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Impact of Globalization and Foreign Direct Investment on Economic growth: Empirical evidences from Pakistan

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Abstract

Globalization and FDI an important input to future economic growth and in general they are regarded as a positive energy for improved quality of life, acceleration of economic growth, efficient allocation of resources and great productivity improvement. Whereas, anti-globalization site squabbled that it adds to poverty and leads to worsening in the distribution of incomes. Pakistan also embarked on a path towards liberalizing like many other developing countries, its trade and investment with the expectations that it will stimulate economic growth. This study examines the impact of globalization and FDI on economic growth in Pakistan using ARDL bound testing technique over the period 1980-2016.

Keywords: Globalization• Economic growth• Foreign direct investment • ARDL (Auto Regressor Distributive Lag)

Introduction

Rodrik et al. defined that the significance of globalization can be to different people to different discipline. Globalization or liberalization is the procedure of development of global market production and as well as factor of productivity. Globalization exist in an economy of free mobility of merchandises and services, transfer of advanced technology, mobility of workers which has brought and made them strongly the advanced economies closer to one another. The fundamentals of globalization include free movement of services and goods in one place to another, transfer of modern technology in developing countries, flow of capital, and increase infrastructures for development which has brought established economies made the more powerfully integrated. Many developing countries have benefited that's the best technique of development and growth of global marketplace in products as well as factor of manufacture through globalization and liberalization. 'Globalization' is much more than the growth, increase in trade within two countries and also enhance factor of production. Kurtz proposed that Globalization is not a one-direction phenomenon and different elements of globalization, like trade openness and FDI effect the economy. Globalization creates struggle to global investment while just in time manufacture may increase firm exposure to strike and rise the bargaining power of worker. It has various effects on working class objection because the impact of globalization on working class group and objection tend to be arranged around the familiar "race to the bottom" versus "race to the top" [1,2]

According to Obstfeld and Taylor, All over the world there is a large heterogeneity in globalization within the passage of time across countries, economic and graphic regions. With the passage of time Globalization in changed part of the world is changed. For example economic globalization change also sparks the culture change in economic purpose. The services of homogenous worldwide culture attempt to extent across countries. Political environmental also change global economy and its effects quickly changing its resemblance the downfall of Soviet Union role to the development integration of the nation [3].

Tanzi defines that in the process of globalization Government plays a main role to the help of the country adjustment. The current stage of trade liberalization tends to decline the degree of efficiency independence for countrywide government to purse their own goals of growth, social equality and political stability in an economy. Countries are well educated and full information about present polices and are not bounded by past polices and have more information of income distribution and will be able to benefit from globalization [4].

According to Murillo and Schrank, Globalization is a multi-faceted procedure can be predictable have different effects on protest in different markets, like as labor right, FDI and international trade in different organization. Globalization factors at the same time, such as increase and support of labor based gatherings; significantly impact the rise in labor and secure political protection from greater experience to market services. Globalization is also increasing the efficiency of utilization of resources and attaining the economic growth the highest level from all kind of aspects. Main goal of globalization is to provide is higher completion of organizations with lowest cost and gain greater productivity of goods and services from advanced to emerging countries. This approach is increased of higher utilization of resources and new creation of development and investment chances by opening up additional market and access raw materials in fewer developing countries [5].

According to Feenstra and Hanson FDI is an engine of the adoption of new and current technology, and in this way the extra required of the work force to work the new applied skills guide that it may also affect the skilled labor increase. The productiveness of developing country increased, in the equal way the demanded of the labor also increase. In conclude that in growing nations the more labors are higher to work the poverty reduce. There is a profitable relationship. FDI have large productivity, more labor availability, the wages of the host labor are increased. In this way extra labor pressure are prepared to work and unemployment reduce [6].

