

# THE EFFECTS OF FOREIGN CAPITAL INFLOWS ON ECONOMIC GROWTH IN PAKISTAN: AN ECONOMETRIC ANALYSIS

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# MOTIVATION

## ➤ IMPORTANCE OF CAPITAL FLOWS

- ✓ IN GENERAL

- ✓ PAKISTAN

- HISTORICALLY – SMALL MAGNITUDE WITH MIXED EFFECTIVENESS; SO NEED TO UNDERSTAND MORE CLEARLY
- CPEC IS COMING! (IS HERE)

## FOCUS OF THIS STUDY

- EFFECT OF FDI ON ECONOMIC GROWTH OF PAKISTAN



- AIM: TO OBTAIN ‘GOOD’ -  
ECONOMETRICALLY DEFENSIBLE ESTIMATES
- THEORY CLEARER, EMPIRICS NOT AS MUCH.

# A BIT OF THEORY

## ➤ NEOCLASSICAL GROWTH THEORY

- ✓ FDI 'FED' K IS GENERICALLY NOT DIFFERENT FROM ITS DOMESTIC COUSIN
- ✓ THUS AFFECTS ONLY LEVEL OF GDP AND IS SUBJECT TO DECREASING RETURNS
- ✓ MOTIVATED EMPIRICAL SPECIFICATION OF FDI'S IMPACT ON LEVEL OF GDP, NOT ITS GROWTH RATE.

## ➤ ENDOGENOUS GROWTH THEORY

- ✓ FDI 'FED' K HAS POSITIVE SPILLOVERS IN TERMS OF TECHNOLOGICAL IMPROVEMENTS, BENEFICIAL LINKAGES
- ✓ MOTIVATES EMPIRICAL SPECIFICATIONS THAT RELATE FDI TO RATE OF GROWTH OF GDP

# EMPIRICS

- THE EMPIRICS OF THE FDI'S IMPACT ON ECONOMIC GROWTH ARE FAR LESS CLEAR.
- IN THIS PAPER:
  - ✓ SAMPLE IS FOR ONE COUNTRY VS POOLING OVER TIME AND ACROSS COUNTRIES: THE ISSUE OF 'HETEROGENEITY'
  - ✓ SPECIFICATION TO ADDRESS POSSIBLE ENDOGENOUS NATURE OF DOMESTIC SAVINGS AND ECONOMIC GROWTH
  - ✓ SAMPLE FROM 1973-2015; OLS & 2SLS

# MODEL SPECIFICATION

$$GR = \alpha_0 + \alpha_1 S + \alpha_2 FDI + \alpha_3 DISB + \alpha_4 XM + \mu \quad (1)$$

$$\alpha_1 > 0 \quad \alpha_2 < 0 \quad \alpha_3 < 0 \quad \alpha_4 > 0$$

$$S = \beta_0 + \beta_1 GR + \beta_2 FDI + \beta_3 DISB + \beta_4 RINT + v \quad (2)$$

