

# Foreign Direct Investment, Governance and their Impacts on Poverty Reduction: Application on Dynamic Panel Data (GMM)

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## Abstract

The objective of this article is to study the different aspects of the relationship between the flows foreign direct investment and the quality of governance in an attempt to achieve a better understanding of the contribution of FDI to reducing the poverty. In particular, the thesis will empirically examine how the interdependence and complementarity between FDI and governance allow FDI to contribute to the reduction of poverty. Thus, this work will take a progressive course starting from the determinants FDI in developing countries and going as far as their effects on poverty, through governance, economic growth, development aid, external debt and international fund transfers. We expect, through this econometric study that FDI, in the presence of a good quality of governance can contribute to the reduction of poverty. We will pay particular attention to the identification of mechanisms, to through which FDI and governance affect poverty reduction.

Empirically, we are dealing with a study that takes into consideration the classical approach of FDI contribution to poverty reduction. Then, we treat a study taking into account institutional aspects on the basis of a sample made up of 102 countries, we estimate a dynamic panel model and we use the GMM method according to the Arellano and Bond (1998) approach. In this context, the basic hypothesis consisted of the existence of an indirect effect of FDI on poverty reduction through the channel of governance. The study of this hypothesis was formulated in a dynamic model applied to the data available on the countries of Sub-Saharan Africa, Asian countries (ASEAN), Latin American countries (MCAC) and Eastern European countries (Transition economy) between 1996-201. The results validate the hypothesis that institutional quality promotes the effect of FDI on poverty reduction.

**Keywords:** FDI • Institutions • Pauvrety • Data from the Dynamic Panel (GMM)

**JEL classification:** P45, I32, C01, O50

## Introduction

Little work has analyzed the impact of foreign direct investment (FDI) on the poverty reduction and the effect of governance on poverty reduction, and to our knowledge, this work is the first to focus on the impact of FDI and governance on poverty, according to a comparative study between countries in development, African countries (sub-Saharan Africa), Latin American Countries (MCAC), from Asia (ASEAN) and Eastern European Countries [1,2]. Globalization is a controversial, complex phenomenon and a major problem, in particular at the level macroeconomic, e.g. international trade, direct investment foreigners and labor migration. In addition, commercial enterprises, in particular multinational corporations (TNC) play a key role in these mechanisms. One Another important aspect is that the impact of the phenomenon of globalization is uneven. So the globalization has affected the level of average incomes around the world in recent decades (including reducing poverty levels in many countries), in especially foreign direct investment, and in achieving the reduction of poverty. Globalization can play an important role in the development process and poverty reduction.

Countries like Korea South, Singapore, Taiwan and Hong Kong, are countries that have got on the way to growth at a high level, have succeeded in reducing poverty considerably [3]. On the contrary, others argue that economic growth is necessary but see that it remains insufficient to bring about the reduction of poverty. Indeed, the process of economic growth in general exacerbates inequalities and poverty in the company.

The international community committed to the Millennium Goals Summit for the development (MDG) of the United Nations in New York in 2000 to halve the extreme poverty rate by 2015, and outlined eight axes. The achievement of these goals would contribute to human development and poverty reduction. As such, what are the factors that are at the origin of economic growth and which, at the same time, can contribute to poverty reduction? Would FDI make it possible to stimulate growth and contribute to poverty reduction?

The main objective of this study is to encourage FDI and governance that have played a decisive role in poverty reduction. One of the outstanding phenomena of decade in Africa and other regions of developing countries has been the strategies for reducing poverty rates. The objective of this study is to locate the main determinants of poverty. We learned from the literature review that the main factors explanations likely to determine poverty are economic growth, creation jobs, government transfer payments, income inequality. Being given the downward trend in funding from Development Aid. Given the particular characteristics and important roles of the governance and FDI on poverty reduction, this paper aims to examine in detail their triangular relationship. More precisely, the study, through its regression model in two steps, aims to explore the impact and the mechanism by which FDI affects the reduction of poverty, directly and indirectly through the quality of governance. For to complete this regression analysis, a case study on developing countries is provided to study their relationship, in particular the impact of the interaction between FDI is the quality of governance on poverty reduction. In general, better governance is seen to attract more FDI to developing countries and the presence of FDI in itself can be an important factor in improving the quality

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of governance in these countries by exerting pressure on the government. If so improving the quality of governance can then be further justified by the attraction of FDI.

## Research Methodology

### Section 1- Transmission channels FDI on poverty reduction

FDI contributes to development in at least three ways: (a) it is a perpetual source of new investment capital, enabling countries to increase imports and accumulate capital more quickly, (b) they encourage the transfer of technologies and increase the stock of human capital and boost productivity and the growth of domestic enterprises in the long term, and (c) they help to accelerate the process of economic integration and competitiveness by helping to link economies developing to global supply and production chains. FDI as a factor key to generating growth are therefore the most important ingredient for reducing poverty. FDI has the potential to improve the quality of growth through, (a) reducing the volatility of capital flows and income, (b) Improving assets and income distribution at the time of privatization, (c) contribute to the improvement of social and environmental standards and (d) contribute to the improvement of social security and basic services for the poor. According to Ozturk "during fluctuations in capital flows in the years 1990, FDI was the main source of flows in developing countries development" Asserted: "knowing that FDI contribute to growth, little empirical work on FDI focused on Africa, which is nevertheless the poorest region in world".

**Review of the literature on foreign direct investment FDI, economic growth and poverty:** A large number of studies have analyzed the relationship between FDI and growth economic. The main concern of research is whether FDI has an impact on the economic development of a country and to what extent. The implicit assumption assumes that economic growth naturally leads to improved well-being. The most research concludes that FDI stimulates growth economic. Let us first examine the causal link between FDI and economic growth. Then, we present the role of the development of a country's financial market on the link between FDI and growth. Finally, we present the theories on the mechanisms of transmission of the relationship between FDI and poverty.

**The direct relationship between FDI and economic growth:** Foreign direct investment has been recognized as an important source for economic development. Many studies claim that FDI could fill the gap between investment and national savings. It can also increase tax revenue and improve management, technology as well as the skills of the workforce in host countries. Many researchers believe that the benefits acquired from FDI may include the acquisition of new technologies, job creation, development of human capital, contribution to the integration of international trade, improving domestic investment and increasing tax revenues generated by foreign direct investment. All these benefits are expected to contribute to economic growth and increased employment which is an effective tool to achieve improvement in poverty reduction.

FDI play a positive role in the economic growth of host countries. The research that has examined the relationship between FDI and economic growth using the FDI variables and GDP growth has shown mixed results. Several studies analyzed the relationship between FDI and economic growth to determine the effects of FDI on economic development. Economic growth improves well-being while FDI is a factor that stimulates economic growth. In general, foreign direct investment leads to an increase in total investment. He represents an investment in addition to domestic investment. FDI can also have an impact on domestic investment [4]. Studied the impact of FDI on domestic investment. They perform a cross-sectional analysis covering 69 countries and a period from 1970 to 1989. The authors lead to a complementarity effect between the two, in some estimates.

**The role played by the development of financial markets in the link between FDI and economic growth:** Although it is possible to test the direct relationship between FDI and growth economic, it is legitimate to think that

FDI will flow to countries which have better developed the financial market or assume that FDI flows will contribute to development of the financial market, which leads to more economic growth.

With this point, some authors analyze how the development of the financial system can contribute to the relationship between FDI and economic growth since obvious empirical evidence that seems to suggest that an advanced financial market is a good indicator of flow IDE. For example, Hermes and Lensink studied the role that the development of financial system plays in strengthening the positive relationship between FDI and growth economic. Foreign direct investment helps develop financial markets, thus leading to economic growth. Indeed, empirical evidence suggests that an advanced financial market is a good predictor of FDI inflows.

More recently, Alfaro, Chanda, Sebnem and Sayek [5] developed a model theoretical to formalize a mechanism that emphasizes the role of financial markets premises, promoting the growth of FDI [6]. studied empirically the role of political risk in the association between FDI and development financial. Using a panel of 97 countries over 20 years, they establish a non-linear association between financial development and FDI inflows. They found that the financial development leads to greater FDI inflows up to certain level financial development assistance. The authors also found that the political risk understands factors that influence the relationship by altering the threshold of development financial.

**Theoretical arguments: The link between FDI and poverty:** Since the Second World War, two major trends have characterized the evolution of FDI in developing countries First of all from the end of the second war global. During this period, stocks of FDI flows increased throughout the world, in particular, in developing countries. During this period, FDI flows mainly due to politics rather than economic reasons. Second, at the end of the Cold War (in the 1990s), FDI was concentrated mainly in countries that offer tax benefits, subsidies and other incentives (FDI incentive policies). The impact of FDI on development human can be analyzed from at least two points of view. On the social level, the reduction of poverty and improved well-being are the priorities of governments in developing countries. Development Foreign direct investment can help achieve these goals because investments create jobs, develop local skills and stimulate technological progress.