According to Investopedia, Globalization is increasing substantially in industrial and financial sectors and is also producing new jobs for both developing and under emerging countries and industrialized. Both industrialized developed and emerging countries have much expectation in this procedure. In developing countries integration and globalization have initiating industrialization rise the rate of mechanization for developing nations and they are benefited. According to Mapsofindia from theoretical aspect, trade ensure allocation of different resources that's has a good

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effect on the economy. This specialization in the procedures leads to superior productivity. As a result if only the resources are full used in host countries increase economic growth and benefits. The enhancing of foreign investment and MNCs is a better suggestion of increasing rank of Multinational corporations for overall economy [7,8].

Markusen and Venables the more capital flow can increase host international location as productivity and GDP growth rate, free supply of technology and capital and enhance enterprise productivity. FDI increase more production, superior knowledge and R&D would also impact economic growth and GDP per capita. This study relates and influence on economic progress and is an important indicator of FDI flow. In an economy increasing more FDI flow would generate more economic growth [9].

Objectives of the study

This research is built on the following purposes:

- To observe the impact of globalization and economic growth in Pakistan.
- To observe the impact of FDI, globalization and economic growth in Pakistan.
- In the light of experimental findings to provide policy implication for Pakistan.

Research question

This research is based on the following questions:

1. Does globalization affect the economic growth of Pakistan?
2. Does FDI affect the economic growth of Pakistan?

Hypotheses of the study

H_0: Globalization has insignificant influence on economic growth.

$H_{1:}$ Globalization has significant influence on economic growth.

H_0: Globalization has insignificant influence on economic growth.

$H_{1:}$ Globalization has significant influence on economic growth.

Significance of the study

Every developing country achieves to higher economic growth in any social and economic system. Developing countries all over the world trying to increase economic growth with globalization. Globalization cause free mobility of goods and services, knowledge and management skills and thus increases the productivity and growth. Globalization is not only creates employment for unskilled labor but also cause a rise in unskilled wage and improve living standard that the result increase economic growth. Thus the present research is designed to explore the association between globalization and economic development in Pakistan.

Globalization and FDI has been broadly standard as a progress of economic development. From a historical perspective, there is no paved road in the course of FDI and globalization. It has discovered that FDI increase saving, income, employment, transfer science and right contribution to the financial improvement. In different ways Most of the researchers give an explanation the influence of FDI and globalization on economic development. Xu, B, Wang, J. planned the outcome of and trade openness and FDI for advanced technology spread to developing countries. In this study the sample was used of 21 OECD countries to check the effect of advanced technology on TFP in emerging nations by covering the time period from 1971 to 1990. Three transmission channels were considered for technology transmission like capital product trade, inward and outward FDI. The result showed that the import of capital goods and knowledge which comes from the developed countries has a significant outcome on a country's overall output [10].

Mahler VA observed the association among the globalization and economic growth. The conclusion showed that with little evidence is that systematic relationship between trade openness, FDI and disposable income. The result showed that integration into the all worldwide economy and the approaches of the globalization are positively but weakly related to the income distribution countries [11]

Richards explored the relationship between different macroeconomics variables by used the Granger causality test and Engle-Granger two-step cointegration with deference to investment, economic growth, trade and labor force. The results displayed that economic development has a long run and positive effects on the export and countrywide production. The existence showed a positive relationship among the variables Krishina et al. explored the relationship export and GDP by used a panel data for 39 emerging nations throughout from 1951 to 1998. Involving developing countries exports were revealed to be much more significant in gross domestic product development with GDP growth rates below the mean panel GDP progress rate than in those with GDP growth rates above the panel mean. Their outcomes showed that at the individual nation may provide very suitable evidence for exposure the factors of economic development. For Pakistan economy the outcomes also explained that there is no causality among trade and economic progress [12].