$$\beta_1 > 0 \quad \beta_2 < 0 \quad \beta_3 < 0 \quad \beta_4 > 0$$

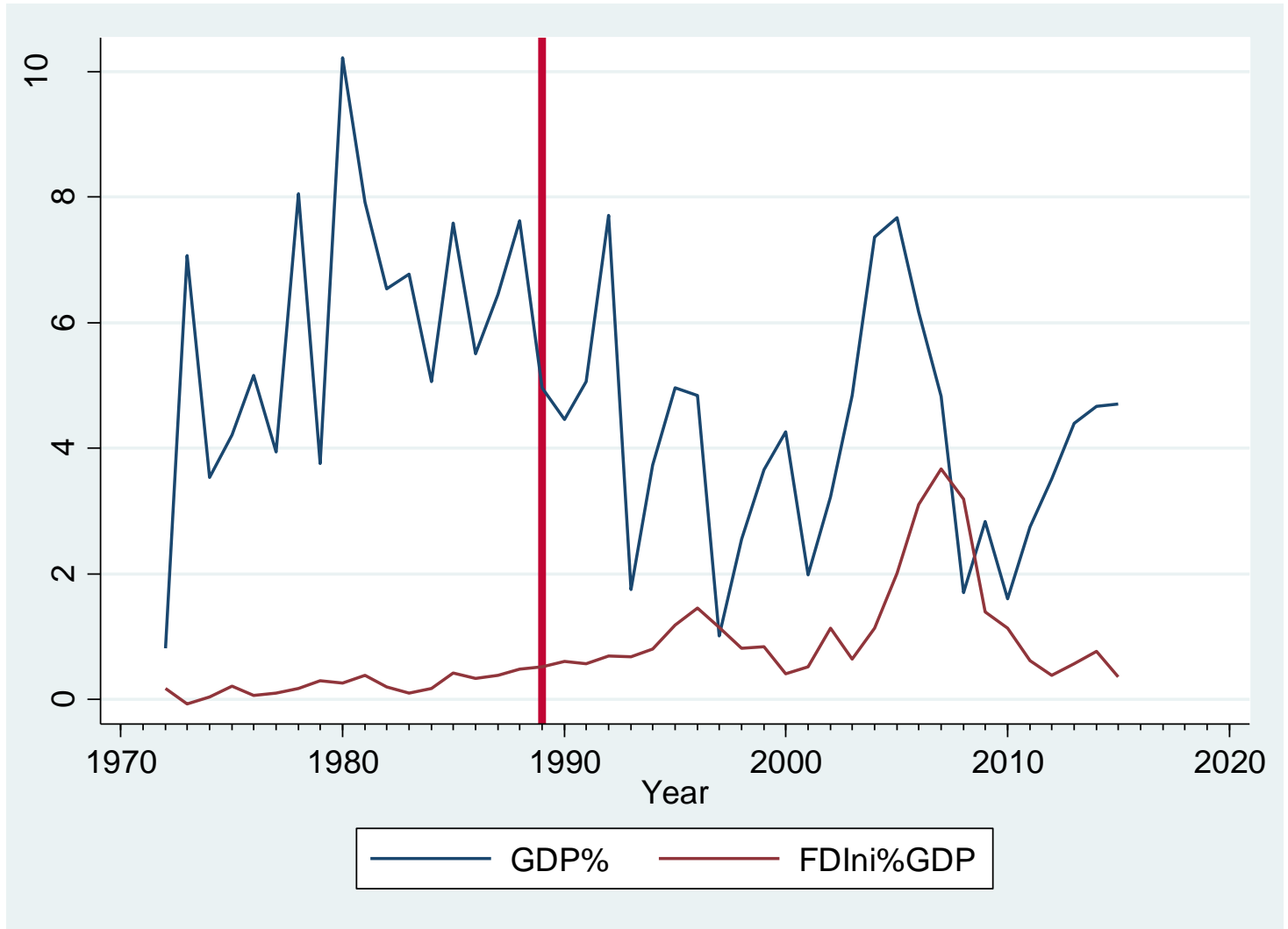
Shabbir & Azhar (1992) PDR

# DATA SOURCES

1973-2015

FOR MOST VARIABLES, WORLD DEVELOPMENT INDICATORS FOR PAKISTAN, WORLD BANK EXCEPT REAL INTEREST RATE WHICH IS FROM STATE BANK OF PAKISTAN.

# A GRAPHICAL PEEK AT THE DATA





# EMPIRICAL RESULTS/REPORTING

## OVERARCHING FINDING:

Occasionally positive (at times negative or zero coefficient estimate) for FDI on GR

Even when controlled for 'endogeneity' via simultaneous equation modeling and 2SLS estimation procedure.

Extensive RF estimation of FDI equation has similar estimated coefficient estimates.

# EMPIRICAL RESULTS/INTERPRETATION

(MECHANICAL/STATISTICAL) NON-SIGNIFICANCE OF COEFFICIENT ESTIMATES AS SUGGESTIVE OF THE FACT THAT PAKISTAN ‘MAY NOT BE READY FOR THE PRIME TIME’ – AT LEAST IN THE PAST HAS NOT MET THE ‘THRESHOLD’ NECESSARY CONDITIONS.

Foreign Direct Investment and Development: Where do we stand? JBIC Research Paper # 15, June, 2002

Le, Minh Hang and Ali Ataullah (2006) “Foreign Capital and Economic Performance of Pakistan.” Lahore Journal of Economics, Vol. 7, No. 1

Waheed, A. (2004) “Foreign Capital Inflows and Economic Growth: A Critical Survey of Selected Empirical Studies”, Journal of Economic Cooperation 25, 1; pp. 1-36

Ahmad M. Khalid (2018) this Conference

○ WHITHER CPEC? (SO WHAT ABOUT THE FUTURE)

## POLICY IMPLICATIONS

- INITIATE/ENSURE/ENCOURAGE VARIOUS POLICIES TO ALLOW US TO MEET THE ‘THRESHOLD’ THAT MAY MAKE FDI GROWTH-ENHANCING
- THESE NECESSARY CONDITIONS ARE SUGGESTED BY THE LITERATURE AND COMMONSENSE
- LIST?

# LIST

- ✓ LAW & ORDER (TO ATTRACT, KEEP AND MAKE FDI EFFECTIVE)
- ✓ EFFECTIVE INFRASTRUCTURE – PHYSICAL, ENERGY, INTERNET, INSTITUTIONAL
- ✓ GOOD GOVERNANCE
- ✓ TECHNOLOGICAL IMPROVEMENTS – NOT ONLY PATENTABLE ITEMS BUT ALSO ABSORPTIVE CAPACITY TO RECEIVE POSITIVE SPILL-OVERS IN MANAGEMENT AND OPERATIONAL ‘BEST PRACTICES’ (INCLUDE HC)
- ✓ FINANCIAL DEVELOPMENT, INTEGRATION AND INCLUSION
- ✓ EXCHANGE RATE, CAPITAL ACCOUNT REFORMS
- ✓ FILL IN THE BLANK, PLEASE

## SUGGESTED FUTURE RESEARCH

- UNIFORMITY OF MEASURES USED
- MICRO: FIRM LEVEL. LINKAGES.
- MACRO:
  - ✓ PANEL DATA YET RESOLVE HETEROGENEITY ISSUE TECHNICALLY AS WELL AS LIMITING POOLING TO PERHAPS VERY SIMILAR ECONOMIES
  - ✓ CHANNELS – MORE DETAILED STRUCTURAL MODELS

Thank you !

Q & A / Comments

