratic, Republic of Congo, Chad, Cote d'Ivoire, Egypt, Ethiopia, Gabon, Gambia, Ghana, Guinea, Guinea-Bissau, Kenya, Lesotho, Liberia, Libya Madagascar, Malawi, Mali, Mauritania, Mauritius, Morocco, Mozambique, Namibia, Nigeria, Rwanda, Sao Tome, Senegal, Sierra Leone, South Africa, Sudan, Tanzania, Togo, Tunisia, Uganda, Zambia, and Zimbabwe.

The desire of countries blanketed in the observation was primarily based on the availability of information on the variables chosen for this study. The omitted countries include Eritrea, Comoros, Swaziland, South Sudan, Djibouti, Seychelles, and Eswatini. The study adopted the heuristic that each nation should have at least ten observations for each variable, per the recommendations of Asiedu (2002), Adams (2009), and Yazdi et al. (2017). This indicates that all the individual variables of interest have ten or more observations across the 45 countries included in the research. To the degree that the panel data is devoid of survival bias, this quota was required (Kiviet & Poldermans, 2017; Mosconi & Paruolo, 2017). Additionally, the nations that had a minimal influence on the study due to a lack of data were eliminated (Woodridge, 2002; Brooks, 2008; Yang & Lee, 2017).

### **Nature and Source of the Data**

Data refers to all the information a researcher collects for her study from a circumstance or action (Chandran, 2004). The information a researcher collects from research publications, books, casual interviews, and other sources is secondary data. Mugenda and Mugenda (Mugenda & Mugenda, 2003). The study used secondary sources to get its data. They include information from library sources, reports, national statutes, casual interviews with colleagues and local experts, newspapers, and internet sources. Secondary data is readily available from existing sources, and there are no specific collection methods (Shipman, 1997). The data was

collected through analysis of historical records and analysis of documents. The data of the study were sourced from several databases such as the World Governance Indicators (WGI), World Development Indicators (WDI), Global Competitiveness Index (GCI), International Monetary Fund (IMF), Price Waterhouse Coopers worldwide reports (PWC), Ernst & Young report's global database, World Economic Forum (WEC) databases. The Worldwide Governance Indicators (WGI) is a long-running research initiative to provide cross-country governance indicators, according to Kaufmann et al. (2008).

The World Governance Index (WGI) was established in 1996 and consisted of six composite measures reflecting broad aspects of governance. These indicators include governance perceptions expressed by survey respondents, non-governmental organizations, commercial business information suppliers, and global public sector organizations. They are based on several hundred variables acquired from 31 distinct data sources. They then apply a statistical technique known as an Unobserved Components Model to each cluster to standardize the data from these extremely varied sources into comparable units and create an overall governance indicator as a weighted average of the underlying source variables (Kaufmann et al., 2008).

The six governance indicators selected for the study include government effectiveness, corruption control, the rule of law, political stability, regulatory quality and voice, and accountability. The independent variables selected for tax incentives of the study include corporate tax rate (CTR), tax withholding (TaxW), tax holiday (TaxH), and tax concession (TaxC). The aggregated governance indicators are made up of raw data gathered from various sources and perspectives from the public and commercial sectors, non-governmental organizations (NGOs), multilateral organizations, citizens within countries, score firms, and other sources. The figures from the World Economic Forum's Opinion Survey estimate give the country's score on the aggregate indicator in units of standard normal distribution, i.e., ranging from approximately -2.5 to 2.5. in the World Governance Indicator Reports (WGI). This means that if a country receives a score of -2.5 for corruption control, the country's corruption control is abysmal, but several 2.5 indicates that the country's corruption control is excessive or ideal.

These data sets were chosen because they contain the qualitative and quantitative characteristics of the current economic situation, despite the data reflecting prior policy practices. As a result, the impact of existing restrictions is unknown. Despite this challenge, a survey was undertaken to include many respondents from various establishments in the chosen international areas to ensure a fair representation. As a result of the characteristics of the data, panel data methods can be used, which involves pooling observations from a cross-section of

units across twenty years. This provides outcomes that are not detectable in pure cross-sectional or time-series investigations. A general model for panel data was developed, which allows the researcher to estimate panel data with great flexibility and formulate variations in the behavior of cross-section parts. This strategy was used because it allowed the researcher to select samples that would provide sufficient data on the established and unbiased variables for at least two decades.

## **Procedure for Sampling**

The researcher used purposive sampling to select the facts of African countries protecting the period 2000-2020. The respondents were chosen using a purposeful sampling strategy (Kumekpor, 2002).

## **Variables of the Study**

In this part of the study are described the methods applied to estimate the models. The data used in this study are of the panel type.

### **Dependent Variable**

#### **Foreign Direct Investment (FDI)**

Foreign direct investment, according to the OECD (2008), is the net inflow of funds used to buy a long-term controlling interest (10 percent or more of the voting shares) in a company that operates outside of the investor's home country. As indicated in the stability of bills, it is the sum of equity capital, reinvested earnings, various long-time period capital, and short-time period capital. The logarithm of net foreign direct funding is used to calculate FDI, and the numbers are in current US dollars. This foreign direct investment data shows net inflows (new investment inflows less disinvestment) in the reporting economy from foreign investors and is divided by GDP (UNCTAD, 2003). As a result, the FDI variable is defined as net inflows of funds to acquire a long-term interest in or managerial control over an organization that operates in a financial system other than the investor's (Agbloyor et al., 2014). The data on foreign direct investment as a percentage of GDP were sourced from World Development Indicators (WDI) from 2000 to 2020.

### **The Explanatory Variables and Rationale**

#### **Past Foreign Direct Investment ( $\text{lagFDI}_{it-1}$ )**

It is critical to include the lag of the dependent variable with the explanatory variables when examining the long-term effect of foreign direct investment in promoting future FDI in



African countries. By lagging the foreign direct investment means that when analysing the data, the software will take previous year's data. This means that the year 2000 will be 1999 and year 2001 will be year 2000. The current investment climate in a nation is expected to influence future investments in a rustic. This is because the capabilities and advantages a country enjoys today are likely to encourage investors to maintain or increase their current investments. As a result, today's investment could catalyze FDI inflows in the coming years. Previous FDI inflows are estimated to positively affect current FDI inflows, much like the findings of Brennan and Cao (1997).

### **Government Effectiveness (GOVEF)**

Government Effectiveness is one of the governance indicators that describe the execution of the great civil and public offerings developed with the government's aid. Thus, the lifestyles of powerful government tools present to implement dependable and unprejudiced guidelines to overseas effects. Effective authorities are essential to lure foreigners to personal shares in a nation to guarantee economic development (Kaufmann et al., 2008). Alam (2017) discovered that government effectiveness drastically influences the amount that developing markets receive as Research and Development (R&D) investment in his study on the governance structures aspects of research and development financing in emerging markets from 2006 to 2013. According to Kaufmann et al. (2008), the estimate of government effectiveness gives the country's score on the aggregate indicator in units of standard normal distribution, i.e., ranging from approximately **-2.5 to 2.5**. This means that if a country receives a score of -2.5 for government effectiveness, the country's government effectiveness is abysmal, but a score of 2.5 indicates that the country's government effectiveness is ideal or perfect. The data for government effectiveness (GOVEF) were sourced from World Governance Indicators (WDI) from 2000 to 2020.

### **Political Stability (POS)**

According to Kaufmann et al. (2008), political equilibrium is the absence of political battles, terrorism, and unconstitutional overthrows of governments. This demonstrates the likelihood of macro-financial standards, social regulations, and political opinions being applied clearly, consistently, and consistently. Even though Africa has become more open to foreign investment over the years, the percentage of foreign ownership on the continent remains low, which is attributed to political stability, according to Agyemang et al. (2016). Kim (2010)

investigated the relationship between political stability and foreign direct investment, finding that political instability reduces the amount of FDI a country can attract. According to Kaufmann et al. (2008), the assessment of political stability provides the nation's score on the overall indicator, which ranges from around **-2.5 to 2.5** in units of a standard normal distribution. This means that if a country receives a score of -2.5 for political stability, the country's political stability is abysmal, but a score of 2.5 indicates that the country's government effectiveness is ideal or perfect. The data for political stability (POS) were sourced from World Governance Indicators (WDI) from 2000 to 2020.

### **Regulatory Quality (REQ)**

As per Kaufman et al. (2008), satisfactory regulation is the government's ability to develop regulations within the promotion and law of growth and development of the private sector. The most efficient and effective non-public law is a beneficial strategy to assure the sector's performance, particularly when privatization is advocated in developing countries (Kirkpatrick et al., 2006). Because competition is severe, the privatization of efficient sections of the economy allows these industries to run correctly, but when there is a market failure, the authorities intervene. Regulations are necessary to create an environment that boosts investor trust in the market. The regulator must be unbiased to acquire traders' trust, and policies must be implemented transparently and consistently. (Alfaro et al., 2005).

According to Kaufmann et al. (2008), the assessment of regulatory quality provides the nation's score on the overall indicator, which ranges from around **-2.5 to 2.5** in units of a standard normal distribution. This means that if a country receives a score of -2.5 for regulatory quality, the country's regulatory quality is abysmal, but a score of 2.5 indicates that the country's regulatory quality is ideal or perfect. The data for regulatory quality (REQ) were sourced from World Governance Indicators (WDI) from 2000 to 2020.

### **Rule of Law (ROL)**

The design, execution, and enforceability of contractual rules, safety and security, property rights, the legal system, and the possibility of crime and violence are all examples of the rule of law as a governance structure (Kaufmann et al., 2008). In the literature, private property rights are referred to be market-making institutions (Rodrik, 2005). They are also referred to as a signal of buyer protection. Indeed, rights on vulnerable items raise the risk of expropriation, which reduces traders' profits. Property rights have empirically been the World

Governance Indicators regulation's rating rule (Kaufmann et al., 2008). This is the closest proxy for property rights security among the six governance dimensions assessed by Kaufmann et al. (2008).

Through these surrogates, it is observed that quality establishments are remarkably associated with foreign ownership flows (Alfaro et al., 2005). According to Kaufmann et al. (2008), the assessment of the rule of law provides the nation's score on the overall indicator, which ranges from around **-2.5 to 2.5** in units of a standard normal distribution. This means that if a country receives a score of -2.5 for the rule of law, the country's rule of law is abysmal, but a score of 2.5 indicates that the country's rule of law is ideal or perfect. The rule of law (ROL) data was sourced from World Governance Indicators (WDI) from 2000 to 2020.

### **Control of Corruption (CORR)**

The extent to which public authority and position are used for private gain or not and the absence of a political framework, according to Kaufmann et al. (2008). Corruption has turned into a moving issue lately. Debasement contrasts across economies; however, as per the Transparency International (2016) report on corruption insight list, Africa was evaluated as the worst landmass. There are many debasement expenses, including payoff costs, unfortunate frameworks, and lining costs, which do not advance speculation, mainly from foreigners. Nations described by degenerate public authorities will generally extricate cash from the organizations that work in such economies (Agyemang et al., 2016).

Studies on debasement and foreign venture have observed clashing outcomes concerning corruption's effect on foreign speculation. Per Castro (2013), the distinction in outcomes is because each economy has an alternate degree of defilement. According to Kaufmann et al. (2008), the assessment of regulatory quality provides the nation's score on the overall indicator, which ranges from around **-2.5 to 2.5** in units of a standard normal distribution. This means that if a country receives a score of -2.5 for control of corruption, the country's control of corruption is abysmal, but a score of 2.5 indicates that the country's control of corruption is ideal or perfect. The data for control of corruption (CORR) were sourced from World Governance Indicators (WDI) from 2000 to 2020.

### **Voice and Accountability (VOA)**

Voice and Accountability include the opportunity for articulation, affiliation, and citizens' ability to engage in and choose their management. It represents the government's duty and the

amount to which fair cycles are followed until residents make their decisions (Kaufmann et al., 2008). Voice and Accountability connect with voting-based systems where the majority runs the show. Voice and responsibility suffocate the promoting force of multinationals; therefore, most foreign funders are not attracted to vote-based nations (Agyemang et al., 2019). Besides, with the element of the right to speak freely, more incompetent work can impact choices of strategies that overturn foreign possessions (Agyemang et al., 2016).

A study on governance and FDI conducted by Jadhav (2012) in Brazil, Russia, India, and China from 2000 to 2010 discovered that voice and Accountability have a negative impact on FDI. According to Kaufmann et al. (2008), the assessment of voice and Accountability provides the nation's score on the overall indicator, which ranges from around **-2.5 to 2.5** in units of a standard normal distribution. This means that if a country receives a score of -2.5 for voice and Accountability, the country's voice and Accountability are abysmal, but a score of 2.5 indicates that the country's voice and Accountability are ideal or perfect. Voice and Accountability (VOA) data were sourced from World Governance Indicators (WDI) from 2000 to 2020.

### **Corporate Tax Rate (CTR)**

A corporate tax is a tax on a corporation's profits. Taxes are deducted from a business's taxable income, comprising revenue less cost of goods sold, general and administrative expenditures, selling and marketing, research and development, depreciation, and other operational expenses (OECD, 2008). Corporate tax rates vary widely between countries; some have low rates and are known as tax havens. Because various deductions and government subsidies can decrease corporate taxes and tax loopholes, the effective and efficient company tax percentage, or what a firm pays, is often lower than the statutory rate, the stated amount before any deductions (Kraushoff, 2013).

According to Price Water Coopers (PWC) statistics on Africa, resident corporations or non-resident firms having a permanent tax establishment pay corporate tax on income from commercial operations conducted in African nations (PE). For instance, the corporate tax rates of some of the selected African countries in 2020 include Algeria (26%), Angola (25%), Chad (35%), Ghana (25%), Egypt (22.5%), and many others. The data for corporate tax rate (CTR) was sourced from Price Water Coopers reports (PWC), Organisation for Economic Co-operation and Development (OECD) Corporate Tax Statistics, and Ernst and Young Tax reports databases from 2000 to 2020.

### **Tax Withholding (TAXW)**

Withholding tax, as defined by (OECD, 2008), is the annual assessment paid to the government by the partner or management, not the employee. This shows how an economy addresses critical areas it needs to develop to help the entire economy. In other words, withholding tax on income levied at the origin means that the employer is tasked with withholding the appropriate tax from special payments and repaying it to the authorities. Almost all tax systems have withholding taxes, frequently applied to dividends, interest, royalties, and other related tax payments. Tax treaties usually lower the withholding tax rates (OECD, 2008). Wilson and Wildasin (2004) characterize billing as an annual duty paid to the government through the organization rather than by the worker, where nations administer billing fee systems to direct the company towards globally portable capital.

The current perception of the connection between valuation and interest in global business areas cannot be extrapolated to developing nations alone. For instance, the withholding tax rates of some of the selected African countries in 2020 include Algeria (15%), Angola (15%), Chad (20%), Ghana (8%), Egypt (10%), and many others. The data for withholding tax rate (TAXW) were sourced from Price Water Coopers reports (PWC), Organisation for Economic Co-operation and Development (OECD) Corporate Tax Statistics, and Ernst and Young Tax reports databases from 2000 to 2020.

### **Tax Holiday (TAXH)**

According to OECD (2008) tax policy statistics, a tax holiday is a short-term tax reduction. Tax holidays frequently suspend consumer-paid state and municipal sales taxes in African nations. Authorities may employ tax holidays as investment opportunities to temporarily exclude a new facility from paying property taxes. These actions are the most significant opportunity given to the financiers of the economy each year. If the individual government does not provide an occasion of duty, the study will expect a score of zero. A score of 1 is assigned for a period of tax holiday service of five years or less, and a score of 2 is waived for a period of more than five years of tax holiday service. As one of the chosen nations in Africa, Ghana, for instance, has implemented a tax holiday by guaranteeing that residents are entitled to a credit concerning any foreign income tax paid, to the extent that the tax paid concerns the resident's foreign taxable income.

The maximum foreign tax credit allowed for a particular income category should not be more than the resident's annual average rate of income tax in Ghana. Accordingly, businesses

authorized to act as free zone developers or businesses must not pay CIT for the first ten years of operation. This will result in Ghana receiving a score of 2 for tax holidays. Egypt, another African nation included in this research, does not provide any tax benefits unless a business is a free environment entity, exempt from taxes for approved and licensed operations, or an entity created following the legislation governing special economic zones. Egypt will thus receive a score of 0 as a consequence. The data for tax holidays (TAXH) were sourced from Price Water Coopers reports (PWC), Organisation for Economic Co-operation and Development (OECD) Corporate Tax Statistics, and Ernst and Young Tax reports databases from 2000 to 2020.

### **Tax Concession (TAXC)**

Chai (2006) described tax concessions as favorable tax treatment for particular businesses or entities, which is a frequent practice in developed and developing nations. Tax breaks are given to encourage investment, known as "investment incentives," or to accomplish specific social goals (Goyal & Chai, 2008). In order to encourage investment, exemptions from import-related customs and taxes may also be granted. These exemptions may apply to other imported items for statutory, civic, or charitable organizations (Goyal & Chai, 2008). It is a question of whether state administrations are specific in their arrangements for granting rights or whether rights are granted in all cases.

Thus, assuming that an African country like Benin does not offer any subsidy for expenditures, the variable receives a score of 0. If billing concessions are announced for a specific number of enterprises, the variable earns a 1-point score; if all organizations are expected to receive a billing concession, the variable receives a 2-point score. Beyer and Schwefel (2002) find no search between charging concessions and offering FDI in temporary savings. While different investigations incorporating Klemm and Van Parys (2012) consider that collection drivers are vital for deceiving foreign direct interest in low-wage countries, Van Parys and James (2010) also track collection concessions to have an efficient effect, effective safe, within the Caribbean. Island nations.

