Foreign direct investment and economic growth in Tanzania

Prosper Charie

Master of Arts (Economics)

University of Dar es Salaam, College of Social Science, 2001

The last two decades have witnessed a remarkable evolution in the contemporary thinking about economic growth and empirical issues surrounding it. While traditionally, growth was seen as being dependent mainly on domestic capital accumulation and, or savings, recently there has been a shift of attention to foreign created assets. The importance of foreign capital, especially in developing economies has increased substantially due to increased international capital mobility. Foreign Direct Investment (FDI) in particular, has recently been viewed as an engine of growth. FDI stimulates growth by addressing the two major constraints, namely shortages of financial resources and technology and skills. Tanzania has been receiving inflows of FDI, and these inflows have been increasing reasonably during the 1990s. given this trend, it is necessary to examine whether these inflows have contributed to the economic growth or not. This study set out therefore to examine the impact of FDI on the Tanzanian economy during the 1970-1999 period. The analysis was done using econometric model. The results indicated that FDI contributed positively to the economic growth of Tanzania during the period covered by the study. The impact was found to be more stable in the past decade, that began in the late 1980s. However, formal analysis revealed that FDI inflows did not have *crowding in* effect on domestic investment during the reviewed period. This means that FDI has no macroeconomic externalities-via spillovers (diffusion of technology and skills), implying that the contribution of FDI to growth was mainly through direct additions the capital stock. These results imply that, in order to enjoy fully the benefits associated with FDI, measures should be taken to build the absorptive capacity, so as to absorb and internalize the technologies associated with FDI. In this respect, the key areas identified are: emphasis on human resource development through education and training establishment of well functioning markets, emphasis on the development of the financial system, promoting private sector participation in the economy, and Intellectual property right protection sp as to create favourable environment for high technology FDI.