

Macroeconomic Variables and Foreign Direct Investment: An Analysis of the Oil and Gas Sector in Nigeria

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ABSTRACT

Foreign direct investment (FDI) has historically been significantly influenced by Nigeria's oil and gas industry, but ongoing inflationary pressures continue to threaten the stability of investments. The overall increase in price levels, or inflation, affects macroeconomic factors including interest rates, currency rates, and investor confidence. Nigeria's inflation rate has fluctuated over time, which has affected capital inflows into important economic sectors. This study investigated the relationship between macroeconomic variables, sustainable development goals (SDGs), and foreign direct investment (FDI) in Nigeria while focusing on the oil and gas sector in Nigeria. The study specifically examined how inflation, exchange rate, global oil price, SDG goal 8 of economic growth measured by economic growth rate, and the control variable interest rate impacted FDI in Nigeria using time series data from 1990 till 2023. The study adopted the ex post facto research design and secondary data from the reports of the World Development Index, Central Bank of Nigeria, National Bureau of Statistics, and the Organization of Petroleum Exporting Countries were used in this study. The estimation techniques used in this study was the Autoregressive Distributive Lag. Findings showed that inflation, exchange rate, and the control variable interest rate had negative and significant impacts with significant probability values of 0.0138, 0.0000, and 0.0263 (lower than 0.05) while economic growth rate, global oil prices, and the second control variable sustainability index had positive and significant impacts on Nigeria's foreign direct investment with significant probability values of 0.0312, 0.0000, and 0.0334 (lower than 0.05). The study thus recommended that the Central Bank should focus more in managing inflation by controlling excess money in the economy.

Keywords: Economic Growth Rate, Exchange Rate, Foreign Direct Investment, Global Oil Prices, Inflation, Sustainability Index

INTRODUCTION

Inflation is a persistent increase in the general price level that reduces the purchasing power of money (Idisi et al., 2023). It affects production costs, the prices of raw materials and finished goods, interest rates, exchange rates, savings and investor confidence. Inflation may emerge through excess aggregate demand, rising production costs, structural constraints or excessive money-supply growth (Eke et al., 2023). In an inflationary environment, businesses face higher operating costs and uncertainty over future returns. These conditions can discourage long-term foreign investment, particularly where investors cannot reliably forecast costs, revenues and the real value of repatriated profits.

Exchange rate is the price of one currency in relation to another and is a central variable in international trade and investment (Enemuo, 2024). A stable currency supports planning and preserves investor returns, whereas persistent depreciation may increase the domestic cost of imported machinery, inputs and services. Nigeria's naira depreciated considerably over the study period, while inflation also remained volatile. This combination increased production costs, weakened purchasing power and made business projections more difficult (Ukachukwu & Odionye, 2020). Although currency depreciation may make domestic assets cheaper to foreign investors, continued and unpredictable depreciation can increase risk and deter FDI.

The investment environment is also influenced by economic growth and global oil prices. Economic growth signals market expansion, profitability and stability, which may attract foreign investors. Global oil prices affect revenue prospects, exploration and production decisions in Nigeria's oil and gas sector. Because oil is a major source of public revenue and foreign exchange, fluctuations in international prices affect sectoral output, government finance and investment conditions (Donwa et al., 2015). Furthermore, Nigeria's progress towards the Sustainable Development Goals, including Goal 8 on economic growth, provides an additional indication of the country's development environment. The sustainability index is therefore included as a control variable alongside the interest rate.

The central problem is that Nigeria's FDI growth has remained lower and more concentrated than might be expected for a resource-rich economy seeking industrialisation. The World Development Indicators reported growth in FDI from ₦5,233,188 to ₦5,544,630 between 2021 and 2023, while most inflows remained concentrated in oil and gas. Persistent inflation, naira depreciation, volatile oil prices and the challenge of sustaining economic growth raise questions about the determinants of investment inflows. Existing evidence is mixed. Some studies report that inflation discourages FDI, while others find an insignificant relationship. Many studies also examine aggregate FDI rather than sector-specific investment. This study addressed that gap by focusing on Nigeria's oil and gas sector and by jointly examining inflation, exchange rate, GDP growth rate and global oil prices, with interest rate and sustainability index as controls.