According to Gorg and Greenaway [7] FDI is considered to be: a key factor in economic growth and development, most governments consider FDI as a priority, in particular, in developing and transition economies.

**The indirect effects of FDI on poverty reduction:** In this context, we cite technological improvements, taxes paid by FDI and the way these taxes are spent, the productivity of investments and wages. In addition, due to the economic and political conditions of the country effect, they can be considered the most important determinants of the effect of foreign direct investment in poverty reduction. For this reason, if a country wants to achieve better results in the reduction of poverty, thanks to FDI, it is necessary to take into account its economic conditions and policies to be attractive for these investments. The study by Ahmad et al, [2] indicated that FDI is positively and significantly associated with poverty reduction in the ASEAN and SAARC regions over the period 1990-2014, but significant differences exist between these two regions. FDI has an impact more important for well-being in SAARC countries than in ASEAN countries.

Magombeyi & Odhiambo [1] used three indirect indicators to measure the poverty reduction (household consumption expenditure, mortality rate life expectancy) in the case of Botswana between 1980 and 2014. They concluded that FDI has a positive impact on poverty reduction in the short term and an impact negative in the long term when life expectancy is used as an indicator of the poverty. When the infant mortality rate is used, a non-significant relationship is recorded both in the short and long term.

Using the same measurement indicators, Ngueta, et al. [8] found that FDI does not have a large enough effect on poverty reduction in Cameroon on the period 1984-2014. Similarly, Tsaura [9] found that FDI in the natural resource extraction reduce poverty in southern African countries and Western between the years 2002 and 2012. Many studies of countries in the Asian region have

found a relationship positive effect between FDI on poverty reduction. For example, the Jalilian & Weiss study [10] indicated that FDI inflows into ASEAN over the period 1991-1997 were associated with stronger economic growth and that there is a close relationship between growth in the middle income and growth in the income of the poor. The authors therefore have found a positive impact of FDI on the poor by increasing their incomes. Nevertheless, these authors found no evidence that FDI reduces the incomes of the poor. For six countries in the same region and over the period 1995-2011, Utama found that FDI promotes poverty reduction [11].

**Tax revenues:** Direct (corporate tax) and indirect (VAT, etc.) taxes paid by FDI have an increasing effect on total tax revenue. They are dependent on how these additional increases occurring in tax revenue are used, which may be effective on poverty. According to this study, if these tax revenues are used in the financing of services, the investment from which the poor can use directly (in kind or cash assistance, etc.) or indirectly (training course professional, etc.). Then FDI makes a positive contribution to reducing the poverty. If there is an increase in investment, the services will be used by the poor segment as long as the tax revenue increases. In this case, it can be argued that the increase will take place in tax revenues due to taxes paid by foreign investors and have a reducing effect on poverty.

**Economic growth and technological change:** FDI influences poverty reduction and can be categorized into direct effects and indirect. Indirect impacts through the contribution of FDI on growth given the increasingly accepted role of economic growth in the poverty reduction. The rate average poverty is reduced in the situation of high economic growth but in the event of contrary (negative economic growth, war and economic crisis) poverty increases. Since economic growth is the most important determinant of enrichment, it is also one of the most important factors effecting the reduction of poverty. However, the effect of economic growth on poverty shows the differences between countries. The fundamental reason for this effect is to see countries with levels of economic growth and as a result, levels of per capita income differentiate. In addition, the determinants of groups that use more of the production, the increase in income, are implemented with economic growth (distribution primary income) which is another important factor in the effect of growth on poverty (World Bank 2001).

The increase in the amount of production will reduce the general level of price. Those who consume the products produced by FDI will be positively affected by this process. If the poor population benefits more from the use of increased incomes thanks to the products and services (clothing, accommodation and food) offered by the IDE and the courtesy of these investments, the effect of these investments in reducing the level of poverty increases (because of the consumption expenditure of poor people who will be reduced compared to the previous situation and their obtained income will be increased [13]).

The role of foreign direct investment has been crucial in stimulating growth economic and poverty reduction in developing countries, especially in the context of globalization and liberalization. In recent years, countries in development have shown a huge penchant for attracting FDI from high and middle income to accelerate the pace of industrialization by improving efficiency and competitiveness and fight against poverty. Recent studies suggest that growth tends to raise the incomes of poor in proportion to overall growth. The main expected results of the study are as follows:

- Knowledge of the links between the policies of rich countries and development poor countries improved
- The impact of the country's wealth development policy influences FDI
- The impact of FDI in the manufacturing sector on poverty reduction.

According to Obwona, the relationship between FDI and poverty reduction is indirect: if foreign direct investment contributes to the growth of exports and productivity, it has benefits for poor populations. In this case, the IDE has an impact by creating a favorable environment. According to Hayami and Todaro and Smith the contributions of foreign direct investment (FDI) to the development of a du capital humain local, in the sense that the higher the level of local human capital, the greater the impact of FDI on economic growth. The effect of FDI on economic growth is positively associated with the level

**The direct effects of FDI on poverty:** Use FDI can have direct effects on poverty reduction in countries reception through increased employment and work force training. However, it is necessary that the employment and training of the workforce must mainly favor the poor (low income groups or the unemployed). The work that will take place in these groups will gain the allocation of skilled labor with the training followed and they will have the opportunity to obtain a high income that allows them to achieve a standard of living above the poverty line. The successes achieved by poor due to labor training, under normal conditions (validity of the profession in the market), could offer to maintain this standard of living, throughout their life.

On the other hand, some poor people who do not have a regular income have become employees and started to earn income, higher FDI (especially main work) provide direct and significant contributions to poverty reduction due to unemployment. If foreign direct investment provides the contribution to the employment of people the unqualified poor is the effect of poverty reduction stemming from the fact that the unemployment increases even more. This is because the employment of the unskilled unemployed is more difficult compared to employing the skilled unemployed. For this reason, the effect of foreign direct investment on poverty reduction through increasing of employment is the most important effect [14].

The effect of foreign direct investment on poverty reduction through of employment is not just limited to having one's own job. Thanks to these investments, the increase in business employment which takes place in the ancillary industry and which should be establishment, from the beginning and expanding, is an indirect and important factor that contributes to poverty reduction [15]. This follows from the reason that this indirect increase in employment caused by FDI, in some cases perhaps more than the increase in employment occurring in direct jobs. When we compare it with direct and indirect effects of foreign direct investment on poverty reduction, sometimes this indirect factor may be more dominant.

## Section 2- The effect of governance on development and poverty reduction

The Millennium Development Goals (MDGs) policy for contribute to the debate on international development, and post-MDG policy for example in September 2000, delegates from around the world came together to reduce the poverty and increase growth in developing countries. All members of United Nations (UN), including 147 heads of state and government, adopted the Declaration of the Millennium in which they pledged to do their best for those who suffer of poverty, hunger and disease.

### Link between good governance and poverty reduction

**Good governance and the fight against poverty:** Strictly speaking, good governance can simply mean efficiency with which a government does its job and promotes the public good. The public good is broadly defined as law enforcement and order, revenue collection, allocation resources to meet specific demands, the provision of infrastructure and promotion of human rights. Although democracy strengthens good governance, the latter is not necessarily equivalent to democracy. A single party and Authoritarian regimes generally do not have good governance, as they are easily loans to corruption and human rights abuses. Democratic regimes, which are much more open to public scrutiny and periodic legitimacy testing through elections, tend to be more sensitive to good governance.

Indeed, evidence over the three decades, since the 1980s, shows With the exception of a few countries such as China, Malaysia and Singapore, where some progress Considerable economic development was achieved under autocratic or semi-dictatorial regimes. In the majority of countries in Africa, Asia and Latin America, the poor governance has been a cause of continued poverty and underdevelopment.

### Good governance and capacity building within government for poverty reduction strategies:

- Good governance can build capacity within government to implement poverty reduction strategies. This can be accomplished by the

following institution:

- Basic political order: where internal conflicts and war have undermined public authority in almost all spheres of life.
- Political legitimacy: through free and fair periodic elections during of which the results are acceptable to both winners and losers.
- The rule of law: as an aspect of government without privileged regard to any person based on tribe, region of origin, race, gender, income or any other ground of discrimination.
- Popular participation: the development of policies and decisions on the allocation of resources from the grassroots to the national level.
- Effective formulation of the review: of public policy to avoid "routine" making 'plan' as a response to pressure from donors or "external conditionality".

### The effect of governance indicators on poverty reduction

**The impact of democracy on development and poverty reduction (Democracy):** democratic states have neither the best nor the worst performance, when it comes to economic performance and poverty reduction, and there is evidence to show that democratic systems prevent the worst crises humanitarian. Other researchers are more positive about the impact of democracy on economic growth, and emphasize indirect connections. For example, we can do argue that democracy tends to create political stability which is a good prerequisite for the development. From a peak of 36 countries engaged in war in 1991, that number has plummeted by two-thirds at the start of 2003. In addition, democracies are less likely to trigger a military confrontation, with incentives from democracies generally less conflict. Halperin and Allen also asserted that democracy has an impact on the likelihood of civil war in developing countries, the 49 countries low-income groups were facing civil war between 1990 and 2000, only 8 were democracies. In contrast, the 25 low-income autocracies were engaged in war civil.

