CONTRIBUTION OF FDI IN ECONOMIC GROWTH
AN EMPIRICAL STUDY ON PAKISTAN

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Abstract
The aim of this paper is to determine the contribution of FDI inflows in economic growth of Pakistan. The data used in this analysis is time series data for the span of 25 years from 1990 to 2015. The findings of the study are based on Unit root test which gives the evidence that data was stationery, Johansen Co-integration test which provides the strong evidences for the correlation between variables for long-run, and the regression model used to carry out this process was VECM model which finalize the results related to this study. The findings of the empirical study show that there is significant effect of FDI inflows on economic growth in long-run and labor force is much correlated with FDI to boost up economic growth if given proper skills and trainings regarding modern technology. The findings of paper describe that in long-run FDI and Labor force are significant but in short-run both are not much significant and the reason of their low significance is worse conditions of political policies which are unpredictable at every moment so investors are not certain for returns of their investment.

Keywords: Economic Growth, FDI inflows, Labor force, Unit root test, Johansen Co-integration test, VECM model
INTRODUCTION

Over the last decade Foreign Direct Investment (FDI) has got fierce competition for inward FDI inflows in developing countries, so FDI is playing a significant role in the ongoing process of integration and liberalization of the world economy, especially in developing countries. In developing countries FDI is applied as fastest and highest source of development. A recent analysis of effects of FDI on local firms in developing and transition countries suggests that foreign investment increases local productivity growth. FDI has very direct influence on economic growth of host country through the transfer of new technologies and know-how, formation of human resources, integration in global market, increase of competition, and firm’s development and reorganization. Liberalization policy in developing world since 90’s has revolutionized the economy and provided a flip to their Gross Domestic Productions (GDP). The developed countries poured in form of foreign direct investment into developing nations to transform them from agrarian to industrial economies, beside this FDI is proved a boon for such countries.

Foreign Direct Investment (FDI) is defined as if a company from one country known as home country makes some physical investment in other country known as host country. It is a process in which one country (home country) acquires the ownership of the assets of the firm in the other country (host country) so that they can have a control over the production, manufacturing, distribution and all the other activities. According the World Bank the foreign investor must own at least 10 percent or more of the ordinary shares in the company or enterprise operating in an economy other than that of investor (Investee Company). It can be done either by setting up subsidiary company in host country, or acquiring the shares or through mergers and acquisitions. FDI refers to the flow of capital between countries. United Nations Conference for Trade and Development (UNCTAD) defines FDI as, an investment made in such enterprises operating beyond the borders of the economy of the investor in order to gain long-lasting interest. FDI is associated with cross-border mergers and acquisitions that can be; Horizontal-where the firm are at same stage of production; Vertical- where firms are at different stages of production; and Conglomerate-where firms are in different industries. In developing countries FDI has remained the largest form of capital flow over last couple of decades for supporting portfolio equity investment, private loans, and official assistance. According the findings of [Perkins (2001)], FDI contribution was 45 percent of net foreign resource flows to developing countries in 1997, while reported 16 percent in 1986. More ever the World Bank (2002) reported that in 1997 developing countries received 36 percent of total FDI flows. Now FDI is considered as most important source of development in most of developing countries, but its economic effects are almost impossible to either predict or measure with precision.
Many reasons have been given for importance of FDI inflows, includes employment creation, enhance competition as well as transfer skills though training. FDI assists foreign investors in utilizing their assets and resources more efficiently as well as host counties can acquire better technologies and getting entangled in international production and trade networks (Athukorala 2003). Developing countries have started to see FDI as a source of economic development and modernization; many governments have developed policies to encourage inward FDI flows. Furthermore, FDI gives developing countries the opportunity reduces dependence on foreign aid, by boosting the state’s sovereignty from donor policies.

Investors tend to invest in such countries and projects where expected highest returns and lowest risks relative to alternative investments and opportunities. Pakistan is among such developing countries which has a great potential to attract foreign investment due to highest returns. Pakistan is suitable for all type of businesses because it is a country enrich with abundant resources, large market, and better geographical location as compare to other countries. For any country policies and strategies to attract foreign investment are very important, they are the key and basic tools a country uses to attract investors and other profit looking entities. To maximize the contributions of FDI to Pakistan’s economic development Government has took many initiatives, they have initiate the special programs to promote the linkages between domestically and foreign owned private enterprises, such as local supplier, sub-contractor or joint venture programs, this will help the enterprises to improve the quality, will create the competition, and a mutual corporation which will help the local suppliers to assist foreign markets easily, secondly due to such programs the local market can enjoy the resources which are not easily available in domestic markets, like new technologies, advances skills and know-how about foreign markets.

Every coin has two sides, positivity and negativities, similarly FDI also have positive effects and negative effects also. The possible positive effects of FDI are as: FDI provides capital which is usually missing from host country, Foreign corporations create new work places, FDI bring new technologies which are not available in host country, Foreign corporations provide better access to foreign markets, Foreign corporations can help to change the economic structure of host country, Crowding in effect, Competitive economy, Elimination of monopoly, Human resources, and Revenue to the host country. On other side FDI is not beneficial for host country, the possible negative effects of FDI are as: Foreign corporations may buy a local company to shut it down, Foreign corporations may cut working positions, Repatriation of the profits can be stressful on balance of payments, Possible environmental damages, Loss of business for local companies, Missing tax revenues, The emergence of a dual economy, Draining of money, and Exploitation of labor laws. Meanwhile many studies have been made to
analyze the possible outcomes of FDI in host country, so majority of results show that FDI has over all positive effects for developing countries like Pakistan.

The concrete policies, the strong infrastructure, and investment friendly policies of host countries always give confidence to foreign investors for investment in those countries. These policies representing the true interests of the host countries and also guide foreign investments into right areas where they are needed most.

Pakistan is a South Asian developing country having population over 190 million, based on semi-industrialized economy which mainly encompasses textiles, chemicals, food processing, agriculture and other industries, economy has a per capita income of US$ 1,550 (nominal GDP per capita), it has achieved a GDP growth rate around 4.8% in recent years, being a developing country it has about 29.30% population living below poverty line and facing inflation (CPI) of about 1.8% recently. Economy has potential to grow fast instead of facing the serious problems of internal political disputes, a fast-growing population, terrorist attacks and worldwide economic crises of 2008.

Since last decades Pakistan received large bulk of Foreign Direct Investment (FDI), during the period of 2005-6, FDI increased to $ 2.224 billion from $ 792.6 million and portfolio investment to $ 407.4 million, where it was $ 108.1 million in corresponding period last year. In the financial year of 06/07, Pakistan achieved almost $ 8.4 billion, while target was $ 4 billion, in 2010 FDI had significant decline, FDI dropped by 54.6% in the end of year, and afterwards economy is facing fluctuations in FDI inflows.