## **Control Variables**

### **The Inflation Rate (INFR)**

Inflation estimates the development pace of the purchaser value list of a country. It shows the dependability of macroeconomic basics. In this manner, changes in the pace of expansion may demonstrate interior monetary shakiness (IMF, 2008). High inflationary periods, in theory,

raise the cost of participating in venture initiatives, which might restrict the number of assets put resources into such economies. Thus, efficiency diminishes, which leads to slow monetary development (Khan and Senhadji (2000). High expansion regarding capital streams is a disincentive for foreign firms' ventures (Sneider & Frey, 1985) since it diminishes the increases acknowledged from speculation exercises. Financial backers will like this search for better open doors in different nations where expansion is somewhat lower. Since portfolio streams are typically momentary speculations, the impact of expansion might be more modest. Barro defined a negative coefficient as expected for this variable (1996).

### **The Exchange Rate (EXCH)**

Exchange rate is entirely set in stone by public specialists or to still up in the air in the legitimately authorized trade market. It is determined as a yearly normal in light of month-to-month midpoints (neighbourhood cash units comparative with the U.S. dollar) (OCED,2008). The conversion standard is relied upon to influence the FDI stream decidedly. Various sentiments have been shed because of swapping scale and FDI inflows: A contextual analysis by Kyereboah and Agyire (2008) on the unpredictability of genuine conversion standard features the impact of conversion scale on foreign direct interest in Africa. They observed a negative connection between swapping scale instability and foreign direct speculation inflow. Various studies (Brahmasrene & Jiranyakul, 2001; Deventer, 1995) have shown no evidence of a positive or negative relationship between conversion standard and FDI inflows.

### **Gross Domestic Product (GDP)**

According to OECD (2008), the midyear population is divided by 100 to determine gross domestic output. GDP is determined by adding up the entire gross value produced by all inhabitants of the economy, subtracting any unreported subsidies, and adding relevant product taxes (IMF, 2021). It is estimated without considering the deterioration and depletion of natural resources or the depreciation of manufactured assets. The 2015 constant dollar is used throughout (OECD, 2008). The connection between the GDP of a host nation or locale and the inflows of FDI is represented in most experimental examinations (Anderson, 1979; Dunning, 1980; Kim, 2000). In addition, the Gross Domestic Product level is a significant driver of the FDI stream to rising economies, particularly for market searchers (Guerin, 2006). Gross domestic product and its capacity are relied upon to be critical for the inflow of foreign interest in Africa. Homegrown result assumes a critical part in drawing in speculation. This is because

higher financial development is related to expanding financial action and opening doors for financial backers, subsequently, a higher pace of profits.

### **Trade Openness (TRADOP)**

OECD (2008) defines trade openness as the amount of a country's total exports and total imports as a percentage of its GDP. The impact of capital constraints is determined by the kind of twists they introduce (Asiedu & Lien, 2004). Exchange receptiveness plays a crucial role in developing foreign capital (Asiedu, 2002; Lane & Milesi-Ferretti, 2003). This is because the rising hunger of worldwide financial backers suggests that financial backers who center around direct creation might participate in trade-situated exercises and consequently may not exclusively be keen on the neighborhood market yet in addition to the global market. The amount of a nation's complete commodities and absolute imports as a negligible portion of (GDP) to quantify exchange transparency was utilized. The study anticipates a positive sign for exchange transparency with the inflows of FDI.

### **Physical Infrastructure (INFRAS)**

Fixed telephone service was substituted with physical infrastructure. The total number of active analog fixed telephone lines, voice-over-IP (VoIP) subscriptions, fixed wireless local loop (WLL) subscriptions, ISDN voice-channel equivalents, and fixed public payphone subscriptions is referred to as fixed telephone subscriptions (WTU, 2021). As per Suh and Boggs (2011), the world has seen sensational innovative changes during the most recent twenty years. The development in media transmission and the boundless web use are not many yet a portion of the progressions that have happened worldwide lately. Various studies compared the number of phone/cell phone users per 1000 people in a country to an intermediary foundation (Agbloyor, 2011; Suh & Boggs, 2011; Agbloyor et al., 2013).

Observationally, research has found a good link between the internet and the attraction of FDI in developing countries (Choi, 2003; Zekos, 2005; Ko, 2007). Choi (2003) calculated that a 10% increase in the number of online clients results in a 2% increase in FDI entry into China in his study of the influence of the web on domestic FDI into China. Regarding FDI inflow, excellent telecom is critical (Binh & Haughton, 2002). The evidence in the text suggests that an ICT foundation boosts FDI inflow into countries. This contention has been supported over the long run-on account of the capacity of the web to decrease scan time for business sectors,



colleagues, and individual clients overall. The study, consequently, theorizes a positive connection between physical infrastructure and FDI.

**Human Development Index (HDI)**

The Human Development Index (HDI), according to IMF (2021), is a summary indicator of average performance in three critical areas of human development: living a long and healthy life, having access to information, and having an acceptable quality of life. The normalized indices for each of the three dimensions' geometric means make up the HDI (World Inequality Database, 2021). The geometric mean of life expectancy, education, and GNI per capita, equally weighted, is used to construct the HDI, as shown below: The education component (mean years of schooling and predicted years of schooling) is what the two education indices' arithmetic refers to (IMF, 2021). The range of the HDI score is from 0 to 1. The HDI estimates human improvements in a country as far as the populace's well-being, instructive level, and standard pay. The HDI consolidates GNI per capita, training (a blend of grown-up education and school enrolment rates), and the future upon entering the world (Globerman & Shapiro, 2003).

According to the Human Development Report (2015), the well-being aspect is determined by the future when they enter the world, the training aspect is determined by the average of long stretches of tutoring for adults aged 25 and up, and the sky is the limit from there and expected long stretches of tutoring for school-aged children. Gross public pay per capita is used to measure the quality of living. Nigeria's inability to profit from massive FDI inflows, according to Osuji (2011). (Third biggest beneficiary in Africa by 2014). According to Willems (2015), the HDI is used to assess a country's available resources (pay) and educational and healthcare framework. Alan et al. (2006) tracked down those nations with higher futures (excellent medical services) and more elevated pay levels to get more FDI.

Table 2: Summary of Data Description and Sources

<b>Factors</b>	<b>MEASUREMENT</b>	<b>Provenance</b>
<b>Foreign Direct Investment (FDI)</b>	This is the amount of FDI as a percentage of GDP.	World Development Indicators, 2000 to 2020
<b>Government Effectiveness (GOVEF)</b>	The nation's score on the overall indicator, which ranges from around -2.5	The Worldwide Governance Indicators, 2000-2020

	to 2.5, in units of a standard normal distribution	
<b>Political Stability (POS)</b>	The nation's score on the overall indicator, which ranges from around -2.5 to 2.5, in units of a standard normal distribution.	The Worldwide Governance Indicators, 2000-2020
<b>Regulatory Quality (REQ)</b>	The nation's score on the overall indicator, which ranges from around -2.5 to 2.5, in units of a standard normal distribution	The Worldwide Governance Indicators, 2000-2020
<b>Rule of Law (ROL)</b>	The nation's score on the overall indicator, which ranges from around -2.5 to 2.5, in units of a standard normal distribution.	The Worldwide Governance Indicators, 2000-2020
<b>Control of Corruption (CORR)</b>	The nation's score on the overall indicator, which ranges from around -2.5 to 2.5, in units of a standard normal distribution	The Worldwide Governance Indicators, 2000-2020
<b>Voice and Accountability (VOA)</b>	The nation's score on the overall indicator, which ranges from around -2.5 to 2.5, in units of a	The Worldwide Governance Indicators, 2000-2020

	standard normal distribution.	
<b>Corporate Tax rate (CTR)</b>	The corporate assessment rate calculates how much a company's salaries, perks, and capital additions are burdened. It is measured in percentage rate.	The Price Waterhouse Coopers Global data base, Ernst & Young worldwide database, International Monetary Fund (2000-2020)
<b>Tax Holidays (TAXH)</b>	If no tax holiday is supplied by the individual government, a score of 0 is assigned. A score of 1 is assigned to a tax holiday period of 5 years or less, and a score of 2 is assigned to a tax holiday period of more than 5 years.	The Price Waterhouse Coopers Global data base, Ernst & Young worldwide database, International Monetary Fund (2000-2020)
<b>Tax Withholding (TAXW)</b>	This demonstrates how an economy approaches critical areas that need to be developed to support the overall economy. It is measured in percentage rate.	The Price Waterhouse Coopers Global data base, Ernst & Young worldwide database, International Monetary Fund (2000-2020)
<b>Tax Concession (TAXC)</b>	If a country does not offer any duty concessions, the variable receives a score of 0. If tax concessions are declared for a specific number of enterprises, the	The Price Waterhouse Coopers Global data base, Ernst & Young worldwide database,

	variable receives a score of 1; if all organizations are expected to receive charge concessions, the variable receives a score of 2.	International Monetary Fund (2000-2020)
<b>The Inflation Rate (INFL)</b>	Yearly rate (%) change in the consumer price index	Global Competitiveness Index, World Economic Forum, World Development Indicators (2000-2020)
<b>The Exchange Rate (EXCHR)</b>	Exchange rate is the nominal effective exchange rate divided by a price deflator or index of costs	Global Competitiveness Index, World Economic Forum, World Development Indicators (2000-2020)
<b>Gross Domestic Product (GDP)</b>	GDP per capita is gross domestic product divided by midyear population. Data are in constant 2015 U.S. dollars.	Global Competitiveness Index, World Economic Forum, World Development Indicators (2000-2020)
<b>Trade Openness (TRADOP)</b>	Trade openness is the sum of exports and imports of goods and services measured as a share of gross domestic product.	Global Competitiveness Index, World Economic Forum, World Development Indicators (2000-2020)
<b>Physical Infrastructure (INFRAS)</b>	The quantity of dynamic fixed phone landlines per 100 populaces	Global Competitiveness Index, World Economic Forum, World Development Indicators (2000-2020)

<b>Human Development Index (HDI)</b>	The HDI combines GNI per capita, education (a combination of adult proficiency and school enrolment rates), and future prospects upon entering the world with ratings of 0 and 1.	Global Competitiveness Index, World Economic Forum, World Development Indicators (2000-2020)
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Source: Researcher's computations from the World Bank World Development Indicators (WDI), World Competitiveness Index Report, World Resources Institute, and Price Waterhouse worldwide database (2000–2020).

## Model Specification

Arellano and Bond (1991) defined panel information as the pooling of perceptions on a subset of units of perception through time. Arellano and Bond (1991) defined panel information as the pooling of perceptions on a subset of units of perception through time. This conquers a few limits of utilizing stringently cross-sectional or time-series information (Arellano & Bover, 1995). The study adopts seven models to assess the impact of governance structures on the inflow of FDI in Africa. The first model runs the six leading governance indicators and lag of FDI over the dependent variable under consideration, FDI. This helps the study know the effect of governance structures without controlling for other factors. The subsequent six models will take each indicator with some control variables, including the lag of FDI, to find the effect of the governance indicator on FDI after controlling for other factors. Below are the models:

### Model 1

$$FDI_{it} = \beta_0 + \beta_1(FDI)_{i,t-1} + \beta_2(GOVEF)_{it} + \beta_3(POS)_{it} + \beta_4(REQ)_{it} + \beta_5(ROL)_{it} + \beta_6(CORR)_{it} + \beta_7(VOA)_{it} + v_{it} \quad (1)$$

Where  $v_{it} = \lambda_t + \mu_i + \omega_{it}$

$(FDI)_{i,t-1}$  denotes the lag of FDI, GOVEF denotes government effectiveness, POS denotes political stability, REQ denotes regulatory quality, ROL represents rule of law, CORR represents corruption and VOA denotes voice of accountability.

**Model 2**

$$FDI_{it} = \beta^1_0 + \beta^1_1 (FDI)_{i,t-1} + \beta^1_2 (GOVEF)_{it} + \beta^1_3 (Control Var)_{it} + v^1_{it} \quad (2)$$

Where  $v^1_{it} = \chi^1_t + \mu^1_i + \omega^1_{it}$

$(FDI)_{i,t-1}$  denotes the lag of FDI and ControlVar represents a vector of control variables explained in sub-section variables of study.

**Model 3**

$$FDI_{it} = \beta^2_0 + \beta^2_1 (FDI)_{i,t-1} + \beta^2_2 (POS)_{it} + \beta^2_3 (Control Var)_{it} + v^2_{it} \quad (3)$$

Where  $v^2_{it} = \chi^2_t + \mu^2_i + \omega^2_{it}$

**Model 4**

$$FDI_{it} = \beta^3_0 + \beta^3_1 (FDI)_{i,t-1} + \beta^3_2 (REQ)_{it} + \beta^3_3 (Control Var)_{it} + v^3_{it} \quad (4)$$

Where  $v^3_{it} = \chi^3_t + \mu^3_i + \omega^3_{it}$

**Model 5**

$$FDI_{it} = \beta^4_0 + \beta^4_1 (FDI)_{i,t-1} + \beta^4_2 (ROL)_{it} + \beta^4_3 (Control Var)_{it} + v^4_{it} \quad (5)$$

Where  $v^4_{it} = \chi^4_t + \mu^4_i + \omega^4_{it}$

**Model 6**

$$FDI_{it} = \beta^5_0 + \beta^5_1 (FDI)_{i,t-1} + \beta^5_2 (CORR)_{it} + \beta^5_3 (Control Var)_{it} + v^5_{it} \quad (6)$$

Where  $v^5_{it} = \chi^5_t + \mu^5_i + \omega^5_{it}$

**Model 7**

$$FDI_{it} = \beta^6_0 + \beta^6_1 (FDI)_{i,t-1} + \beta^6_2 (VOA)_{it} + \beta^6_3 (Control Var)_{it} + v^6_{it} \quad (7)$$

Where  $v_{it}^6 = \chi_t^6 + \mu_i^6 + \omega_{it}^6$

where for all the seven models above, subscripts  $i$  and  $t$  represents cross-sectional country and time dimensions,  $i = 1, \dots, N$  ( $N=47$  countries), and time-series dimensions,  $t = 1, \dots, T$  ( $T=20$  years) respectively. The composite error terms,  $v, v^1, \dots, v^6$  take into account the relevant time effect, country fixed effects, and the random error term that captures the effect of all omitted variables. The betas ( $\beta, \beta^1, \dots, \beta^6$ ) represent the various parameters on the individual explanatory variables yet to be estimated in models 1 to 7.

Four models are developed for objective 2, which examines the impact of tax incentives on the inflow of FDI in Africa. The first model projects corporate tax rates as the primary explanatory variable, the second withholding taxes, the next are tax holidays, and the last is tax concessions.

Below are the models:

#### Model 8

$$FDI_{it} = \alpha_0 + \alpha_1(FDI)_{i,t-1} + \alpha_2(CTR)_{it} + \alpha_3(TAXW)_{it} + \alpha_4(TAXH)_{it} + \alpha_5(TAXC)_{it} + u_{it} \quad (8)$$

Where  $u_{it} = \sigma_t + \lambda_i + \mu_{it}$

$(FDI)_{i,t-1}$  denotes the lag of FDI, CTR represents corporate tax rate, TAXW denotes withholding tax, TAXH represents tax holiday and TAXC represents tax concession.

#### Model 9

$$FDI_{it} = \alpha^1_0 + \alpha^1_1(FDI)_{i,t-1} + \alpha^1_2(CTR)_{it} + \alpha^1_3(\text{ControlVar})_{it} + u^1_{it} \quad (9)$$

Where  $u^1_{it} = \sigma^1_t + \lambda^1_i + \mu^1_{it}$

ControlVar represents a vector of control variables explained in sub-section control variables.

#### Model 10

$$FDI_{it} = \alpha^2_0 + \alpha^2_1(FDI)_{i,t-1} + \alpha^2_2(TAXW)_{it} + \alpha^2_3(\text{Control Var})_{it} + u^2_{it} \quad (10)$$

Where  $u^2_{it} = \sigma^2_t + \lambda^2_i + \mu^2_{it}$

#### Model 11

$$FDI_{it} = \alpha^3_0 + \alpha^3_1(FDI)_{i,t-1} + \alpha^3_2(TAXH)_{it} + \alpha^3_3(\text{Control Var})_{it} + u^3_{it} \quad (11)$$

Where  $u^3_{it} = \sigma^3_t + \zeta^3_i + \epsilon^3_{it}$

### Model 12

$$FDI_{it} = \alpha^4_0 + \alpha^4_1(FDI)_{i,t-1} + \alpha^4_2(TAXC)_{it} + \alpha^4_3(\text{Control Var})_{it} + u^4_{it} \quad (12)$$

Where  $u^4_{it} = \sigma^4_t + \zeta^4_i + \epsilon^4_{it}$

For all the 5 models above, subscripts  $i$  and  $t$  represents cross-sectional country and time dimensions,  $i = 1, \dots, N$  ( $N=47$  countries), and time-series dimensions,  $t = 1, \dots, T$  ( $T=20$  years) respectively. The composite error terms,  $u, u^1, u^2, u^3$  and  $u^4$  take into account the relevant time effect, country fixed effects, and the random error term that captures the effect of all omitted variables. The alphas ( $\alpha, \alpha^1, \alpha^2, \alpha^3, \alpha^4$ ) represent the various parameters on the individual explanatory variables yet to be estimated in models 8 to 12.

To empirically and theoretically determine social-economic and political variables that contribute to the inflows of FDI in Africa, model 13 is developed as shown below:

### Model 13

$$FDI_{it} = \beta * _0 + \beta * _1 (FDI)_{i,t-1} + \beta * _2 (INFLA)_{it} + \beta * _3 (EXCHR)_{it} + \beta * _4 (GDP)_{it} + \beta * _5 (TRADOP)_{it} + \beta * _6 (INFRAS)_{it} + \beta * _7 (HDI)_{it} + s_{it} \quad (13)$$

Where  $s_{it} = \gamma_t + \theta_i + \mu_{it}$

INFLA denotes inflation rate, EXCHR represents exchange rate, GDP represents economic growth, TRADOP represents trade openness, INFRAS denotes infrastructural development and HDI represents Human development index.  $\beta^*$  denotes the various parameters on the individual explanatory variables yet to be estimated in model and  $s$  denotes the error term decomposed as shown above.  $i$  and  $t$  represent the cross-sectional countries and time dimensions respectively.