**The impact of justice and the rule of law on the development and poverty reduction:** Justice and the rule of law: the literature widely recognizes the negative impact of a weak Rule of law over the poor, including property rights and the inadequacy of different settlement mechanisms. However, there is little conclusive evidence that the "offer" rule promotion of the law by donors has had an impact on poverty levels. On the "Asks" there are some positive case studies of attempts to improve the lack of access to popular justice which could be a means of reducing poverty.

Grandvoinnet makes a similar case: access to legal information and the system judicial process is necessary for poverty reduction, in that it decreases the vulnerability of the poor to exploitation or deception. This access can allow them to take advantage of economic opportunities. However, access to law is generally limited educated sectors, and generally the urban population [16]. The poor are more at risk of abuse of political power, and are less able to protect against injury and economic loss over this abuse. In countries all over the world, the poor are more likely to be victims of police violence than the poor.

The poor are also negatively affected by the low protection of property rights. Assess the link between improving the rule of law and poverty reduction is further problematized by a lack of research into this domain. As Anderson points out, "There has been little systematic exploration of the role that the rule of law plays in improving poverty [17,18] the links between access to justice and poverty Reduction has been "hardly explored". Although Hasan and Ulubasoglu considered that property rights stability and the rule of law are prerequisites for a dynamic private sector but they are cautious about the impact of this situation on income inequality.

**The impact of corruption on development and reduction of poverty:** To date several empirical, evidence has been generated on the impact of combating corruption on poverty levels and more generally on development. The goal main focus is in the literature on the link between corruption and economic growth, where the impact on poverty reduction is implicit or indirect. Many initiatives anti-corruption have yet to demonstrate success.

The prevalence of high levels of corruption in some of the poorest countries in the world is well documented in academic literature. It is also widely accepted that the poor are the hardest hit by corruption. As a result, the policymakers and academics say efforts to fight corruption will lead to poverty reduction. This presumed link between the fight against corruption and the fight against poverty is often based on the assumption that efforts to curb corruption can stimulate economic growth which, in turn, benefits all members of society, rich and poor. To date, very little empirical evidence were generated on the impact of the anti-corruption initiative on poverty levels, or more broadly, on development.

The World Bank now refers to the fight against corruption as "Central mission of its fight against poverty". Other funders followed suit: a body of empirical work and other evidence over the past decade shows the impact of corruption on investment, economic growth and poverty, on this basis, both bilateral and multilateral development. The activities of corruption are believed to have an impact on the poverty levels of various manners. Many authors focus on the macro level, and highlight the costs of economic growth.

### Section 3: Review of empirical literature of the relationship between FDI, governance and poverty

We have shown previously that the economic theory relating to the question: what are the favorable factors for economic development and the reduction of poverty? What about empirical work now?

#### A review of empirical literature of the relationship between governance and FDI

**Relationship between governance and FDI:** Several empirical studies, have been carried out, through a sample of 21 foreign companies in Bangladesh in order to test empirically the effects of bad governance on direct investments foreigners. This work concluded that the government's ineffectiveness in combating corruption, improving political stability and strengthening the rule of law and the creation of a physical and political infrastructure are associated with the most important determinants influencing FDI flows to Bangladesh. In 2005, Bangladesh ranked 110, the most low among 117 countries, both in the corruption index and in the index of institutions public. Bangladesh is experiencing deterioration in foreign direct investment and the business climate index. They say Bangladesh must improve the conditions of base in the business environment to strengthen the strategy to improve governance.

Similarly Buchanan, Quan and Rishi econometrically examined the impact the quality of institutions on the volatility of foreign direct investment. Their study which covered a sample of 164 countries over the period 1996-2012. They find that the quality of institutions is significantly negative to the volatility of FDI which can have an effect negative on economic growth. However, their empirical results also show that there are institutional determinants of FDI that are associated with growth lower economic.

Kenisarin and Andrews Speed examined the relationship between FDI and three sets of indicators such as governance, economic freedom and the perception of corruption. Modernizing the economies of the Soviet Union will require levels substantial foreign direct investment (FDI). The purpose of this study is to examine the factors that may play a role in determining this level of FDI. She succeeds by establishing quantitative relationships between the levels of FDI per capita for the year 2004 and three indicators relating, respectively, to governance, economic freedom and perception of corruption. The authors concluded that the level of FDI in developing countries the Soviet Union (AUS) was determined by the degree of reform of a centrally planned economy towards a market economy, through a sample of 6,288 American multinationals investing in various parts of China during the period from 1993 to 2001, that American multinationals prefer to invest in regions that have better protection of intellectual property, property rights, the lower degree of government intervention in business operations, a lower level of government corruption and better contract enforcement. They concluded that the results are robust in terms of the impact of economic institutions, including the protection of property rights and the exclusion of contracts, on the choice of the location of the foreign direct investment.

Dumludag [19] examined the relationship between political, social and economic and foreign direct investment for a sample of 67 countries in development for the period from 1984 to 2005. Researchers focused on the quality of institutions, as determinants of FDI in developing countries.

They conclude that economic, political and social institutions explain variations between countries in foreign direct investment flows. The results suggest that better perceptions of the quality of institutions have an overall effect positive and economically significant on FDI. On the other hand, the unpredictability of laws, political and economic instability, government instability and the high level of corruption play a major role in deterring FDI.

In a study by Ahn and Chan-Lee covering fifty-five countries developed and developing, the two authors conclude that "the improvement of functioning of regulatory and governance systems and their implementation application seem to be much more important than the actual foundations of law in terms of impact on development." Transparency is a crucial factor for foreign direct investments.

**Relationship between corruption and FDI:** Studies on corruption and its relationship with foreign direct investment (FDI) have yielded mixed results. Jose and Ling Liu (2015) examined the relationship between corruption and foreign direct investment. They conclude that corruption discourages FDI, but others have found the opposite. Previous studies in the OLI paradigm, also seek to advance our understanding of this relationship, by introducing the notion of "corruption distance" between the countries of Latin America. After the check transaction costs and institutional variables, the results show that the distance from corruption has an asymmetric impact on FDI. Countries with the distance from the "positive" corruption compared to the levels of the host countries of origin of the corruption, experienced no significant increases or decreases in FDI levels. However, the distance from the "negative" corruption experienced by host countries is associated with significantly lower inward FDI. We show that companies with host countries with relatively low levels of corruption are unfamiliar with formal and informal institutions associated with corruption. Conversely, the home country companies with great corruption are discouraged by high corruption in host countries. Thus, the distance of corruption can be considered as a determinant of FDI.

Freckleton, Wright and Craigwell examined the relationship between investment direct, corruption and economic growth for a sample of 42 countries in development, they used a dynamic panel. They found that corruption has a significant influence on GDP per capita in the short term, but it is not significant in the long run. These studies highlight that lower levels of corruption improve the impact of foreign direct investment on development and economic growth. Found a positive and clear relationship between corruption and FDI, on a panel of 73 developed and less developed countries during the period 1995-1999. Previous research has assumed that corruption between directly in the cost function of multinationals, suggesting a negative relationship between corruption and FDI. They have shown that corruption can be beneficial, the relationship positive relationship between FDI and corruption shows that official government officials use administrative controls and bureaucratic discretion to extract profits from foreign investors.

**The relationship between political stability and FDI:** Some more recent studies such as those by Gouenet and Nguena have examined the effect of the business environment on investment. The results of regression suggest that the business environment remains the main determinant of foreign direct investment. Sociopolitical instability creates an environment unfavorable and represents a risk for private investment, in general and for FDI, in particular. The coexistence of factors of socio-political instability such as civil wars, the coups d'etat and the various civil problems pushed to use a specific context of Cameroon to assess the relationship between socio-political instability and FDI. Gouenet examined the impact of socio-political instability on private investment in Cameroon during the period 1960-2002. Sociopolitical instability is highlighted as a risk factor for the investment which generates transaction costs for the economic activity. The combination of the economic crisis with political crises contributes to the deterioration of the business environment in general, and explains, in particular, the hesitant behavior of private investment. Using the econometrics of OLS, their results clearly show a negative

correlation between the coefficient of instability policy and developments in private investment.

The literature shows that uncertainty can become a powerful deterrent of investment. A review of the literature identified the implications of the policy macroeconomic and measured the practical importance, in particular, for Africa sub-Saharan Africa, the link between uncertainty and investment. He suggests that instability and uncertainty are important factors for a bad investment record of Africa over the past two decades. Likewise, Rodrik.