The main purpose of this thesis is based on to investigate and analyze the contribution of FDI inflows in economic growth of Pakistan, and formulate the effective strategies and policies to attract large bulk of FDI inflows in Pakistan, more important to formulate a frame work which soar the FDI inflows in Pakistan, and future incentives and opportunities to economic growth of economy. In this regard, this thesis is organized as follows: Chapter 2 presents trends and policies of FDI inflow in Pakistan. Chapter 3 highlights the relationship between research on FDI and economic growth. Chapter 4 provides theoretical background, sources of data collection and methodology of the study. Chapter 5 is based on results which analyzes and interprets the empirical findings, and concludes the overall results of the paper with some policy recommendations of research.

**Problem of statement**
For the consecutive years Government has failed to achieve economic growth target, as estimated target for year 2015-16 was 5.5 percent, as it could achieved 4.7 percent. Apart from this the Investment-to-GDP was recorded at 15.2% against the target of 17.7%. The fixed
investment also decreased 13.6% against the target of 16.1 percent. The public investment slightly increased 3.9% of the GDP, but remained below the targeted 4%. Savings remained almost stagnant 14.5% of GDP, while the target was 16.8%. The overall foreign private investment plunged by 55% to $405.5 million during July-February 2015-16 from $898.3 million in the same period last year, this drastic decline was due to a massive outflow of $345 million during the period.

**Purpose of Study**

The purpose of the study is to analyze economic conditions and effect on economic growth, and to introduce Investment friendly policies which can help to attract large bulk of FDI inflows in Pakistan.

**Research Objects**

- To find out the drawbacks of low economic growth & economic stability.
- To evaluate policy actions related to increase FDI inflows in Pakistan.

**Research questions**

- How FDI inflows bloom economic growth in Pakistan?
- What are incentives for foreigners to invest in Pakistan?
- Does any competing narratives for host and guest countries?

**Importance of the Study**

During last decades there have been found fluctuations in trends of FDI inflows and economic growth of Pakistan, many studies have been done on this topic by researchers and they found different trends due to continuous fluctuations in flow of FDI which influence economic growth of Pakistan. This study will contribute to policymakers and Government, to find out the reasons of fluctuations in FDI inflows and to implement investment friendly policies that can attract huge bulk of FDI inflows in country and will be helpful to enhance the economic growth of Pakistan. This study can be helpful for policymakers to focus on necessary areas and resources which can create incentives for Pakistan.

**Hypothesis**

H= GDP and FDI have co-integration with each other  
Ho= GDP and FDI do not have co-integration with each other
POLICIES OF FDI INFLOWS AND TRENDS IN PAKISTAN

Concrete policies of the host country portrait the real picture of the interests of the host countries and also give guideline to foreign investors which area of economy is need of investment; it gives confidence to investors for investments in such areas. The investment policies of host countries influence on foreign investment decisions, these policies may stimulate foreign investment or they can restrict foreign investment flows in economies in different ways, so these policies are considered basic framework of economies to attract or restrict foreign investors for investment in host countries.

Pakistan is considered as semi-industrialized economy, but if we put glance on its grassroots Pakistan was an Agricultural economy up to got independence in 1947. In initial phase it was out of capacity of Pakistan to process locally produced raw materials into industrial products. In order to improve the manufacturing capacity various types of industrial policies have been implemented in different time periods. These policies implemented in various ways focusing on private or public sectors. During 1960s and 1980s, private sector and public sector played leading role, but during the decade of 1990s, Pakistan adopted liberal, market-oriented policies and private sector was declared as engine of economic growth. The dimensions of FDI inflows soar during the decade of 1990s, Pakistan received high amount of FDI due to changing in policies, and concrete environment for investment.

In the initial phase from 1970s until mid-1980s, FDI inflow was modest due to restrictive investment policies, in 1970 FDI inflows increased from $ 23 million to $ 64 million in 1980. This period from 1970s until mid-1980s is remarked as restrictive period. The second phase started in late 1980s, this period is considered as process of liberalization and privatization (post-1988 period). FDI inflows accelerated from $ 110 million in 1987 to $ 711 million in 1997. After 1997 FDI inflows declined to $ 183 million in 2000, the reason of decline was economic sanctions after nuclear tests, Pak-US ties, Asian Financial Crisis of 1997 and some other regional problem. After that a new Investment policy have been initiated, as a result since 2004 a significant increase in net inflows of capital recorded. In 2008 FDI accounted to $ 5.4 billion, which is reported as 443 percent higher than in 2004. In 2009, FDI declined to $ 3.21 billion, this adverse decline was recorded due to Global Financial Crisis, which weakens the macroeconomic stability of economies around the world. For last few years FDI in Pakistan was in decline position because of some domestic and external issues, such as; energy crisis, worse law and order situation and improper infrastructure. In year 2013 FDI net flow was $ 1.4 billion which increased up to $ 1.6 billion in 2014. The fluctuations in FDI inflows have been found in all periods, which represent inconsistency in social, economic, and political system of the economy which remained the cause to suffer economy a lot.
A Brief Review of FDI policies of Pakistan

The 1950s, 1960s, and 1970s

During 1950s and 1960 private sector was considered as main engine for industrial investment, only a limited number of standard units was set up for public sectors. In late 1960s private sector got dominancy in the important areas of economy.

In early 1972, an Economic Reforms Order was issued by Government which took over the management of some major categories of industries, commercial banks, financial institutions, and insurance companies, as a result in 1975 started nationalization round, due to this sudden shift of private sector into nationalization tattered the confidence of private investors, as that time public sector accelerated direct investment in new industries which were ranging from basic manufacturing to final production. This changed the status of economy; all foreign investment was exempted from the horizon of nationalization.

The 1980s and 1990s

After the performance of nationalization followed in 1972, Government attribution changed towards the role of public and private sectors in September 1978. In June 1984 government articulate an industrial policy statement which states that there would be mixed economy, public and private sectors reward each other, there must be a supportive relationship between public and private sectors in managerial and entrepreneurial foundations. The basic aim of this industrial policy statement was to give equal importance to the public and private sectors, and also to encourage private sector. In order to improve the business environment and to attract FDI, a number of policy and regulatory frames were established; in 1989 a new industrial policy was introduced based on identification of the importance of private sector.

Before 1990s, there were special protocols regarding authorization of foreign investment (promotion and protection) which states that there is special registration required for FDI, act 1972.

