The impact of foreign direct investment (FDI) on economic growth

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Introduction:

Foreign direct investment (FDI) has gotten distinguished and the most gainful strategy for drawing streams originating from external assets. The use of this technique has likewise transformed into a significant piece of making financing capital flow into nations around the world. For developing nations far and wide, this productive impact joined with foreign transactions has developed constantly well and is referred to as an instrument for investment development (Muhammad, 2007). FDI has numerous benefits on creating better economic output, for example, it raises profit level for entrepreneurs, reduces unemployment and opens avenues for fares and innovative headways for financial gurus and nations.

The role of FDI in creating better national output is crucial, it increases opportunities for work and use of human resources, FDI serves to lessen planning shortages by executing new business approaches. An alternative benefit of FDI is that it does incorporate the risk and regulation of foreign commitment[1] and increments that worth the human capital via obtaining skilled workers for countries that suffer from the deficiency of capital and imaginative smoothness regularly experience the advancement slower than those that doesn't. As per numerous studies, foreign business prompt can undoubtedly give a path toward growth associated with both mechanical skill and information (Dunning &Hamdani, 1997).

[1] Chaudhuri, S., & Banerjee, D. (2010). FDI in agricultural land, welfare and unemployment in a developing economy. *Research in Economics*, *64*(4), 229-239.

The specific examination objective is to investigate this effect associated with foreign direct investment (FDI) in Pakistan. Pakistan is generally a small area having a chronicled legacy with quickly developing populaces. Pakistan's ex general economy to a great extent is subordinate after cultivating, and every capita benefits is decreased.

In this paper we will look at the relationship between FDI and GDP for the period 2002 to 2012. Pakistan is creating output with quickly expanding populaces. Agribusiness has prevailing impact in economy according to capita salary is low because of which it confronts destitution issues. Subsequently the fundamental goal of macroeconomic strategy producers is to build FDI in nation. Pakistan is struggling to go in the present day world and being the first part of SAARC (South Asian Association for Regional Cooperation) and a standout amongst the most paramount nations of this region favoured with huge amount of assets as mineral possessions, dense labour population, agribusiness innovation and other good skilled characteristic assets. FDI assumes an extremely crucial part in its future development and improvement. FDI is vital for creating nations as well as offers profit to speculators additionally we can say that it produces winning circumstances to both ends.

Living a better life by earning is considered as IBADAT in every religion. As we know that Islam provides a complete code of conduct for every person and at every level. Our beloved Prophet Muhammad (PBUH) was himself atrader and he took merchandise from one city to another and invested the profit he earned in the business, favouring retained earnings in a business for the business to grow.

There are many Qur'anic verses and Ahadith that cover this topic such as:

"There is no sin on you if you seek the Bounty of your Lord (during pilgrimage by trading etc.)."(Aayah No. 198, Surah Al-Baqarah, Chapter No. 2, Holy Qur'an).

“Hazrat Abu Hurairah (May Allah be pleased with him) said: The Messenger of Allah (PBUH) said, "O people! Allah is Pure and, therefore, accepts only that which is pure. Allah has commanded the believers as He has commanded His Messengers by saying:
`O Messengers! Eat of the good things, and do good deeds.' (23:51) And He said: `O you who believe (in the Oneness of Allah - Islamic Monotheism)! Eat of the lawful things that we have provided you..."' (2:172). Then He (PBUH) made a mention of the person who travels for a long period of time, his hair are dishevelled and covered with dust. He lifts his hand towards the sky and thus makes the supplication: `My Rubb! My Rubb!'But his food is unlawful, his drink is unlawful, his clothes are unlawful and his nourishment is unlawful, how can, then his supplication be accepted?"[Muslim Hadith # 2214].”Holy Quran directs us ‘O those who believe, become true believers. Quran also says,” ‘O those who believe! Should I guide you towards a trade which shall save you from a painful punish’’In the light of these directions, there is a need to spell out the challenges which may hinder the complete Islamization of whole economy and society. We don’t have any other option as Allah directs us to enter into the fold of Islam entirely and completely

From these references we can understand that Islam appreciates trade because trade brings investment and flow of money in society. What we should consider is just not to invest or bring investment from prohibited resources. The first thing is to understand what Halal and Haram is. Halal is permissible, Haram is to be avoided. Whether it is earning the income or expenditures, production or exchange; whatever may be the form of economic activity, Halal (Permissible) and Haram (Forbidden) have to be kept in mind.

Literature review:

There are many studies on the foreign direct investment and economic growth that has been conducted by various scholars few were done locally and major were internationally, Pakistan was one of those countries where empirical studies has been reviewed critically the purpose of those researches was to evaluate most critical consequences and policy recommendations by Falki (2009) Foreign direct investment had a statistically destructive result on the

gross domestic product. Likewise, Agarwal (2000) also believes that FDI has a negative impact on GDP till 1980, but its impact seems to be positive afterwards.