## The Panel Data Estimation

### The System Generalised Method of Moments (GMM)

This study used panel regression analysis using STATA 14 as the logical programming to complete the experimental investigation on the effect of governance systems and tax incentives on foreign direct investments. Ordinary Least Square Estimation (OLS), Fixed Effect



and Random Effect (FE and RE), Instrumental Variable Method (IV), Two-Stage Least Square Estimation (2SLS), and Generalized Methods of Moments GMM) are some of the model assessment procedures used in formal regression analysis. However, there are biases in panel regression research that can result in coefficient gauges that differ in different processes. The dynamic panel model would be assessed using the System Generalized Method of Moment (GMM) assessment technique to manage any potential predispositions.

The Generalized Methods of Moment (GMM) dynamic panel assessment system was presented by Arellano and Bond (1991). "The essential recognizable proof condition for this model is the severe homogeneity of a portion of the logical factors (or the accessibility of stringently exogenous instrumental factors) condition on the undetectable individual impacts" (Arellano & Bond, 1991). In contrast to the ordinary least square (OLS) method, which expects that the logical factors should be exogenous,  $E[\epsilon_{it}] = 0$  (Greene, 2012 GMM may detect regressor errors as well as synchronization or endogeneity of informative components. The GMM, for example, can defeat circumstances like a missing subordinate variable and autocorrelation in the blunder term.

Because the study is deconstructing a panel informative index, Generalized Methods of Moment (GMM) are also considered helpful for this review. Other sources of inspiration for the Generalized Methods of Moment's decision, as identified by Edison, H. J., Levine, R., Ricci, L., and Slok, T. (2002), include the following:

1. It accounts for the endogeneity of the dreadfully exogenous components that could arise from the model's potential concurrence or opposing causality.
2. It also accounts for country-specific effects, which are sometimes overlooked by some assessment methodologies.
3. The GMM dynamic panel model explores the cross-sectional and time-series components of data collecting, broadening the possibilities.
4. The information test contains modest periods and enormous elements (nations).
5. There is no autocorrelation across nations in the blunder term, but there is country-explicit autocorrelation and heteroscedasticity.

In the literature, two types of Generalized Methods of Moment (GMM) assessors are mentioned, namely the Difference Generalized Methods of Moment (GMM) and the System Generalized Methods of Moment (GMM). Arellano and Bond (1991) proposed the distinction Generalized Methods of Moment (GMM) to address the issue of irregularity caused by endogeneity among various elements in the model by applying the significant contrast of the situation being assessed. Condition 5 henceforth dispenses with country-explicit impact

accordingly, settling irregularity and predispositions because of endogeneity by involving slacks of endogenous factors as instruments. The distinction between the Generalized Methods of Moment (GMM) procedure depends on the moment condition with the suspicion of frail homogeneity of regressors and no sequential relationship individually indicated.

Albeit the distinction in Generalized Methods of Moment (GMM) tackles endogeneity among factors, it has some impediments. The interaction appropriately wipes out time-invariant country-explicit impacts, which might be of interest, prompting model misspecification. The distinction assessor might endure feeble instrument issues when the relapse is profoundly tenacious, given that the distinction method represents a few genuine inclinations. A frail instrument subverts the asymptotic properties of the differenced assessor and might be destructive to little examples bringing about an expanded fluctuation of the coefficient and inclinations in the coefficient of the little examples.

Arellano and Bover (1995) and Blundell and Bond (1998) devised a system Generalized Methods of Moment (GMM) technique to address the issue of feeble instruments associated with the distinction GMM procedure using level and differenced conditions. The efficacy of scenario misjudgment is improved if the level structure's moment states are consolidated, and the differenced structures are consolidated (Roodman, 2009). In the level conditions, lag contrasts are used as instruments for endogenous components since these qualities become the proper instruments when extra moment conditions are considered. The additional moment conditions assume a link between the country-explicit fixed impacts and the foreordained components in the scenario, whereas there is no link between slack contrasts and country-explicit fixed impacts.

The Generalized system Methods of Moment (GMM) is viewed as the most proper panel regression assessment strategy because of the accompanying qualities intrinsic to its interaction:

1. It settles the endogeneity issues by using slacked upsides of logical factors as instruments.
2. It permits a level and slacked upsides of the factors utilized in the situation under assessment.
3. The data misfortune related to cross-sectional regression is wiped out since the Generalized Methods of Moment (GMM) system utilizes numerous perceptions for every element (country) across time.
4. System Generalized Methods of Moment (GMM) can deliver steady and unprejudiced evaluations of boundaries even with modest periods (T) and a vast number of nations (N).

As indicated by hypothesis, the dynamic panel Generalized Methods of Moment (GMM) assessor takes care of the issues of endogeneity, discarded factors predisposition, and estimation mistakes inside panel OLS assessment; however, it highlights the issue of a powerless instrument (Bazzi & Clemens, 2009; and Roodman, 2009). System Generalized Methods of Moment (GMM) is the most preferred approach, according to Hauk and Wacziarg (2009) and Kumar and Woo (2010), even though it occasionally exhibits feeble instrument disadvantage. To guarantee the legitimacy of instruments inside the system Generalized Methods of Moment (GMM), the Sargan Test of over-recognizable proof would be led to testing the theory of substantial over-distinguishing limitations. Additionally, Arellano-Bond Test would be utilized to test the theory of no sequential relationship.

For the most part, Generalized Methods of Moment (GMM) assessors have one-and-two-stage variations. The review embraces the two-venture variations. As a general rule, the two-system Generalized Methods of Moment (GMM) can give an asymptotically proficient assessor. Two-venture System GMM, Windmeijer (2005) revises standard mistakes, little example changes, and symmetrical deviations are utilized. The two-stage variation, which employs residuals from one-venture appraisals, is asymptotically more effective than the one-venture variation. The legitimacy of the acquired consequences of system Generalized Methods of Moment (GMM) assessment is heavily reliant on the satisfaction of certain suspicions. The following presumptions must be valid for the system Generalized Methods of Moment (GMM) to work: no autocorrelation in blunder terms, instrument homogeneity, and the legality of forced moment conditions for the distinction and the system Generalized Methods of Moment (GMM). The Arellano-Bond test under a 1% significance level dismisses the idea of autocorrelation of orders one and two in contrast to the mistake term. The Sargan trial of over-distinguishing limitations examines the joint legitimacy of moment conditions. After the regression evaluation, the test is given as a matter of course. The idea that forced moment conditions about regressor homogeneity are genuine is supported by P-upsides of the test greater than 0.05. Furthermore, the Difference-in-Sargan test verifies if each group of assessment instruments is exogenous.

To look at the heartiness of our outcomes and defeat any conceivable endogeneity of our example information, this review embraces a few analytic tests to guarantee that the assessed model experiences no inclinations inside the panel regression examination. These tests incorporate autocorrelation endlessly tests for the legitimacy of the over-distinguishing conditions. The Arellano-Bond test for second-order autocorrelation in first differenced mistakes is used to determine whether the quirky mistake terms are serially related, and the results of the system Generalized Methods of Moment (GMM) analysis are considered

powerful, assuming there is no proof of higher-order autocorrelation within the blunder terms. Furthermore, system Generalized Methods of Moment (GMM) results are anticipated to illustrate the validity of the instruments used in the assessment. The legality of the instruments requires that the informative endogenous variable and the instrument have a relationship and that the instrument be uncorrelated with the blunder term. The instrument should achieve a condition of pertinence and homogeneity in this way. Hansen (1982) proposed an interaction for determining the legitimacy of instruments; however, as the number of instruments grows, the test becomes increasingly weak.

The Sargan test is used in this study to determine the validity of the over-distinguishing limitation since it is seen as more appropriate for determining the instrument's legitimacy. It is asymptotically dispersed as a chi-square factor under the flawed theory of legitimate moment circumstances (Arellano & Bond, 1991; Arellano Bover, 1995), and it is relied on to build steady and productive boundaries gauges when used in the Generalized Methods of Moment (GMM) method (Blundell & Bond, 1998). It is used to test the notion that the instrumental factors are uncorrelated with some set of residuals and are along these acceptable instruments, which is incorrect. Sargan's test is also known as the Hansen test or J-Test for over-recognizing constraints.

## **Correlation Matrix**

Correlation tests are utilized to ascertain the linear relationship between the two variables. The correlation coefficient is the number obtained from this test. It is rated from -1 to 1 on a scale. The direction of any potential linear link between the two variables under inquiry is indicated by the correlation coefficient's sign. It describes if there may be a direct or indirect link between the variables. There is no linear connection when the value is 0, there is a strong negative linear correlation when the value is close to -1, and there is a strong positive linear link when the value is close to 1.

## **Descriptive Statistics**

Table 3 below shows the descriptive analysis of governance structures, tax incentives, control variables, and foreign direct investment. For each factor, the table includes the number of observations, the mean, the minimum and maximum, and the standard deviation of each variable. The highest element had 945 opinions, indicating a representative sample of 45 African countries from 2000 to 2020, which span 21 years. The positive mean worth observed

for foreign direct investment inflows in the results during the survey period was 4.461, with a standard deviation of 7.394 within the ranges of 0.02 and 86.99. This clearly suggests that although most African economies attract foreign direct inflows over time, these economies have not been able to match up well with other regions in the world. The study also included descriptive statistics for each of the variables in order to provide a thorough knowledge of the unique status of governance structures, tax incentives, and control factors in the studied African countries. The governance structures variables had the country's score on the aggregate indicator in units of standard normal distribution, i.e., ranging from approximately **-2.5 to 2.5**.

In general, government effectiveness and political stability had averages of -0.615 and -0.602 with standard deviations of 0.770 and 0.716, respectively, within the ranges of -2.191 and 1.2 and -2.148 and 1.219. Regulatory quality and the rule of law had means of -0.635 and -0.590 with a standard deviation of 0.579 and 0.689, respectively, within the ranges of -2.032 and 1.126, and -1.983 and 0.983. Furthermore, the averages for corruption control and voice and accountability were -0.641 and -0.599, with standard deviations of 0.624 and 0.600, respectively, within the ranges of -1.922 and 1.217 and -1.734 and 0.998. All these statistics on the various governance structures' scopes reveal that corruption control is the lowest of all the institutional quality dimensions, followed by regulatory quality, political stability, government effectiveness, and the rule of law in African economies, whilst voice and accountability are the strongest.

The average company tax rate was 26.522, with a standard deviation of 5.157 within the ranges of 15 and 35. The mean of tax withholding is 13.232, with a standard deviation of 4.625 within the ranges of 0 and 25, respectively. The average tax holiday for a typical country in the scenario was 1.533 with a standard deviation of 0.600 and minimum of 0, and a maximum of 2. The average tax concession was 1.384 with a standard deviation of 0.758 within the ranges of 0 and 2. Regarding the control variables which were selected for the study, inflation had a mean of 8.433 with a standard deviation of 24.61, within limits of -9.798 and 513.907, and this shows that there are still inflationary pressures in the 45 sampled countries in Africa.

The exchange rate had a mean of 929.735 with a standard deviation of 1909.868, within limits 1.006 and 16114.7. The gross domestic product recorded an average of 2159.291 with a standard deviation of 2739.429 within the limits of 258.629 and 16989.959. Trade openness had a mean of 70.005 with a standard deviation of 32.48 within the ranges of 16.141 and 311.354. This clearly shows that most African countries have engaged in major imports and exports over time, and these are essential because international foreign organizations grant help to developing economies based on the condition of greater trade openness. Infrastructure had a

mean of 3.384 with a standard deviation of 5.641 within the ranges of 0.006 and 36.128. Finally, the human development index recorded an average of 0.052 with a standard deviation of 0.119 within the ranges of 0.287 and 0.817

**Table 3: Descriptive Statistics of the variables (2000-2020)**

<b>VARIABLE</b>	<b>Obs</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
<b>FDI</b>	945	4.461	7.394	0.02	86.99
<b>GOVERNANCE STRUCTURES</b>					
<b>GOVEF</b>	945	-0.615	0.770	-2.191	1.2
<b>POS</b>	945	-0.602	0.716	-2.148	1.219
<b>REQ</b>	945	-0.635	0.579	-2.032	1.126
<b>ROL</b>	945	-0.590	0.689	-1.983	0.983
<b>CORR</b>	945	-0.641	0.624	-1.922	1.217
<b>VOA</b>	945	-0.599	0.600	-1.734	0.998
<b>TAX INCENTIVES</b>					
<b>CTR</b>	945	26.522	5.157	15	35
<b>TAXW</b>	945	13.232	4.625	0	25
<b>TAXH</b>	945	1.533	0.600	0	2
<b>TAXC</b>	945	1.384	0.758	0	2
<b>CONTROL VARIABLES</b>					
<b>INFL</b>	945	8.433	24.61	-9.798	513.907
<b>EXCHR</b>	945	929.735	1909.868	1.006	16114.7
<b>GDP</b>	945	2159.291	2739.429	258.629	16989.959
<b>TRADOP</b>	945	70.005	32.48	16.141	311.354
<b>INFRAS</b>	945	3.384	5.641	.006	36.128
<b>HDI</b>	945	0.052	0.119	0.287	0.817

Source: Author's own computations based on data retrieved from sources mentioned in the text, 2022. FDI represents foreign direct investment. Institutions represent the simple average of the six governance indicators. CORR represents control of corruption. GOVEF represents government effectiveness. POS represents political stability. ROL represents rule of law. REQ represents regulatory quality. VOA represents voice and accountability. CTR represents corporate tax rate. TAXH represents tax holidays. TAXW represents tax withholding. TAXC represents tax concession. INFL represents inflation. EXCHR represents exchange rate. GDP represents gross domestic product. TRADOP represents trade openness. INFRAS represent infrastructure. HDI represents human development index

## **Correlation Matrix**

The pairwise correlation matrix for all the variables used in all the models' empirical analyses is shown in Tables 4 and 5 (see Appendix 2). To represent the direction of the association, Pearson is ranked correlation coefficient accepts a value between 0 and 1, with either a positive or negative sign. While a negative correlation suggests an unfavourable link between two variables, a positive correlation suggests a good association. If the correlation is more robust near zero than near one, it indicates a poor correlation; otherwise, it indicates an ideal relationship. A pair of variables with a correlation more significant than 0.5 is considered to have a strong connection since a correlation of zero indicates that there is no link at all between the variables. The following pairs of variables were examined for correlations: government effectiveness and foreign direct investment, political stability and foreign direct investment, regulatory quality and foreign direct investment, the rule of law and foreign direct investment, control of corruption and foreign direct investment, voice and accountability and foreign direct investment, corporate tax rate and foreign direct investment, withholding tax and foreign direct investment, tax holidays and foreign direct investment, inflation and foreign direct investment, exchange rate and foreign direct investment, gross domestic product and foreign direct investment, trade openness and foreign direct investment, physical infrastructure and foreign direct investment, human development index and foreign direct investment. The correlation matrix of the governance structures variables and the tax incentives variables with foreign direct investment can be found on Appendix 2.

The overall foreign direct investment has a high pairwise connection with the six governance structure indicators, tax incentives, and control variables, as one might expect. In addition, the correlation matrix shows that FDI has a tangible link. Because there are no multicollinearity issues in the empirical specification and the other independent variables have correlation coefficients less than 0.90, the correlation matrix does not pose multicollinearity or autocorrelation problems (Gyamfi, 2015).

