THE IMPACT OF FOREIGN DIRECT INVESTMENT ON POVERTY REDUCTION IN ETHIOPIA

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ABSTRACT

This paper examines the impact of foreign direct investment on poverty reduction in Ethiopia. The study seeks to test the hypothesis that foreign direct investment has no contribution in economic growth and has no direct effect on poverty reduction in Ethiopia. The methodology involves estimating error correction model using time series data for the period 1981-2012. The results indicate that foreign direct investment has significant positive effect on economic growth as well as on the poverty reduction of Ethiopia. Domestic economic conditions such as domestic investment and infrastructure have significant positive effect on both human development index and economic growth, whereas openness has a positive effect merely on economic growth. The study recommended that effort should be made to encourage the inflow of foreign direct investment. Even if, foreign direct investment contributes to poverty reduction, parts of the revenues from the investment, which are collected through tax revenue, rental fees, and export and import activities, should be used to promote further economic activities, safety nets as well as investment in infrastructure.

KEY WORDS: Foreign direct investment, Poverty reduction, Economic growth.

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