Showed that political uncertainty can act as a hefty tax on investment and Sensitive contrary reforms can be harmful if they raise doubts, as to their performance. Alesina, Ozler, Roubini and Swagel, examined the relationship between political instability and economic growth in a sample of 113 countries, for the period from 1950 to 1982. The main result of this study is that in countries with high propensity of government fall, growth is significantly lower. This effect remains strong when we limit our definition of "change of government" in the event of significant changes in government.

Ngbesso examined the impact of political risk on net inflows foreign direct investment (FDI), using panel data for a sample of 31 countries in sub-Saharan Africa for the period 1984- 2008. Results indicate a negative and significant relationship between political risk and input of FDI in sub-Saharan Africa. Indeed, the political risk indicator is negatively linked to FDI flows. This means that any increase in political risk leads to a decrease in net inflows of FDI in Sub-Saharan Africa. The results of the study obtained are robust to all the tests performed in our analysis. Likewise, Jun and Singh examined the relationship between political risk and FDI, using a sample of 31 developing countries. They concluded that countries with high levels of risk policy attract less FDI. Gastanaga, Jeffrey and Pashamova, examined the link between the different political variables and foreign direct investments. They found that low levels of corruption, risk and better enforcement of contracts are associated with high levels of FDI. They stress, however, that their results should not be generalized because of the smallness of their sample (22 countries).

Busse and Hefeker analyzed the relationship between political risk, institutions and foreign direct investment. Using different econometric techniques for a sample of data from 83 developing countries and the period 1984 to 2003. They identified the metrics that matter most to the business of companies multinationals. The results show that government stability, internal conflicts and externalities, law and order, ethnic tensions, bureaucratic quality and to a lesser extent degree corruption and democratic accountability are the most important determinants of FDI flows.

**Review of empirical literature of the relationship between governance, FDI and poverty:** The relationship between FDI and poverty reduction on the one hand and the relationship between governance and poverty has been the subject of several empirical studies. A few empirical studies have been carried out on the subject of the relationship between FDI, governance and poverty reduction. Assad zadeh and Pourgoly studied the relationship between direct investment foreign exchange, institutional quality and poverty for a sample of countries in the region MENA over the period 2000 to 2009. They examined the effects of direct investment and the quality of institutions (rule of law) on poverty reduction. Using an econometric technique of random-effect panel data, their results show that foreign direct investment and the appropriate institutional quality have positive and significant on reducing poverty and increasing well-being. They have used the generalized least squares estimation (GCS) method, the software is used to STATA 11, fixed-effects or random-effects panel data.

Velde reviewed host country government policies regarding the choices available to policy makers in order to attract direct investment foreigners and their effects on human capital and income inequality. They looked at the host country government policy options available to decision makers policies to attract foreign direct investment and influence the behavior of transnational corporations (TNCs), focusing on their effects on capital formation human rights and income inequality. They looked at FDI policy first to discuss FDI policies affecting the formation of the human capital. They introduce a framework of the demand and simple supply of the skill market, which allows us to analyze the effects of transnational corporations on capital rights and income inequality.

The FDI policy options are analyzed in this framework, in order to see how the FDI policy FDI can influence the formation of relevant human capital and income inequality.

Tsai and Huang examined how economic growth, openness and the role of the government contribute to reducing poverty in Taiwan over the period 1964-2003. Sustained economic growth is found to be the major driving force for the poverty reduction in Taiwan, and openness or foreign trade help the poor by a direct distribution effect, as well as the effect of indirect growth, both in the long term and short term, although FDI inflows have no significant impact on the average income of the poor. FDI outward from Taiwan in the last two decades seem to have had a negative effect on the poorest (20% of the population). Nunnenkamp, Schweickert and Wiebelt presented the impact of investment foreign direct on poverty and income distribution in Bolivia. The analysis addresses several important transmission channels that have been overlooked in the empirical literature by i) studying the impact of FDI on household income in urban and rural areas, ii) taking into account informal activities and iii) the difference between different segments of the urban workforce.

**The simulation results suggest that FDI inflows increase the ratio investment, enhance economic growth and reduce poverty:** However, the distribution of income generally becomes more unequal. In particular, the FDI widens the income disparities between urban and rural areas. These results indicate two levers through which the Bolivian government can promote growth and improve poverty. First, it seems important to overcome the segmentation of the Market. Second, public investment in complementary infrastructure can help remove bottlenecks in the absorptive capacity of the economy that tends to limit the employment of the poor. However, political reforms, simulated or alternative productivity scenarios are hardly effective in bridging the divide between urban and rural areas.

Alesina and Perotti examined the effect of income inequality, fueling social discontent, which increases socio-political instability. Who, by creating uncertainty in the political and economic environment, reduces investments? In a result, income inequality and investment are inversely proportional. Since investment is an essential engine of growth, we measure instability socio-political with clues that capture the appearance of more or less phenomena violent, political unrest. All in all, we note that, until today, the empirical literature has not resolved the adequate factors for poverty reduction.

#### Section 4: The contribution of FDI to the reduction of poverty: Empirical study

Developing countries (Asia, Africa, Latin America and Europe in East) increasingly see foreign direct investment as a source of economic development, modernization, income growth, employment and poverty reduction. This is reflected by their continued economic policies currently which are explicitly intended to improve the conditions for attracting FDI and to maximize the benefits of the presence of FDI in their domestic economy. To our knowledge, no studies using the role of the four international funding sources (foreign direct investment (FDI), official aid, international remittances and external debt) in poverty reduction. The objective of this study is to locate the main determinants of poverty reduction in developing countries in during the years 1996-2017.

**Presentation of the econometric study:** In this section, we will present the methodology we will adopt for estimate the relationship between FDI and poverty, in the presence of a developed financial system and external financing, as well as the results of each estimate. The interest of this study is to try to shed some more detail on a topic that has not been much debated, namely, this link between foreign direct investment and the reduction of poverty with a direct or indirect effect, through financial development, financing exterior and other variables. Our study is gaining further interest because it concerns a sample made up of developing countries. In what follows we will study empirically, the nature, reality and intensity of these links between FDI and poverty. The econometric method specific to panel data will be used, the data of static panel estimated by the Hausman method.

**Model:** To study the impact of foreign direct investment on poverty reduction in African countries (Sub-Saharan Africa), Latin American Countries

(MCAC), Asia (ASEAN), and the countries of Eastern Europe (Transition economy) between 1996 and 2017, in using static panel data from 102 countries, we will adopt a model based on the Theoretical framework of Gohou and Soumare, the model is as follows:

$$P_{it} = a + b_1 GDP_{it} + b_2 IDE_{it} + b_3 TRANSF_{it} + b_4 AIDE_{it} + b_5 DETTE_{it} + b_6 OUV_{it} + b_7 INF_{it} + b_8 G_{it} + b_9 LC_{it} + b_{10} DP_{it} + b_{11} EDUCAT_{it} + b_{12} DF_{it} + b_{13} (FDI.DF)_{it} + \epsilon_{it}$$

**The sample:** Our study covers the period from 1996 to 2017 in African countries (Sub-Saharan Africa), Asian countries (ASEAN), Latin American countries (MCAC) and the countries of Eastern Europe (Transition economy). Our sample covers 44 countries from sub-Saharan Africa, 7 countries (ASEAN), 29 countries (MCAC) and 22 countries in Eastern Europe (Transmission economy). The data, we have collected it, when it is available, for all variables on all countries. All variables have at least 1700 observations (country-year). Therefore, the choice of our sample will be made according to the statistical availability of control variables. However, we will use in our estimate a set of heterogeneous countries. The availability of data forces us to limit the number of countries and the period of analysis. When data is not available for a given country, we remove the country from the dataset before running the panel regressions. In our regional analysis, we drop the variables with incomplete data to maintain consistency across regions.

One of the goals in this section is to study the differences between regions in the relationship between FDI and poverty. We will take into account the four African free trade zones (UNCTAD; 2009) which are the following: (1) the Economic Community of Central African States (ECCAS); The Western Economic Community of African States (ECOWAS); (3) the Authority Intergovernmental for Development (IGAD); (4) the Community of Development of Southern Africa (SADC). Within these areas there are five customs and monetary unions with higher levels of integration. Our sample includes these lists of countries established by regional economic communities (REC)

#### African region African free trade area

Economic Community of Central African States (ECCAS): Angola, Burundi, Cameroon, Republic of Central Africa, Chad, Republic of Congo, Republic Democratic Republic of Congo, Equatorial Guinea, Gabon, Sao Tome and Principe, Rwanda. Economic Community of West African States (ECOWAS): Benin, Burkina Faso, Cape Verde, Ivory Coast, Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, Togo. The Intergovernmental Authority on Development (IGAD): Djibouti, Eritrea, Ethiopia, Kenya, Somalia, Sudan, South Sudan, Uganda. Southern African Development Community (SADC): Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia, Zimbabwe, Namibia, Africa South, Mauritius, Democratic Republic of Congo, Madagascar, Seychelles.