## **Regression results**

Steps followed for evaluation were taken by observing the outcomes regarding the significance level of the model, as well as the degree of explainability of the variables and the statistical significance of the coefficients. This part presents the result of the system GMM assessments on the experimental model expressed in section three. The regression results depend on the sample of 45 African nations for the 21 years frame (2000-2020). Thirteen (13)



model specifications were used for estimation. To assess the impact of governance structures on the inflow of FDI in Africa, the study adopted seven models. The first model (model 1) runs the six main governance indicators and lag of FDI over the dependent variable under consideration which is FDI. The subsequent six models (models 2-7) will take each governance indicator with some control variables, including the lag of FDI, to find the effect of the governance indicator on FDI after controlling for other factors. Six models (models 8–13) were created to study how tax incentives affect FDI inflows into Africa. The first model (model 8) projects the tax incentives variables, which include corporate tax, withholding taxes, tax holidays, tax concessions and lag of FDI over the dependent variable under consideration which is FDI. The subsequent five models (models 9-13) will take each tax incentives variable with some control variables, including the lag of FDI, to find the effect of the tax incentives on FDI after controlling for other factors. The summary for the models (1-13) can be found below:

$$FDI_{it} = \beta_0 + \beta_1(FDI)_{i,t-1} + \beta_2(GOVEF)_{it} + \beta_3(POS)_{it} + \beta_4(REQ)_{it} + \beta_5(ROL)_{it} + \beta_6(CORR)_{it} + \beta_7(VOA)_{it} + v_{it} \quad (1)$$

$$FDI_{it} = \beta^1_0 + \beta^1_1(FDI)_{i,t-1} + \beta^1_2(GOVEF)_{it} + \beta^1_3(Control\ Var)_{it} + v^1_{it} \quad (2)$$

$$FDI_{it} = \beta^2_0 + \beta^2_1(FDI)_{i,t-1} + \beta^2_2(POS)_{it} + \beta^2_3(Control\ Var)_{it} + v^2_{it} \quad (3)$$

$$FDI_{it} = \beta^3_0 + \beta^3_1(FDI)_{i,t-1} + \beta^3_2(REQ)_{it} + \beta^3_3(Control\ Var)_{it} + v^3_{it} \quad (4)$$

$$FDI_{it} = \beta^4_0 + \beta^4_1(FDI)_{i,t-1} + \beta^4_2(ROL)_{it} + \beta^4_3(Control\ Var)_{it} + v^4_{it} \quad (5)$$

$$FDI_{it} = \beta^5_0 + \beta^5_1(FDI)_{i,t-1} + \beta^5_2(CORR)_{it} + \beta^5_3(Control\ Var)_{it} + v^5_{it} \quad (6)$$

$$FDI_{it} = \beta^6_0 + \beta^6_1(FDI)_{i,t-1} + \beta^6_2(VOA)_{it} + \beta^6_3(Control\ Var)_{it} + v^6_{it} \quad (7)$$

$$FDI_{it} = \alpha_0 + \alpha_1(FDI)_{i,t-1} + \alpha_2(CTR)_{it} + \alpha_3(TAXW)_{it} + \alpha_4(TAXH)_{it} + \alpha_5(TAXC)_{it} + u_{it} \quad (8)$$

$$FDI_{it} = \alpha^1_0 + \alpha^1_1(FDI)_{i,t-1} + \alpha^1_2(CTR)_{it} + \alpha^1_3(Control\ Var)_{it} + u^1_{it} \quad (9)$$

$$FDI_{it} = \alpha^2_0 + \alpha^2_1(FDI)_{i,t-1} + \alpha^2_2(TAXW)_{it} + \alpha^2_3(Control\ Var)_{it} + u^2_{it} \quad (10)$$

$$FDI_{it} = \alpha^3_0 + \alpha^3_1(FDI)_{i,t-1} + \alpha^3_2(TAXH)_{it} + \alpha^3_3(Control\ Var)_{it} + u^3_{it} \quad (11)$$

$$FDI_{it} = \alpha^4_0 + \alpha^4_1(FDI)_{i,t-1} + \alpha^4_2(TAXC)_{it} + \alpha^4_3(Control\ Var)_{it} + u^4_{it} \quad (12)$$

$$\begin{aligned}
\text{FDI}_{it} = & \beta *_{0} + \beta *_{1} (\text{FDI})_{i,t-1} + \beta *_{2} (\text{INFLA})_{it} + \beta *_{3} (\text{EXCHR})_{it} + \beta *_{4} (\text{GDP})_{it} \\
& + \beta *_{5} (\text{TRADOP})_{it} + \beta *_{6} (\text{INFRAS})_{it} + \beta *_{7} (\text{HDI})_{it} \\
& + s_{it}
\end{aligned}
\tag{13}$$

The aftereffects of the pattern FDI regression of the system GMM dynamic panel model is introduced in Table 4 and Table 5 beneath.

**Table 4: System GMM Estimation Result (2000-2020) Dependent variable: FDI**

	<b>Model 1</b>	<b>Model 2</b>	<b>Model 3</b>	<b>Model 4</b>	<b>Model 5</b>	<b>Model 6</b>	<b>Model 7</b>
<b>Lag of FDI</b>	0.455***	0.426***	0.422***	0.420***	0.422***	0.420***	0.419***
	(0.0115)	(0.00785)	(0.00802)	(0.00752)	(0.00781)	(0.00826)	(0.00778)
<b>GOVERNANCE STRUCTURES</b>							
<b>GOVEF</b>	1.590***	0.222**					
	(0.321)	(0.0878)					
<b>POS</b>	1.474***		0.114***				
	(0.408)		(0.116)				
<b>REQ</b>	0.381			0.391**			
	(0.511)			(0.178)			
<b>ROL</b>	1.117***				0.0240		
	(0.393)				(0.0715)		
<b>CORR</b>	-1.174**					-0.394***	
	(0.500)					(0.0675)	
<b>VOA</b>	6.515***						0.456***
	(0.705)						(0.121)
<b>CONTROL VARIABLES</b>							

<b>INFL</b>		0.00530	0.00303	0.00283	0.00273	0.00277	0.00128
		(0.00396)	(0.00428)	(0.00403)	(0.00420)	(0.00375)	(0.00384)
<b>EXCHR</b>		-0.00014 <sup>***</sup>	-0.000097 <sup>**</sup>	-0.000094 <sup>**</sup>	-0.000096 <sup>**</sup>	-0.00012 <sup>***</sup>	-0.000105 <sup>**</sup>
		(0.000037)	(0.000042)	(0.000045)	(0.000039)	(0.000041)	(0.000042)
<b>GDP</b>		0.000191 <sup>***</sup>	0.000186 <sup>***</sup>	0.000144 <sup>***</sup>	0.000182 <sup>***</sup>	0.000162 <sup>***</sup>	0.000172 <sup>***</sup>
		(0.000035)	(0.000042)	(0.000049)	(0.000038)	(0.000036)	(0.000045)
<b>TRADOP</b>		0.0292 <sup>***</sup>	0.0310 <sup>***</sup>	0.0296 <sup>***</sup>	0.0307 <sup>***</sup>	0.0317 <sup>***</sup>	0.0328 <sup>***</sup>
		(0.00231)	(0.00257)	(0.00282)	(0.00242)	(0.00232)	(0.00250)
<b>INFRAS</b>		-0.123 <sup>***</sup>	-0.126 <sup>***</sup>	-0.0946 <sup>***</sup>	-0.119 <sup>***</sup>	-0.0946 <sup>***</sup>	-0.0991 <sup>***</sup>
		(0.0190)	(0.0197)	(0.0223)	(0.0201)	(0.0194)	(0.0198)
<b>HDI</b>		-1.589	-1.762 <sup>*</sup>	-0.503	-1.684	-0.912	-1.175
		(1.141)	(1.018)	(1.251)	(1.038)	(1.146)	(1.204)
<b>_cons</b>	1.255 <sup>***</sup>	1.328 <sup>**</sup>	1.287 <sup>**</sup>	0.376	1.199 <sup>**</sup>	0.431	0.455
	(0.285)	(0.652)	(0.553)	(0.671)	(0.560)	(0.601)	(0.626)
<b>DIAGNOSTICS</b>							
No. of obs.	944	944	944	944	944	944	944
No. of Inst.	38	38	38	38	38	38	38
Prob > chi2	0.000	0.000	0.000	0.000	0.000	0.000	0.000
AR(2): Z (p-	1.67	1.71	1.70	1.71	1.71	1.70	1.69

value)	(0.904)	(0.807)	(0.808)	(0.807)	(0.807)	(0.809)	(0.901)
Hansen J:	32.84	31.57	28.95	31.18	29.67	28.49	31.88
(p-value)	(0.329)	(0.339)	(0.417)	(0.357)	(0.431)	(0.492)	(0.325)
SarganX <sup>2</sup>	32.00	31.37	28.92	30.92	29.64	28.49	31.72
(p-value)	(0.320)	(0.301)	(0.417)	(0.321)	(0.381)	(0.439)	(0.286)

The values in parentheses are p-values; values denoted by \*\*\*, \*\*, and \* represent 1%, 5%, and 10% significant levels respectively. FDI represents foreign direct investment. Institutions represent the simple average of the six governance indicators. CORR represents control of corruption. GOVEF represents government effectiveness, POS represents political stability, ROL represents rule of law, REQ represents regulatory quality. VOA represents voice and accountability. INFL represents inflation. EXCHR represents exchange rate. GDP represents gross domestic product. TRADOP represents trade openness. INFRAS represent infrastructure. HDI represents human development index. The insignificant probability (J-stats) value suggested that there is no overriding identity, and the instruments adopted are efficient and do not correlate with the error term. Source: Researcher's own calculation, 2022.

**Table 5: System GMM Estimation Result (2000-2020) Dependent variable: FDI**

	<b>Model 8</b>	<b>Model 9</b>	<b>Model 10</b>	<b>Model 11</b>	<b>Model 12</b>	<b>Model 13</b>
<b>Lag of FDI</b>	0.363***	0.400***	0.419***	0.366***	0.399***	0.422***
	(0.00520)	(0.00729)	(0.00852)	(0.00607)	(0.00697)	(0.00773)
<b>TAX INCENTIVES</b>						
<b>CTR</b>	-0.132***	-0.108***				
	(0.0155)	(0.0149)				
<b>TAXW</b>	0.133***		0.0318**			
	(0.0308)		(0.0132)			
<b>TAXH</b>	2.743***			2.380***		
	(0.0974)			(0.185)		
<b>TAXC</b>	-0.335**				-0.809***	
	(0.162)				(0.163)	
<b>CONTROL VARIABLES</b>						
<b>INFL</b>		0.00268	0.00204	0.00402	0.00261	0.00271
		(0.00362)	(0.00417)	(0.00424)	(0.00360)	(0.00400)
<b>EXCHR</b>		-0.000105**	-0.000107**	-0.0000421	-0.0000446	-0.0000982**
		(0.0000454)	(0.0000471)	(0.0000284)	(0.0000365)	(0.0000390)
<b>GDP</b>		0.000204***	0.000173***	-0.000162***	0.0000664***	0.000178***

		(0.0000358)	(0.0000410)	(0.0000605)	(0.0000447)	(0.0000366)
<b>TRADOP</b>		0.0336***	0.0293***	0.0192***	0.0302***	0.0308***
		(0.00268)	(0.00256)	(0.00321)	(0.00306)	(0.00234)
<b>INFRAS</b>		-0.115***	-0.109***	-0.0839***	-0.113***	-0.119***
		(0.0165)	(0.0191)	(0.0215)	(0.0174)	(0.0188)
<b>HDI</b>		-0.392	-1.606*	-2.920**	-0.849	-1.595
		(0.814)	(0.852)	(1.277)	(1.379)	(1.001)
<b>_CONS</b>	2.142***	-0.517*	1.257***	6.303***	3.619***	1.134**
	(0.541)	(0.278)	(0.193)	(0.208)	(0.198)	(0.546)
<b>DIAGNOSTICS</b>						
<b>No. of obs.</b>	944	944	944	944	944	944
<b>No. of Inst.</b>	38	38	38	38	38	38
<b>Prob &gt; chi2</b>	0.000	0.000	0.000	0.000	0.000	0.000
<b>AR(2): Z (p-value)</b>	1.65 (0.908)	1.69 (0.901)	1.70 (0.808)	1.66 (0.907)	1.69 (0.902)	1.71 (0.807)
<b>Hansen J: (p-value)</b>	36.98 (0.212)	31.88 (0.325)	30.44 (0.397)	29.91 (0.418)	30.38 (0.345)	31.05 (0.413)
<b>SarganX<sup>2</sup> (p-value)</b>	37.32 (0.241)	31.72 (0.286)	30.31 (0.349)	28.92 (0.416)	30.39 (0.395)	30.83 (0.373)

The values in parentheses are p-values; values denoted by \*\*\*, \*\*, and \* represent 1%, 5%, and 10% significant levels respectively. FDI represents foreign direct investment. CTR represents corporate tax rate. TAXW represents tax withholding. TAXH represents tax holidays. TAXC represents tax concession. INFL represents inflation. EXCHR represents exchange rate. GDP represents gross domestic product. TRADOP represents trade openness. INFRAS represent infrastructure. HDI represents human development index. The insignificant probability (J-stats) value suggested that there is no overriding identity, and the instruments adopted are efficient and do not correlate with the error term.

Source: Researcher's own calculation, 2022



## Discussion

The consequence of the regression involving the system GMM assessment for the impact of governance structures variables, tax incentives variables and control variables on FDI inflows in Africa covered in table 7 and table 8 are made sense of individually as follows:

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### **Previous Foreign Direct Investment Inflows (Lag of FDI) and Foreign Direct Investment (FDI)**

The GMM system's findings in Table 5 and Table 6 revealed that the FDI lag has a positive and significant impact on Africa's present foreign direct investment, which is at a high of 5% in all the models 1 - 7. The positive coefficient of the lag of FDI in all the models means that previous foreign direct investments have a positive impact on the inflows of FDI in African economies. Also, the significance of the lag of FDI implies and supports several claims that a country's speculating climate is critical in ensuring high levels of future investment (Agyemang et al., 2019). A favourable and inviting venture environment combined with the accomplishment of the normal return will encourage FDI development. The finding reveals that FDI inflows will generally persevere over the long haul. This might mirror a propensity arrangement impact as financial backers gain insight into portfolio speculation activities.

Simultaneously, FDI may improve the host country's macroeconomic situation, resulting in more portfolio speculation. The significance of the FDI lag implies and supports several claims that a country's speculating climate is critical in ensuring high levels of future investment. A favourable and inviting venture environment combined with the accomplishment of the normal return will encourage FDI development. The outcome of these procedures supports discoveries from existing examinations by Brennan and Cao (1997), Kamaly (2002) and Appiah-Kubi et al. (2020).

### **Government Effectiveness (GOVEF) and Foreign Direct Investment (FDI)**

At a 5% importance level of model 2, the coefficient of government effectiveness (GOVEF) variable recorded a positive and strong measurably link with direct foreign interests in African nations, according to the regression results (Table 5). The coefficient of 0.222 demonstrates that an improvement in a country's level of government effectiveness can result in an increase in foreign direct investment in African economies of 0.222 units. This indicates that a key factor in the influx of foreign direct investment into African nations is the efficacy

of the government. In this regard, the analyzed African countries with sound and persuasive state-run administrations played a crucial role in convincing foreign financial backers to put their faith in their economies. According to the World Governance Indicators (2008), government effectiveness measures perceptions of the calibre of public services, the calibre of the civil service and the extent of its independence from political pressures, the calibre of policy formulation and implementation, and the credibility of the government's commitment to such policies.

Government adequacy also refers to a country's government's ability to authorize and carry out plans and strategies to create appropriate infrastructure (Barrell & Nahhas, 2018). Our findings were like those of Bokpin et al. (2017), who claimed that government effectiveness is a determining element of economic development through FDI inflow. Furthermore, it agrees with Kirkpatrick et al. (2006), who noted that the ability to attract foreign investments is contingent on the presence of an effective and efficient government. Finally, the results are consistent with Agyemang et al. (2019)'s assertion that one of the most significant determinants of FDI inflows is an effective and favourable governance framework. They went on to say that investing in governance effectiveness will not only attract foreign investors but will also create favourable conditions for domestic and international businesses. As a result, the study reveals that foreign investors succeed in African countries' economies impacted by effective government.

### **Political Stability (POS) and Foreign Direct Investment (FDI)**

Political stability had a strong and positive significant impact on foreign direct investment, as presented in the results from Model 1 and Model 3 in Table 5. Increased political stability and strength in African countries have a 1% impact on foreign investment decisions, given the strong and positive correlation between political stability and inflows of foreign direct investment. The coefficient of 1.474 demonstrates that an improvement in a country's level of political stability can result in an increase in foreign direct investment in African economies of 1.474 units. Political stability and Absence of Violence measures the perceived possibility of political instability and/or politically motivated violence, including terrorism (Kauffman et al., 2008).

The degree of violence and terrorism expressed in the country and by citizens linked with the country is used to determine that (WGI, 2021). Many African countries face significant political risks, and FDI inflows to these countries are restricted. A lack of democracy exacerbates societal tensions, increasing the risk of a country experiencing serious political

crises (Appiah-Kubi et al., 2020). The outcome is consistent with Smarzynska and Wei's (2000) results, which suggested that political upheaval might impede financial flows. Similarly, the findings support those of Anyawu (2013) and Agyemang et al. (2016), who claim that democracy and FDI have a beneficial association. However, research like Adam et al. (2007) and Paniagua et al. (2014) revealed that democracy had a detrimental impact on FDI. The findings of the study support those African economies with stable political stability positively impact the inflows of foreign direct investment.

### **Regulatory Quality (REQ) and Foreign Direct Investment (FDI)**

Based on the Model 4 results in Table 5, it can be shown that the regulatory quality and the influx of foreign companies into African nations are positively correlated. The positive regulatory quality coefficient is a strong indicator that foreign direct investment in African economies is essential. According to the model 4 results, regulatory quality significantly increases foreign direct investment at the 5% level of significance. The correlation coefficient of 0.391 shows that a rise in foreign direct investment in African economies can increase by 0.391 units for every unit increase in a nation's regulatory quality. The coefficient for regulatory quality indicates that it is particularly significant for African countries' foreign direct investment. As a result, governments in Africa bear a huge obligation to guarantee that regulatory quality is in place and that the economy is run in accordance with those laws and policies in order to stimulate economic development, increase social welfare, and attract foreign investment (Rodrik, 1999). Dupasquier and Osakwe (2006) stated that changes in the quality of government regulatory efficacy and governance practices have an impact on the direction of FDI inflows.

According to their research, a decline in the effectiveness and enforcement of investment laws has a negative impact on FDI inflows. This suggests that improving the regulatory quality of an economy has a favourable impact on FDI inflows. The results are in line with studies by Agyemang et al. (2019); Appiah-Kubi et al. (2019); Bokpin (2017); Maitah et al. (2014), and Glass and Saggi (2002), who emphasized three primary reasons why regulatory features are important in attracting foreign investors and increasing FDI inflows. They talked about how a capable and efficient state institution operating within a strong regulatory framework will increase production and attract foreign investment. Foreign investors are more inclined to invest in African countries that adhere to sound ethical standards. Most African countries, according to studies conducted by the United Nations Economic Commission for Africa (2016), have inadequate regulatory administration. Effective regulatory management systems would

decrease unnecessary constraints on foreign corporations and increase their transparency and security, impacting their investment decisions in African economies. Thus, the findings of the study support that the quality of guidelines in African countries is inextricably linked to the inflow of foreign direct investments.