Makki & Somwaru observed the association among TOP and foreign direct investment that is increasing economic growth for 66 emerging countries. They establish that the main sources of economic growth are considered TOP, FDI, human capital and domestic saving. Moreover, they found a substantial and helpful link among FDI and trade openness in attaining the economic growth. There exists a positive association between these variables. Giuliano and Ruiz investigated the example of 73 nations during the 1975– 2002 periods, at that point established five-year averages for all factors utilized as a part of their examination to smooth out regular varieties. Once more, remittances were characterized as the aggregate of employees remittances, representative compensation, and passing exchanges. This investigation focused OLS and settled effects panel estimation, used a Generalized Method of Moment (SGMM) system. The investigation's essential determination relapsed per capita gross domestic product development on the aggregate remittances to GDP proportion to increase [13-15].

Qayyum investigated and checked the dual variables influence of financial growth and trade openness on GDP development rate in Pakistan economy throughout the era of 1961 to 2005 by using the growth index as a proxy for government expenditure. The study used bound testing approach of co integration financial policy to measure its impact on real GDP. Empirical results showed long-run association between real GDP, trade openness, financial progress. Moreover, in the long-run financial growth has greater impact on economic growth than trade liberalization. There exists a positive association among the variables [14,16]

Gourdon et al. examine and used tariff as a proxy trade openness, and also find that the trade liberalization and inequality are connected with factor benefactions. The result showed that a decrease in import tariffs on technology products raises encouragements for firms to more invest, which in turn raises development. On intermediate goods lower rate tariff increase output, and also increase subsequently steady state growth. Other studies showed that there exist a helpful association among economic growth and trade is focused by decrease in tariffs on raw materials and capital product. These findings provide country-level provision for the effects of trade liberalization on improved productivity of production through imported contributions and technology [15].

Cuaresma et al. observed the position of foreign machinery effect on the developing counties. Sample of a 21 OECD countries was used during a specific time period 1973 to 1997. Foreign technology imports and capital goods two major channels are used. Foreign R&D stokes were used to build by their import share biased averages of the country's own R&D stock. The consequences shown that the foreign R&D have helpful and substantial effect on increasing economic progress of the countries, employment defense, market regulation and lower barriers to the entrepreneurship which have lower levels Dutt et al. explored association among TOP and unemployment by cross country data for many developing countries. They found strong suggestion supportive the Ricardian estimate and indicated that unemployment ratio and trade openness are negatively connected. Though when more capital are available, in this result the more worker are ready to work unemployment reduce [16,17].

Skabic and Zubin examined the effect of FDI on macroeconomic concepts (i.e. employment rate, GDP growth and trade) from the developing economy. The consequences indicated that foreign direct investment has a harmful effect on employment while on the other side it does not have a positive outcome on GDP development rate and trade. Because of the low share of undeveloped investments, GDP had failed to expect the positive effect Ahmadi and Ghanbarzadeh observed for Iran country which displays that the outcome of TOP and foreign direct investment on economic development covering the time from 1970-2008 by using Bounds testing approach. In short runs and the long run the results presented TOP is significantly and positively determinant the development. The result also showed that in the short time for FDI is positively associated but negatively related in the in the long run [18-20].

Naude and Rossouw investigated the outcome of export expansion on employ for (Brazil, China, India and South Africa) for the time period 1962-2000. The authors founded that the linkage between export variation and employment opportunities. The result showed a positive and significantly effect on employees opportunities only in South Africa, whereas export attention taken a more encouraging impact on employment in India Brazil, China and India. The results also showed a U-shaped association exists between a nation's export basket and economic development, that is, the positive effects of exports diversification can be realized at early stages of development. Belloumi observed the association among FDI, TOP and economic progress used ARDL to Cointegration from1970 to 2008. When foreign direct investment is dependent variable the results showed that there exist a long run association exists between the variables. This result also investigated that there is no substantial relationship and Granger causality between FDI to economic growth and from economic progress to trade in short run [21].