Whereas, Adam &Tweneboah (2009), found that FDI has a positive impact on economic growth and stock exchange of a country. The positive impact of FDI depends on many factors. Along with the economic factors, social and environmental factors of the receiving country effect the result of FDI on GDP (Buckley, et al. 2002).Anyamele (2010) inspected the crash of education, export and FDI upon economic extension in SSA (Sub-Saharan African Nations). He reasoned that and FDI had remarkable effects on fares and financial development of Sub-Saharan African Nations.Authokorala (2003) endeavoured to look into the effect of FDI on the economic development of Sri Lanka. The key discoveries recommended that there had been the weakest connection between economic development and FDI on account of Sri Lanka. He inferred that this negative relationship is an aftereffect of political instability, absence of great administration, and the bureaucratic latency. Zhou at al., (2002) confirmed the effect of FDI on the effectiveness of the provincial firms utilizing yearly information over the period 1970-2001 in China. Similarly (De Gregorio, 1992) examined 12 Latin American Countries and found the positive and significant impact of FDI on economic growth the study also showed that efficiency of FDI is higher the national investment.

In numerous surveys, FDI could increase unemployment in developing countries as argued by Jaouadi (2014)[2], for the author, foreign investment could have negative effects on the employment of youth.

The exact examination indicated that FDI had pushed a positive impact on the local level against on the industrial level.An imperative study by Abbas et al. (2011) was conducted on SAARC countries,by using multiple regressions they found that FDI has appositive relationship with GDP whereas negative relationship was found between CPI and GDP.They used threshold regression analysis.According to a study the GDP and human capital are dependent by the FDI expressively.Which show that initial GDP and human resources are key drivers of FDI. Alfaro et al (2004) also carried out a parallel examination to find relationship between FDI and GDP. The study showed that solid financial system of a country is capable of attracting FDI. A study by Shabir and Mahmood (1992) examined the relationship between foreign private investment FPI and economic growth in Pakistan,the study determined that net foreign private investment (FPI) had a positive impact on the rate of growth of real GNP. Likewise (Ahmed, et.al, 2003) also found positive relationship of FDI on domestic growth. As we said above that FDI along with economicdevelopment also brigs technological reforms Boreztien et al. (1998) found that FDI carries technology and advanced growth in rising countries' if these countries have minimum stock of human capital.

Hypothesis:

FDI (Foreign Direct Investment) has positive impact on GDP Gross Domestic Product).

3. RESEARCH METHODOLOGY:

[2] Said Jaouadi (2014), "Could Foreign direct investment increase unemployment: case of KSA", The international journal's research journal of economics and business studies, Vol 3, N°9, pp: 51 – 56.

The objective of this research paper is to find the impact of FDI on GDP. We use data of 10 consecutive years from 2002 to 2012. As the ministry of finance is consideredone of the most reliable and authentic sources of data collection therefore secondary data of above mentioned variablesare collected from ministry of finance (economic survey of Pakistan).

The centralaim of the paper is to study the effect of FDI on GDP of Pakistan. In Pakistan relevance is observed between foreign direct investment inflows and economic growth of the country. To evaluate the relationship between economic growth of Pakistan and foreign direct investment, thefollowing regression model is used:

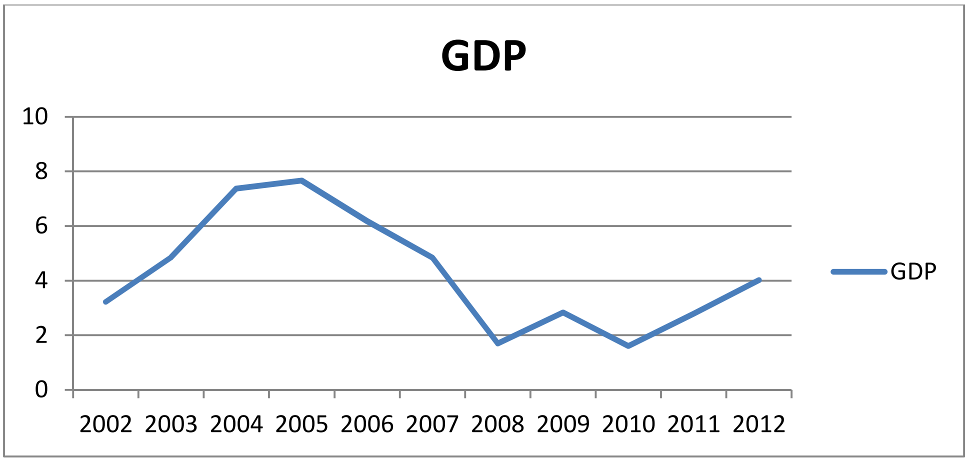
$$GDP = \alpha + \beta 1\ FDI + \mu$$

Where, FDI = Foreign DirectInvestment, GDP = Gross Domestic Product. The above-mentioned Regression Model was run on SPSS to discover the impact of FDI on the Gross Domestic Product of Pakistan. Regression model is run to discover the impact of FDI on GDP for the period 2002 to2012.FDI is used as independent whereas GDP as depended variables. Following are the descriptive statistics of GDP and FDI,

3.1 Measures the Output (GDP)

We used GDP,as adependent variable in regression model mentioned in equation 1.Data from 2002 to2012 was taken from the Ministry of Finance.Years are showed on X-axis whereas GDP in % on Y-axis. Fluctuation trend of GDP can be seen in 10 years.