In May 1991, such requirements were eliminated except few specific industries like explosive, radioactive substances, arms, and alcoholic beverages, all investors only required a NO Objection Certificate (NOC) related to their location of projects. In 1 July 1994, government took an initiative for attracting FDI by liberalizing the foreign exchange regime, as residents and nonresidents can assess easily to capital markets. During 1996/97 many reforms were brought and import policies were more liberalized by giving relaxation in tariff and nontariff barriers were removed, special industrial zones (SIZs) were established to attract foreign investment in export-oriented industries.
The 2013-17

The investment policy 2013 is enhancement of 1997s policy; the new policy consists of components of old policy and a frame of existing policies, and introduces modern liberalized policy and strategic programs of future. Due to changing in scenario of global economic slowdown, the investment policy 2013 is aimed to adjust and address economic priorities, domestic difficulties like power outages and war on terror, and to achieve the targets given in National policy Documents. The goal of policy 2013-17 is to provide a comprehensive environment of business for attraction of FDI; the policy is supported by FDI strategy for 5-years (2013-17) which will elaborate the facilitation procedures and role of Board of Investment (BOI) as one-widow-operation. Here are some basic principles which provide them of the policy:

- Reducing the cost of doing Business in Pakistan.
- Reducing the processes of doing Business.
- Creation of industrial clusters and Special Economic Zones.
- Linkages of trade, industrial and monetary policies for greater convergence.

FDI net inflows and Trends in Pakistan

Pakistan gradually adopted liberalization trends to attract the FDI and implemented its economic policies gradually; this gradual adaptation provided the enough time to the local industry to become competitive, from 1947 to 1958 Pakistan followed very strict role on FDI. In 1977 introduced Nationalization program, from 1988 to1999 trade liberalization undertook in Pakistan under a series of Structural Adjustment Program (SAP). In Pakistan FDI inflows increased since mid-1990s, different policies were implemented and changed with passage of time, but period of 2000 to 2007 is considered as most successful period of economic policies for FDI inflows. In 2013 a new policy was introduced which contained various new incentives to attract the foreign investors, the target of this policy was to attract the 20% of GDP as FDI stock but government failed to achieve its target. The figure 1 shows the highlights of FDI inflows from 1990 to 2015:

![Figure 1. FDI net inflows Current US $ (billions)](Source: World Development Indicators (WDI))
The flows of FDI in Pakistan are fluctuating due to various reasons like instability of Politics, Economic problems, Terrorism and weak infrastructure of country. During 1990s to 1996 FDI inflows increased, but during the period of 1997 to 2000 FDI inflows decreased in Pakistan periodically due to instable political system and many changes in foreign trade policies. After 2000 the establishment of Military government (3rd period of Dictatorship in Pakistan) the situation of Pakistan again came into stability and new policies were formulated to attract foreign investors, it resulted to increase in flows of FDI again in Pakistan continuously up to 2007, this period is considered as Golden period of policies in history of Pakistan. After 2007 due to increase in terrorist activities and unbalanced situation of economy these flows decreased period to period still 2012, during fiscal year 2013 this flow is going to increase gradually, up to the end of 2014 it remained in increasing proportion. During last year 2015 this flow again decreased due to inappropriate policies and instable political system.

**FDI net inflows and Gross Capital Formation (GCF)**

The size of capital inflows determines the level of FDI amount in a country. Pakistan was basically an Agriculture dependent country since its independence 1947. After the period of 1970s the period of liberalization and advancement of policies for FDI inflows encouraged foreign investors to invest in country, it was start of modernization and liberalization for Pakistan, the period of 1990s is considered as the significant period of FDOI inflows in Pakistan, in this period almost all restrictions laid down for foreign investment which were implemented according to Act 1976, in which each investment was subject to separate authorization, but in May 1991 this requirement was eliminated, in which no special registration was required for FDI, and same rules and regulations were applied to FDI as to domestic investors.

The dimensions of FDI inflows in Pakistan can be explained in terms of size and percentage of Gross capital formation (%GCF), a term used to describe net capital accumulation during an accounting period. The table below describes the details of FDI inflows in Pakistan for the period of 1990 to 2015:

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI US $ (Billions)</th>
<th>%GCF</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>245.2629635</td>
<td>5.14404803</td>
</tr>
<tr>
<td>1991</td>
<td>258.414487</td>
<td>3.013821089</td>
</tr>
<tr>
<td>1992</td>
<td>336.4798571</td>
<td>10.38626099</td>
</tr>
<tr>
<td>1993</td>
<td>348.5569578</td>
<td>3.945843693</td>
</tr>
<tr>
<td>1994</td>
<td>421.0246385</td>
<td>0.765118963</td>
</tr>
<tr>
<td>1995</td>
<td>722.6315607</td>
<td>3.8253255</td>
</tr>
</tbody>
</table>
Term Capital formation referring to net additions of capital stock in form of equipment, buildings and other intermediate goods. Capital stock is used by nation in combination with labor to provide services and produce goods; any type of increase in this capital stock is known as capital formation. Generally, if higher the capital formation of an economy, the faster an economy can grow its aggregate income. In practice if increasing an economy’s capital stock it increases its capacity for production also, which means an economy can produce more. Producing more goods and services can lead to an increase in national income levels. Pakistan has received significantly higher amount of FDI over last two decades. The FDI inflows during period of 1990s increased significantly. The pace of FDI inflows in Pakistan has remained slower as compare with other developing countries of Asia. Table 1: portraits a brief picture of FDI net inflows in Pakistan during the period from 1990 to 2015 from all over the world as shown in column 1 in current US dollars and column 2 shows the Gross Capital formation in form of current US dollars from period of 1990 to 2015. FDI that Pakistan receiving shows fluctuations of increasing and decreasing with the passage of time. This data is obtained from World Development Indicator (WDI), according to this data and research investigations of different Authors, during last two decades there are huge inflows of FDI in Pakistan but Gross
capital formation is not increased as compare to FDI inflows, there is always fluctuations in formation of capital so still economy of country is suffering serious situations of finance, management and deficits of trade balance and many related problems. Although Pakistan is enrich with Natural resources, higher number of labor force and fertile land and having many opportunities of investments in different sectors but still remained failed to capture a good position in development, and bearing a weak infrastructure and low level of awareness.

**Currently Country wise FDI net inflows in Pakistan from all around the world**

Due to the global integration of world economies Pakistan also adopted liberalized policies to attract FDI. The main goal of these policies is to address and adjust the economic priorities, reduce the difficulties, encourage and facilitate domestic and international investors by providing a comprehensive framework for business environment, which proved helpful to attract FDI inflows in Pakistan. These policies include Free trade Agreements (FTAs), Special Economic Zones (SEZs) and Friendly regulatory reforms to meet the global competitiveness effectively and efficiently. These policies brought fruitful results by attracting bulk of FDI inflows, here is portrayed a brief picture of these inflows attracted recent years, the table below shows FDI inflows from different countries in Pakistan for the period of 2007-8 to 2015-16 (July-Jan).