**African customs unions:** Central African Economic and Monetary Community (CEMAC): Cameroon, Republic of Central Africa, Chad, Republic of Congo, Equatorial Guinea, and Gabon. East African Community (EAC): Burundi, Kenya, Rwanda, Tanzania, Uganda. Southern African Customs Union (SACU) is a customs union between the five countries of Southern Africa: Botswana, Lesotho, Namibia, South Africa and Swaziland. West African Economic and Monetary Union (UEMOA): Benin, Burkina Faso, Cote d'Ivoire, Guinea Bissau, Mali, Niger, Senegal, Togo. West African Monetary Zone (WAMZ): Gambia, Ghana, Guinea, Nigeria, Sierra Leone.

**Other emerging regions of the world:** Association of Southeast Asian Nations (ANASE or ASEAN): Brunei, Cambodia, Indonesia, Laos, Malaysia, Burma (Myanmar), Philippines, Singapore, Thailand, Vietnam. Central American Common Market (MCAC): Antigua and Barbuda, Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominica, Ecuador, Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Saint Kits and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, Trinidad and Tobago, Uruguay and Venezuela.

## European transition economy (Mainly the Countries of Eastern Europe)

Albania, Armenia, Azerbaijan, Belarus, Bosnia, Bulgaria, Croatia, Czech Republic, Estonia, Georgia, Hungary, Kazakhstan, Kyrgyz Republic, Latvia, Lithuania, Moldova, Mongolia, Poland, Romania, Slovak Republic, Slovenia, Tajikistan, Turkmenistan, Ukraine, Uzbekistan.

### Definition of the model variables

The main variables we use to explain the impact of FDI on poverty are FDI flows and household consumption expenditure (the indicator of poverty rate). We also use a number of control variables. Our model is completed by a series of variables generally used in this type estimates. All the variables are defined as follows:

**FDI:** The first variable of interest in the model is that of the flows of foreign direct investments as a percentage of GDP, they are defined as the flows of capital by which a company in one country creates or develops a subsidiary in another country. Few empirical studies have shown the existence of a positive impact between the flows of FDI and poverty. For this, we choose the ratio of net inflows of FDI per relative to GDP as a measure of FDI. Foreign direct investment promotes economic growth and growth is a necessary condition for the reduction of poverty. These studies generally have focused attention on the indirect impact of foreign direct investment on reducing poverty through growth. Ucal in (2014) examined the relationship between foreign direct investment and macro-level poverty reduction in countries in development. The results show that there is a statistically significant relationship between FDI and poverty and it is evident that FDI reduces poverty in developing countries development.

**Poverty (P):** This is the dependent variable of our model; it is expressed by per capita consumption expenditure of households and calculated on the basis of World Bank Group data. The literature has used several measures to assess the progress of countries towards improving well-being, including GDP per capita and the indicator of the incidence of poverty. On the one hand, GDP per capita is widely used; it captures only one dimension of well-being: the economic dimension. This poses the problem that poverty is a multidimensional phenomenon and that well-being depends on various factors, it not only depend on the economic factor, such as healthcare, education and other factors. On the other hand, the incidence of poverty is a measure overall well-being in a country because it takes into account all aspects of a life individual (health, education, access to basic services, food, etc.).

### We also use a number of control variables

**Control variables:** To improve our empirical analysis, we also consider three sets control variables:

- a) Economic and political variables
- b) Control variables the business environment and c) political risk variables.

These variables are the following:

The economic and political variables are:

**GDP per capita:** This indicator measures the annual growth rate of GDP per capita inhabitant. Several empirical studies, (for example, have shown that economic growth and poverty reduction are indeed strongly and positively correlated. Dahal, Nepal and Aryal examined the crucial relationship between economic growth and the reduction poverty in developing countries.

**The ratio of total debt (Debt/GDP):** it is measured by the total debt compared to GDP. The effect of external debt on a country's poverty is crucial. The studies earlier studies focused on the debt linked to the relationship between debt and growth or on the growth and poverty reduction but few studies of the link between debt and poverty reduction. According to Rina and Benedict, the heavy debt service absorbs funds that could be allocated to essential anti-poverty spending and divert public investment resources.

**Official development assistance (AIDE):** as a percentage of GDP, it represents disbursements of loans and grants on concessional terms (excluding reimbursement of capital) and grants by public bodies of the organization for

cooperation Development Committee (OECD) meeting in the Development Assistance Committee (CAD).

**International remittances (TRANSF):** as a percentage of GDP, they include current transfers by migrant workers and wages and salaries earned by non-resident workers. They are also defined as transfer's private flows of migrant workers who reside in the host country for more than one year, to beneficiaries in their countries of origin. There is a very limited empirical literature on the macroeconomic impact on poverty. However, recent fund studies find more evidence of the positive impact of remittances on poverty reduction. A World Bank study, Adams and Page (2005) showed that a 10% increase in official international remittances will lead, on average, to a decrease of 3.5% from people living in poverty. Likewise, the IMF study (2007) found that, on average, a 10% increase in the share of remittances in a country's GDP is associated with about a 1.5% decrease in the poverty workforce and a 1.1% decrease in the poverty gap.

**Government public expenditure ratio (GS):** it is measured by the share of total government consumption relative to GDP. Theoretically, this indicator positively affects poverty reduction. Indeed, a higher level of government consumption should translate into poverty reduction. This variable is also used to capture the size of government. The theory of endogenous growth emphasizes that government spending can act positively on growth, by stimulating demand for goods and services, thus leading to increase of production and growth. But these expenses can have negative effects when the increase in public spending leads to an increase in the supply of money. The choice of this variable results in the fact that it can be as representative of the role as can play the state in the process of accumulating economic growth and reduction of inequalities.

**Inflation (INF):** it is measured by the percentage change in the deflator of the GDP, which reflects the percentage increase in the consumer price index (CPI). This is the variable that represents macroeconomic policy. The choice of this variable is legitimacy through the importance of adopting an adequate macroeconomic policy within the of a foreign direct investment policy. It is introduced into the model to capture the impact of stabilization on poverty. Inflation is an aggravating factor in the poverty because it has a negative impact on the real value of heritage and on power purchasing household income. The poor tend to have enough wealth liquid, so in relative terms they will be more affected by inflation.

**Education variable (Education):** it is measured by the percentage of secondary schooling. The theory of endogenous growth suggests that there is a positive relationship between human capital and economic growth. The studies carried out by pointed out that the level of education was a important determinant of economic growth. Investment in human capital improves the productivity of individuals and their well-being. In our study, we chose education and specifically the gross enrollment rate in secondary education as human capital indicator. The gross enrollment rate in secondary education represents the number of students enrolled in secondary education, regardless of their age, expressed as a percentage of the total population of individuals belonging to the age group corresponding.

**Degree of openness (OUV):** it is measured by the total of exports and imports to GDP; it is included in our model as a variable explanatory. Always within the framework of a macroeconomic policy adequate to a system financial development promoting economic growth, it would be more judicious to start with a policy of opening up to external trade. FDI entries are supposed to increase the competitiveness of countries' exports. As exports increase investments, they will have a multiplier effect on GDP.

The variables of the business environment is made up of all the variables following:

**Financial market development:** In our work, we examine whether the economies with a developed financial system can benefit from FDI flows and therefore if they have a role in poverty reduction. It is measured by the total credit by the financial intermediaries to the private sector relative to GDP. The empirical literature uses generally the ratio of domestic credits granted to the private sector to GDP.

Hermes and Lensink studied the role that the development of the financial system plays in strengthening the positive relationship between FDI and economic growth. Foreign direct investment helps develop financial markets, leading thus to economic growth. Lack of access to financial services is one of the most important factors behind the persistence of poverty, more recently; the researchers have shown that financial development can be beneficial, particularly for the poor, thereby reducing income inequality.

**The interactive variable between FDI and financial development (FDI, DF):** for see if economies with a developed financial system can benefit from the flow of FDI. It is necessary to study the impact of the interaction of these variables with FDI on the reduction of poverty.

Political risk variables (Freedom House): among the most commonly used by academics and those in the political community and society civil are the indicators proposed by Freedom House, such as political law measures (DP) and civil liberty (LC). These two Freedom House indicators have the advantage of being available annually for several countries over a long period. They include two variables obtained from Freedom House.

Les variables des risques politiques comprennent deux variables obtenues à partir de Freedom House:

**Droits politiques (DP):** Qui mesurent la liberté pour l'activisme politique.

mesure la jouissance des libertés civiles dans les différents pays, cet indice est estimé par Freedom House.

## Empirical analyzes: Estimation method

**Preliminary tests:** After performing the main hypothesis tests necessary for estimating static panel, a series of usual econometric tests will be carried out on all models and estimated variables. These are, first of all, the stationarity tests, bivariate collinearity and multivariate collinearity. Then we move onto the presentation of the main results obtained, their interpretations and discussions by comparison to previous studies.

