THE FELDSTEIN HORIZOKA PUZZLE AND CAPITAL MOBILITY:
EVIDENCE FROM SUB-SAHARAN AFRICA

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ABSTRACT

Capital mobility is the ease with which financial flows can occur across borders. Knowledge of its prevalence is beneficial for not only economic but also political reasons. We test the degree of capital mobility by using the Feldstein-Horioka framework. Unlike other studies, we divide Sub-Saharan Africa into resource-rich, coastal and landlocked samples. The fixed effects estimator, the Swamy-Arora random effects Generalized Least Squares estimator and the random effects Maximum Likelihood estimator, are used. Three main results come to the fore. First, that comparatively when the whole sample is used, the saving coefficients are lower than for those of developed countries reported in literature. Second, while saving coefficients for sub-samples are generally in line with those obtained for the whole sample there are marked differences in the sub-samples. Landlocked countries have the lowest saving coefficients and coastal countries have higher rates than for both landlocked and resource rich samples. While the Feldstein-Horioka puzzle is generally viewed as high saving-investment correlations in countries with well-developed financial markets, we conclude that in Africa, the puzzle is that of low saving-investment correlations in sub-samples with poorly developed financial markets.

Keywords: Saving-Investment Correlation, Feldstein-Horioka Puzzle, Fixed Effects Model, Random Effects Model.

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