Accordingly, the study sought to determine how inflation, exchange rate, economic growth rate and global oil prices affected FDI inflows into Nigeria's oil and gas industry. The null hypotheses stated that each of these four variables had no significant effect on FDI. The study is relevant to policymakers seeking macroeconomic stability, investors assessing sectoral risk and scholars examining investment dynamics in emerging economies.

LITERATURE REVIEW

Conceptual Review

Inflation describes a sustained rise in the prices of goods and services and a corresponding decline in the purchasing power of money. Moderate inflation may accompany growth, but high and persistent inflation can cause instability (Krugman & Obstfeld, 2023). Demand-pull inflation occurs when aggregate demand exceeds supply; cost-push inflation follows increases in wages, fuel, imported inputs or other production costs; built-in inflation reflects a wage-price cycle; and monetary inflation is associated with excessive expansion of money supply. Nigeria's inflation reflects overlapping fiscal, structural, monetary and external pressures. The Consumer Price Index is the principal measure used by the National Bureau of Statistics, while the Wholesale Price Index, Producer Price Index and GDP deflator provide additional measures of price changes.

FDI is a long-term foreign investment that normally involves ownership, lasting interest or control in a host-country enterprise (Moosa, 2002). It may take the form of greenfield investment, acquisition of an existing enterprise, or a joint venture. Investors may be market-seeking, resource-seeking, efficiency-seeking, diversification-oriented or interested in strategic assets. Nigeria's large market and resource base attract both market- and resource-seeking investment, while its oil reserves have historically made the petroleum sector a major FDI destination (UNCTAD, 2023). FDI can provide capital, employment, technology transfer, infrastructure and export opportunities. Its benefits, however, may be constrained by profit repatriation, competition with domestic firms, political interference, environmental concerns, weak infrastructure, corruption and exchange-rate volatility.

Inflation and FDI are linked through purchasing power, operating costs, exchange rates and risk-return considerations. High inflation can increase input costs, reduce real profits and make future returns uncertain, thereby discouraging investment. Inflation-related depreciation may initially lower the foreign-currency price of domestic assets, but high exchange-rate volatility increases hedging costs and uncertainty. In resource-based sectors with potentially high returns, investors may continue to invest despite inflation, while industries with lower risk-adjusted returns may be more strongly discouraged (Ezeoha & Cattaneo, 2022). Interest rates

also affect the cost of finance, while economic growth influences market prospects and the sustainability index reflects progress towards the development environment associated with the SDGs.

Nigeria's oil and gas sector includes upstream exploration and production, midstream transportation and storage, and downstream refining, distribution and marketing. It is central to government revenue, foreign exchange receipts and FDI. Both indigenous and multinational companies operate in the sector. Nevertheless, investment and production are affected by volatile oil prices, regulatory uncertainty, pipeline vandalism, oil theft, infrastructure limitations, environmental concerns, inflation and exchange-rate instability (Olujobi et al., 2024). These conditions make the sector suitable for examining the interaction between macroeconomic variables and FDI.

Theoretical Review

The study was anchored principally on Purchasing Power Parity (PPP) and supported by Keynesian, monetarist, neoclassical and dependency perspectives. PPP, associated with Gustav Cassel, explains how differences in price levels affect exchange rates. A country with relatively high inflation is expected to experience currency depreciation. For Nigeria, depreciation may reduce the foreign-currency price of local assets, but persistent inflation and exchange-rate fluctuations can undermine investor confidence. Relative PPP is particularly relevant because it links changes in exchange rates to inflation differentials. The oil sector may show some resilience because international oil prices are denominated in United States dollars.

Keynesian theory explains inflation as a consequence of aggregate demand exceeding available supply and emphasises the role of demand conditions in economic activity. In Nigeria, rising government spending, urbanisation and higher production costs may contribute to inflation. Excessive inflation reduces purchasing power and makes costs and returns less predictable, thereby discouraging long-term investment. Monetarist theory, associated with Friedman (1968), attributes sustained inflation mainly to excessive money-supply growth and supports stable monetary policy as a condition for investment. The neoclassical theory holds that capital moves in response to differences in expected returns, factor costs and resource endowments. It therefore explains continued investment in Nigeria's oil and gas sector when expected returns compensate for inflation and exchange-rate risks (Popovici & Călin, 2014). Dependency theory presents a contrasting view, arguing that resource-focused FDI may reinforce external dependence through control of assets and profit repatriation rather than deliver broad diversification.

