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EFFECT OF INTERNATIONAL FINANCIAL INFLOWS ON PRODUCTIVE CAPACITIES IN AFRICA

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Abstract: This study investigated the effect of international financial inflows on productive capacities in Africa from 2010 -2022. Panel data robust standard error analytical technique and Generalized Method of Moments (GMM) were deployed to test for the effects of foreign direct investment (FDI), remittances (REM), and official development assistance (ODA) on productive capacities (PCI) in Africa with special focus on countries from different regions in Africa. Data for the analysis was sourced from the World Bank Development Indicator (WDI) and the United Nations Conference on Trade and Development (UNCTAD). The result showed that foreign direct investment harms productive capabilities in northern Africa but exerts a positive effect in the eastern and southern African regions. Remittances are statistically significant and have a positive effect on productive capacities only in eastern Africa. Official development assistance is also statically significant and exerts a positive effect on productive capacities in northern and eastern Africa. However, the effect of ODA in southern Africa is negative. The generalized method of moments results for the four regions revealed that foreign direct investment exerts a negative effect on productive capacities while remittance contributes significantly to productive capacities within Africa. Following the findings, the study concluded that international financial inflows play an important role in boosting productive capacities in Africa. The study therefore recommended governments of various

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countries to create an enabling environment and formulate policies that would stimulate foreign financial inflows especially remittances to strive.

Keywords: Productive capacities, International financial inflows, and Generalized method of moment (GMM).

1. INTRODUCTION

One of the many challenges facing developing countries, particularly Africa, is low domestic savings, which poses a barrier to African economies financing capital investment. According to Ogbuabor et al (2023), statistical findings from the United Nations Conference on Trade and Development (UNCTAD 20222) show that Sub-Saharan Africa (SSA) has domestic savings of 17.5% of Gross Domestic Product (GDP) compared to other regions of the world, such as East Asia (45%), Pacific (45%) and South Asia (35%). Aside from being lower compared to other regions, savings rates in Africa have been steadily declining and stagnating for some years due to lower per capita income. To boast Africa's low saving and investment gap, international financial inflows play an important role in stimulating investments and executing capital projects to raise productive capacities and reduce poverty and unemployment in Africa. Remittances, official development assistance, and foreign direct and portfolio investments all contribute to international financial or capital inflows (Chorn and Siek,2017) The benefits of foreign financial inflows on investment in recipient nations, as well as how they further boost productive capacity and enhance commerce, have been underlined by economic theories and some empirical shreds of evidence. (Gnangnon 2023; Saha 2023 and Emako and Menza 2022).

Productive capacities refer to production resources, entrepreneurial capacities, and production linkages which together determine the capacity to produce goods and services and enable a country to grow and develop (UNCTAD, 2006). Schouame (2023) and Gnangnon (2019) regarded productive capacities as an indispensable element for LDC development. The 2006 UNCTAD report further demonstrates that in the least developed nations, particularly in Africa, the fundamental processes of capital accumulation, technological advancement, and structural change have been very weak, which has led to low labor productivity and widespread underemployment. The report classified natural resources, human resources,