Ying et al. explained the impact of globalization as a proxy of (TOP) and FDI on economic progress of Asian countries by used the panel data analysis from1970 to 2008. The result showed that globalization has a positively result on economic progress. The result also showed that there exist a meaningfully association among economic growth and globalization. Suci et al. examined the impact the globalization on economic growth including 6 Asian countries (Cambodia, Indonesia, Thailand, Malaysia, Vietnam, Philippines) by using panel data. The overall result showed that globalization had positively impact on economic development. The result also showed that economic and political globalization had positively impact on economic growth [22,23].

Historical Review of Pakistan's Economy

In this section, the historical trend of FDI, REM, and EXD in Pakistan are discussed.

In an economy globalization is an important indicator of international trade. During a period of time it is considered by dividing of all the aggregate worth of imports and exports by the gross domestic product for the same period. Although called a ratio, it is typically expressed as a percentage. It is used as an amount of the trade openness of a country to worldwide, and so may also be seen trade openness ratio. For an economy it may be called as sign of the degree of globalization.

Graph shows fluctuating trends in for 37 years. The basic reason is that Pakistan is an agrarian country for these reason only exports raw materials whose prices are very low in international market and on the other side Pakistan import technical goods whose prices are very high. Since independence Pakistan has suffered from large scale deficit import have more as compared to export. Export of a country are considered as a main pillar of the country, main source of earning, employment opportunities, foreign exchange and provide more ability to achieve higher economic growth for a country (Figure 1).

Economic growth

For each person of a country Per capita income is considered an average income to increase economic growth. Now in the present time period, per capita income is taken as a symbol of improvement and prosperity of a country. Countries having more per capita income are measured as rich and developed nations. Pakistan per capita income is very low as related to advanced countries. Use of more technological goods and control of population is necessary to increase per capita income. The largest reason of vicious circle of poverty is low per capita income. Including Pakistan most of the developing countries are trapped into VCP. Due to VCP a poor country is poor forever. In Pakistan 21.0% population is very poor.

This graph shows economic growth of Pakistan in different years and shows continues increasing trend in Pakistan. GDP per capita record was lowest in 1980 and highest in 2016.The per capita income was registered an increase in dollar due to stability of the rupee in international market. Per capita income of the country has recorded an increase from $1, 531 in fiscal year 2016 to $1,629 in fiscal year 2017. In Pakistan the GDP per capita is equal to 9% of the world's average. From 1960 until 2016 in Pakistan GDP per capita has averaged 703.68 USD. In 1960, South Korea had a GDP per capita three times of Pakistan. Today, its per capita income is 22 times more. To enhance further growth Pakistan does not generate more saving and investment. There is a low private investment and major infrastructure deficit, spending on worker skills, education and other needs. This is the basic reason macro-economic does not support economic growth and development (Figure 2).

Foreign direct investment

The role of FDI especially in the emerging countries has been a passionate debate. FDI is built on host country s circumstances and good

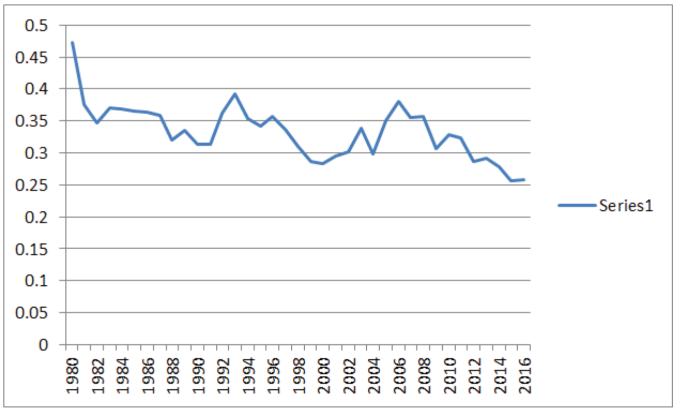

Figure 1. Globalization.