Empirical Review and Research Gap

International evidence remains mixed. Li (2006) found a nonlinear relationship between inflation and investment across developing and developed countries, with low to moderate inflation supporting investment but higher inflation reducing growth through investment efficiency. McClain and Nichols (1994) reported a positive long-run relationship between inflation and investment. In the United Arab Emirates, Alshamsi et al. (2015) found that GDP per capita positively affected FDI while inflation had no significant effect. Koojaroenprasit (2012) reported a positive effect of FDI on economic growth in South Korea, while Khamis et al. (2015) similarly found a positive relationship between GDP per capita and FDI but no significant inflation effect in the UAE.

Nigerian studies also report differing outcomes. Ehimare (2011) found that inflation had no significant direct effect on FDI, although exchange-rate movements influenced inflows. Njoku et al. (2023) identified a long-run relationship between inflation and FDI but found the effect statistically insignificant. Ukachukwu and Odionye (2020) reported that exchange rate and crude-oil prices positively and significantly affected FDI in both the short and long run, while inflation had a significant negative long-run effect. Udoh and Egwaikhide (2008) reported that exchange-rate volatility and inflation uncertainty significantly affected FDI.

The literature therefore does not provide a uniform conclusion on inflation and FDI. It also concentrates largely on aggregate investment and gives limited attention to the distinct conditions of Nigeria's capital-intensive oil and gas sector. Few studies jointly evaluate inflation, exchange rate, economic growth, global oil

prices, interest rate and sustainability performance. This study filled that gap through a sector-focused time-series analysis covering 1990–2023.

The theoretical perspectives are complementary. PPP provides the direct link between inflation and exchange-rate changes. Keynesian theory explains how excess demand and production constraints can generate inflation and reduce purchasing power. Monetarism emphasises money-supply control and the role of credible monetary policy in maintaining price stability. Neoclassical theory explains why investors compare expected returns, costs and resource advantages across locations. Dependency theory warns that resource-oriented FDI may deepen external dependence where profits are repatriated and local linkages remain limited. Together, these theories provide a basis for expecting inflation, exchange rate, economic growth, global oil prices, interest rates and sustainability conditions to influence FDI.

METHODOLOGY

The study adopted an ex post facto quantitative research design because the events had already occurred and the variables could not be manipulated. Annual time-series data for 1990–2023 were used. The data were obtained from the World Development Indicators, Central Bank of Nigeria Statistical Bulletin, National Bureau of Statistics, Organization of Petroleum Exporting Countries reports and United Nations Sustainable Development reports. The dependent variable was FDI inflow into Nigeria’s oil and gas sector. Inflation rate, exchange rate, GDP growth rate and global oil prices were the independent variables, while interest rate and sustainability index were control variables.

The model was adapted from Adeniyi (2020) and specified as:

$$FDI_t = f(INF_t, EXCR_t, GDPR_t, GOP_t, INT_t, SI_t)$$

Where

FDI_t = Total foreign direct investment in the Nigerian oil and gas sector in time t

INF_t = Inflation Rate in time t

$EXCR_t$ = Exchange rate in time t

$GDPR_t$ = Economic growth rate in time t

GOP_t = Global oil prices in time t

INT_t = Interest rate in time t

SI_t = Sustainability Index in time t

The model explicit form was:

$$FDI_t = \alpha_0 + \beta_1 INF_t + \beta_2 EXCR_t + \beta_3 GDPR_t + \beta_4 GOP_t + \beta_5 INT_t + \beta_6 SI_t + \varepsilon_t$$

Where

α_0 = Constant

$\beta_1, \beta_2, \dots, \beta_6$ = Coefficients to estimate the independent variables

ε_t = Error term

The study used the Autoregressive Distributive Lag to estimate the sourced secondary data. The technique was employed to ascertain the type of relationship that existed between FDI and all the independent variables in the model whether positive or negative. The technique also showed the nature of relationship whether significant or not.