**Stationarity tests:** Recall that to test the stationarity of the panel data, we can use the first generation stationarity tests. The first generation tests concerning panel data are tests by Levine and Lin. That being said, it is important to point out that for these first generation tests, they are only applicable on cylindrical panels, i.e. without missing data; this is the case with our variables. So using M. H. Pesaran, we note that the majority of the variables are all stationary in level. In Pesaran and Shin and Levine and Lin tests show the presence of a unit root for the majority of variables.

## Study of multi-collinearity between independent variables

Before moving on to the estimation of linear regression models, we judged useful to first test the existence of a multi-collinearity problem at the data level, in order to obtain efficient estimators. Subsequently, we distinguish the multi bi-varied collinearity and multi-varied multi-collinearity. The problem of multi collinearity bi varied arises when two independent variables are strongly correlated, while the Multivariate multi collinearity arises, if several independent variables are correlated. Recall, first of all, that to test the bivariate correlation, the limit drawn by Kervin is 0.7, while the limit drawn by Kennedy is 0.8. The results of Tables 1 and 2 announce that the different correlation coefficients are lower than the limit traced by Kervin, 0.7. Which implies the absence of bi-varied multicollinearity between the different explanatory variables?

## Hausman method: fixed and random effect

The estimation of our econometric model was carried out using the software STATA 12. The objective of this work is to examine the financial development channel, the society and external financing and the other variables through which FDI can reduce poverty. We determined in the second and the third chapter a theoretical and empirical relationship between foreign direct investment and poverty, in presence of several variables. The model estimate is based on panel data.

To perform the regressions, two solutions are available: a fixed effects

estimate (FEM) or in random effects (MEA). Before getting into the discussion, estimate analysis, we explain why the study is done with panel data. In other words, the countries studied are homogeneous? The F-test statistic often used to examine the homogeneity of countries.

(Prob super  $F = 0.0000$ ). Hausman introduced a test of specification of effects individual which makes it possible to discriminate between MEF and MEA.

The Hausman test makes it possible to distinguish whether the model is fixed effect or random. It is a question of performing the regression first on the fixed effects model, save the result and then performs the estimation on the random effects model. The test Hausman specification allows us to test which of these two hypotheses is appropriate to data. If the probability of the test is less than 10%, then the fixed effects model is prior to the random effects model. If, on the other hand, the probability of the test is greater than 10%, this does not allow us to differentiate the fixed effects model from the effects model random.

## Comparative study between regions

Having studied the effect of FDI on poverty in Africa and other regions, we let's move on to our third research question: (3) are there any differences between Africa and other regions of the world on the role of FDI in poverty reduction? That is to say does FDI have a greater impact on poverty in poor countries than in rich countries? For example, the relationship between FDI and poverty reduction is positive and significant for the countries of sub-Saharan Africa and it is not significant for the countries from Eastern Europe (Transition Economy), Asian countries (ASEAN) and American countries Latin (MCAC). In this section, we will try to test if this effect will remain the same in rich countries than in poor countries.

To answer this question, we consider three regions outside Africa: the countries from Asia (ASEAN), Latin American countries (MCAC) and Eastern European countries (Transitional economy). Levin's test results show that all variables are stationary. The study of the specificity of the estimated models validates the use of random effects models in Asian region and Eastern European countries and fixed effects for the Latin American region. According to the results of Table 1, the null hypothesis of homogeneity, suggests that the panel data method should be used.

Regarding the effects of FDI on the incidence of poverty, the results shown in Table 1, shows that the coefficients are positive and significant for the three groups of countries in Africa (sub-Saharan Africa), Asia (ASEAN) and Latin America (MCAC) but are not significant in Eastern European countries (Economy of transition). We find a strong direct positive effect of FDI on poverty. The positive impact noted for the whole region could be a consequence of the growth economic, through the creation of more jobs for the poor, the accumulation of human capital and the increase in tax revenues of countries, allow them to finance development programs. Klein, Aaron and Hadji Michael examined the link between FDI and poverty reduction and argue that since economic growth is a key factor in poverty reduction, FDI can benefit the poor, if it stimulates economic growth. Thus, an increase in the level of FDI of 1 point in Asian countries, increases household consumption expenditure by 0.676 and therefore, poverty reduction. Indeed, the equality of income distribution in Asia is a decisive in poverty reduction. Which suggests that the most effective method to reduce the poverty rate is certainly the reduction of inequalities by means of a better redistribution of wealth?

It is clear that economic growth is a central requirement for a reduction lasting poverty. In East Asia in general and several ASEAN countries, in particular, rapid growth has been accompanied by falling poverty levels mainly it appears through the mechanism of the labor market, that it must be supplemented in some cases by relatively heavy investment in education and development of human capital in general. Kakwani and Pernia decomposed the causes of poverty reduction such as growth and income redistribution.

Warr found that for six Asian countries, including Thailand, Indonesia, Malaysia and the Philippines, per capita income growth explains about 40% of the poverty reduction (defined as a decline in the poverty index). In ASEAN,



where FDI has played a particularly important role in growth, its consequences on poverty may differ from that elsewhere.

As for the effects of FDI on poverty reduction in Latin America. We can see that there are positive and significant effects. This result goes back to the work theoretical assumptions that FDI is conducive to poverty reduction. Indeed, with a 1 point increase in FDI, household consumption expenditure increase by 0.445 point. Regarding the effects of GDP per capita on the reduction of poverty, the results show that there is a negative, but not significant, relationship that this or the sample studied except Africa. Reading the results of the model reveals that the human capital has a negative effect on the poverty rate in the entire sample except MCAC, a positive effect.

They finally established that the impact of the stock of FDI on poverty varies between countries. Calvo and Hernandez have shown that the effect of FDI on poverty varies according to the countries. Koc, showed that the poorest individuals receive a lower share income generated by FDI than the wealthiest individuals in these countries. Ucal in a showed that FDI reduces poverty in developing countries.

Data collected in Latin American countries support the idea of Goldstein and Quenan have argued that the trade integration efforts of these countries over the past fifteen years, have helped attract foreign direct investment (IDE), to establish the legitimacy of democracy, to reduce social tensions between and inside countries, and collaborate on common projects to help them achieve integration complete of this region of the world. The main idea is: if the integration is not a miracle solution, it is at least part of the reform process and a means effective incentive to sacrifice national interests on the altar of regional integration. The investors are also concerned about the smallness of the markets and the lack of progress in terms of economic development and poverty reduction.

However, once the IDE operates in a foreign country, it usually exercises a huge impact on well-being and poverty reduction in these countries. For example, FDI in resource research tend to generate less job creation effects, though it is capital intensive, such as the pursuit of natural resource FDI. Labor-intensive FDI, such as low-skill manufacturing, tends to generate high level of employment for the host country. In this case, FDI in search of markets and efficiency research, on the whole, tend to affect the low-income host more than the IDE of resource research. Regarding the impact of FDI on reducing poverty, it is considered to be different depending on the type of FDI and the income group of beneficiary countries for example, in the countries of sub-Saharan Africa, the technology accumulated is rather rare, it tends to target the IDE of finding resources at a time natural and non-natural resources. For FDI in resources natural, the effect of job creation is small, but it generates significant income for the state safe that can be used for national development, including the infrastructure. In terms of FDI in the labor-intensive manufacturing sector, the effect of job creation is great.

### **FDI and governance: strengthening poverty reduction in through the interaction between FDI and governance**

To understand the complex role of FDI and governance in reducing the poverty, we need a model that helps organize our thinking about reducing poverty; such a model should show all the possible interactions and the feedbacks between FDI and poverty, and the relationship to governance. This section exposes the research model to be tested in this study. First, we present the theoretical relations of the model to be used. We will then proceed to the description of the specifications of this model.

### **Relationship between governance, FDI and reduction of poverty (dynamic panel) 4-3-1-The Generalized Moments Method**

**Panel Estimator of Arellano and Bond (1991):** The approach of Arellano and Bond consists in putting the equation to be estimated in first difference in order to eliminate the individual effect and to use the lagged values of explanatory variables as instruments.

We have:

$$Y_{it} = Y_{it-1} + x_t + u_{it}$$

The problem with the Arellano and Bond method lies in the weak correlation of the instruments with the model variables which causes a lack of robustness of the estimates obtained. However, Arellano and Bover, then Blundell and Bond, added an additional hypothesis, namely that the differences first of the instrumental variables are uncorrelated with the fixed effects. Allowing introduce more instruments and significantly improve efficiency. This allows also coming up with two equations, the original equation and the transformed one to which we give the name of the system GMM. From a simulation study, the authors show that the use of this system of equation results in estimators that are more efficient than those of the Arellano and Bond method.