![Figure 2. FDI inflows in Pakistan ($ millions)](chart.png)

<table>
<thead>
<tr>
<th>Year</th>
<th>USA</th>
<th>UK</th>
<th>Japan</th>
<th>Hong Kong</th>
<th>Switzerland</th>
<th>Saudi Arabia</th>
<th>Germany</th>
<th>Korea (South)</th>
<th>Norway</th>
<th>China</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015-16 (July-Jan)</td>
<td>-86.5</td>
<td>24.5</td>
<td>12.8</td>
<td>94.3</td>
<td>-74.4</td>
<td>-30.6</td>
<td>-2.3</td>
<td>1</td>
<td>409</td>
<td>162.4</td>
<td></td>
</tr>
<tr>
<td>2014-15</td>
<td>209</td>
<td>174.3</td>
<td>71.1</td>
<td>83.4</td>
<td>2.8</td>
<td>-64.8</td>
<td>-20.3</td>
<td>14.3</td>
<td>2.7</td>
<td>255.3</td>
<td>-93</td>
</tr>
<tr>
<td>2013-14</td>
<td>212.1</td>
<td>157</td>
<td>30.1</td>
<td>228.5</td>
<td>209.8</td>
<td>-40.1</td>
<td>-5.7</td>
<td>24.4</td>
<td>-21.6</td>
<td>695.8</td>
<td>224.4</td>
</tr>
<tr>
<td>2012-13</td>
<td>227.1</td>
<td>633</td>
<td>30.1</td>
<td>242.6</td>
<td>149</td>
<td>3.2</td>
<td>5.5</td>
<td>25.8</td>
<td>0</td>
<td>90.6</td>
<td>285.5</td>
</tr>
<tr>
<td>2011-12</td>
<td>227.7</td>
<td>205.8</td>
<td>29.7</td>
<td>80.3</td>
<td>127.1</td>
<td>-79.9</td>
<td>27.2</td>
<td>25.4</td>
<td>-275</td>
<td>126.1</td>
<td>289.7</td>
</tr>
<tr>
<td>2010-11</td>
<td>238.1</td>
<td>207.1</td>
<td>3.2</td>
<td>125.6</td>
<td>110.5</td>
<td>6.5</td>
<td>21.2</td>
<td>7.7</td>
<td>-48</td>
<td>47.4</td>
<td>631.3</td>
</tr>
<tr>
<td>2009-10</td>
<td>468.3</td>
<td>294.6</td>
<td>26.8</td>
<td>9.9</td>
<td>170.6</td>
<td>-133.8</td>
<td>53</td>
<td>2.3</td>
<td>0.4</td>
<td>-3.6</td>
<td>1,019.6</td>
</tr>
<tr>
<td>2008-09</td>
<td>869.9</td>
<td>263.4</td>
<td>74.3</td>
<td>156.1</td>
<td>227.3</td>
<td>-92.3</td>
<td>76.9</td>
<td>2.3</td>
<td>101.1</td>
<td>-101.4</td>
<td>1,964.2</td>
</tr>
<tr>
<td>2007-08</td>
<td>1,309.3</td>
<td>460.2</td>
<td>131.2</td>
<td>339.8</td>
<td>169.3</td>
<td>46.2</td>
<td>69.6</td>
<td>1.2</td>
<td>274.9</td>
<td>13.7</td>
<td>2,005.2</td>
</tr>
</tbody>
</table>

Source: Board of Investment of Pakistan (BOI)
4.8% increase in Net FDI in July-February 2015-16 as compared to July-February 2014-15. Note: Pakistan’s Fiscal Year runs from 1st July till 30th June.

Factors that influencing FDI flows in Pakistan

According Liberal School of thoughts, FDI is considered beneficial for developing countries; this assumption is based on the idea that FDI can generate positive spillovers for rest of the country. Moreover, FDI can bring new technology and information which a developed country may share with host country, and host country will enjoy the technology transfer, foreign funds, and creation of employment. There are lots of factors which are influencing on the flow of FDI, but most influential factors are as below;

Market Size
The market size is always remained as main source of attraction for investors, beside this Pakistan is a populated country of about 190 million people offering a potential for marketing consumers and durable goods. Economy of Pakistan is world’s 23rd largest economy in terms of GDP growth, and 26th largest country in terms of Purchasing power parity. Beside these all incentives, the inflow of FDI in Pakistan remained far from developments, although numerous incentives given to foreign investors. Recently if we look at the amount of FDI in Pakistan the results are significantly successful in limited areas, but not as significant as in other Asian countries like; China, Hong Kong, Malaysia and Thailand.

Political Stability
Political stability plays very important role for attracting foreign investors, because it creates confidence for foreign investors. According to World Bank survey of 2014, those countries which are politically stable attract 67 percent more foreign investment than those countries which are politically unstable, Pakistan is considered as semi-stable country in this regard. Due to unstable situation of politics many investors worry about their incentives, and remained the reason of low level inflows of foreign investment in last decades. During 1988/96, political situation in Pakistan remained very worse, even within 90 days the elected governments were dismissed; such frequent changes in government bring changes in policies and programs which are very hard for foreign investors.

Labor Force
In terms of human resource, the adult population (age 15-59) is considered as wealth of a nation. Those countries remained center of attraction who has technically trained, educated,
and disciplined labor with cheap wages. Pakistan has 9th largest labor force in the world which has comparatively lower wages in South Asia. Regarding the education, health and skills, Pakistan has shortage of technically trained and educated labor, which may cause to discourage foreign investors. As compare to other developing countries, Pakistan has lower position in terms of health, education and awareness; foreign investors may not find the workforce they need. Beside these all, Pakistan’s labor laws are very complicated and posing problems for management and causing productivity losses.

**Infrastructure**

The most important ingredient for business environment to attract foreign investment is availability, reliability, and cost of infrastructure facilities (power, telecommunication, transportation and supply of water etc). Those countries which have poor infrastructure ultimately face increasing transaction cost and limited access to local and international markets which is considered serious hurdle and discouraging factor for FDI in such countries. In most developing countries infrastructure is not well developed so they are unable to attract sufficient amount of FDI.

Pakistan is one of those developing countries, in past Pakistan was not able to attract sufficient amounts of FDI due to low level of infrastructure but in recent years Pakistan has developed better infrastructure as compare to other developing countries in the world.

Pakistan has improved telecommunication, water supply and somehow power sectors but still need to remove power shortage in country. In transportation, railway is considered as cheap way to transport the goods and traveling, the railways system of Pakistan become very slow and damaged so it needs to improve, if new policies are introduced to improve railways tracks and durable engines it will be helpful to reduce the cost of transportation.

**Economic Strength**

Here economic strength refers the stability of economy of a country and its policies for long time growth; the assurance of high growth, increasing opportunities for business, more government development projects and private investments and purchasing power of people. Investors before investing in any country look deeply on above fundamentals of the country where they are going to invest. If these fundamentals are weak, government policies are unpredictable that what they are going to do in next year investors will not invest in such economies.

In last decades economic policies of Pakistan remained very poor, these policies have been changed with change in governments, even change in tenure of government changed the policies. Due to these abrupt changes in policies FDI remain slow and discouraging in Pakistan.
In recent years especially after 1997, these policies become very flexible, concrete, investment oriented. Many incentive are given to foreign and local investors to invest in country, since 1997 to 2016 the flows of FDI in Pakistan soared in significant level, but still there exist internal political problems therefore these flows are effected in a drastic manner, in whole history political stability remained as quite common in instable situation while other factors are changed significantly in a positive way.