Variable	Measurements	Types	Source
Foreign Direct Investment [FDI]	This is the term used to describe the total value of foreign direct investment inflows towards the Nigerian oil and gas industry.	Dependent variable	World Development Indicators (2024)
Inflation Rate	This is the annual percentage change in the average price of goods and services over a given time period.	Independent variable	CBN Statistical Bulletin (2024)
Exchange Rate	This is the annual average official exchange rate (for example, the Nigerian Naira to the US dollar).	Independent variable	CBN Statistical Bulletin (2024)
GDP Growth Rate	This is the annual percentage growth of the economic growth rate.	Independent variable	CBN Statistical Bulletin (2024)
Variable	Measurements	Types	Source
Global Oil Prices [GOP]	Global Oil Prices (GOP) is the annual average crude oil prices (USD per barrel) set by the market on international markets.	Independent variable	Organization of Petroleum Exporting Countries Report (2024)
Interest Rate	This is the annual monetary policy benchmark rate set by the CBN to regulate borrowing costs and control inflation.	Control variable	CBN Statistical Bulletin (2024)
Sustainability Index	This is the measurement of how Nigeria has gone so far in achieving the SDG goals	Control variable	United Nations SDG Report (2024)

The a priori expectation for the study's variables is as follows:

- Inflation would have a negative relationship with FDI. This was because Ukachukwu and Odionye (2020), opined that high inflation rates create economic uncertainty, reduce the real value of returns on investment, and discourage long-term capital inflows.
- Exchange rate fluctuations would have a negative impact on FDI. This was due to the fact that as fluctuations in the value of the Naira increase transaction costs and introduces risks for foreign investors (Aderemi et al., 2020).
- GDP growth rate is expected to have a positive relationship with FDI. This was because higher economic growth signals market stability and profitability, attracting foreign capital (Aderemi et al., 2020).
- Global oil prices (GOP) will be positively related to FDI inflows in Nigeria's oil and gas sector. This was due to the fact that higher oil prices improve revenue prospects and encourage foreign firms to invest in exploration and production (Sami & Taiwo, 2023).
- Higher interest rates will deter FDI. This was because increased borrowing costs discourage capital investment and reduces investor confidence in the sector (Ozekhome, 2016).
- Sustainability report is expected to have a positive relationship with FDI as it shows how the nation has done so far in achieving all the SDG goals like SDG goal 8 of economic growth.

The conduct and completion of this study will be under the direction of Covenant University's College of Management and Social Science. The research should explain the investigation's aims. The study's data sources will be carefully selected and verified across many sources.

DISCUSSION OF RESULTS

Preliminary and Long-run tests

The analysis used 34 annual observations. The Augmented Dickey-Fuller results showed that logged FDI, inflation, exchange rate and interest rate were stationary at level, $I(0)$, while global oil prices, GDP growth rate and the sustainability index became stationary at first difference, $I(1)$. This mixed integration order supported the use of ARDL. The bounds-test F-statistic of 6.551835 exceeded the 5% upper bound of 3.45, indicating a long-run relationship among the variables. The Johansen trace and maximum-eigenvalue tests each indicated two cointegrating equations at the 5% level. The Akaike Information Criterion selected two lags.

Test	Key result	Inference
ADF unit-root test	Variables were a mixture of $I(0)$ and $I(1)$	ARDL was appropriate
ARDL bounds test	$F = 6.551835$; 5% upper bound = 3.45	Long-run relationship existed
Johansen cointegration	Two cointegrating equations	Long-run relationship confirmed
Lag selection	AIC selected lag 2	Two lags used

ARDL Estimates

The ARDL results showed that all six current explanatory variables were statistically significant at the 5% level. Inflation, exchange rate and interest rate had negative effects on FDI, while GDP growth rate, global oil prices and the sustainability index had positive effects. The R-squared was 0.971064 and the adjusted R-squared was 0.856392. The F-statistic of 249.1057 had a probability value of 0.000000, indicating that the explanatory variables jointly affected FDI. The Durbin-Watson statistic was 2.016385.

Variable	Coefficient	p-value	Reported effect on FDI
Inflation rate	-0.579147	0.0138	Negative and significant
Exchange rate	-2.368976	0.0000	Negative and significant
GDP growth rate	0.039349	0.0312	Positive and significant
Global oil prices	0.076751	0.0000	Positive and significant
Interest rate	-0.337023	0.0263	Negative and significant
Sustainability index	0.000261	0.0334	Positive and significant

Discussion by study objective

Inflation had a negative and significant effect on FDI, so the first null hypothesis was rejected. The result indicates that inflation is an important determinant of long-run foreign investment in Nigeria. Rising prices increase the costs of factors of production, raw materials, finished products and services. They also reduce the purchasing power of the naira and create uncertainty over profitability. Consequently, higher inflation discourages FDI inflows into the oil and gas sector. This result agrees with Ukachukwu and Odionye (2020), who reported a significant negative long-run effect of inflation on FDI, but differs from Njoku et al. (2023), who found the effect statistically insignificant.