### **The Rule of Law (ROL) and Foreign Direct Investment (FDI)**

The Rule of Law coefficient found a positive but insignificant link between the rule of law and inflows of foreign direct investment into African countries, according to the results from model 5 in Table 5. The insignificant level of the results from model 5 showed that rule of law had a coefficient of 0.0240. The insignificant correlation coefficient of 0.0240 shows that a rise in regulatory quality in African economies does not increase 0.391 units for every unit increase in foreign direct investment. The term "the rule of law" refers to perceptions of how much people respect and uphold social norms, particularly those pertaining to property rights, contract enforcement, the police, the courts, and the possibility of crime and violence (WGI, 2008). According to Kaufmann et al. (2008), the rule of law refers to how citizens engage with the institutions that help to govern those relationships. The finding reveals that institutions such as the judiciary that exhibit characteristics such as fairness and efficiency in their delivery do not play an important role in facilitating or limiting government power to interfere in business activities and the market situation and unbiased enforcement of contracts.

Many researchers like Staats and Biglaiser (2011); Agyemang et al. (2016); Bokpin et al. (2017) have stated that the prevalence of foreign ownership in African countries is not solely dependent on the country's moral character, legitimacy, sincerity, and political and authoritative leadership in terms of the rule of law. The findings of the study contradict those of Seidman et al. (1999) and Hewko (2002), who found that while transaction fees increase the costs of private investment, foreign investors do not avoid economies with increased transaction fees and instead prefer to invest in more effective or sound legal and judicial systems. Thus, the findings of the study support that economies with a strict rule of law do not attract more foreign assets to African countries. The findings of the study support those African economies with the rule of law do not impact the inflows of foreign direct investment.

### **The control of Corruption (CORR) and Foreign Direct Investment (FDI)**

Furthermore, table 5 demonstrated that at a 1% level of Model 6, corruption and foreign direct investment had a negative yet significant relationship in African countries. The

coefficient of 0.394 shows that a unit increase in the control of corruption in African economies can lead to a 0.394 unit decrease in foreign direct investment. Control of Corruption examines views of the degree to which public authority is used for personal benefit, encompassing both minor and significant types of corruption as well as the elites and commercial interests capturing the state (WGI, 2008). Overall, effective embezzlement control is critical for reducing abuse of public power for private gain, reducing social complexity, and resolving political and financial issues that aid nations in building and enhancing their economies, trying to influence the trust and surety of international investment backers' decisions (Agyemang et al., 2019). As a result, even though the selected African countries are recognized for corruption, the extent of their corrupt practices has reached a position where overseas firms may be influenced to invest in their country (Castro et al., 2013). The findings were consistent with Rower's (2009) prior research, which dubbed this phenomenon the "helping hand theory." He emphasized that paying off important government officials might allow investors to circumvent bureaucratic red tape.

This might also entail more accessible admission into a country and a looser regulatory environment for foreign businesses. The study also revealed that corruption helps supplement low wages in developing countries, allowing multinational corporations to keep their tax costs low while contributing to growth. In the presence of insufficient laws, Rower (2009) argued, corruption can smooth the economic system, resulting in a Pareto optimal conclusion. This result was in line with studies by Castro et al. (2013), Mathur (2013), Bokpin (2017), Agyemang et al. (2019) and Appiah-Kubi et al. (2021), who claimed that while corruption has restrictive impacts, it also has stimulative consequences in nations with poor frameworks. As a result, attempting to eradicate corruption in African countries that serves a growth-promoting function can be a costly war that will be met with resistance. The findings contradicted Qazi et al. (2014) and Al-Sadig (2009), who claimed that corruption is a grabbing hand, reducing FDI inflows. Thus, the study's findings support that corruption impacts the predominance of foreign direct investment in African countries.

### **Voice and Accountability and Foreign Direct Investment (FDI)**

Model 7 in Table 5 shows that at a 1% significance level, voice and accountability significantly positively affect foreign direct investment in African economies. The coefficient of 0.456 shows that a unit increase in voice and accountability will lead to a 0.456 unit in foreign direct investment in African countries. According to World Governance Indicators (2008), voice and accountability measure perceptions of a nation's citizens' capacity to choose their government and their freedom of expression, association, and access to a free press. One of the

mainstays of governance and democracy is accountability, which drives the state and its institutions, the public sector, and civil society to work toward specific goals and outcomes, achieve their objectives, and develop compelling strategies through solid monitoring and reporting mechanisms (OECD, 2008).

Voice accountability significantly impacts multinational businesses' market power and the inflow of foreign capital into African economies. The study's findings revealed that African countries' degree of voice and accountability has a bearing on foreign direct investment. The results were consistent with previous investigations by (Agosin, 2005; Qazi, 2014; Appiah-Kubi et al., 2019), who established that more significant inflows of foreign direct investment to a country are influenced by media freedom. This means that African countries that are characterised by voice and accountability would have a great impact on foreign direct investment. UNECA (2016) and Kuril and Yalta (2017) have also identified voice and accountability as strong pillars of a majority-rule government, in which citizens have access to data and the ability to express their views on financial development and improvement. Thus, the findings of the study support that freedom of media and speech has an impact on the predominance of foreign direct investment in African nations.

### **The Corporate Tax rate (CTR) and Foreign Direct Investment (FDI)**

The results from Model 8 and Model 9 in Table 6 reveal that at 1% significance levels, the company tax rate (CTR) has a substantial significant but negative impact on foreign direct investment in African economies. The coefficients of 0.132 and 0.108 show that a unit increase in the percentage of company tax in African economies can lead to a 0.132 and 0.108 units decrease in foreign direct investment. The result means that an increase in the corporate tax rate reduces foreign direct investment inflows into African countries. Corporate tax rates vary significantly amongst nations, with some having meagre rates and being labelled tax havens. The effective corporate tax rate, or the rate a corporation pays, is typically lower than the statutory rate, which represents the stated sum before any deductions since corporate taxes can be lowered by a variety of deductions, government subsidies, and tax breaks (Kraushoff, 2013).

The results also mean that African countries should reduce the corporate tax rate for foreign companies to entice them, which would increase the inflows of foreign direct investment in their economies. This result lends credence to the idea that raising the corporate tax rate will raise business expenses and discourage investment. As a result, investors desire fair treatment in all sectors in resource-constrained African nations in order to facilitate simpler diversification. The results were consistent with previous findings (Kraushoff, 2013; Obeng,

2014; Majavu & Kapingura, 2016; Lodhi, 2017; Abille, 2020; Appiah-Kubi et al., 2022). Thus, the findings of the study support that the corporate tax rate in African countries influences foreign direct investment inflows.

### **Withholding Tax (TAXW) and Foreign Direct Investment (FDI)**

Tax withholding (TAXW) had a strong and positive significant impact on foreign direct investment, as presented in the results from Model 8 and Model 10 in Table 6. Increased withholding tax in African countries has a 5% impact on foreign investment decisions, given the strong and positive correlation between withholding tax and inflows of foreign direct investment. The coefficient of 0.133 and 0.0318 demonstrate that an improvement in a country's tax withholding (TAXW) can result in an increase in foreign direct investment in African economies of 0.133 and 0.0318 units. Withholding tax, as defined by (OECD, 2008), is the annual assessment paid to the government by the partner or management, not the employee. This shows how an economy addresses key areas that it needs to develop to help the entire economy. In other words, withholding tax on income that is levied at the origin means that the employer is tasked with withholding the appropriate level of tax from particular payments and repaying it to the authorities.

Almost all tax systems have withholding taxes, which are frequently applied to dividends, interest, royalties, and other types of related tax payments. Tax treaties usually lower the withholding tax rates (OECD, 2008). Wilson and Wildasin (2004) characterize billing as an annual duty that is paid to the government through the organization rather than by the worker, where nations administer billing fee systems to direct the company towards globally portable capital. The significant positive link between tax withholding and inflows of direct foreign speculation demonstrates that higher African economies prioritize crucial sectors that need to be improved in order to aid their complete economies and sway foreign financial backers' navigation. With prior investigations by Peters and Kiabel (2015), Kransdoff (2010), Obeng (2014), and Van Parys (2010), our results are supported. Thus, the findings of the study support that significant tax withholdings in African countries have an impact on foreign direct investment inflows.

### **Tax Holidays (TAXH) and Foreign Direct Investment (FDI)**

Based on the Model 8 and Model 11 results in Table 6, it can be shown that the tax holiday (TAXH) and the influx of foreign companies into African nations are strongly positively

correlated. The positive tax holiday (TAXH) coefficient is a strong indicator that foreign direct investment in African economies is essential. According to the model 8 and model 11 results, tax holiday (TAXH) significantly increases foreign direct investment at the 1% level of significance. The correlation coefficient of 2.743 and 2.380 show that a rise in foreign direct investment in African economies can increase by 2.743 and 2.380 units for every unit increase in a nation's tax holiday (TAXH). According to OECD (2008) tax policy statistics, a tax holiday is a short-term tax reduction. Tax holidays frequently suspend consumer-paid state and municipal sales taxes in African nations. Authorities may employ tax holidays as investment opportunities to temporarily exclude a new facility from paying property taxes. These actions are the biggest opportunity given to the financiers of the economy each year.

According to a report by the United Nations Economic Commission for Africa (2016), African economies have been praised for attempting a fair arrangement approach to achieving development and improvement. As such, most countries in Africa are making implementations to improve their tax holiday system to entice the inflows of foreign direct investment. The result of the study is in support of the findings by Klemm et al. (2009) that in developing countries, tax holidays are important in enticing foreign investment. Tax holidays in Africa reduce costs to investors, thus encouraging investment in less attractive sectors. This means that countries are making deliberate efforts to increase the tax holiday rate, lowering the unnecessary burdens on international enterprises and thereby influencing their investment decisions in African economies. The results of the study were consistent with earlier studies by Kransdoff (2010), Peters and Kiabel (2015), Obeng (2014), and Ocheni (2014). Thus, the findings of the study support that higher tax holidays in African countries have an impact on the influx of foreign direct investment.

### **Tax Concession (TAXC) and Foreign Direct Investment (FDI)**

Furthermore, tax concession (TAXC) had a strong and negative significant impact on foreign direct investment, as presented in the results from Model 8 and Model 12 in Table 6. Increased tax concession in African countries has a 5% and 1% significant impact on foreign investment decisions, given the strong and negative correlation between tax concession (TAXC) and inflows of foreign direct investment. The coefficient of 0.335 and 0.809 show that a unit increase in the control of corruption in African economies can lead to a 0.335 and 0.809 unit decrease in foreign direct investment. The coefficient of tax concession clearly demonstrated that, while the link between tax concession and foreign direct speculation inflow is negative, it is also significant. Chai (2006) described tax concessions as favourable tax



treatment for sorts of businesses or entities, which is a frequent practice in both developed and developing nations.

Tax breaks are given to encourage investment, in which case they are known as "investment incentives" or to accomplish certain social goals (Goyal & Chai, 2008). To encourage investment, exemptions from import-related customs and taxes may also be granted. These exemptions may apply to a variety of other imported items for statutory, civic, or charitable organizations (Goyal & Chai, 2008). It is a question of whether state administrations are specific in their arrangements for granting rights or whether rights are granted in all cases. The findings show that economies with broad-based tax breaks do always attract the same level of foreign direct investment as nations with narrower tax breaks. The study's findings agreed with those of prior research by Obeng (2014) and Ocheni (2014). Thus, the findings of the study support that higher tax concessions in African countries have an impact on the influx of foreign direct investment.

## **Control Variables and FDI**

The outcomes of the control variables used in the models determine how governance and tax incentives affect the inflows of foreign direct investment in African nations. All of the models (1–13) in Tables 5 and 6 accounted for six macroeconomic variables that are made up of the following: inflation (INFL), exchange rate (EXCHR), gross domestic product (GDP), trade openness (TRAOP), physical infrastructure (INFRAS) and human development index (HDI).

### **Inflation (INFL) and Foreign Direct Investment (FDI)**

The inflation (INFL) coefficient found a positive but insignificant link between the inflation and inflows of foreign direct investment into African countries, according to the results from models 1-13 in Tables 5 and 6. The insignificant level of the results from all 13 models showed that inflation had a coefficient of 0.0240. The insignificant correlation coefficient of 0.0530 shows that a rise in inflation in African economies does not increase 0.0530 units for every unit increase in foreign direct investment. Inflation estimates the development pace of the purchaser value list of a country. It shows the dependability of macroeconomic basics. In this manner, changes in the pace of expansion may demonstrate interior monetary shakiness (IMF, 2008). High inflationary periods, in theory, raise the cost of participating in venture initiatives, which might restrict the number of assets put resources into such economies.

Thus, efficiency diminishes, which leads to slow monetary development (Khan and Senhadji (2000)). The insignificant relationship suggests that expansion as a proportion of macroeconomic stability contrarily impacts the inflows of FDI in Africa. Basically, the crowding impact of inflation is to be blamed (Boyd et al., 2001). Aside from the reason provided, during inflationary periods, the prices of goods and services increase, causing demand for goods and services to fall. This implies that any investor who invests during those periods would experience a downward trend in its performance (Law, 2009). To prevent that experience, investors should avoid investing during inflationary periods. These results were consistent with earlier studies by Sneider and Frey (1985); Dodge et al. (2007). On the other hand, the results were inconsistent with earlier studies by Noorbarksh et al. (2001) and Blomstrom & Kokko (2003).

### **Exchange Rate (EXCHR) and Foreign Direct Investment (FDI)**

Based on the models from 1-13 results in Table 5 and Table 6, it can be shown that the exchange rate (EXCHR) and the influx of foreign direct investment into African nations are strongly negatively correlated with the exception of models 11 and 12 of the results of models. The negative exchange rate (EXCHR) coefficient is a strong indicator that foreign direct investment in African economies is essential. According to the models (1-10) results, the exchange rate (EXCHR) significantly increases foreign direct investment at the 1% and 5 % levels of significance. The coefficient of 0.000105 (Model 8) shows that a unit increase in the exchange rate of African economies can lead to a 0.000105 unit decrease in foreign direct investment. This suggests that the exchange rate does affect the levels of foreign investment in Africa. Exchange alludes to the not entirely set in stone by public specialists or to still up in the air in the legitimately authorized trade market.

It is determined as a yearly normal in light of month-to-month midpoints (neighbourhood cash units comparative with the U.S. dollar) (OCED,2008). A contextual analysis by Kyereboah and Agyire (2008) on the unpredictability of genuine conversion standards features the impact of conversion scale on foreign direct interest in Africa. This conclusion implies that, contrary to popular belief, the exchange rate has a significant role in determining foreign direct investment in Africa. Whilst macroeconomic stability has been long held to be a critical cause of investment levels, the current study has shown that the volatility of the exchange significantly affects how much money is invested in Africa. The ramifications are that the enthusiasm for the African nations' homegrown monetary forms does impact the inflows of direct foreign

speculation. The outcomes of the study supported the discoveries of Ahmed et al. (2005), Appiah-Kubi et al. (2019), Agyemang et al. (2019).

### **Gross Domestic Product (GDP) and Foreign Direct Investment (FDI)**

Gross domestic product (GDP) had a strong and positive significant impact on foreign direct investment, as presented in the results from all of them models 1-13 and in Table 5 and Table 6. Increased gross domestic product (GDP) in African countries has a 1% impact on foreign investment decisions, given the strong and positive correlation between gross domestic product (GDP) and inflows of foreign direct investment. The coefficient of 0.000191 (Model 2) demonstrates that an improvement in a country's gross domestic product (GDP) can result in an increase in foreign direct investment in African economies of 0.000191 units. The effect of GDP on the inflows of foreign direct interest in Africa was viewed as sure and huge at 1% in all the models. GDP is calculated as the total gross value created by all producers who are residents of the economy, plus any applicable product taxes minus any unaccounted-for subsidies (IMF, 2021).

It is estimated without considering the deterioration and depletion of natural resources or the depreciation of manufactured assets. The gross domestic product gives signals to prospective investors about the viability of an economy such that a higher gross domestic product means the high productive capacity of a country; hence investment activities are likely to surge or increase. These findings suggest that international companies consider African countries with greater GDP to be reasonable for speculating, implying that Africa has a huge market potential for attracting FDI. This is predictable with the examinations by Asiedu, 2003; Schneider and Frey, 1985; Naude and Krugell, 2003; Blomstrom and Kokko, 2003; Bevan and Estrin, 2002; Borensztein et al., 1998; Malec et al. (2016) and Appiah-Kubi et al. (2020).

### **Trade Openness (TRADOP) and Foreign Direct Investment (FDI)**

Furthermore, trade openness (TRADOP) had a strong and positive significant impact on foreign direct investment, as presented in the results from all of them models 1-13 and in Table 5 and Table 6. Increased trade openness (TRADOP) in African countries has a 1% impact on foreign investment decisions, given the strong and positive correlation between trade openness (TRADOP) and inflows of foreign direct investment. The coefficient of 0.0336 (Model 9) demonstrates that an improvement in a country's trade openness (TRADOP) can result in an increase in foreign direct investment in African economies of 0.0336 units. The OECD (2008)

defines trade openness as the amount of a country's total exports and total imports as a percentage of its GDP.

The impact of capital constraints is determined by the kind of twists they introduce (Asiedu & Lien, 2004). In the development of foreign capital, exchange receptiveness plays a crucial role (Asiedu, 2002; Lane & Milesi-Ferretti, 2003). This is because the rising hunger of worldwide financial backers suggests that financial backers who centre around direct creation might participate in trade-situated exercises and consequently may not exclusively be keen on the neighbourhood market yet in addition to the global market. The outcomes uncovered a positive coefficient and consequential relationship with the inflows of FDI in Africa in all the models. The ramifications are that an open economy does guarantee to tempt the inflows of foreign speculation. The outcomes of the study were supported by prior investigations by Aseidu (2002), Nnadozie and Osili (2004), and Kucera et al. (2017).