The Incentives for Foreigners and Pakistan to Invest

Pakistan has a potentially big market with about 190 million, which is considered as natural wealth of a nation. Pakistan is gifted with abundant natural resources, favorable demographic location, large number of trainable labor force with very cheap wage, and a rising number of domestic consumers which provide large number of opportunities for investors. The demographic location of Pakistan in South Asia makes it premier in trade, energy, and transport. Its sea routs connect middle-east with rest of world by providing reduced transportation cost. These advantages make Pakistan a market place pour with opportunities and a good reason to attract foreign investors to invest.

Incentives for Foreigners

1. Abundant Land and Natural Resources: Crop production, mineral reserves, fisheries and livestock production.
2. Large and Growing Domestic Market: A growing middle-class consumers with growing incomes.
3. Well-Established Infrastructure and Legal System: inclusive road, rail and sea link, quality telecommunication and IT Services.
4. Strategic-Location as Regional Hub: strong and long-standing links with Middle-East and South Asia.
5. Strong Human Resources: Labor force with cheap wages.

Incentives for Pakistan

1. Transfer of modern Technology.
2. Financial Assistance.
3. Employment creation.
4. Development in Labor skills and improvement in Infrastructure.
5. Enhanced competition in markets.
REVIEW OF LITERATURE

Foreign direct investment has great influence on economic condition of any country, particularly on developing countries like Pakistan, sub-Saharan African countries and like these poor and developing countries. Many studies have been made earlier by different economists which shows the relationship between investment and growth, this relation is proved empirically and theoretically, there are different views about the relationship between investment and growth some economists argue that there is positive relationship between investment and growth while others argue that there is negative relationship between investment and growth, which have been proved empirically and theoretically. The aim of this paper is to find out the impact of FDI on Economic Growth of Pakistan through empirical analysis. The research is conducted on the basis of following literatures of earlier studies.

(2016). Foreign Direct Investment, Terms of Trade, and Quality Upgrading: What is so special about South Asia? By the Konstantin M. Wacker, Phillip Grosskurth, and Tabea Lakemann, the existing literature has highlighted positive effect of FDI on export upgrading and associated terms of trade in developing economies. However FDI effect is found to be negative in South Asia. This paper elaborates on the South Asia specific effect by emphasizing the role of human capital in the positive link between FDI and terms of trade. These patterns demonstrate for two South Asian economies (Bangladesh and Pakistan) and two East Asian economies (Malaysia and Thailand) for which historical breakdowns of FDI data are available.

(2016). Determinants of Intra Regional Trade and Intra Regional Foreign Direct Investment (FDI) in South Asia: A Gravity model approach, Thesis, By Hossain Mohammad Imran. This thesis investigates and analyzes the various aspects of intra-regional trade and intra-regional FDI inflows of South Asia. It also focuses on economic integration in South Asia in an attempt to access the impact of various bilateral and multi-lateral treaties on regional trade and FDI. This thesis tests the impact of economic liberalization reforms on South Asia’s foreign trade and FDI. Findings of an empirical estimation on impact of economic liberalization suggests that reform measures such as trade liberalization, Capital market liberalization and fiscal reforms are positively correlated with foreign trade and inward FDI flow of these countries. This thesis empirically examines the determinants of intraregional trade and intraregional FDI in South Asia by the gravity trade model using different sets of panel data from 1990 until 2012. The final results of this thesis show that the initiatives taken so far toward an expansion of intraregional trade and intraregional FDI in South Asia have not been effective. Weak institutional framework, interstate hostility and ineffective regional agreements have been accused for not push regional integration forward to a level commensurate with the potential.
Growth effect of FDI in Developing Economies: The role of institutional quality, By Cristina Jude and Gregory Leiveuge. This paper investigates the effect of FDI on economic growth conditional on the institutional quality of host countries. To analyze the results Panel Smooth Regression model is used on the basis of a large Sample of developing countries. The results of study show that FDI has a positive effect on growth only beyond a certain threshold of institutional quality.

Does inward FDI crowd-out Domestic Investment? Evidence from Uganda: By Kasule Twaha Ahmed, Gairuzazmi M. Ghani, Noorihsan Mohamad and Alias M.Derus. This paper investigates whether FDI crowds-out Domestic Investment in Uganda. To analyze the effect on aggregate economy and at sectorial level data is used from 1992 to 2012. The analysis result obtained a robust neutral effect on the overall economy and on sector level there is found a crowding-out effect. In this paper there is used Exogeneity and Endogeneity test, Unit Root test, ADF and OLS to estimate the data results.

Impact of Foreign Direct Investment on Economic Growth of Pakistan: By Malik Khola Gul and Imran Naseem, this paper analyzes the impact of FDI and trade openness on economic growth of Pakistan. For this study they used time series data from 2008 to 2013, and the methods they used for this purpose are co-integration analysis, regression analysis, correlation and Durbin Watson test which check the long run relation and association among variables. The findings of this paper suggest that FDI, trade openness and domestic Capital are positively affecting the Economic Growth of Pakistan as compared with other variables.

Contribution of Foreign Direct Investment to Economic Growth in Bangladesh: Thesis, By Muhammad Abu Rayhan. This paper examines the contribution of FDI to economic growth in Bangladesh over the period from 1975 to 2012. The methods used in this study are OLS, 2SLS, VAR and Granger Causality. The findings of results show there is positive relationship between FDI and economic growth.

Foreign Capital Flows and Economic Growth in Pakistan: An Empirical Analysis, by Sharafat Ali, this study is focused on the examination of effects of foreign capital inflows (FCI) on economic growth of Pakistan. To estimate the empirical results johansen co-integration technique and Granger causality test has been used for the analysis for the span of 1972-2013. The results reveal negative impacts of these flows on economic growth of economy in long-run. Short-run analysis confirmed unidirectional causality running from debt service, FDI, inflation and literacy rate to growth. Bidirectional causality between remittances and growth has been found.

Impact of Foreign Direct Investment on Economic Growth in Pakistan: by Zia Ur Rahman. This paper conducts the impact of FDI on economic growth of Pakistan, time series
data is utilized which is comprises from 1981 to 2010. To analyze the results, Multiple Regression technique is used. The findings of estimation indicate that there is positive relationship between the FDI and GDP and have a negative relationship with CPI. Here GDP is used as dependent variable, while Foreign Direct Investment (FDI) and Consumer Price Index (CPI) are independent variables.

(2013). Foreign Direct Investment Inflows in Pakistan: A Time Series Analysis with Autoregressive Distributive Lag (ARDL) Approach, by Sober Mall. This paper attempts to model, Determinants of FFI inflows in Pakistan: A time series analysis with ARDL approach using data for the period 1977 to 2010. However in a specification, FDI is found important with the elasticity of GDP growth rate 10% level of significance and infrastructure at 1% level of significance.

