The Empirical Investigation of the Capital Inflow Which Influence the Economic Growth of Pakistan: A Block Exogeneity Approach

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Abstract: The speculation of foreign financial resources to a country helps to boost up the available resources, increase the capital formation and availability of funds not only to encourage the private investment but also promote more speculation of the resources. The capital inflow does not mean only the flow of currency notes, it means the mobilization of the skilled labor, technology and machinery and all other resources, which are unavailable in the developing economy to assist the growing process. That's why this study is conducted to capture the influence and association of the capital inflow to the economic development of Pakistan. The finding of the study states that all the variables are co-integrated in the short as well as in the long term, along with sharp convergence to equilibrium. And the availability of resources leads the economy towards stabilization. All the diagnostic and stability test states that the model is normal, no problem of heterogeneity and serial correlation even parameter is also stable. While impulse response analysis determines that the response of all variables would be positive in the future. The study proposed that the government should not create the scenario for crowding out along with the easy excess to the capital.

Keywords: Gross Fixed Capital Formation, Foreign Private Investment, Foreign Direct Investment, ZA Test and Block Exogeneity.

JEL Codes: F2, F21, F36

I. Introduction

A private foreign investment is a speculation made by a private individual or a private element in a remote nation. This sort of speculation contrasts from different ventures made by an outside open or legislative element in another nation in that it is made by an individual or a private element. Otherwise called an individual outside speculation, conjointly referred to as a private foreign investment, this type of investment oftentimes provides economic stimulation in different countries. It isn't generally the situation, yet certain remote speculations are in some cases viewed as a sort of outside guide, particularly when made in underdeveloped countries or other battling economies. Strict tenets apply to remote speculations and may shift as indicated by the nation where a private outside venture is being made. (Ugochukwu & Peter, 2013, Bouchoucha, et al. (2019).

The foreign private investment is an unconditional flow of capital from other countries to yours (home) country rather than the aids, finance lendingand external direct speculation, etc. In the survey of in 1988 World Development states that foreign financial speculation in more as compared to the all other types of resource borrowing to finance to the emerging economies. However, the conditional capital flow from outside also assist the domestic investment (Economic Survey). In the real world, the inflow of the FDI not only promotes the skills, training, latest technologies, other relevant and vital materials, they also familiarize efficiency in their top management and production (Hossain and Hossain, 2012).

An important issue in this context is the harmony and the consent, which justifies the role of foreign capital in developing financial growth in emerging economies (Mosley, 1980). While analysis concluded that the foreign capital has encouraging effect on the economic development Chenery and Strout (1966). In additionally, the foreign capital, for residential saving money on two records: (a) remote capital inflows could prompt government winding up less excited about its income, age endeavors; the country could build its utilization use and additionally change imports. Also, (b) to the degree that spring is controlled by accessible venture openings, by swarming out local speculation, outside private speculation could make household investment funds fall Chenery and Strout

(1966).

In our dynamic period of privatization, advancement and globalization, FDI has risen as a critical type of universal capital stream. Perceiving the significance of speculation without any outskirts, the World Bank has dedicated its 2010 issue of "World Development Report" to the issue of exchange and investment, examining in detail the significance of outside capital stream to the economies of the host nations. As per the World Bank, "couple of nations have developed without being available to exchange. the offer of creating nations in world FDI inflows has expanded to 36% of worldwide FDI, the largest amount since 1997 (UNCTAD, 2005). The capital stream of FDI towards the creating nations are expanding every year however China and India getting the lion offer of the expansion.

The net settled capital course of action joins spending upgrades (divider, trench, channels, and so on); plant, equipment purchases and device; the advancement of lanes, railways, private homes, and business and mechanical structures. Joined Nations Conference on Trade and Development (UNCTAD's) World Investment Report (2004) definite that Africa's point of view of Foreign Private Investment (FPI) is encouraging; the normal flood is until now to show. FPI has as yet amassed in just a couple of nations for some, reasons, running from the dangerous appearance of the locale, defilement, deprived structure, scarcity of foreign exchange and uncomplimentary macroeconomic policy environment among others World Investment Report (2004).

Many views about private remote speculation as a comprehensive system when attempting to enhance a venture (asset) portfolio, as one nation's economy might be in an ideal situation or more regrettable off than another at some random time and can be utilized in a productive manner. A private remote venture is likewise on occasion valuable as a support system when buying an alternate nation's cash to counterbalance the expense of provisions or items from a nation. Some additionally utilize a private outside venture to resign in a remote area while profiting from the value when putting resources into genuine property. Specialists caution, be that as it may, that a private remote speculation can be unsafe when a legislature is insecure or in spots encountering political unsettling influence Orji (1995).

Capital formation alludes to the procurement of the new processing plant alongside hardware, gear and all the gainful capitals merchandise. The capital development is comparable with an expansion to physical assets, the supply of a country with interest in the social and monetary framework Bakare and Munir (2011). Many creating nations has throughout the years depended especially on the flow of monetary assets from external in different structures, official and private capital streams and additionally coordinate remote speculation, as a method for accelerating their financial advancement Olaniyi (1988; Orji (1995); Ekpo (1997); Uremadu (2006).

The motivation to choose this topic is to capture the hidden benefits of the foreign capital in terms of mobilization of the skilled labor, technology and the latest machinery which affects the growing process of the country and to imprison the impact of the gross fixed capital formation, foreign private investment, along with the foreign direct investment which gradually enhance the developing process in the economy. The study is interested to know about the short as well as long term association between the variables. This work also interested to find out the shockwave/fluctuation generated by a variable, then all the other variables fluctuate from their equilibrium position. Moreover, all the variables individually as well as cumulative influence the economic development of Pakistan.