### **The estimator of the system generalized moment's method**

The 'system-GMM' estimator developed by Arellano and Bover, consists of estimate a system of equations (in each period) specified in level and first difference. This is how we are going to use the generalized method of moments (GMM). The estimator obtained from this method has several advantages because it is robust to the wrong specification of the model insofar as its derivation does not require hypothesis on the particular distribution of residuals. He is closer to the relationship theoretical because this estimator is chosen so as to minimize the weighted distance between the theoretical values and observed values. Only this estimator can produce biased coefficients for small samples. To remove this limit, we will retain the system GMM method which simultaneously estimates the first difference equation and the equation in level. Thus, the potential existence of a (sampling) bias of GMM estimates in first difference in our study led us to choose the system GMM estimator.

An endogenous variable is both explanatory and explained. There are several sources main endogeneity, the most important of which are: omission of variables, errors measures and selection bias. To remedy this problem, we have used the dynamic panel method and more precisely the method of moments generalized on a dynamic panel from Blundell and Bond. The method of moments generalized allows the endogeneity problem to be solved by the use of a series of instrumental variables which consist of the lags of the variables. This use of lagged variables has the advantage of this method over other methods of instrumental variables. The latter require a determination of variables instrumental which must be correlated with the explanatory variables and not correlated with the disturbances and therefore with the variable to be explained. But the problem of the generalized moments lies in the absence of any theoretical basis in the determination of instruments. The method of Blundelle and Bond is based on and follows the method by Arellano and Bond, That's why we start in the following by developing the latter. Then, we will detail the contributions of the method of Bulundelle and Bond. The system GMM estimator performs better than the first difference one.

In order to test the validity of the instruments, we use two tests: (i) the test of Sargan (ii) the test for the absence of autocorrelation of the disturbances of first and second-rate. The Sargan test is used to ensure that there is no correlation between instrumental variables with the perturbations of the model. Under the hypothesis  $H_0$ , the variables instrumentals are not correlated with the perturbations of the estimated model. If we accept  $H_0$ , the instruments are valid and the estimates converge, If we refuse  $H_0$ , the selected instruments are not valid. An autocorrelation test is also necessary to ensure the validity of the instruments. Our econometric approach will start with the estimation of the different models by the method of Blundell and Bond then, the validity of the instruments used will be verified by the Sargan test and by the 1st order and 2nd order autocorrelation tests.

To empirically study the effect of governance and FDI on poverty, he needs to specify a model that allows us to capture the interrelationships that exist between FDI, governance and poverty. In particular, we need a model that allows the governance with FDI included as a determinant of the quality of governance. We will conduct our own study econometric to see if the quality of governance affects the impact of FDI inflows on poverty reduction.

### **Model, estimation method and empirical results of the regression in the impact of FDI and governance on poverty**

To study the impact of foreign direct investment and governance on the

poverty reduction, we hoped to keep the same sample as before, in African countries (sub-Saharan Africa), Latin American countries (MCAC), Asia (ASEAN), and the countries of Eastern Europe (Transitional economy). We will use panel data for the period 1996 and 2012. We will adopt a model based on the theoretical framework of Gohou and Soumare, the model is as follows:

$$P_{it} = a + b_1 P_{it-1} + b_2 PIB_{it} + b_3 IDE_{it} + b_4 TRANS_{it} + b_5 AIDE_{it} + b_6 DETTE_{it} + b_7 OUV_{it} + b_8 INF_{it} + b_9 G_{it} + b_{10} GOV_{it} + b_{11} (IDE.GOV)_{it} + b_{12} EDUCAT_{it} + b_{13} CRED_{it} + \varepsilon_{it}$$

The estimation of our econometric model was carried out using the software STATA 12, using system GMM. With the dependent variable which is poverty measured by household consumption expenditure denoted by ( $P_{it}$ ). Each time, the instruments of the variables obey the method developed by Roodman, creator of the Stata command program appropriate to the Arellano and Bond method. This command is known by `xtabond2`. It allows by default to obtain the Sargan test with the null hypothesis of the exogenous nature of the instruments. To remedy the problem heteroscedasticity, we will use in our study the robust evaluation (method of Woodridge). In this case, Stata reports the J stat from the Hansen test instead of the Sargan, with the same null hypothesis as the Arellano and Bond autocorrelation tests at orders 1 and 2. The null hypothesis of this test is the absence of autocorrelation and it is applied to residuals indifference. The AR (2) test is the most important because AR (1) usually rejects the null hypothesis.

The generalized method of moments is the most efficient of the variable methods instrumental, it seemed judicious to us to estimate our model by this method. Therefore, we adopt the same estimation methodology as before. We note that the endogenous variable is poverty measured by consumption expenditure Household. AR (1) and AR (2) statistics represent autocorrelation tests of Arellano and Bond of order (1) and order (2).

**The poverty equation:** The first equation explains the poverty rate. The estimation of this equation is the ultimate goal of our work. Indeed it this involves determining the direct effects of each endogenous or exogenous variable on poverty.

The analysis of the poverty equation consists of two stages. First, our interest goes focus on understanding specific variables, mainly: GDP, debt external, money transfers, and international aid. Second, we will analyze the effects of endogenous variables, namely FDI and governance. The first variable endogenous in the model is poverty which is measured by household consumption over the period (1996-2017). The specification of the poverty equation commonly follows the form accepted in the literature and includes a group of economic variables that have been identified by the empirical literature of the poverty. In addition to FDI and governance, the poverty equation includes five variables. The first variable is economic growth. Many empirical studies have shown that economic growth and poverty reduction are effect, strongly and positively related.

The other four variables capture the impact on poverty reduction. In what concerns the interactions between FDI and governance, the two variables should have a positive impact on poverty reduction, because they have positive externalities that increase the incomes of the poor and the productivity of economic resources. For the money transfer, Anyanwu and Erhijakpor, examined the impact of money transfers on poverty in Africa. The other two variables capture the impact on poverty is development aid and foreign debt.

## Governance indicator variables

- **Representation and participation (Voice and Accountability; ACNT):** measures the perception of the extent to which the citizens of a country are able to participate in the selection of their government, as well as freedom of expression, freedom of association and freedom of the press.
- **Political stability and the absence of violence (Political Stability and Absence of Violence; STAB):** measures the perception of the probability that the government will be destabilized or overthrown by unconstitutional or violent means, including the politically motivated violence and terrorism.

- **Government effectiveness (Government Effectiveness; GEFCV):** measures the perception of the quality of public services, the quality of public training and the degree of independence from political pressures, the quality of policy formulation and implementation, as well as the credibility of the government's commitment to its policies.
- **The quality of the regulations (Regulatory Quality; REQTY):** measures the perception government capacity to formulate and implement sound policies and regulations that promote private sector development.
- **Rule of Law (RLAW):** measures the perception of the extent to which the agents have confidence and respect the rules of the company in particular the quality contract enforcement, property rights, police and courts, as well as likelihood of crime and violence.
- **Control of corruption (Control of Corruption; CRP):** measures the perception of extent to which public power is exercised to obtain an advantage personnel, including large and small forms of corruption, as well as "the capture" of the state by elites and private interests (Table 2).

We present the basic results relating to the associated coefficients to the different control variables used. Secondly, we are interested in results relating to the various variables of interest (GDP, FDI, GOV, and FDI.GOV) and particularly to the most significant results.

## Miscellaneous result

**GDP per capita:** The household expenditure rate is inversely related to its level of GDP per capita. According to our results, there is an effect of GDP per capita on the rate of household spending for the countries of Eastern Europe (Transition economy) significant and negative. The regression results for Eastern European countries show that the GDP coefficient has a negative impact at the 5% level. For the other groups of countries, the coefficient associated with GDP per capita is either negative or insignificant.

**Human capital:** Production requires both machines and labor. As physical capital, human capital plays as important a role in production as the physical capital. In our econometric results, the sign of the coefficient associated with human capital is negative and significant for the group of countries Eastern European (Transitional Economy). UNICEF reports that the quality of Education is a concern in a number of countries in Europe and Asia. Those countries have experienced conflicts that have undermined education and harmed the region with social problems, in general. Real public spending on education has declined in many countries in the region.

**Commercial opening:** Trade openness appears with a positive sign for the Africa sample sub-Saharan. The various econometric studies carried out to test the impact of trade openness on poverty reduction have led to results in general positive. This confirms the theoretical predictions thus predicting the beneficial effects of policy of openness to international trade on poverty reduction. Indeed, an increasing the opening rate by one percentage unit increases the level of household consumption of 0.088 point.

**Debt:** The coefficient of external debt is negative and significant in Asian countries (ASEAN) but it is not significant for the majority of regions. The more a country is in debt, the more likely he is to find himself in financial difficulty because of his obligations under the debt service and the more difficult it is to access financial resources for social spending.

**Development assistance:** The coefficient of development aid is positive and significant in the Europe of East (Transition economy) and negative in Latin America, but it is not significant for other regions.

**Transfers:** The level of international remittances has a positive and significant impact at the threshold of 5% on poverty reduction in Eastern Europe. An increase in transfers makes it possible to increase the rate of household consumption expenditure and therefore the reduction of poverty.