### **Physical Infrastructure (INFRAS) and Foreign Direct Investment (FDI)**

Moreover, physical infrastructure (INFRAS) had a strong and positive significant impact on foreign direct investment, as presented in the results from all of them models 1-13 in Table 5 and Table 6. Increased physical infrastructure (INFRAS) in African countries has a 1% impact on foreign investment decisions, given the strong and positive correlation between physical infrastructure (INFRAS) and inflows of foreign direct investment. The coefficient of 0.0292 (Model 2) demonstrates that an improvement in a country's gross domestic product (GDP) can result in an increase in foreign direct investment in African economies of 0.0292 units. Fixed telephone subscription was used as a proxy for physical infrastructure. The total number of active analogue fixed telephone lines, voice-over-IP (VoIP) subscriptions, fixed wireless local loop (WLL) subscriptions, ISDN voice-channel equivalents, and fixed public payphone subscriptions is referred to as fixed telephone subscriptions (WTU, 2021).

As per Suh and Boggs (2011), during the most recent twenty years, the world has seen sensational innovative changes. The development in media transmission and the boundless web use are not many yet a portion of the progressions that have happened worldwide lately. Various studies compared the number of phone/cell phone users per 1000 people in a country to an intermediary foundation (Agbloyor, 2011; Suh & Boggs, 2011; Agbloyor et al., 2013). The physical underpinnings of African economies showed a favourable and measurably critical association with inflows of foreign direct investment. This means that African countries with a greater variety of suitable infrastructures are more likely to influence the decisions of foreign

financial backers since better infrastructures would aid their tasks in achieving the optimal level of effectiveness (Musila & Sigue, 2006). The study's findings agreed with those of prior research by Choi (2003), Zekos (2005), and Ko (2007).

### **Human Development Index (HDI) and Foreign Direct Investment (FDI)**

Finally, based on the models from 2-7 results in Table 7 and models from 9-13 in Table 6, it can be shown that the human development index (HDI) and the influx of foreign direct investment into African nations had an insignificant correlation with the exception models 10 and 11 which revealed a negative and significant relationship between human development index (HDI) and foreign direct investment. The negative and insignificant human development index (HDI) coefficients in models 2,3,4,5,6,7,9, 12 and 13 are a strong indicator that foreign direct investment in African economies with a stable human development index (HDI) isn't essential. According to the models 10 and 11 results, the human development index (HDI) significantly decreases foreign direct investment at the 5 % and 10 % levels of significance. The coefficient of 1.606 (Model 10) shows that a unit increase in the human development index (HDI) of African economies can lead to a 1.606 unit decrease in foreign direct investment.

According to the HDR (2015), the well-being aspect is determined by the future when they enter the world, the training aspect is determined by the average of long stretches of tutoring for adults aged 25 and up, and the sky is the limit from there and expected long stretches of tutoring for school-aged children. Gross public pay per capita is used to measure the quality of living. This infers those foreign financial backers are not impacted by the human improvement list in a country as far as the well-being, instructive level, and the normal pay of the populace. The outcomes of the study were supported by earlier studies by Musila & Sigue (2006) and Appiah-Kubi et al. (2021).

### **Diagnostics of Results**

The study examined autocorrelation and the legitimacy of the instruments used in the assessment to ensure the precision of the system Generalised Methods of Moments (GMM). The Wald Chi-squared and F-measurements for each regression are enormous at 1 per cent, indicating the significance of the illustrated variables cooperating. The Autocorrelation test is based on the incorrect assumption that the data set has no autocorrelation. Most critically, the study carried out a similar test on the AR (2) process, which is moderately dependable and fit for identifying autocorrelation at levels. The AR (2) test brings about the results of all the

models from 1 to 13 in Tables 5 and 6 showed insignificant p-values. The p-values of the AR (2) of the models are 0.904 (model 1), 0.807 (model 2), 0.808 (model 3), 0.807 (model 4), 0.807 (model 5), 0.809 (model 6), 0.901 (model 7), 0.908 (model 8), 0.901 (model 9), 0.808 (model 10), 0.907 (model 11), 0.902 (model 12), 0.807 (model 13). Since all the p-values are higher than the standard 0.05 benchmark, the study neglect to dismiss the invalid speculation of no autocorrelation Arellano & Bover (1995); Blundell & Bond (1998).

As a result, the study may assume that the Generalised System Method of Moments (GMM) assessment model has no autocorrelation, so the assessor is productive. Sargan's test is also used to examine the validity of the instruments used in the Generalised System Method of Moments (GMM) evaluation. The test is based on the erroneous assumption that the over-identification limitations are legal. The results of the Sargan X2 p-values of all the models 1-13 in Table 5 and Table 6 were insignificant because they were higher than 0.05. The p-values of Sargan X2 of the models are 0.320 (model 1), 0.0301 (model 2), 0.417 (model 3), 0.321 (model 4), 0.381 (model 5), 0.439 (model 6), 0.286 (model 7), 0.241 (model 8), 0.286 (model 9), 0.349 (model 10), 0.416 (model 11), 0.395 (model 12), 0.807 (model 13). As a result, the study failed to dismiss the flawed hypothesis and conclude that the over-identification limitations are justified. The results imply that the instruments used in the Generalised System Method of Moments (GMM) evaluation are significant and that the instruments as a group are exogenous. In addition to this, the research also employed the addition of some variables to assess the sensitivity of the results and robustness of the results. Other control variables, such as total oil rents as a percentage of GDP, mineral rents as a percentage of GDP, and natural resource rent, were included in the baseline specifications to see if the results of the study would stay the same. The two robustness checks' findings, which are shown in Tables 7 and 8 of Appendix 2, are quite comparable to those in Tables 5 and 6.

## **Summary of Chapter**

This part of the review investigates the panel dataset of 45 African nations to discover the effect of governance structures and tax incentives on the inflows of foreign direct interest in the African district from 2000 through 2020. I likewise introduced and talked about the aftereffects of the data analysis to give importance to the outcomes and work with the comparison with other related writing. In my journey to explore the effect of governance structures and tax incentives on FDI in Africa, the review dissected the dataset by utilizing the System Generalized Method of Moments dynamic panel assessment model.

The consequences of the system GMM model propose that government effectiveness, political stability, regulatory quality, control of corruption, voice and accountability, lower corporate tax, tax holidays, tax withholdings, tax concession, exchange rate, gross domestic product, trade openness, physical infrastructure affect the inflows of FDI in African economies. Moreover, the review results uncovered that rule of law, inflation, and human improvement records did not affect the inflows of FDI in Africa.

# CONCLUSIONS

## Summary

This research primarily focuses on the impact of governance frameworks and tax incentives on foreign direct investment inflows in the African region, using a sample of 45 countries from 2000 to 2020. Past FDI streams, government effectiveness, political stability, regulatory quality, the rule of law, control of corruption, voice, and accountability, corporate tax rate, tax holidays, tax withholding, and tax concessions were among the independent variables used to achieve the goals of laying out the effect of governance structures and tax incentives on the inflows of foreign direct investment into Africa. The estimated control variables included inflation, exchange rate, gross domestic product, trade openness, physical infrastructure, and human development index. The study assessed the pattern of FDI inflows with variables regression utilizing the Generalized system Method of Moments dynamic panel models. The review got to whether hypothetical proclamation that governance structures and tax incentives affect by bolstering or refuting previous investigations in this line of thought, the study can determine whether FDI inflows are actual or not.

Foreign direct investment is undeniably essential to many countries' improved economic models. Regardless, Africa has seen little growth in foreign direct investment throughout the years. Many studies have investigated the factors that influence foreign direct investment into African economies in this regard. A portion of the variables/determinant examinations incorporates the average assets, framework, and human resources as determinants of FDI in Africa. (Aseidu, 2002; Dupasquier and Osakwe, 2005). Cavallari and D'Addona (2011) additionally contemplated the worldwide and different factors, for example, profit from an investment, gross domestic product, and expansion rates of the only nations. In conclusion, financial factors, for example, the host economy's conversion scale, loan cost, and transparency (Nnadozie & Osili, 2004; Aseidu, 2002; Udoh E. furthermore, Egwaikhide F. O. 2008). Considering these factors, the study aimed to determine the impact of governance frameworks and tax incentives on FDI inflows to Africa. In light of the findings, the review reached the following conclusions.:

First, there is a clear relationship between previous foreign direct investment flows (lag of FDI) and foreign direct investment in African economies. This implies and supports several claims that a country's speculating climate is critical in ensuring high levels of future investment (Agyemang et al., 2019). A favourable and inviting business environment combined with the accomplishment of the expected return will encourage foreign direct investment development.



This might mirror a propensity arrangement impact as foreign owners gain insight into portfolio speculation activities. Simultaneously, foreign direct investment may improve the host country's macroeconomic situation, resulting in more portfolio speculation. Also, the study shows that the clear significant relationship between government effectiveness (GOVEF) and foreign direct investment in African economies means that a critical factor towards the influx of foreign direct investment into African nations is the efficacy of the government. In this regard, the analyzed African countries with sound and persuasive state-run administrations played a crucial role in convincing foreign owners to put their faith in their economies.

Similarly, tax withholding (TAXW) exhibited a significant positive link with foreign direct investment inflows into African economies. This implies that African countries should treat critical sectors predicted to create to benefit the entire economy, as it is a significant factor influencing foreign companies' investment decisions. In addition, voice and accountability (VOA) significantly positively affect foreign direct investment in African economies. One of the mainstays of governance and democracy is accountability, which drives the state and its institutions, the public sector, and civil society to work toward specific goals and outcomes, achieve their objectives, and develop compelling strategies through solid monitoring and reporting mechanisms (OECD, 2008). Voice accountability significantly impacts multinational businesses' market power and the inflow of foreign capital into African economies. The study's findings revealed that African countries' degree of voice and accountability has a bearing on foreign direct investment. UNECA (2016) identified voice and accountability as a strong pillar of a majority-rule government, in which citizens can access data and express their views on financial development and improvement.

Second, political stability (POS) had a strong positive correlation with foreign direct investment inflows into African economies. The result shows that political stability is a crucial factor influencing foreign investors' investment decisions. Many African countries face significant political risks, and FDI inflows to these countries are restricted. Lack of democracy exacerbates societal tensions, increasing the risk of a country experiencing severe political crises, and political unrest could stifle foreign direct flows to African economies. Also, the study showed that regulatory quality (REQ) and the influx of foreign companies into African nations are positively correlated. The favourable regulatory quality coefficient strongly indicates that foreign direct investment in African economies is essential. As a result, international financial backers are more confident and willing to invest in African countries that follow sound, quality norms. As a result, African countries with inadequate regulatory administration should work to reduce unnecessary burdens on foreign companies and improve

the transparency and certainty of their investments, which will impact their investment decisions. According to studies conducted by the UNECA (2016), most African countries have inadequate regulatory administration. Effective regulatory management systems would decrease unnecessary constraints on foreign corporations and increase their transparency and security, impacting their investment decisions in African economies.

Furthermore, the findings revealed a significant positive relationship between tax holidays (TAXH) and foreign direct investment inflows into African economies. In this approach, global companies are enticed and able to invest in African countries that offer the most generous tax breaks for a limited time. As a result, African countries with limited tax holidays for international organizations should try to enlarge their tax holidays, which would impact their investment decisions.

Third, the findings revealed that corruption (CORR) and foreign direct investment had a negative yet significant relationship in African countries. The result means that foreign direct investment dominates in African countries where corruption is well controlled. African countries that can reduce abuse of public power for private gain, as well as social intricacy, political and financial issues, will aid in the structure and reinforcement of their economies and will have an impact on the trust and certainty with which foreign financial backers choose to invest in their economies. Overall, effective embezzlement control is critical for reducing abuse of public power for private gain, reducing social complexity, and resolving political and financial issues that aid nations in building and enhancing their economies, trying to influence the trust and surety of international investment backers' decisions (Agyemang et al., 2019). As a result, even though the selected African countries are recognized for corruption, the extent of their corrupt practices has reached a position where overseas firms may be influenced to invest in their country (Castro et al., 2013).

Similarly, the company tax rate (CTR) had a significant but negative impact on foreign direct investment in African economies. The results mean that an increase in the corporate tax rate reduces foreign direct investment inflows into African countries. Corporate tax rates vary significantly amongst nations, with some having meagre rates and being labelled tax havens. The effective corporate tax rate, or the rate a corporation pays, is typically lower than the statutory rate, which is the declared amount before any deductions since corporate taxes can be reduced by government subsidies and tax loopholes (Kraushoff, 2013).

The results also mean that African countries should reduce corporate tax rates for foreign companies to entice them, which will increase the inflow of foreign direct investment into their economies. Investors desire fair treatment in all sectors in resource-constrained African nations

in order to facilitate simpler diversification. In addition, tax concession (TAXC) had a substantial negative impact on foreign direct investment in African economies. The coefficient of tax concession demonstrated that, while the link between tax concession and foreign direct speculation inflow is negative, it is also significant. To encourage investment, exemptions from import-related customs and taxes may also be granted. These exemptions may apply to other imported items for statutory, civic, or charitable organizations (Goyal & Chai, 2008). It is a question of whether state administrations are specific in their arrangements for granting rights or whether rights are granted in all cases. The findings show that economies with tax concession attract foreign direct investment into African nations.

Fourth, the study revealed that the rule of law (ROL) had a positive but insignificant link between the rule of law and the inflows of foreign direct investment into African countries. According to Kaufmann et al. (2008), the rule of law refers to how citizens engage with the institutions that help to govern those relationships. The prevalence of foreign possession in African nations does not incredibly rely upon the particular country's moral lead, respectability, trustworthiness, and political and authoritative direction regarding the rule of law. The results mean that institutions such as the judiciary that exhibit fairness and efficiency in their delivery do not play an essential role in facilitating or limiting government power to interfere in business activities and the market situation and unbiased enforcement of contracts for foreign investments.

Lastly, regarding the control variables, Inflation (INFL) and foreign direct investment into African nations have a positive but minor link, according to the study's inflation (INFL) coefficient. The insignificant relationship suggests that expansion as a proportion of macroeconomic stability contrarily impacts the inflows of FDI in Africa. Aside from the reason provided, the prices of goods and services increase during inflationary periods, causing demand for goods and services to fall. Similarly, the human development index (HDI) and the influx of foreign direct investment into African nations had an insignificant correlation. According to the Human Development Report (2015), the well-being aspect is determined by the future when they enter the world, the training aspect is determined by the average of long stretches of tutoring for adults aged 25 and up, and beyond that, the sky is the limit expected long stretches of tutoring for school-aged children. The results infer those foreign investors are not impacted by the human improvement index of African economies. Also, the study revealed that the exchange rate (EXCHR) and the influx of foreign direct investment into African nations are strongly negatively correlated. This suggests that the exchange rate does affect the levels of

foreign investment in Africa. This result implies that the exchange rate is a critical determinant of foreign direct investment in Africa, as commonly perceived.

Whilst macroeconomic stability has long been held to be the critical cause of investment levels, and the current study has shown that the volatility of the exchange significantly impacts the level of investment in Africa. The ramifications are that the enthusiasm for the African nations' homegrown monetary forms does impact the inflows of direct foreign speculation. Gross domestic product (GDP) had a substantial and positive significant impact on foreign direct investment in the African economies. The gross domestic product signals prospective investors the viability of an economy such that a higher gross domestic product means a high productive capacity of a country; hence investment activities are likely to surge or increase. This study revealed that international companies consider African countries with greater GDP reasonable for speculating, implying that Africa has a vast market potential for attracting FDI.

Similarly, trade openness (TRADOP) had a substantial and positive significant impact on foreign direct investment in African economies. This is because the rising hunger of worldwide financial backers suggests that foreign owners who centre around direct creation might participate in trade-situated exercises and may not exclusively be keen on the neighbourhood market yet in addition to the global market. The implications are that an open economy does not ensure that foreign direct investment will be enticed to flow into African countries. In addition to this, physical infrastructure (INFRAS) had a substantial and positive significant impact on foreign direct investment in African economies. The development in media transmission and the boundless web use are not many yet a portion of the progressions that have happened worldwide lately. The physical underpinnings of African economies showed a favourable and measurably critical association with foreign direct investment inflows. The results mean that African countries with a greater variety of suitable infrastructures are more likely to influence the decisions of foreign direct investment since better infrastructures would aid their tasks in achieving the optimal level of effectiveness.

## **Contributions and Implications**

This study sought to determine how foreign direct investment in African nations is impacted by governance structures and tax incentives. The one-of-a-kind element of this review from other writing on the African district is that the review covers periods previously, during, and after the monetary emergencies in 2008. Furthermore, the exact writing on Africa zeroed in on the macroeconomic and financial variables, for example, GDP, expansion, conversion

standard, loan fee, joblessness, and numerous others (Asiedu, 2006; Fahad & Ahmed, 2016; Okafor et al., 2017). This study adds to the writing by the consideration of governance structures and tax incentives in my model and the foundation of the long-run connection between governance structures and FDI inflows to Africa. The system chose the Generalized Method of Moment because of its relative advantages over other approaches, such as ordinary least squares (OLS).

If the regressors are endogenous, the essential aftereffect of this thesis is high conviction affirmation through the receipt of the Generalized Moment Method (GMM), which overcomes the inclinations and irregularities of the Ordinary Least Squares (OLS) technique. This concentration additionally gives another commitment to the current writing by zeroing in on the effect of governance structures and tax incentives on the inflows of foreign direct investment in Africa.

## **Limitations and Recommendations for Future Research**

The discoveries from the analysis of the review achieve extremely intriguing suggestions for both policymakers and different researchers who might need to concentrate on this field from now on. These proposals are examined underneath:

1. First, African nations ought to embrace hearty and strong measures, reinforce their approaches and organizations to advance control of corruption, give quality guidelines, and limit political viciousness and instability.