(2013). Foreign Direct Investment (FDI) and Economic Reforms: The South Asian Perspective, by Mohammad Imran Hossain. This paper examines some aspects of FDI inflow in four major South Asian countries namely Pakistan, Bangladesh, India and Sri Lanka. Various trend of FDI flow to these countries are analyzed. An empirical estimation of the impact of economic liberalization reforms on inward FDI flow of these countries is conducted by using a data set ranging from 1991 to 2012 by the panel fixed effect model. The empirical findings of the paper suggest that trade liberalization; capital market liberation and fiscal reforms are positively correlated with FDI flow. The study suggests that economic liberalization reforms need to be continued in these countries in order to support more and more FDI flows.

(2013). Effect of Macro Variables on the FDI inflows: The Moderating Role of Political Stability: An Evidence from Pakistan, by Arfan Shahzad and Abdullah Kaid Al-Swidi. This paper examines the moderating role of Political Stability on the relationship between macroeconomic variables and FDI inflows in Pakistan. The methods used in this estimation are ADF to check stationary of data and for regression used Eviews and SPSS statistical software package. The findings of the study show that GDP growth rate, exports, import and balance of payment have positive significant effects on FDI inflows in Pakistan. Based on findings of this study, it is strongly suggested that political stability is crucial for the country's domestic and foreign investment expansion in the future course of direction.

(2013). Role of Foreign Direct Investment in Economic Growth of Pakistan: by Nayyra Zeb, Fu Qiang and Sundas Rauf. The aim of this paper is to investigate the effect of FDI on Pakistan’s economic growth during 1972 to 2012. Besides FDI, three other variables such as trade openness, political instability and terrorist attacks are also used in this study. The method used to obtain result is Least Square Method (OLS) which concludes the possible effect of these variables on GDP of Pakistan. The results show that FDI has positive significant effect on economic growth of Pakistan.
(2013). Factors Affecting Foreign Direct Investment in Pakistan: by Dr. Abdul Ghafoor Awan, Waqas Ahmed, Pervaiz Shahid and Jahanzeb Hassan. FDI inflows of Pakistan started fluctuating from 1990s to 2012 and this high volatility of FDI inflows drew the researchers’ attention to examine the factors affecting FDI inflows in Pakistan by using annual data from 1988 to 2012. Multiple Linear Regression model is used to study the relationship between dependent and independent variables. The empirical results show that Gross Capital Formation (GCF), Gross National Income (GNI) and Exports (X) have significantly positive affect on FDI inflows of Pakistan. Beside this, external debt and imports are negatively related with FDI inflow in Pakistan. The results also show negative relationship between military expenditures and FDI inflows in Pakistan.

(2012). Spillover Effect of Foreign Direct Investment on Economic Growth in Pakistan: By Muhammad Kashif Khan, Muhammad Aslam Khan, Sajjad Latif Awan, Abid Usman and Amen Imran, this paper is geared at underpinning the impact of FDI on economic growth in developing economy, particular references with Pakistan. The paper considers a timeline of 2001 to 2010 measuring the effect of FDI on Economic growth, the empirical results of paper reveals a weak positive correlation of FDI with economic growth, this paper suggests that there is insignificant effect of FDI on economy. In this study Pearson correlation and Multiple Regression Model is used to analyze the results.

(1991-2012). Determinants of FDI inflows in Pakistan: An Empirical study by Sadaf Alam and Anum Iqbal, they used Ordinary Least Square method (OLS) to get results, they found overall positive relationship between FDI and macro-economic variables they used. To make their evidences more strong and significant they used Augmented Dickey Fuller (ADF) and Johnson co-integration test.

(2012). Investment and Growth in Rich and Poor countries by Yin-wong Cheung, Michael P.Dooley and Vladyslav Sushko: this paper shows the association between Investment and Growth and empirical findings highlights the substantial heterogeneity for the effect of investment on economic growth and suggests a possible negative association, results are based on cross-sectional and time-series regression.

(2011). working paper: Foreign Direct Investment and Economic Growth in Pakistan: A Sectorial Analysis by Mohammad Arshad Khan and Shujaat Ali Khan, this paper establishes an empirical relationship between industry-specific Foreign Direct investment (FDI) and output under the framework of Granger causality and panel co-integration for Pakistan over the period of 1981-2008. The results supports that FDI has positive effect on output in the long run.

(2011). Foreign Direct Investment in Pakistan: The role of International Political Relations, by Muhammad Arshad Khan. The main focus of this paper is to investigate the
impact of Pakistan’s international political relations on FDI inflows. The analysis has been carried out over the period of 1972 to 2009, the results found suggests that U.S policies produce no significant influence on long-run capital inflows to Pakistan in the long-run, while in short-run U.S diplomatic policies produces negative influence on inward FDI to Pakistan. This implies the deterioration of U.S-Pak diplomatic relations exerts significant negative impact on capital inflows to Pakistan in the short-run. The results also reveal that domestic investment; financial development, infrastructure and natural resources endowment exerts significant positive impact on FDI in the long-run as well as short-run. Trade openness influences FDI inflows negatively in long-run, but produce no significant impact on FDI in short-run.

RESEARCH METHODOLOGY

Research variables

. Dependent variable is: Gross Domestic Product (GDP)
. Independent variables are: 1) Foreign Direct Investment (FDI) 2) Labor Force (LABOR)

Expected signs for variables

The variables used to conduct the research are: GDP as dependent variable and FDI, and LABOR FORCE as independent variables. The expected signs for these variables are given as bellow in table 2.

<table>
<thead>
<tr>
<th>Independent variables</th>
<th>Expected Signs</th>
<th>Sources of Data</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI</td>
<td>+</td>
<td>World Development Indicator</td>
</tr>
<tr>
<td>Labor force</td>
<td>+</td>
<td>World Development Indicator</td>
</tr>
</tbody>
</table>

The purpose of this research is to study and analyze the effect and relationship of these variables and prove either positive or negative relationship between these variables, how these variables are effected and influenced with in economic modeling.

Data Description of Variables

This paper will analyze the relationship between GDP, FDI, LABOR FORCE, and their effect on Economic growth of Pakistan. The data for these variables is taken from WDI (world data indicators), as this data is secondary by nature from year 1990 to 2015. So in order to get results we use empirical Analysis, along with FDI these other variables also may affect the economic growth of the country, as inflow of the FDI is dependent of labor skills, infrastructure,
financial system, socio-political and governance performance because if these institutions are strong the FDI inflows will increase and show progressive and significant results, similarly these other variables also have importance for economic growth of the country.