Exchange rate had a negative and significant effect on FDI, leading to rejection of the second null hypothesis. Exchange-rate movements affect the domestic prices of foreign inputs and the value of returns earned by investors. As the exchange rate rises and the naira weakens, imported machinery, production factors and final outputs become more expensive. Greater fluctuation therefore reduces investment inflows. The significance of exchange rate is consistent with Ehimare (2011) and Ukachukwu and Odionye (2020).

GDP growth rate had a positive and significant effect on FDI, so the third null hypothesis was rejected. A growing economy signals stronger market conditions and creates opportunities for foreign businesses. As economic activity expands, investors are more willing to establish or increase operations, thereby raising FDI inflows. The finding differs from Ukachukwu and Odionye (2020), who found an insignificant long-run effect of real GDP.

Global oil prices had a positive and significant effect on FDI, and the fourth null hypothesis was rejected. Higher international oil prices improve revenue prospects in exploration and production and increase the attractiveness of Nigeria's oil and gas sector to foreign investors. The result is consistent with Donwa et al. (2015), who found a significant link between FDI and the performance of Nigeria's oil and gas sector. Interest rate had a negative and significant effect, indicating that higher financing costs may discourage investment. The sustainability index had a positive and significant effect, suggesting that progress towards the SDGs and economic growth is associated with stronger FDI inflows.

The findings support the PPP framework because inflation and exchange rate were significant determinants of FDI. Mismanaged inflation and exchange-rate instability increase production costs and output prices, reducing profitability and investment. The results also support the neoclassical position that investors respond to expected costs, returns and risk. Although high-return resource sectors may continue attracting capital, greater macroeconomic stability improves their investment prospects.

Descriptive Characteristics

The descriptive statistics covered 34 observations for each variable. FDI recorded a reported mean of 1,680,284 and a median of 1,092,717. Inflation had a mean of 11.06463, exchange rate 14.73951, GDP growth rate 18.29370, interest rate 13.53928 and sustainability index 12.42170. Global oil prices had the highest reported mean and standard deviation, reflecting the large scale and variability of the series used in the estimation. The descriptive results provided an initial view of the differences in scale and movement among the variables before formal time-series testing.

Hypothesis Decisions

For the first hypothesis, inflation recorded a coefficient of -0.579147 and a probability value of 0.0138. Because the probability value was below 0.05, the null hypothesis was rejected. Inflation therefore had a statistically significant negative impact on FDI in Nigeria's oil and gas sector. For the second hypothesis, exchange rate recorded a coefficient of -2.368976 and a probability value of 0.0000. The null hypothesis was rejected, confirming a statistically significant negative exchange-rate effect.

For the third hypothesis, GDP growth rate recorded a coefficient of 0.039349 and a probability value of 0.0312. The null hypothesis was rejected, indicating a positive and significant effect on FDI. For the fourth hypothesis, global oil prices recorded a coefficient of 0.076751 and a probability value of 0.0000. The null hypothesis was also rejected, confirming a positive and significant effect on FDI. The control variables were significant: interest rate was negative, with a coefficient of -0.337023 and probability of 0.0263, while the sustainability index was positive, with a coefficient of 0.000261 and probability of 0.0334.

Model Performance and Interpretation

The R-squared of 0.971064 indicated that the variables in the model explained approximately 97% of the variation in FDI. After adjustment for the number of predictors and observations, the adjusted R-squared was

0.856392. The F-statistic of 249.1057, with a probability value of 0.000000, established that the explanatory variables jointly affected FDI. The Durbin-Watson statistic of 2.016385 was approximately two.