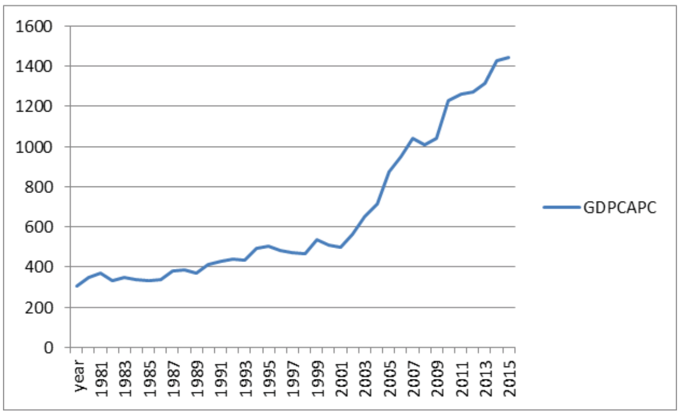

Figure 2. Economic growth.

monetary system also very helpful to attract FDI. During financial crises FDI can improve the efficiency of the economy. It is very helpful increase in productivity, domestic saving, smooth consumption pattern and provides employment opportunities. In this way strong polices, good infrastructure, and investment friendly polices force to foreign investors in a country (Figure 3).

This graph shows that FDI is the main source of external finance for Pakistan. FDI shows a declining trend up 1984 and between1986-1987. Trend increased from 1988 to 1997 and later this trend did not maintain its momentum and it's gone down during 1998-2001 due to nuclear test in Pakistan. In 2001, after the incident FDI slightly fell down due to supporting the war against terrorism and this falling trend ended 2004. Pakistan protected \$32.52 billion FDI in 2005 - 2006. In 2006 to 2007 it also grows to \$5.14 billion, in 2007 to 2008 it was \$5.41 billion. With the decline saving and the dominance of terrorism FDI level dropped \$3.72 billion in 2008 to 2009. As continues terror spells increased, investment continues to reduction, dropping to \$1.72 billion in 2009 to 2010.

Remittances

In Pakistan's economy remittances have become a backbone for higher progress. in the Middle East namely (Saudi Arabia, Bahrain, Qatar, Oman the United Arab Emirates and Kuwait) more than seven million Pakistanis have been located abroad out of which around 96% of the whole is focused Since 1971. In Saudi Arabia, the United Arab Emirates and Oman about 90% of the total Pakistan's are located. Remittances have very good effects on Pakistan economy. Foreign exchange reserves and Pakistan workers who have living abroad play a main role in Pakistan's economy. Remittance income through permitted channels supports for vital imports and decrease the burden on our balance of payment (Figure 4).

This graph shows remittances of Pakistan in different years. It can be seen that remittances in Pakistan have decreasing trend after 1980 and trend slightly decline from 1984 to 1988. The drop in remittances is mostly

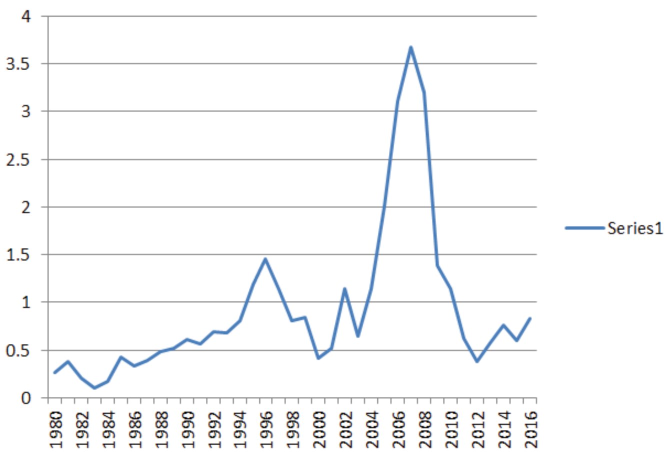

Figure 3. FDI.