2. Second, for African countries to benefit more financially from foreign direct investment, a complete overhaul of Africa's tax incentives plans for foreign direct investment is required. African countries must replace their current specially designed programs with a far-reaching monetary system that is aligned with their country's development goals.

3. Third, African countries should upgrade their framework improvements, use their normal assets successfully, and take on fair and open laws in light of compelling money-related strategies, taxation, and global exchange to bait foreign interests into their economies.

4. Moreover, without legitimate execution, even all that tax motivator strategy can deliver awful outcomes. Accordingly, African economies ought to embrace a comprehensive and complex administration approach enveloping execution, showcasing, organization, and assessment. Accordingly, these methodologies positively would assist with mitigating Africa's advancement battle for monetary inspiring and reasonable financial turn of events.

5. Lastly, African nations ought to partake in worldwide monetary gatherings where foreign financial backers' specialists would impart their insights with regard to the elements that impact their venture choices. African countries should eliminate optional incentives that are granted without transparency in favour of tax incentives that are not separated. A tax incentive framework should be clear and simple, time-bound, and consistent with the nation's benefits. This would assist African countries in achieving the Millennium Development Goals of eradicating poverty by 2025 (MDGs).

Future investigations on African nations with information accessibility can break the informational index into nations whose centre is the effect of governance structures and tax incentives on foreign direct ventures. Likewise future scientists may likewise take a gander at various channels which can affect FDI in Africa, like industrialization, monetary turn of events, and normal assets, by growing my models.

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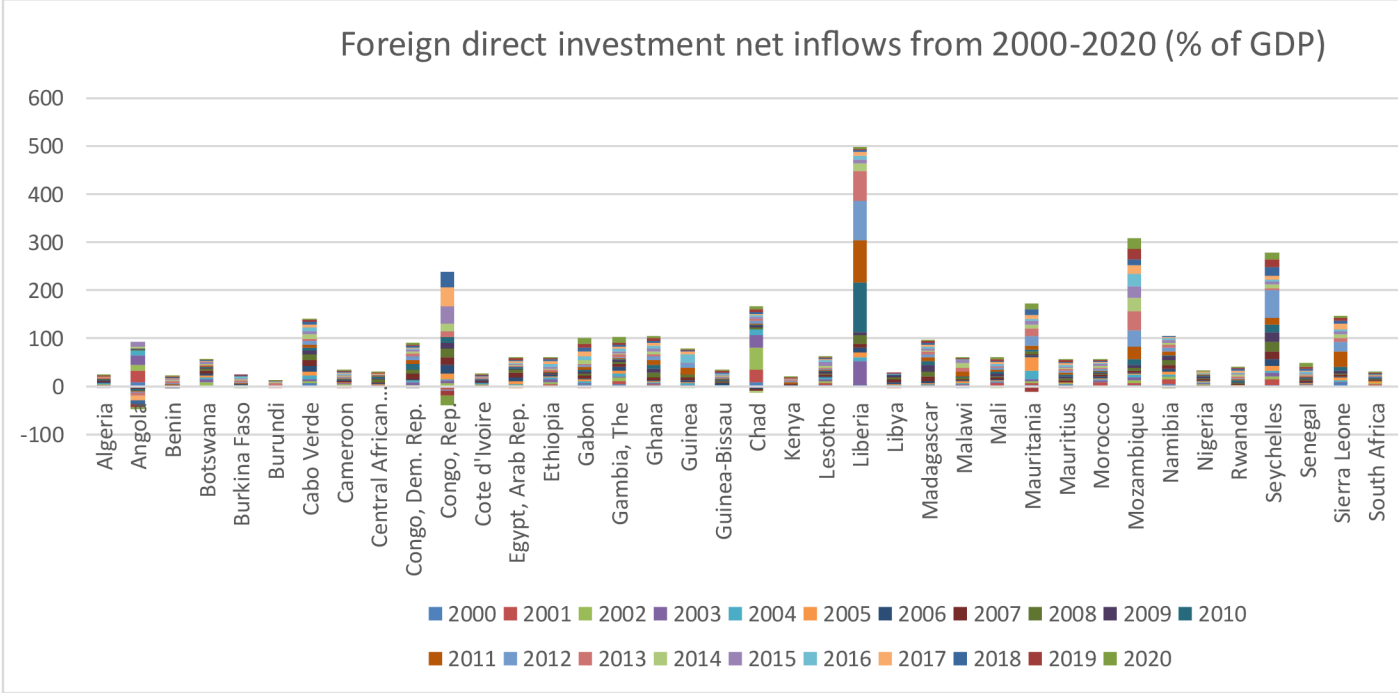
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# APPENDICES

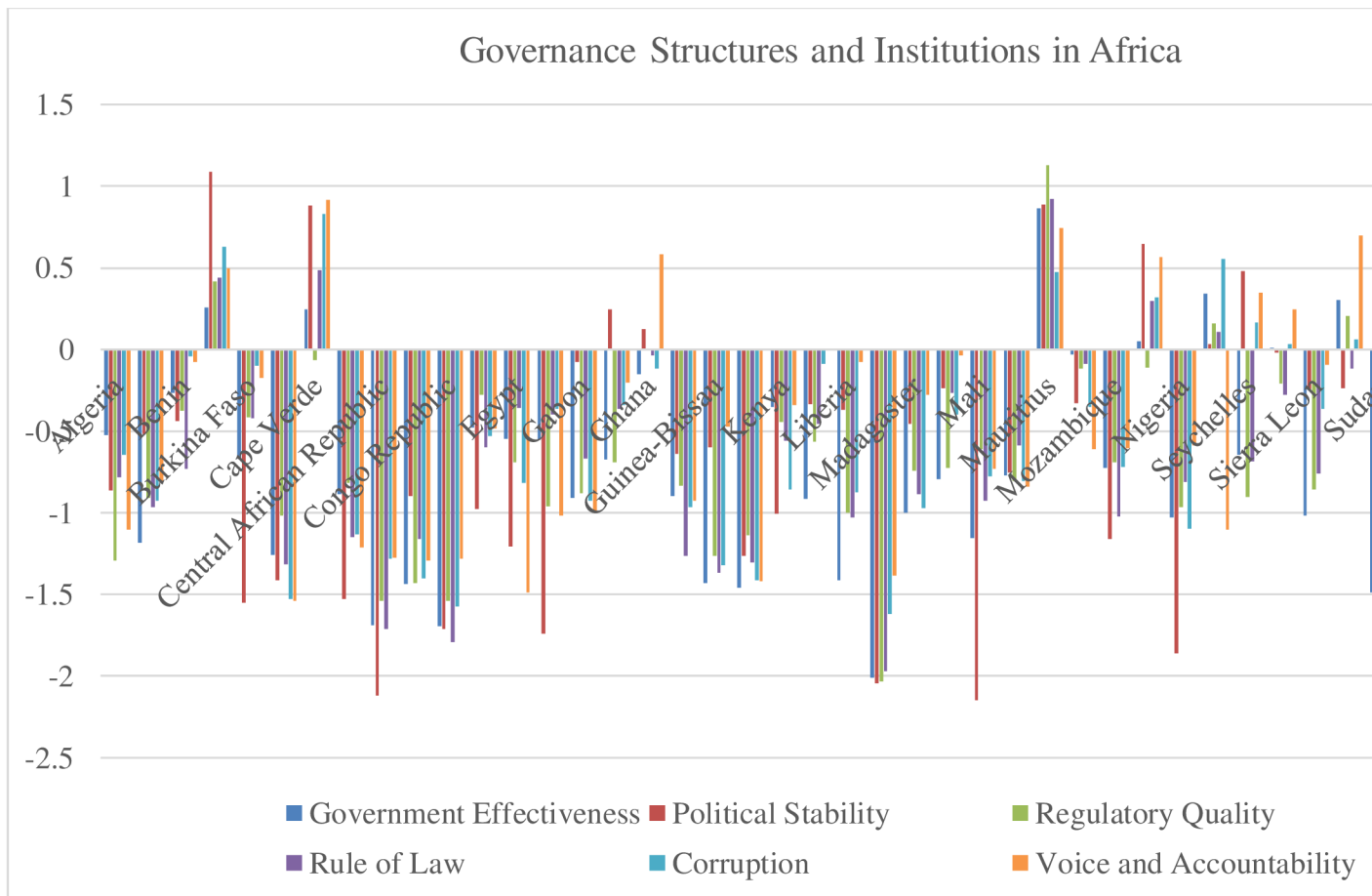
## Appendix 1 – Governance Structures, Tax Incentives and FDI inflows to Selected 45 Countries to Africa

**Figure 3: African countries' foreign direct investment net inflows from 2000-2020 (% of GDP)**



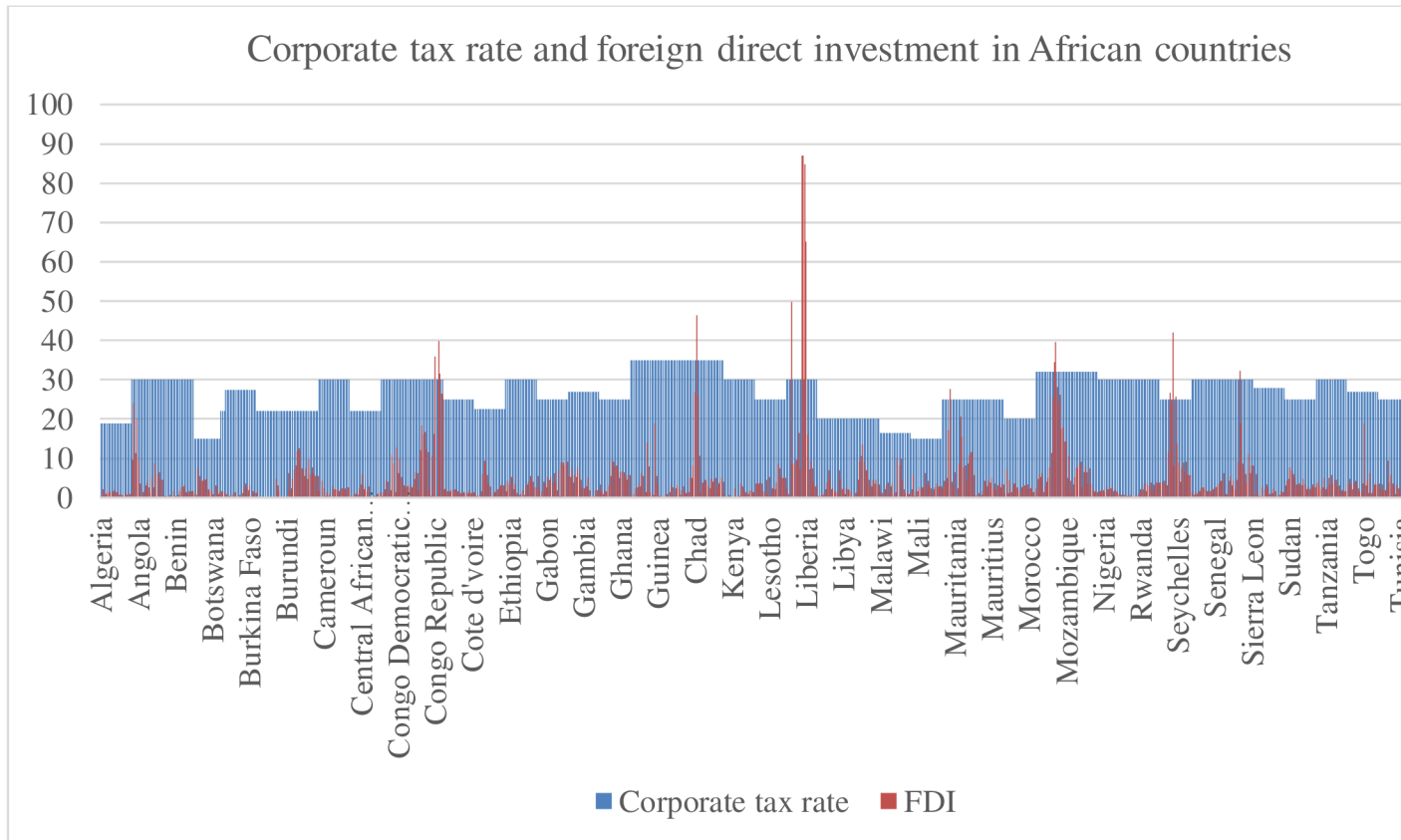
Source: Researcher’s computation via data from World Bank World Development Indicators from 2021.

**Figure 2: African countries' governance structures and institutions in 2020**



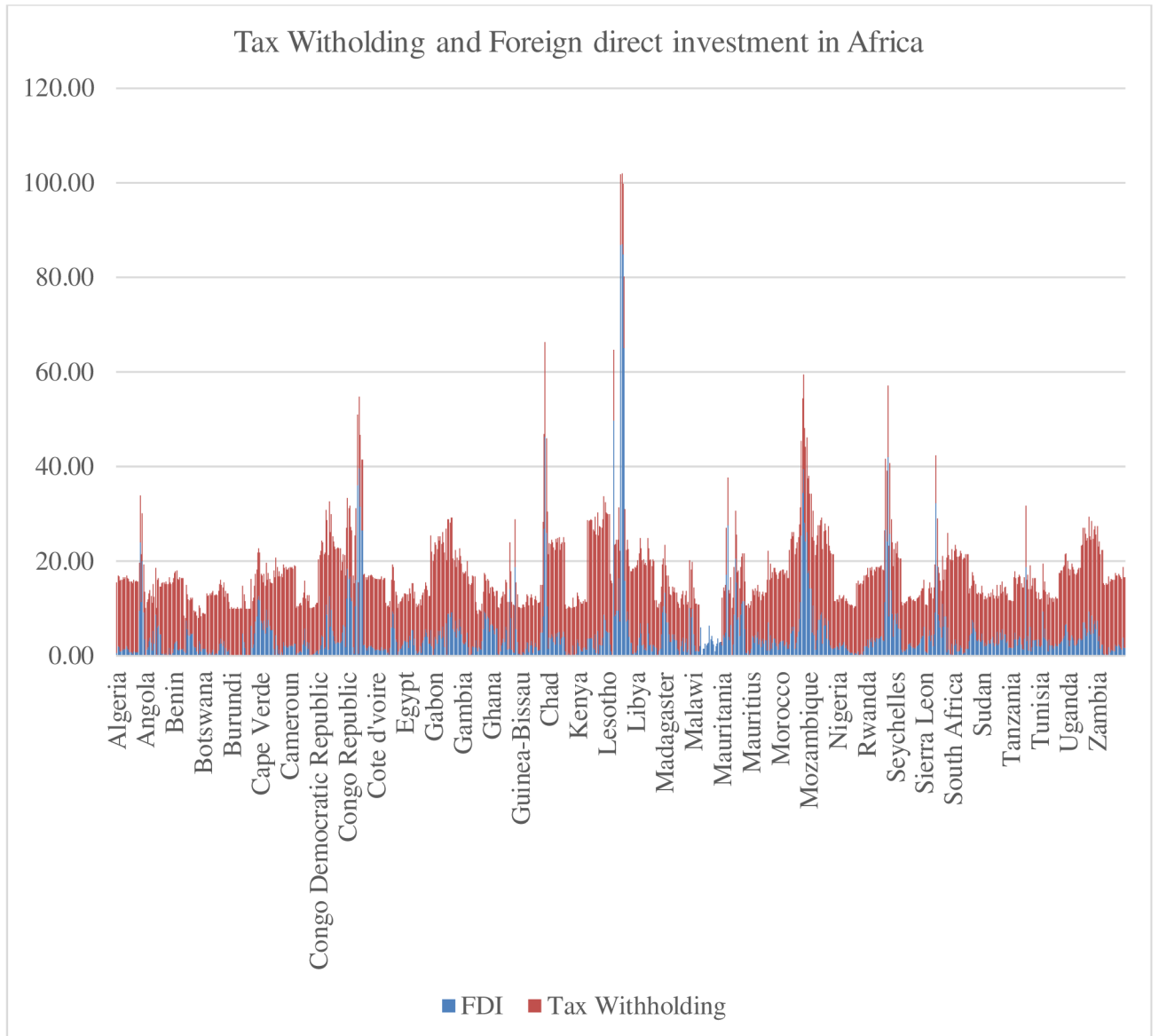
Source: Researcher's computation via data from World Development Indicators, 2021.

