

Foreign Direct Investment: A Case Study of Nestle S.A. in Nigeria

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How to cite this paper: Atobatele, O. (2023). Foreign Direct Investment: A Case Study of Nestle S.A. in Nigeria. *Modern Economy*, 14, 825-832.

<https://doi.org/10.4236/me.2023.146044>

Received: April 18, 2023

Accepted: June 27, 2023

Published: June 30, 2023

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Abstract

This study is based on Nestle S.A.'s investment in Nigeria and through this example of foreign direct investment (FDI), the study highlights the reasons multinational firms exist, the roles they play and the impacts they make in our global economy. We present details about Nestle S.A., Nestle S.A.'s investment in Nigeria and the reasons for the investment, its impacts on the Nigerian economy and the ways government policies have affected the strategies of the multinational.

Keywords

Foreign Direct Investment, FDI, Nigeria, Multinational Firms, Nestle Nigeria, Case Study, Developing Economy, Government Policy

1. Introduction

Foreign direct investment refers to investment that firms make outside the country in which they exist. This investment could be by establishing a new firm or by owning a share of an existing firm in another country. Firms involved in foreign direct investment are multinationals and the existing literature shows that many factors encourage multinationals to expand their production activities abroad.

In our world today, data from the World Investment Reports (2019-2021) show that foreign direct investment has increased globally and most of the foreign direct investment flows are absorbed by emerging and developing economies. Many countries and continents now see attracting foreign investors as an important element in their plan to attain economic development and this is most likely because FDI is seen as an amalgamation of capital, technology, marketing and management.

This study presents an example of foreign direct investment in a developing

economy. It is based on a study of Nestle S.A.'s investment in Nigeria and it is aimed at identifying the reasons multinationals exist, the roles they play and the impacts they make in our global economy.

2. Nestle S.A.

Nestle S.A. is a Swiss multinational food and beverage company which has its headquarters in Vevey, Switzerland. The company was established in 1905 by the merger of the Anglo-Swiss Milk Company and Henri Nestlé's Farine Lactee (Nestle Nigeria (2016))¹. Its operations involve the production and processing of baby food, coffee and tea, dairy products, confectionary, bottled water, snacks, frozen food and ice cream. It has grown significantly over the years and began its foreign investment with the acquisition of food production companies such as Crosse & Blackwell (British food production company) in 1950, Libby's (US based canned food company) in 1971, Rowntree Mackintosh (British Confectionery) in 1988 and Gerber (US baby food company) in 2007. When measured in terms of revenues, the company is considered the world's largest food company. It has subsidiaries in over 86 countries of the world and has over 330,000 employees. 44 percent of its sales are in the Americas, 28 percent in Europe and 28 percent in Asia, Oceania and Africa. This study is based on one of its subsidiaries in Africa; Nestle Nigeria PLC.

At the beginning of the 20th century, Nestle S.A. started selling its products in Nigeria through local importers that placed their orders directly with the actively trading British companies in Nigeria (Nestle Nigeria (2011a))². Initially, exports were sporadic but from the 1920s, they became regular. It was during this period that Nestle S.A. decided to establish its office in Nigeria in order to organize the importation and distribution of its products in the country. In 1961, Nestle products Nigeria limited was officially created and so, the first phase of Nestle S.A.'s operations in Nigeria began as a wholly owned subsidiary of Nestle Holdings limited. It was solely involved in the trade and distribution of food products at its headquarters in the Industrial Avenue, Ilupeju Lagos, Nigeria. With the steady increase in sales, Nestlé's industrial presence in Nigeria began in 1971 when the company was encouraged to begin producing part of its bouillon cubes at the Ilupeju factory.

3. Major Expansions and the Reasons for the Expansions

Nestle Nigeria was established in 1961 as a part of Nestlé S.A.'s Central and West Africa Region (CWAR) and it began production activities in 1971 at its headquarters in Ilupeju, Lagos. From that time, Nestle has expanded its operations to other South-western regions in Nigeria. In 1981, it began its operations at its

¹Nestle Nigeria 2015 Annual Report and Accounts (Slide Share),

https://www.slideshare.net/olafusimichael/nestle-nigeria-annual-report-2015?next_slideshow=62268732.