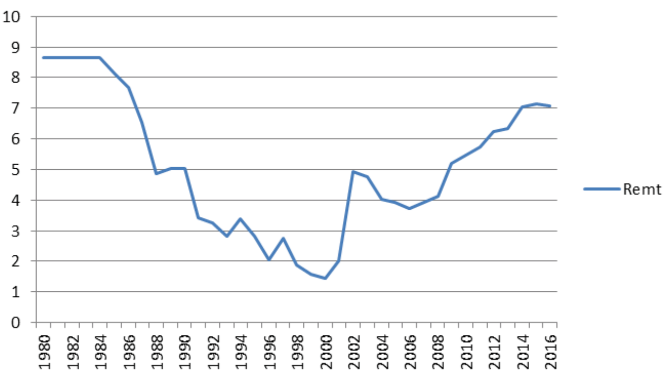

Figure 4. Remittances.

due to the adversarial economic situations of Arabian and gulf countries. Later remittances increased during 1989- 1990 but hereafter 1991 to 2001 it showed a mixed decreasing trend and this fall was due to eruption of this gulf crises the early 1990s. Seizure of Pakistani foreign account and other sensation were imposed due to nuclear explosion in 1998. But after 2002 foreign worker remittances has a sharp rising trend. Workers remittances not only the vital cause of increase in foreign exchange rate but also very helpful in making income distribution in Pakistan economy.

Model

The model of Nunes, Oscatejui and Peschiera based on Econometric model by adding FDI and globalization due to analyses their impact on economic growth Pakistan. The functional form of the model is as given

For this study the functional form of the model is;

$EG = f\,(FDI_{t}, REMT_{t}, GOL_{t}, UE_{t}, GDS_{t})$

In this study the econometric equations of the model is used can be written as;

$EG = \alpha_{o+} \beta_1 FDI_t + \beta_2 REMT_t + \beta_3 GLO_t + \beta_4 UE_t + \beta_5 GDS_t + \varepsilon_t$

The econometric model after taking log of the dependent variable (to make the equation linear) is; $lnEG = \alpha_{o+} \beta_1 FDI_t + \beta_2 REMT_t + \beta_3 GLO_t + \beta_4 UE_t + \beta_5 GDS_t + \varepsilon_t$

Economic growth (EG) is taken as the dependent variable. Foreign direct Investment (FDI), Remittances (REMT), Globalization (GLO), Unemployment (UE) and Gross Domestic Savings (GDS) are used to taken as independent variables. To check the long-run cointegration in the model for this study Distributed Lag (ARDL) is applied. The reason behind to use the ARDL model is; at first difference all variables are became stationary. Augmented Dickey Fuller (ADF) and Phillips Perron (PP) unit root tests are used to find stationary level of the. Optimal Lag Length criteria used to find the optimal lag that is helpful to estimate the equation. Before estimating long-run analysis ARDL bound testing to cointegration used. It shows that long run association exists. To check the stability of the data CUSUM and CUSUM of square are applied. Variance Decomposition Analysis also applied to check the shocks of the variables.

Estimations and Results

For long-run relationship in time series analysis, stationarity properties arechecked by unit root tests, namely Augmented Dickey–Fuller (ADF) (see Dickey & Fuller, 1979), Phillips Perron (PP) (Phillips & Perron, 1988), andDickey–Fuller generalized least squares (DF-GLS) (Elliot, Rothenberg, & Stock (1996). Results of unit root tests are reported in Table 1.

The results of ADF unit root test explained that Gross Domestic Product per capita (GDPpc), Remittances (REMT) and Unemployment (UE) became stationary at 1st difference. Their significance level is 1%. Foreign Direct Investment (FDI) and Gross Domestic Savings (GDS) became stationary at 10% level of significance. Globalization as a proxy Trade Openness (TOP) became stationary 5% level of significance. The ADF unit root test suggests

Table 1. ADF Unit Root Test.