Model specification
In this analysis: used Linear Regression model to conduct fruitful and effective results. The selected variables of this study are GDP, FDI and LABOR which can be represented as:

\[
\text{GDP} = f(\text{FDI}, \text{LABOR})
\]

The data was transformed into log form for regression to get more accurate results.

\[
\text{Log}(\text{GDP})_t = \beta_0 + \beta_1\text{Log}(\text{FDI})_t + \beta_2\text{Log}(\text{LABOR})_t + \epsilon_t
\]

ANALYSIS AND MODEL ESTIMATION
Unit Root Test
In time series data mostly data variables are non-stationary, so unit root test is applied in order to find the stationary of the data variables in the model by using ADF test to test the null hypothesis. In order to get more accurate results original data is transformed into log form in the model. If all variables were found non-stationary at level we cannot reject null hypothesis and to solve this problem we will use ADF test. While conducting unit root test, it’s an assumption of ADF test which states that if absolute values of t-statistic of ADF test are greater than critical test values at 1%, 5%, 10% level or if the probability values are less than 0.5% significance level, null hypothesis can be rejected (means variables are stationary at first difference).

<table>
<thead>
<tr>
<th>Variables</th>
<th>First Difference</th>
<th>1st Difference with ADF constant &amp; Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>LGDP</td>
<td>L(1)</td>
<td>-4.317538**</td>
</tr>
<tr>
<td>LFDI</td>
<td>L(1)</td>
<td>-3.807131**</td>
</tr>
<tr>
<td>LLABOR</td>
<td>L(1)</td>
<td>-3.079450**</td>
</tr>
</tbody>
</table>

Note: *1%, **5%, ***10% Level

The table 3 represents the values of ADF test at first difference with constant and trend. The results revealed to be stationary at first difference which rejects the null hypothesis, in other words the series doesn’t have unit root problem and coefficients of variable of ADF test are significant at 5% level of significance. Hence it is concluded that series is stationary and all variables are interconnected in same order at first difference L (1).
Leg Selection Criteria to check Co-integration

In order to check co-integration between variables of data there is a special criterion in which lag periods are selected in order to find the co-integration among selected variables. In this technique there is given specific criterion to check integration of variables.

Table 4. VAR Lag Order Selection Criteria

<table>
<thead>
<tr>
<th>Lag</th>
<th>LogL</th>
<th>LR</th>
<th>FPE</th>
<th>AIC</th>
<th>SC</th>
<th>HQ</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>0.295415</td>
<td>NA</td>
<td>0.000257</td>
<td>0.245871</td>
<td>0.394650</td>
<td>0.280919</td>
</tr>
<tr>
<td>1</td>
<td>90.88075</td>
<td>148.2306*</td>
<td>1.56e-07*</td>
<td>-7.170978*</td>
<td>-6.575864*</td>
<td>-7.030787*</td>
</tr>
<tr>
<td>2</td>
<td>94.72770</td>
<td>5.245832</td>
<td>2.64e-07</td>
<td>-6.702518</td>
<td>-5.661068</td>
<td>-6.457184</td>
</tr>
<tr>
<td>3</td>
<td>104.4184</td>
<td>10.57169</td>
<td>2.87e-07</td>
<td>-6.765310</td>
<td>-5.277525</td>
<td>-6.414833</td>
</tr>
<tr>
<td>4</td>
<td>113.0978</td>
<td>7.101323</td>
<td>4.04e-07</td>
<td>-6.736164</td>
<td>-4.802044</td>
<td>-6.280544</td>
</tr>
</tbody>
</table>

*Indicates lag order selected by the criterion

LR: Sequential modified LR test statistic (each test at 5% level)
FPE: Final Prediction Error
AIC: Akaike Information Criterion
SC: Schwarz Information Criterion
HQ: Hannan-Quinn information criterion

Table 4 indicated the available criterion on the basis of lag order. Here * denotes lag order selected by the criterion. We will estimate our results on the basis of AIC, the selected criterion for AIC in table 2 is first lag order L (1). Now we will use Johansen Co-integration test in order to test the results of null hypothesis that either there exist co-integration among variables or not.

Johansen Co-integration Test

In time series data when two or more series are individually integrated and become stationary when differenced at first-order in series so we say that variables co-integrated. Co-integration describes a particular long-run equilibrium relationship. The main reason of using co-integration is that when we run simple regression models most of time they produce spurious regressions which leads to a false relation which even don’t exist among variables, in order to avoid such spurious regressions we use co-integration test which presents the actual number of co-integrating equations and the long-run relationship among the variables in given model. Co-integration test mainly relays on results of trace statistic values and Max-Eigen statistic values compared with their 0.5% level of critical values.
Table 5. Unrestricted Co-integration Rank Test (Trace)

<table>
<thead>
<tr>
<th>Hypothesized No. of CE(s)</th>
<th>Eigen Value</th>
<th>Trace Statistics</th>
<th>0.5Critical Value</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>None*</td>
<td>0.957066</td>
<td>83.47175</td>
<td>29.79707</td>
<td>0.0000</td>
</tr>
<tr>
<td>At most 1*</td>
<td>0.544755</td>
<td>17.36168</td>
<td>15.49471</td>
<td>0.025</td>
</tr>
<tr>
<td>At most 2</td>
<td>0.039044</td>
<td>0.836365</td>
<td>3.841466</td>
<td>0.3604</td>
</tr>
</tbody>
</table>

*Note: Trace test indicates No. of co-integrating Equations at the 0.05 Level
*denotes Rejection of the hypothesis at the 0.05 Level

The table 5 presents the results of trace statistics at 5% level. The results show that there are two co-integrating equations at 5% level. In the above table trace statistics value is greater than critical value (83.47175>29.79707) and the probability value is less than 5% level of significance. The results determine the rejection of null hypothesis, in other words co-integration exist among variables used in this model. This is clear from trace statistic results that there is real co-integration among variables. To confirm furthermore we can check the results of Max-Eigen statistic results if they are following the same pattern as trace statistics it means there is confirmation of real results we obtained by applying Co-integration test.

Table 6. Unrestricted Co-integration Rank Test (Maximum Eigen Value)

<table>
<thead>
<tr>
<th>Hypothesized No. of CE(s)</th>
<th>Eigen Value</th>
<th>Max-Eigen Statistics</th>
<th>0.5Critical Value</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>None*</td>
<td>0.957066</td>
<td>66.11006</td>
<td>21.13162</td>
<td>0.0000</td>
</tr>
<tr>
<td>At most 1*</td>
<td>0.544755</td>
<td>16.52532</td>
<td>14.26460</td>
<td>0.0216</td>
</tr>
<tr>
<td>At most 2</td>
<td>0.039044</td>
<td>0.836365</td>
<td>3.841466</td>
<td>0.3604</td>
</tr>
</tbody>
</table>

*Note: Max-Eigen value test indicates No. of Co-integrating Eq(s) at the 0.05 level
*denotes rejection of the hypothesis at the 0.05 level

Table 6 show the results obtained by Max-Eigen test, the test follow the same pattern having two co-integrating equations and Max-Eigen statistics values are greater than 5% level of critical values (66.11006>21.13162), and probability value is less than 5%. On the basis of results of both trace test and Max-Eigen test it’s clear that null hypothesis is rejected (null hypothesis was that there is no co-integration among variables), and there are clear results that co-integration exist among variables and they have association for long-run.
Vector Error Correction Mechanism (VECM) Model