²Nestle Nigeria Fact File. Retrieved from

<http://www.nestle.com/asset-library/documents/library/events/2011-nigeria-factory-opening/nigeria-fact-file.pdf>.

factory in Agbara, Ogun State, Nigeria and during the following years, Nestle added major extensions to this factory in pursuit of efforts to locally source for raw materials. By 1991, the company changed its corporate name to Nestle Foods Nigeria PLC and it was almost completely integrated into the local economy as most of the raw materials and nearly all the packaging materials were sourced domestically.

By 1995, Nestle commissioned another factory in Agbara and the agro-allied factory was conceived as a regional production center for the production of an essential ingredient in the manufacture of Nestlé's range of culinary seasonings. The new factory was the result of intense efforts of research to develop a new technology process, specifically adapted to satisfying the need of local consumers and generate export flows to the West-African sub region (Nestle Nigeria (2014))³.

Having fully utilized its large expanse of land at the Agbara location and buoyed by strong consumer demand, Nestle embarked on the construction of a new factory near Sagamu, Ogun State which was inaugurated in 2011 (Nestle Nigeria (2011b))⁴. The company expanded its operations in order to increase its capacity and meet the surging demand of consumers especially in new markets and regions that had not been reached by its distributors and through this, it was able to expand its share of the Nigerian market.

Following the expansion of production activities to different locations, the number of employees yearly employed by Nestle Nigeria also increased. In 2003, Nestle Nigeria's work force comprised of 1164 employees but today, the number of employees has increased to about 3300. Sales also increased as the company expanded its operations in the Nigerian market. At 1999, the company recorded sales of N7,725,000 (about \$51,500) but by the year 2013, the company recorded sales of N133,084,000 (about \$831,775). The trend of sales and employment are shown in the **Appendix**.

4. Nestlé's Operations in Nigeria Today

Over the years, Nestle Nigeria has expanded its operations to involve the processing and production of Nestlé's food and beverage products. The company operates majorly through two business segments; The Food and Beverage segments. The food segment involves the production and distribution of cereals, confectionaries and culinary. The beverage segment involves the production and sale of table water and beverages. It employs about 3300 people in Nigeria and a larger percentage of the workers are employed in the factory while a smaller percentage of the workers provide skilled labor. It has 3 major factories and several distribution centers in Nigeria.

³Nestle Manufacturing Operations in Nigeria. Retrieved from <http://www.nestle.com/asset-library/documents/library/events/2011-nigeria-factory-opening/manufacturing-operations-in-nigeria.pdf>.

⁴Nestlé opens N12 billion factory in Ogun State. Retrieved from <http://www.nestle.com/asset-library/documents/library/events/2011-nigeria-factory-opening/nestle-nigeria-press-release.pdf>.

5. Sources of Inputs

Nestle Nigeria makes use of Agricultural products such as cocoa, soya bean, maize, palm olein, sorghum and other raw materials for its food and beverage products (Nestle Nigeria (2021)). Currently, about 75 percent of these raw materials are sourced domestically. The company purchases massive tons of raw materials from the local farmers in Nigeria and this rich use of local inputs helps create a market for the local farmers, stabilize prices for them and promote agricultural practices in Nigeria.

6. Location of Sales

Nestle Nigeria's products are distributed and sold across six major regions in Nigeria; Lagos, South-west and South-East Nigeria, North-west and North-East Nigeria and the Federal Capital Territory. Nestle Nigeria also makes distributions to other regions in Africa and in Europe. In the Nigerian market, the distribution system has the widest penetration in the west although it also accesses other regions in the country. Generally, a larger percentage of Nestle Nigeria's sales are within the Nigerian market and a smaller percentage are to other West African sub-regions and European regions. About 20 percent of Nestle Nigeria's bouillon cubes are exported to the West-African regions and about 5 percent to Europe and other regions. The main reason Nestle Nigeria's sales are mostly within the Nigerian market is because of the high local demand for Nestle Nigeria's products, the effects of trade policies, political instability and exchange rate fluctuations.