Sr.no	Variable name	ADF Unit Root Test			
		Level		1st difference	
		t-statistics	p-value	t-statistics	P-value
1	lnEG	0.637991	0.8491	-3.88995	0.0052*
2	FDI	-2.7644	0.0738***	-2.9484	0.0044
3	GDS	-2.7644	0.0738***	-2.9484	0.0044
4	REMT	-1.60915	0.4677	-5.69262	0.0000*
5	UE	-1.67412	0.4343	-6.27636	0.0000*
6	GLO	-3.62027	0.0102**	-7.04154	0

Note: *, **, *** represents 1%, 5% and 10% level of significance respectively.

checking the long run association of this study using Auto Regressive Distributed Lag (ARDL) model.

Long run relationship exists in the model. It is confirmed by the ARDL Test. In Table 2 the estimations of long run analysis are reported. The estimated long run coefficient of FDI has significantly impact on economic growth. This result is in courtesies of the study of Adams (2009). The rise in FDI leads to increase more employment opportunities to the people. The Gross Domestic Saving has helpful and significant effect on economic growth in the long run; this result is in courtesies of the study of Amjad and Khan (2004). Remittances also have helpful and significant impact on the economic progress in long run. This outcome is in courtesies of the study of Ang (2006) result concluded that remittances increase the quantity of funds through the banking system. There is negative and significant association among economic growth as a proxy GDPpc and globalization as a proxy (TOP) in long run. This result is in favors of the study of and the study of Kim et al (2008). Unemployment has negative and significant impact on the economic growth as a proxy GDPpc. This result is in favor Noor et al., 2007 shows a negative relationship exists among unemployment and economic progress (Table 2).

Stability test

To determine the stability of coefficients of independent variable Stability test is used. Stability test is achieved by cumulative sum of recursive residuals (CUSUM) and cumulative sum of square of recursive residuals (CUSUMSQ). If cusum series crosses upper critical line or lower critical line recursive regression, which indicate model is instable. If the cusum series lies between upper and lower critical lines the model is stable. The results of CUSUM and CUSUMsq are shown in the below Figure 5a, Figure 5b & 6.

To check the stability of long run parameters by applying CUSUM and CUSUMsq tests is tested. In Figures 1 and 2 the plots of both CUSUM and CUSUMsq are reported. These figures reveal that plots are of both tests are within the critical bounds therefore; it indicates the test ability of long-run estimations and shows that the model is stable.

Conclusion and Policy Implications

The present investigation have motivated on the empirical association among economic development, FDI and globalization in Pakistan which has a developing economy and been effective in stabilizing its economy

Table 2. Short and Long Run Estimations.

Co integration Form				
Variable	Coefficient	Std. Error	t-Statistics	Prob.
ΔFDI	0.00547	0.00256	2.136753	0.0522***
ΔGDS	0.001928	0.000438	4.405872	0.0007*
ΔREMT	-0.00479	0.001176	-4.07206	0.0013*
ΔTOP	-0.10891	0.036593	-2.97633	0.0107**
ΔUE	-0.00219	0.000704	-3.1073	0.0083*
ECT(-1)	-0.05568	0.024897	-2.23633	0.0435**
Long Run Coefficients				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
FDI	0.145837	0.054835	2.659571	0.0197**
GDS	0.089261	0.035009	2.549674	0.0242**
REMT	0.178574	0.071959	2.481617	0.0275**
TOP	-3.99408	1.220954	-3.27127	0.0061*
UE	-0.02873	0.011542	-2.48881	0.0272**
C	2.594428	0.340826	7.612173	0.0000*
R^2=0.9993				
Adjusted R^2=0.9982				
D.W=2.25				
F-Statistics=978.349 (0.0000)				
***, ** ,* represents the 10%, 5% and 1% level of significance respectively.				