Figure 1: GDP

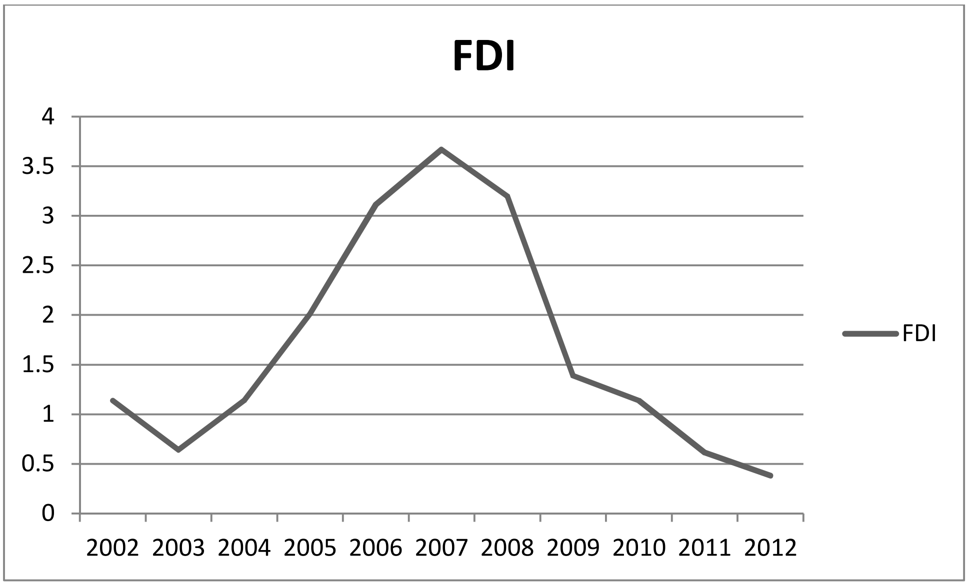


Source:Pakistan Economic survey (Ministry of Finance).

3.2 Measures the Input (FDI)

FDI is used as independent variable on Regression Model mentioned in equation 1.data on FDI was also collected from Ministry of finance for the period 2002 to 2012. The vertical axis (X- axis) is the year and horizontal axis (Y-axis) is FDI in (%).FDI shows fluctuation trends in above mentioned years.

Figure 2: FDI



Source: Pakistan Economic survey (Ministry of Finance).

4. EMPIRICAL RESULTS:

Succeeding regression model is used to test the impact of FDI on GDP

$GDP = \alpha + \beta 1\ FDI + \mu$

Table 1

Empirical results of GDP and FDI

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	3.866	1.451		2.664	.029
	FDI	.243	.692	.123	.351	.734

a. Dependent Variable: GDP
b. Independent variable: FDI

The empirical findings are represented by the above tables. The results of slope coefficients of input(FDI) in regression analyses showed positive impact on gross domestic product.it shows that if there is 1% increases in dependent variable FDI it will effect GDP by.243%.but this effect is not a significance (T=.351) and it must be greater or equal to 1.96. There are many others economic and non-economic factors that affect GDP (μ=.692)of any country such as Capital formation, Naturalresources,Human resources, Power, Education, political instability, social and administrative so that's why the effect of FDI on GDP is not significance.

Conclusion and Recommendations:

Investment plays a vital role in economic growth and infrastructure building of any nation that will ultimately improve living standard of their people. There are many others factors that affect GDP of any country so that's why the effect of FDI on GDP is not significance but we can say that because FDI has a positive impact on GDP is government and other financial sectors work hard to bring more and more inflows of FDI. As we know that I=S and in under developing countries S is very low which so that's y investment is also low.so to increase investment such countries are highly depended on FDI, it is considered as supplement or backbone of economic development of under developed country.

It was proven form literature review and from our results that FDI positively contributes toward economic growth of any nation. Pakistan is under developed country it has very low ratio of savings so to increase investment it is highly depends on FDI.it is a duty of local government to tack such actions that attract investor's to invest and economy of our country can grow. After reviewing literatures we can give some recommendations to increase FDI. Policy makers can take guidelines from these recommendations. First of all, the government should build an environment conducive to business activities such as creating investment opportunities to attract foreign investment and simultaneously encourage local investors, if the local investors' interests are appreciated and carry weight in the eyes of the government, their rights protected, and benefits awarded to them, then foreign investors can easily be attracted. Secondly, there should be proper education for labour to become skilled as by educating the labour force of the country, labour productivity will rise and the investment will be beneficial. Government should bring economic reformation by transfer of resources to more productive sectors from less productive sectors to get optimal benefit from investment. Political stability and law and order situation are important drivers that influence investors' mind so government and other regulatory authorities must improve these two.Self-reliance is must. Unfortunately Pakistan depend on the loans from the west. For the time being it may be unavoidable but we must take care to preserve our identity and not let the loan offerers influence our decisions. We must make our decisions in the light of our vision and values. We must not lose our identity and try to reduce dependence on loans as much as possible.

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