7. Reasons for the Foreign Direct Investment

Apart from the steady increase in sales, some of the other factors that encouraged Nestlé's Industrial presence in Nigeria include; the favorable demographics of the Nigerian market that provide sustainable demand for Nestlé's product, the stability of Nigeria's currency, the purchasing power of the Nigerian population, the petroleum boom in Nigeria in the 1970s, the increasing population of the country that showed the existence of a large market for consumer goods coupled with the increasing adoption of western diet and the nature of Nestlé's products. The Nestle S.A. management in Vevey, decided to integrate its activities gradually into the Nigerian economy in order to progressively substitute imported goods by locally produced goods. Also, based on the proximity concentration trade-off, it was more profitable for Nestle to invest in Nigeria as the gains from avoiding trade costs outweighed the costs of maintaining capacity in the Nigerian market.

8. The Form of the Foreign Direct Investment

Horizontal FDI involves establishing a subsidiary in a host country that essentially replicates the operations of the original firm (Kersting & Wynne (2008)). This form of investment is usually chosen when the aim for going abroad is to

access a new market. Based on this submission, Nestle S.A.'s investment in Nigeria can be characterized as horizontal FDI for the following reasons;

- The main aim of investing in Nigeria was to access the large market size of Nigeria and meet the demands of consumers.
- The production activities are not divided between the Nestle S.A. Switzerland and Nestle Nigeria. Instead, the factory in Nigeria replicates the source firm's production activities.

9. Impacts of Nestle S.A.'s Investment in Nigeria

Nestlé's presence in Nigeria has resulted in multimillion naira investments with the construction of ultra modern plants and distribution centers at several locations in Nigeria. The plant at Sagamu is the largest in the Asia, Oceania and Africa region in terms of the production of bouillon cubes. The company's presence has supported the increase in living standards through employment generation and infrastructure improvements.

10. Positive Impacts of the Multinational

1) Impacts on the local consumers: Nestle provides consumers with a wide variety of nutritious products that are readily available at reduced costs relative to the costs of importing these goods. Through its creating shared value scheme, Nestle implements nutrition education programs to promote good nutrition practices among consumers.

2) Impacts on the local suppliers of inputs: The Company reaches out to its local suppliers of inputs by organizing various programs through which they provide advisory services on farming practices, harvesting techniques and other crop handling processes. Through these programs, the company has helped improve the livelihood of the local farmers for the production of its food and beverage products.

3) Contributions to GDP: Through its presence and operation in Nigeria, it has contributed to the growth of GDP and has been a source of tax revenue.

11. Negative Impacts of the Multinational

1) Although, Nestle helps improve the wellness of the Nigerian community and improve the livelihood of the local farmers, it also jealously guards its technological know-how by refusing to make use of competent staff in Nigeria but brings in expatriate staff to work in the country. A larger percentage of Nestle Nigeria's workforce consists of unskilled laborers. These workers are at the last rung of the production process and this prevents Nigerians from learning the intricacies involved in the production of the goods.

2) Wage premium is considered a means of preventing the local firms from hiring the workers of the multinational firm and gaining its superior technology (Glass & Saggi (2002)). At Nestle Nigeria, the few workers that are employed as skilled laborers are highly paid when compared with the workers in the local

companies and this serves as a means of preventing local firms from hiring Nestlé staff. A study Led by Doyin Soyibo (an economist and dean of the Faculty of Social Sciences at a University in Nigeria), discovered that Nestlé employees earn more than the average workers in the manufacturing industry and their salaries increase faster than the industry norm. More than 75 percent of the workers said that if given the choice to change jobs, they would decline.

12. Impact of Government Policies on the Multinational

Policies and strategies of the Nigerian government towards FDI are formed by two main goals; the need for economic independence and the realization of economic development. Before 1995, Nigeria's FDI policies were rigid and they hindered the access of multinationals to the Nigerian economy but in recent times, the government policies have been more relaxed and laws which had previously hindered multinationals have either been modified or revoked. The Nigerian government has tried to provide foreign investors like Nestlé S.A. with a healthy business environment and with generous tax incentives. Some of the policies that have favored Nestlé in Nigeria include:

Granting of re-investment allowance: This is given to production companies that incur capital expenditure in attempt to expand production capacity and it is aimed at encouraging the reinvestment of profits. Nestlé has benefited from this policy because through this, it has been able to expand its operations within the large Nigerian market.