**Figure 3: African countries corporate tax rate and foreign direct investment net inflows from 2000-2020 (% of GDP)**



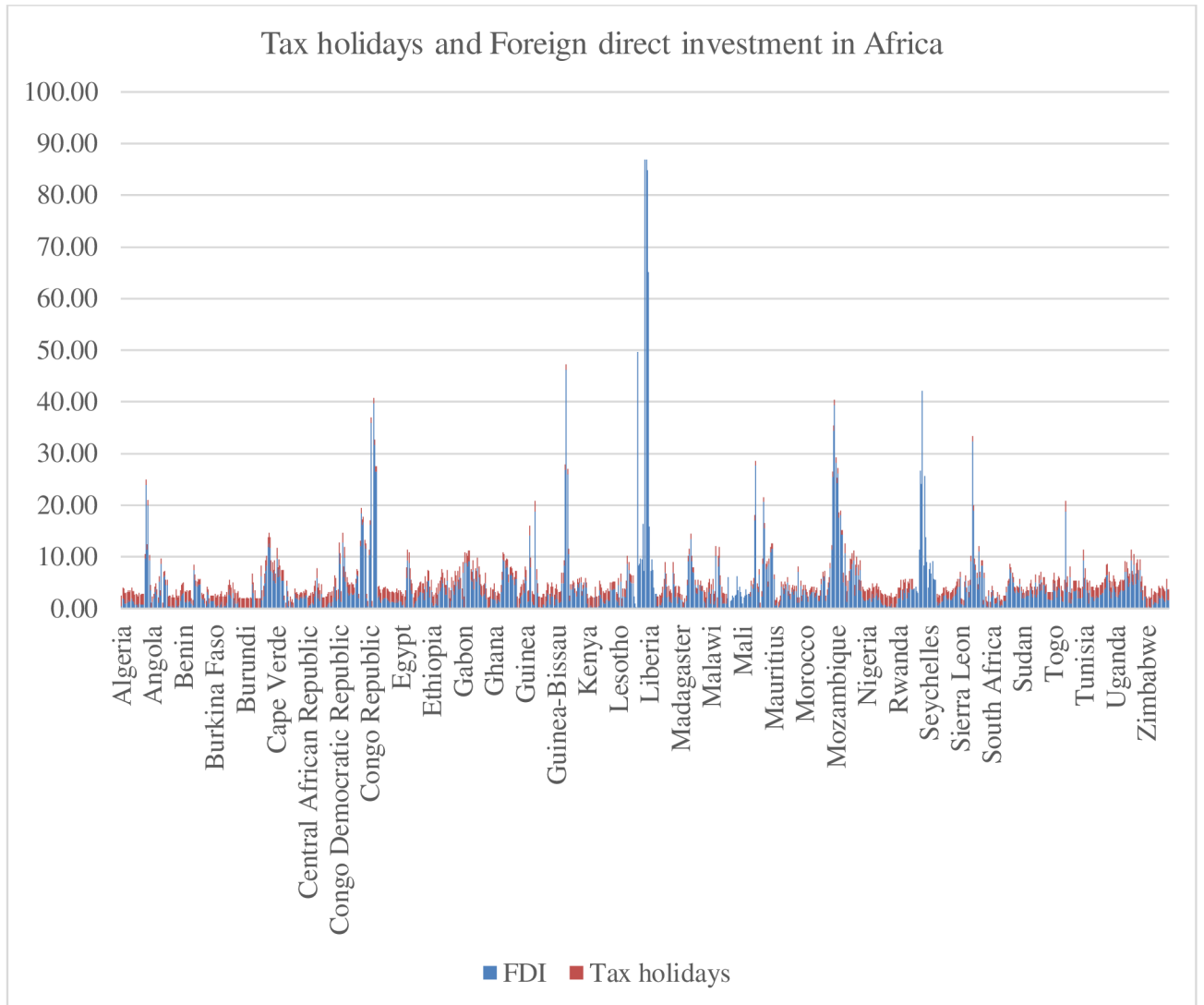
Source: Researcher's computation via data from World Development Indicators and Price Waterhouse Coopers Global, 2021

**Figure 4: African countries withholding tax and foreign direct investment net inflows from 2000-2020 (% of GDP)**



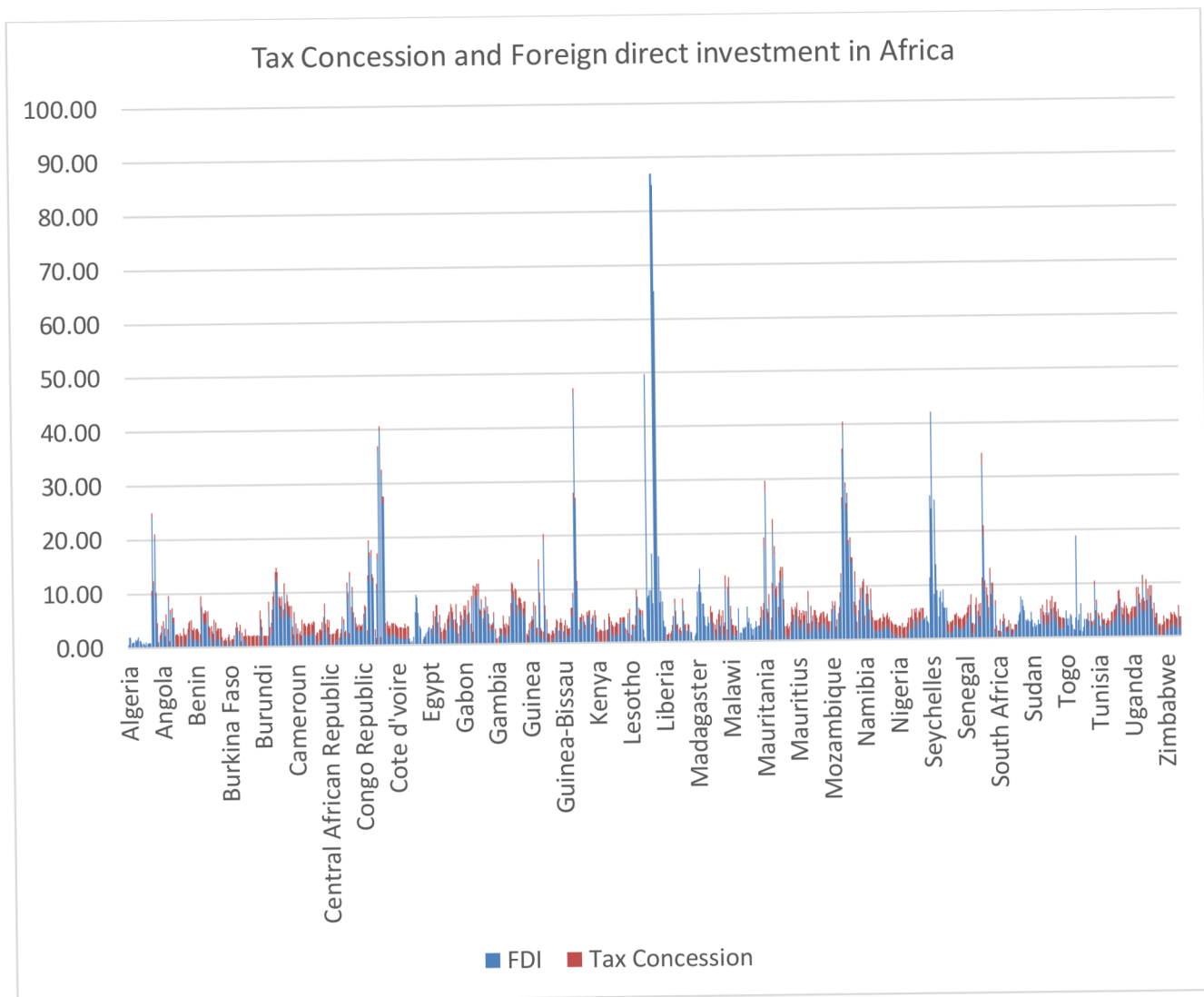
Source: Researcher's computation via data from World Development Indicators and Price Waterhouse Coopers Global, 2021

**Figure 5: African countries tax holidays and foreign direct investment net inflows from 2000-2020 (% of GDP)**



Source: Researcher's computation via data from World Development Indicators and Price Waterhouse Coopers Global, 2021

**Figure 6: African countries tax concession and foreign direct investment net inflows from 2000-2020 (% of GDP)**



Source: Researcher's computation via data from World Development Indicators and Price Waterhouse Coopers Global, 2021



## Appendix 2 – The Basic Model Estimation Results

### Matrix Correlations

**Table 6: Correlation Matrix of Foreign Direct Investment and Governance Structures**

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)
FDI	1.000						
GOVEF	0.044	1.000					
POS	-0.021	0.610	1.000				
REQ	-0.082	0.744	0.805	1.000			
RUL	0.040	0.682	0.716	0.758	1.000		
CORR	-0.106	0.656	0.817	0.871	0.709	1.000	
VOA	-0.029	0.687	0.791	0.825	0.732	0.866	1.000

Source: Author's computations based on data retrieved from sources mentioned in the text, 2022

**Table 7: Correlation Matrix of Foreign Direct Investment and Tax Incentives**

Variables	(1)	(2)	(3)	(4)	(5)
FDI	1.000				
CTR	0.143	1.000			
TAXW	0.114	0.355	1.000		
TAXH	-0.335	0.115	0.139	1.000	
TAXC	-0.191	0.166	-0.012	0.405	1.000

Source: Author's computations based on data retrieved from sources mentioned in the text, 2022.

**Table 8: Correlation Matrix of Foreign Direct Investment and All Variables**

VARIABLES	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
FDI	1.000																
GOVEF	0.044	1.000															
POS	-0.021	0.610	1.000														
REQ	-0.082	0.744	0.805	1.000													
ROL	0.040	0.682	0.716	0.758	1.000												
CORR	-0.106	0.656	0.817	0.871	0.709	1.000											
VOA	-0.029	0.687	0.791	0.825	0.732	0.866	1.000										
CTR	0.143	-0.136	-0.051	-0.203	-0.111	-0.220	-0.151	1.000									
TAXW	0.114	0.123	-0.105	-0.084	-0.098	-0.088	-0.020	0.355	1.000								
TAXH	-0.335	-0.127	-0.103	-0.063	-0.263	0.036	-0.078	0.115	0.139	1.000							
TAXC	-0.191	0.162	0.217	0.208	0.133	0.245	0.191	0.166	-0.012	0.405	1.000						

INFL	0.038	- 0.125	- 0.151	- 0.147	- 0.122	- 0.123	- 0.140	0.072	- 0.001	- 0.018	- 0.065	1.000					
EXCHR	- 0.026	0.152	0.094	0.123	0.076	0.156	0.136	- 0.108	0.083	0.056	0.040	- 0.047	1.000				
GDP	0.015	0.325	0.202	0.254	0.281	0.300	0.288	- 0.252	0.083	- 0.268	- 0.204	- 0.034	0.378	1.000			
TRADOP	0.289	0.252	0.151	0.147	0.254	0.143	0.206	- 0.087	0.250	- 0.252	- 0.068	- 0.011	0.109	0.174	1.000		
INFRAS	- 0.075	0.396	0.402	0.485	0.353	0.548	0.415	- 0.304	- 0.022	- 0.008	- 0.000	- 0.083	0.438	0.626	0.276	1.000	
HDI	- 0.006	0.413	0.357	0.413	0.353	0.452	0.382	- 0.305	0.105	- 0.066	- 0.104	- 0.109	0.358	0.757	0.240	0.675	1.000

Source: Author's computations based on data retrieved from sources mentioned in the text, 2022

**Table 9: Robustness Check 1**

	(1)	(2)	(3)	(4)	(5)	(6)
Lag of FDI	0.690***	0.681***	0.686***	0.682***	0.682***	0.687***
	(0.00785)	(0.00560)	(0.00679)	(0.00686)	(0.00582)	(0.00552)
GOVEF	0.639***					
	(0.0625)					
POS		0.402***				
		(0.0618)				
REQ			0.318***			
			(0.112)			
ROL				0.140***		
				(0.0505)		
CORR					0.160**	
					(0.0744)	
VOA						0.267**
						(0.106)
INFL	0.00838***	0.00724***	0.00675**	0.00836***	0.00661**	0.00693**
	(0.00304)	(0.00280)	(0.00301)	(0.00317)	(0.00290)	(0.00286)
EXCHR	0.0000145**	0.0000258**	0.0000142	0.0000216*	0.0000177**	0.0000164
	(0.00000705)	(0.00000788)	(0.00000894)	(0.0000114)	(0.00000831)	(0.0000103)
GDP	0.0000923**	0.000124***	0.0000954**	0.0000943**	0.000105***	0.000100***
	(0.0000216)	(0.0000191)	(0.0000190)	(0.0000266)	(0.0000212)	(0.0000197)
TRADOP	-0.00226	0.00225	0.00144	0.00153	0.00222	0.000681
	(0.00177)	(0.00201)	(0.00201)	(0.00190)	(0.00198)	(0.00176)
INFRAS	-0.0641***	-0.0778***	-0.0703***	-0.0621***	-0.0671***	-0.0639***

	(0.0101)	(0.00725)	(0.00794)	(0.00734)	(0.00780)	(0.0105)
HDI	-2.325***	-1.805**	-0.911	-1.037	-1.243	-1.521
	(0.732)	(0.729)	(0.642)	(0.998)	(0.884)	(1.081)
MRENT	0.118***	0.129***	0.124***	0.125***	0.126***	0.126***
	(0.0123)	(0.0152)	(0.0126)	(0.0119)	(0.0127)	(0.0122)
ORENT	0.00763*	-0.00200	0.000792	-0.00120	-0.00338	-0.00123
	(0.00419)	(0.00326)	(0.00434)	(0.00478)	(0.00378)	(0.00373)
NAGAS	0.839***	0.879***	0.801***	0.708***	0.823***	0.874***
	(0.137)	(0.129)	(0.115)	(0.0895)	(0.128)	(0.166)
_cons	2.507***	1.913***	1.496***	1.415***	1.538***	1.776***
	(0.304)	(0.347)	(0.264)	(0.435)	(0.412)	(0.616)
No. of obs.	944	944	944	944	944	944
No. of Inst.	55	55	55	55	55	55
Prob > chi2	0.000	0.000	0.000	0.000	0.000	0.000
AR(2): Z (p-value)	1.80 (0.701)	1.80 (0.702)	1.81 (0.701)	1.81 (0.70)	1.81 (0.701)	1.81 (0.701)
Hansen J: (p-value)	31.21 (0.909)	34.37 (0.823)	35.69 (0.783)	31.18 (0.757)	35.56 (0.710)	35.06 (0.773)
SarganX <sup>2</sup> (p-value)	30.64 (0.882)	34.53 (0.725)	35.69 (0.705)	30.92 (0.321)	34.90 (0.806)	35.32 (0.791)

The values in parentheses are p-values; values denoted by \*\*\*, \*\*, and \* represent 1%, 5%, and 10% significant levels respectively. FDI represents foreign direct investment. CORR represents control of corruption. GOVEF represents government effectiveness, POS represents political stability, ROL represents rule of law, REQ represents regulatory quality. VOA represents voice and accountability. INFL represents inflation. EXCHR represents exchange rate. GDP represents gross domestic product. TRADOP represents trade openness. INFRAS represent infrastructure. HDI represents human development index. MRENT represents mineral rent. ORENT represents oil rent. NAGAS represents natural gas. The insignificant probability (J-stats) value suggested that there is no overriding identity, and the instruments adopted are efficient and do not correlate with the error term. Source: Researcher's own calculation, 2022.

**Table 10: Robustness Check Model 2**

	(1)	(2)	(3)	(4)
Lag of FDI	0.818***	0.835***	0.745***	0.827***
	(0.00889)	(0.00932)	(0.00886)	(0.00879)
CTR	0.0241**			
	(0.0110)			
TAXW		0.0238**		
		(0.00938)		
TAXH			-1.179***	
			(0.200)	
TAXC				-0.130
				(0.101)
INFL	-0.00176	-0.00109	-0.00200	-0.00250
	(0.00392)	(0.00388)	(0.00427)	(0.00367)
EXCHR	-0.0000246	-0.0000190	0.0000401	-0.0000182
	(0.0000336)	(0.0000348)	(0.0000286)	(0.0000314)
GDP	0.0000340	0.0000216	-0.000112***	0.00000312
	(0.0000371)	(0.0000310)	(0.0000412)	(0.0000315)
TRADOP	0.000483	-0.00302	0.000410	-0.00175
	(0.00279)	(0.00243)	(0.00315)	(0.00241)
INFRAS	-0.0228**	-0.0120	-0.0217	-0.0126
	(0.00917)	(0.0104)	(0.0139)	(0.0104)
HDI	0.231	0.0757	0.983	0.516
	(0.759)	(0.748)	(0.958)	(0.883)
MRENT	0.0243	0.0230	0.0587**	0.00652
	(0.0248)	(0.0264)	(0.0255)	(0.0273)
ORENT	0.00464	0.00422	0.00987	0.00606
	(0.00589)	(0.00529)	(0.00668)	(0.00592)
NAGAS	0.149	0.0752	0.232	0.0845

	(0.173)	(0.157)	(0.178)	(0.154)
_CONS	-0.204	0.355	2.434***	0.661
	(0.305)	(0.316)	(0.659)	(0.428)
No. of obs.	944	944	944	944
No. of Inst.	35	35	35	35
Prob > chi2	0.000	0.000	0.000	0.000
AR(2): Z (p-value)	1.83 (0.655)	1.83 (0.651)	1.82 (0.609)	1.83 (0.701)
Hansen J: (p-value)	17.23 (0.417)	19.66 (0.604)	16.43 (0.812)	20.62 (0.544)
SarganX2 (p-value)	84.39 (0.638)	83.47 (0.651)	76.77 (0.812)	84.14 (0.572)

The values in parentheses are p-values; values denoted by \*\*\*, \*\*, and \* represent 1%, 5%, and 10% significant levels respectively. FDI represents foreign direct investment. CORR represents control of corruption. GOVEF represents government effectiveness, POS represents political stability, ROL represents rule of law, REQ represents regulatory quality. VOA represents voice and accountability. INFL represents inflation. EXCHR represents exchange rate. GDP represents gross domestic product. TRADOP represents trade openness. INFRAS represent infrastructure. HDI represents human development index. MRENT represents mineral rent. ORENT represents oil rent. NAGAS represents natural gas. The insignificant probability (J-stats) value suggested that there is no overriding identity, and the instruments adopted are efficient and do not correlate with the error term. Source: Researcher's own calculation, 2022.

### Appendix 3 – Dataset for Africa

The sampled African nations for this examine encompass Algeria, Angola, Benin, Botswana, Burkina Faso, Burundi, Cape Verde, Cameroon, Central African Republic, Congo Democratic, Republic of Congo, Chad, Cote d'Ivoire, Egypt, Ethiopia, Gabon, Gambia, Ghana, Guinea, Guinea-Bissau, Kenya, Lesotho, Liberia, Libya Madagascar, Malawi, Mali, Mauritania, Mauritius, Morocco, Mozambique, Namibia, Nigeria, Rwanda, Sao Tome, Senegal, Sierra Leone, South Africa, Sudan, Tanzania, Togo, Tunisia, Uganda, Zambia, and Zimbabwe