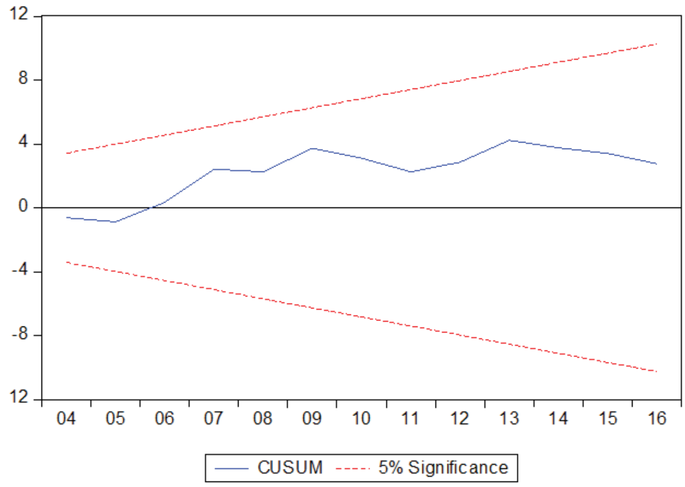

Figure 5A. CUSUMsq.

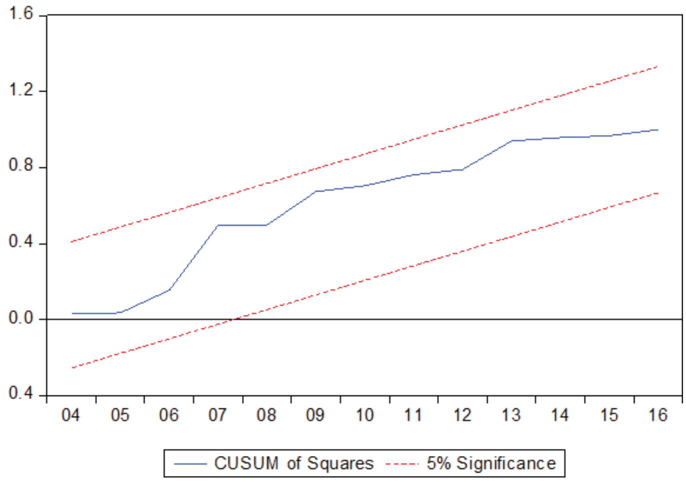

Figure 5B. CUSUMsq.

after 2000s. Results of this research that FDI and globalization in the equilibrium long run association with the economic progress. In this present world's scenario globalization as a proxy (TOP) and FDI are main symbol of economic growth. Supply of the rare resources such as physical and human investment, increase skills and modern expertise, research and development and more employment opportunities are the benefits of the FDI of the host country. In case of Pakistan it is observed that trade and foreign FDI has been focused on services sectors as a result society become more benefited.

This paper is proposed to mark some support in this framework. In this paper it is argued that in this paper that globalization, GDP per capita as an economic growth, FDI, unemployment, gross domestic saving and remittances are closely associated with economic growth in Pakistan. ARDL bound testing technique to co integration is used to check the nature and scale of the association. By covering the period 1980-2016 time series data is used.

We attempted to discover some policy implication to increase economic growth through FDI and globalization as a proxy (TOP).

- Economic growth is not possible unless the economy creates opportunities for investment, entrepreneurship, employment formation and sustainable livings.
- To promote the economic growth of Pakistan, there is a need to diversify the export based and import duties should be removed from the import of technology goods (capital machinery and parts of machinery) and input material at the same time the imports

of unnecessary and luxuries should be reduced through heavy import taxes.

- Export promotion policy and import change policy must be observed, so that the country can take more advantage from trade openness. The financial experts should increase export and domestic goods.
- Safety condition must be make noticeable prefect and trustworthy to improve the FDI. This investment should be used for the development of the economy instead of the consumption purpose.
- To increase the economic growth of any economy infrastructure plays an essential role. The countries which have good infrastructure are the best attractive hosts for FDI.
- The Government of Pakistan should encourage the foreign investment by creating healthy atmosphere and providing incentives to the foreigner investors.

Author Conflict of Interest

The authors declare no conflict of interest.

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