The coefficient signs generally followed the a priori expectations. Inflation and interest rate were expected to discourage FDI because they raise uncertainty and financing costs, and both were negative. Exchange-rate instability was expected to deter investment by increasing transaction costs and risk, and the current exchange-rate coefficient was negative. GDP growth was expected to attract investment by signalling market expansion and profitability, while global oil prices were expected to strengthen revenue prospects in the petroleum sector. Both variables were positive. The sustainability index was also positive, in line with the expectation that stronger development performance supports investment attractiveness.

The combined results show that Nigeria's oil and gas FDI responds to both domestic and external conditions. Domestic price stability, currency performance, borrowing costs and economic growth shape the operating environment. Global oil prices influence expected sectoral returns, while the sustainability index reflects the broader development setting. The concentration of FDI in oil and gas does not make the sector immune to domestic instability; rather, the sector's international revenue prospects coexist with significant local cost and policy risks.

Post-Estimation Results

The study reported the Breusch-Godfrey serial-correlation LM test and the Breusch-Pagan-Godfrey heteroskedasticity test as post-estimation diagnostics. The Durbin-Watson result was also used in interpreting autocorrelation. These tests formed part of the study's assessment of whether the estimated model was suitable for drawing conclusions about the relationship between the selected macroeconomic variables and FDI.

SUMMARY, CONCLUSION, AND RECOMMENDATIONS

Introduction

The chapter concluded and summarized the study. The section summarised the study, displayed the conclusions, recommendations, and suggestions for other scholars.

Summary of the study

The study examined the effects of inflation, exchange rate, GDP growth rate and global oil prices on FDI in Nigeria's oil and gas sector, while controlling for interest rate and sustainability index. It used annual secondary data for 1990-2023 and applied the ADRL approach. The stationarity tests produced a combination of I(0) and I(1) variables. The bounds and Johansen tests established a long-run relationship. The ARDL estimates indicated that inflation, exchange rate and interest rate negatively and significantly affected FDI, while GDP growth rate, global oil prices and the sustainability index positively and significantly affected FDI. The explanatory variables were jointly significant, and the model reported high explanatory power.

Conclusion

The research reached conclusion that the significance of macroeconomic variables and global oil prices in enhancing FDI in Nigeria cannot be overemphasized. A stable inflation and exchange rate would bring down production costs and final output prices and this would boost the profitability of businesses and hence improve FDI. However, a fluctuating and high inflation and exchange rate would increase factor prices, jack up production and raw material costs and this would hamper profitability and ultimately lower FDI inflows into the economy due to distorted profits.

The study also concluded by emphasizing the importance of a working economy to FDI inflow growth. Foreign investors want a safe and secured economy for their investments to boost performance, hence, GDP growth rate is needed to enhance FDI inflows. Finally, the study concluded by showing the relevance of global

oil price to boosting FDI inflow into Nigeria as it would attract foreign investors into the nation's oil and gas sector.

Recommendations

- The Central Bank should focus more in managing inflation by controlling excess money in the economy. This is because a high inflation rate would slow economic growth and ultimately hamper FDI inflows.
- The Central Bank should ensure a stable exchange rate to boost FDI inflows especially to the development of the oil and gas sector. Policies such as having enough foreign exchange reserves and intervening in the foreign exchange market would stabilize the exchange rate.
- The Nigerian government should ensure that policies that would improve the economic growth rate, like lowering the ceiling rate on credit, are made. This would boost investment development and would in turn enhance FDI inflows.
- The Nigerian government should ensure that International oil price regulators like OPEC should

Contributions to Knowledge

The study contributes to FDI literature by demonstrating the importance of inflation, exchange rate, GDP growth rate and global oil prices to Nigeria's foreign investment inflows. It also supports PPP and neoclassical explanations by showing that inflation and exchange rate influence the success of FDI, while expected returns and sectoral conditions remain important. The results emphasise the dangers of high inflation and exchange rate fluctuation and show that a growing economy and favourable global oil prices can enhance investment in the oil and gas sector.

Limitations to the Study

The data was limited to 1990 till 2023 due to data availability for those years. This study only looked at Nigeria's oil and gas industry. The findings might not apply to other significant industries. The model did not incorporate important non-economic factors like political stability, regulatory quality, perceptions of corruption, and governance. FDI decisions can be greatly influenced by these factors, although they were outside of the scope of this study.

Suggestions for Further Studies

- Additional researchers can assess the same subject matter of FDI in other sectors.
- Other studies can look at the same subject matter using other econometric techniques like regression analysis.

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