This research is conducted on the basis of VECM model which shows the long-run and short-run relationship among dependent and independent variables, the results of regression of this model only show the coefficient values of variables, this model don’t show the t-statistic value and probability values of estimation which are very useful tools to signify the effectiveness of a model. In order to get significant results Ordinary Least Square (OLS) model is used within this study to get accurate and clear results. The model is designed as; LGDP is dependent variable and LFDI and LLABOR represents independent variables. The regression model is developed in following way.

\[ \Delta \log {\text{GDP}}_t = \beta_0 + \beta_1 \log \text{FDI} + \beta_2 \log \text{LABOR} + \epsilon_t \]  

(3)

Figure 7. VECM Model Testing

<table>
<thead>
<tr>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C(1)</td>
<td>-0.285856</td>
<td>-1.507551</td>
<td>0.1539</td>
</tr>
<tr>
<td>C(2)</td>
<td>0.025598</td>
<td>1.107397</td>
<td>0.2868</td>
</tr>
<tr>
<td>C(3)</td>
<td>0.088021</td>
<td>0.353409</td>
<td>0.7290</td>
</tr>
<tr>
<td>C(4)</td>
<td>-0.191162</td>
<td>-0.853028</td>
<td>0.4080</td>
</tr>
<tr>
<td>C(5)</td>
<td>0.045418</td>
<td>1.321534</td>
<td>0.2075</td>
</tr>
<tr>
<td>C(6)</td>
<td>-0.001980</td>
<td>-0.053639</td>
<td>0.9580</td>
</tr>
<tr>
<td>C(7)</td>
<td>1.007885</td>
<td>0.556911</td>
<td>0.5864</td>
</tr>
<tr>
<td>C(8)</td>
<td>-0.725025</td>
<td>-0.411917</td>
<td>0.6866</td>
</tr>
<tr>
<td>C(9)</td>
<td>0.069952</td>
<td>0.849185</td>
<td>0.4101</td>
</tr>
</tbody>
</table>

R-squared: 0.441237  Mean dependent var: 0.074520
Adjusted R-squared: 0.121943  S.D. dependent var: 0.072494
S.E. of regression: 0.067930  Akaike info criterion: -2.254498
Sum squared resid: 0.064603  Schwarz criterion: -1.810174
Log likelihood: 34.92673  Durbin-Watson stat: 2.139050

The above table represents the results of VECM model. In this table C (1) represents the coefficient of error correction term which reveals the speed of adjustment or dis-adjustment
towards the equilibrium in long-run, while negative sign (-ve) of coefficients indicates convergence towards equilibrium and vice versa. The findings of the empirical estimation show that GDP and FDI are co-integrating with the rate of 28% which is very slow rate; this reveals that they have long-run relationship but with slow speed towards equilibrium, it will take very long time to get optimal results. R-square results unveil that these variables; FDI, and LABOR force altogether contributes 44.1237% in growth of economy of Pakistan. D-Watson test results presenting the evidence that how much healthy is a regressed model if results are around 2% or greater than 1% level, in our model D-Watson stat is 2.139050 which show that our model is healthy is results obtained are very suitable and there is no serial correlation among variables.

CONCLUSION

For most of economies FDI is considered like blood circulating in the body. FDI is placed as very important economic indicator to boost up economic position of a country, especially in developing countries FDI is considered as rapid source of development and a powerful tool for progress, and best alternative to gain the required sources a country facing shortage. FDI helps to avail opportunities of employment, transfer of technologies, awareness in innovation and inventions, improvements in skills, opportunities to expand business, development in infrastructure, financial support in required areas and diversification in institutions by well know-how of modern methods used all around the world. This all brings a positive response in economic growth of a country. The aim of this study is to find out the contribution of FDI inflows in economic growth of Pakistan over the period of 1990 to 2015 by using Unit root test, cointegration test and vector error correction model.

The findings of the study suggest that, there is strong correlation between GDP, FDI and Labor force in long-run relationship. The negative sign of C(1) coefficient represents the convergence towards equilibrium for long-run relationship, the Probability value is 0.1539 which is greater than 5% Level indicating that these variables will converge towards equilibrium but it will take long time to achieve required results. The findings of the empirical study show that there is significant effect of FDI inflows on economic growth in long-run and labor force is much correlated with FDI to boost up economic growth.

There are some plus points and weaknesses found during this research analysis, which are given bellow.

Plus points;

- Beside market size, Pakistan is most populated country offering potential consumers of durable goods along with satisfactory purchasing power parity.
• In terms of human resources, Pakistan is offering huge number of labor force at cheap wages as compare to other developing nations.
• Pakistan has well developed infrastructure as compare to other developing countries, it will provide ease in transformation of goods and services and will reduce cost of transportation and communication.
• Pakistan has abundant land and natural resources, a strategic location as regional hub for international business and exchange, especially Gowarder sea port which is predicted as center of world business and transportation.

Weaknesses;
• Need political and economic stability. Need of long-term projects and proper policies for long-run which may assure foreign investors for durability of these projects
• Need of technical skills, Proper education and advanced technological knowledge.
• Need to educate local people for competitiveness and better quality of life.
• Still need improvements in transportation system, especially railways system.

It is concluded that due to instability in political and foreign investment policies the growth of economy remain slower and it couldn’t be effective in short-run. In short-run it can be effective if positive measures are taken to strengthen the investment policies and political stability. This paper describes overall effect of FDI on economic growth of Pakistan. In future if worked individually on sectors of economy like Agriculture, Foreign trade, Manufacturing, Industry, Transportation, Communication, Finance, and Energy sector, these sectors have great potential to contribute and enhance economic growth.

RECOMMENDATIONS
Geographically Pakistan has got very important place but it needs to improve some specific areas within the country which will be helpful to attract much more investors to invest in Pakistan.
• Government should provide incentives to local entrepreneurs, give them facilities to grow in a competitive marketplace, if local economy is growing it will cause to attract foreign investors.
• Government should take measure to avail training and proper knowledge to labor. Also educate the people; the literacy rate is very low in Pakistan as compare to other developing nations.
• The FDI policies should be free of politics. Institutions should pileup such rules for FDI environment which couldn’t be effected by political disputes.

• The country is facing electricity shortage since last decade so there must be taken action to overcome the problem, due to electricity shortage many industries are shifting to other countries as a result thousands of people losing their jobs which is not beneficial for growth of Economy.

• Politics plays very important role for the growth and attractiveness of bulk of FDI inflows, so government should take measure to bring stability in politics it will encourage the foreign as well as local investors and also bring confidence in investments by reducing burden of risk and uncertainty.

• The privileges must give with equality to foreign and local investors it will bring efficiency and much more incentives for local consumers.

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