Export Incentives: Export incentives are provided for existing multinationals like Nestlé and other local firms. There is also an export adjustment fund scheme which serves as supplementary export subsidy to compensate exporters for the high cost of local production arising mainly from infrastructural deficiencies, and other negative factors beyond the control of the exporter. This has encouraged Nestlé to achieve its aim of exporting to the West-African sub region and other regions.

13. Limitations of the Multinational

Some factors have limited the rapid growth and expansion of Nestlé Nigeria. They include:

- The Volatility of the Nigerian currency;
- Menacing security challenges in the Northern part of Nigeria;
- Competition with local firms and other multinationals in the industry;
- Poor state of infrastructure (e.g. bad roads and inconsistent power supply);
- Changing government policies.

Despite all these factors, Nestlé Nigeria has thrived and has experienced growth through the years.

14. Summary and Conclusion

This case study presents an example of horizontal FDI in a developing country.

It highlights the reasons for FDI, the impacts of multinationals and the ways government policies affect the strategies of multinationals.

This FDI can be considered successful because despite economic fluctuations and macroeconomic headwinds, Nestle has been able to niche a nest for itself in the Nigerian market as every household in Nigeria purchases at least one of Nestlé's products and sales increase yearly despite economic downturn.

Conflicts of Interest

The author declares no conflicts of interest regarding the publication of this paper.

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Appendix

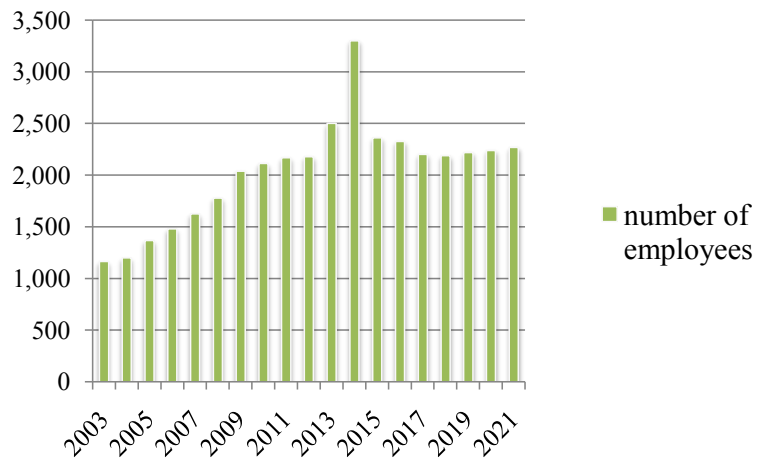


Figure A1. Trend of employment⁵.

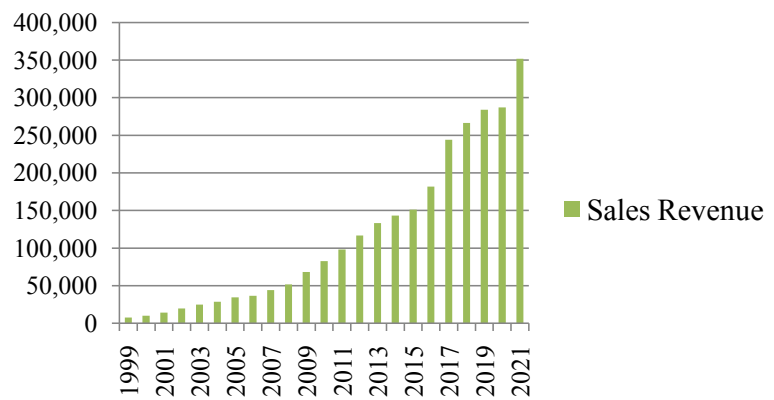


Figure A2. Trend of sales.

⁵Nestle Nigeria Plc 2021 Annual Report and Accounts. Retrieved from <https://www.nestle-cwa.com/sites/g/files/pydnoa346/files/2022-06/NESTLE%20NIGERIA%20PLC%202021%20ANNUAL%20REPORT.pdf>.