**Public spending:** The coefficient associated with public expenditure is positive and significant for the region of ASEAN. This result is consistent

with the various results of econometric studies carried out to determine the relationship between public spending and poverty. But in the countries from sub-Saharan Africa, it is significant and negative. An increase in public spending by 1 percentage point translates into a decrease in the level of consumption of households by -1.719 percentage point, i.e. the increase in poverty.

## Variables of interest

**Poverty (-1):** The poverty variable (-1) shows very important results. We note that this coefficient appears to be positive and significant throughout the sample. The results of the main regressions for the sample (Sub-Saharan Africa, ASEAN, MCAC and Eastern European Countries) are shown in Table 2. On the basis of results obtained by the system GMM method. In column (1), the poverty variable (-1) remarkably affects the initial poverty level by increasing significantly household consumption in Africa of 0.937. The column (2) shows that initial poverty in ASEAN has a positive and significant impact on reducing poverty. The estimate provides that an initial poverty increase of 1% results in an increase in household consumption of 0.764. The column

presents the model estimate with the MCAC countries the results clearly show that poverty initially positively interacts with the poverty indicator. We can see that the effect of initial poverty resists positively and significantly at 1%. Column (4) presents the model estimate with Eastern European countries. The results clearly show that the initial poverty has a positive and significant impact on poverty reduction.

**FDI:** First, as shown in Table 1, the effect of FDI on poverty is significant and positive in Latin America (MCAC) but not significant in the other samples.

**FDI.GOV:** The results relating to the interactions that may exist between

FDI and governance (FDI.GOV) are quite varied. On the one hand, we find the expected result, the positive relationship between interactions between FDI and governance for the group of sub-Saharan Africa and the countries of Eastern Europe. An increase of 1 point of (FDI.GOV) in African countries generates an increase of 0.582 point. This increase is larger for the countries of Eastern Europe; a raise of 1 point of (FDI.GOV) generates an increase in per capita consumption of households of 0.090 point. For Latin American countries (MCAC), the coefficients associated with (FDI.GOV) were negative but not significant.

The result of the regression in the countries of sub-Saharan Africa indicates that the interaction between the quality of governance and FDI (IDE.GOV) is positive and significantly correlated with poverty reduction. However, governance is found positively related to IDE. This result implies that the factors of governance play an important role in promoting FDI and thus in poverty reduction. And FDI is likely to be more sensitive to the structure of governance. He is also supported by the fact that in sub-Saharan African countries, foreign investors have tended to invest in their own country as long as they have more choices and they tend to invest in countries where the basic economic conditions are in place. On the other hand, the positive impact of the interaction between FDI and governance on the poverty reduction in sub-Saharan African countries can also be explained by high resources (human and physical resources) integrated in this group. The quality of governance is seen as the efficiency of resource management, such as natural resources in sub-Saharan African countries. They are still at a high level, their impact on poverty reduction can also be considered high. However, it means that the quality of government is important for poverty reduction. So, the more resources the country receives, the greater the importance and impact of governance on poverty reduction increases. For Asian countries (ASEAN),

**Table 1.** Results of the panel regression of the impact of FDI on poverty between regions.

Variables	Africa	ASEAN	EUTE	MCAC
FDI	0.06 (1.98)**	0.676 (1.98)**		0.202 (1.41)
GDP	-0.208 (-3.34)***	-0.008 (-0.05)	-0.086 (-1.25)	-0.064 (-0.78)
KH	-0.083 (-1.68)*	-0.424 (-7.73)***	-0.533 (-6.32)***	0.111 (3.05)***
OUV	0.091 (4.53)***	-0.050 (-2.88)***	-0.029 (-1.25)	-0.155 (-6.36)***
Cred	0.072 (1.06)	-0.070 (-2.31)**	-0.074 (-1.92)**	-0.023 (-0.60)
Tx INF	0.014 (1.82)*	0.014 (0.37)	-0.009 (-0.40)	-0.028 (-0.76)
Dette	-0.021 (-4.35)***	0.023 (0.88)	0.002 (0.24)	-0.004 (-0.47)
AIDE	-0.004 (-1.72)*	-0.006 (-1.76)*	0.002 (0.63)	-0.000 (-1.23)
Transfer	-0.246 (-1.81)*	1.804 (9.07)***	0.791 (9.76)***	0.565 (4.35)***
Gs	-0.566 (-5.58)***	-0.292 (-0.93)	-0.37 (-2.63)***	-0.653 (-4.65)***
FDI.DF	-0.009 (-3.33)***	-0.003 (-0.66)	-0.004 (-1.68)*	0.001 (0.47)

**Table 2.** Estimation by the system GM.

Variables	Africa	ASEAN	MCAC	EUTE
Pauvry (-1)	0.937 (5.34)***	0.74 (1.94)*		1.102 (7.97)***
FDI	0.371 (1.42)	-0.574 (-1.40)	0.187 (1.96)*	-0.024 (-0.90)
GOV	2.386 (0.37)	-18.627 (-2.35)**	-1.102 (-1.12)	0.839 (0.98)
FDI.GOV	0.582 (1.81)*	1.144 (1.50)		-0.092 (0.56)
GDP	-0.150 (-0.87)	-0.130 (-0.39)	0.036 (0.37)	-0.188 (-2.83)**
KH	-0.132 (-1.42)	-0.567 (-1.24)	-0.004 (-0.23)	-0.106 (-1.73)*
OUV	0.088 (1.73)*	0.049 (0.53)		-0.013 (-1.25)
CRED	0.198 (1.62)	0.078 (0.76)	0.012 (0.57)	-0.030 (-1.39)
Tx INF	-0.015 (-1.00)	0.241 (1.25)	0.051 (1.24)	-0.002 (-0.38)
DETTE	0.039 (1.34)	-0.154 (-2.10)*	-0.055 (-1.07)	-0.000 (-0.12)
AIDE	0.005 (1.00)	-0.001 (-0.48)	-0.006 (-4.07)***	0.000 (1.87)*
TRANSFERTS	0.480 (1.43)	1.798 (1.39)	0.091 (0.50)	0.227 (2.16)**
Gs	-1.719 (-2.02)**	1.482 (2.17)*	-0.084 (0.98)	-0.043 (-0.41)
ObservationsNbr Individual	650 - 42	112 - 7	432 - 28	287 - 20
Sargan test	6.13 (0.524)	4.87 (0.301)	1.94 (0.379)	23.78 (0.014)
Autocorrelation order 1	-1.64 (0.101)	-1.64 (0.102)	-3.24 (0.001)	-2.49 (0.013)
AutocorrelationOrder 2	1.26 (0.209)	-1.60 (0.109)		-1.60 (0.110)
				0.70 (0.484)

the relationship is significant and negative, while for Latin American countries (MCAC) and countries from Eastern Europe, it is not significant. The results of our regressions.

**L'indice des libertés civiles (LC):** La variable des libertés civiles (LC) est un outil de show that the interaction between FDI and governance has a favorable effect on poverty reduction in poor countries such as countries in sub-Saharan Africa. We can believe that the negative effect of the interaction between FDI and governance on poverty reduction in Asian countries (ASEAN) may be due mainly to a mismatch of the legal environment and insufficient efficiency in the quality of governance. There are thresholds of the nature of governance from which FDI comes to have a positive impact on poverty reduction. We believe that poor countries like Sub-Saharan African countries have managed to reach an FDI threshold.

## Discussion and Conclusion

The long-awaited good quality of governance began to be achieved with an open economic policy aimed at attracting foreign direct investment for function as the engine of poverty reduction. Since the mid-years 1990, FDI firms began to come to developing countries to take advantage of its generous tax policy. The presence of FDI companies not only creates economic benefits such as employment, but it also brings positive changes in institution or governance for developing countries. The presence of FDI does not automatically lead to the improvement of the quality of governance, in fact, it would be more correct to say that these are the problems or the difficulties encountered by the companies FDI that lead to improved governance. Three main results can be retained: (i) the existence of a positive and significant effect of the interaction between governance and foreign direct investment (GOV.IDE) on poverty reduction; (ii) the existence of a positive and significant effect of FDI on poverty; (iii) the existence of a negative effect of governance on poverty.

The main argument of this study was that a better understanding of the contribution of FDI to poverty reduction can only be achieved if the interdependence and complementarity between IDE and governance are taken into account. The role of complementarity between FDI and the quality of governance lies in the determining the contribution of FDI to poverty reduction. The relationship between FDI and governance leads to an indirect effect of FDI on poverty reduction through good governance. The different stages of development in countries tend to have different governance structures and attract different types of FDI. As a result, the effects of governance and FDI on poverty reduction may be different. Also, the question of whether FDI inflows positively contribute to reducing the poverty and development is one of the most fundamental issues in the economy international and development economics. She gains this importance not only from its obvious academic relevance but also its practical implication.

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