While, the section II illustrates the literature review, section III explores the theoretical framework and data, IV shows the results and discussion and section V explains the conclusion and suggestions.

II. Literature Review

The connection between the capital arrangement and monetary development have contemplated by various creators with various discoveries. The capital arrangement is the way toward the social occurrence, the supply of affirms to increment in riches or the making of further riches. While on the contrary, foreign private investment is the flow of capital from one nation to another nation to own a significant level of ownership and play an active part in the organizational decision as part of their investment.

The remote financial specialists search for a solid "speculation atmosphere" in creating nations. This is the place society and governmental issues are steady and there is "great administration", with the end goal that the economy is overseen well, the general population benefit is proficient, adaptable and fair, laws and controls are not unduly meddling or mandate, and contracts are upheld in the courts (Godfery, 2013). FPI reacts most of the political, monetary, and infrastructural highlights. Notwithstanding social and political solidness, it is pulled in by prepared markets, high rates of return, modest and gifted work, and shoddy nearby data sources. It is prevented by deficient or costly foundation and hazard. The chances to move items in vast or gainful markets happen locally, in the poor nation getting the speculation, or abroad, including the speculators' nations of origin. Locally, markets are made by a vast or developing white collar class in the populace or by securing, for example, high taxes or substantial controls for imported merchandise (Godfery, 2013).

Rogmans and Ebbers (2013) approved that the inflow of FDI beneficial for the host economy in many ways along with the technology transfer, the transfer of the management expertise and enhancing the production efficiency. While Omri and Kahouli (2014) stated that FDI and trade are the key driver of the economic growth and the transfer of expertise in the host country.

Khan and Reinhart (1990), conducted a study and establish a basic bond between capital arrangement and ratio of development beyond, doubt in Africa and Asia. In an investigation directed by Azam and Daubree (1997), assumed that the private resources have been the most grounded and the most critical supporter of development in Kenya. FDI additionally can possibly improve the development of residential firms through complementary underway and efficiency overflows Borensztein et al., (1998). Phillips et al. (2001) found that FDI invigorates local speculation, with a 1% expansion in the FDI/GDP proportion pursued by as much as a 0.80% increment in future residential venture/GDP proportion in Africa. They presume that FDI gives positive externalities and overflows that make private local venture increasingly productive. In an overview, they found that about all talked with business pioneers in Kenya favored outside speculation and perceived that it offered them financial chances.

Anyanwu (1998) elaborates the change in domestic investment, indigenization policy; the market measures the change in residential yield and the adjustment in transparency of the state as genuine elements of FPI. Additional noticed in 1995 the annulment of the indigenization approach energized FPI drain to Nigeria, that struggle should be done to increase the nation's money related advancement, in order to have the capacity to draw in more FPI. The Hernandez - Cata (2000) finds out a critical relationship between monetary development and capital arrangement in Africa, Asia and Latin America.

Adelegan (2000) explored and discovered that FPI is star utilization and the genius import and identified inversely connected with gross local speculation. Akinlo (2004) analysis the outside money has a little and not authentically basic impact on financial advancement in Nigeria. Uremadu, 2006 conducted an examination and discover that an expansion in outside private venture would supplement local funds to address speculation issues in a specific LDC nation. Along these lines, a lot inflow of wealth (FPI) would prompt ascent in gross household venture, which will thus prompt development.

Balamurali (2004) conducted a study to detect the connection between openness of the trade policy, real GDP, FDI and domestic investment and determines the positive relation among them while utilizing the data from 1977 to 2003 by using Johansen's full information maximum likelihood method.

However, Ilan 2007 conducted a study to capture the linkages between foreign direct investment and economic development for the Indonesian economy while employing the data from 1997 to 2006 and determines a positive relation between them. Be that as it may, when representing the diverse normal development, execution crosswise over parts, the advantageous effect of FDI has been never again clear.

Adam and Tweneboah (2009), the work showed that FDI positively influence the economic growth and the money market in the Ghana along with enhancing the trading system. It is also declared from the findings that FDI and the securities exchange of Ghana assist to improve the economic activity in the long-term.

Orji and MBA (2011) in their investigation took a gander at connection among the capital arrangement, growth and FPI, in Nigeria employ the two-organize minimum squares (2SLS) technique for analyzation. The examination determines the long-run impact of the investment game plan and abroad private venture on monetary improvement is bigger than their short-run affect. Along these lines, a long-run balance linkage between the factors, as the blunder revision term is huge, yet the speed of alteration has been low in the two models. In their result, 2 stage minimum squares gauges are near to the OLS gauges suggesting that OLS gauges are predictable and unprejudiced.

Specifically, the uncertain impacts of capital streams have prompted distinctive perspectives and strategy recommendations for rising economies Bertaut et al, (2012). A few business analysts contend that the ongoing money related downturn has largely affected capital stream designs Fratzscher (2012). Forbes (2014) terms the ongoing improvement as budgetary de-globalization and finds that money related to the stream increment after some time, feel strongly in the midst of an emergency and don't bounce back to anything near the pre-emergency levels. The concerns have been brought up specifically to raise the showcases as their capital streams will stay at low levels in 2016 [IIF, 2016]. Nonetheless, the structure of universal capital streams has additionally changed as to the level of capital streams from and to cutting edge economies has diminished while the heaviness of developing markets in worldwide GDP has expanded. Multinational likewise progressively influence capital streams by moving their assessable benefits to stay away from expenses Jones and Temouri (2016).

Our general discoveries demonstrate that the impacts of capital streams for developing markets are for the most part positive, however contrast for streams from developing markets and mechanical economies and among FDI and portfolio streams (Beckmann, Joscha; Czudaj, Robert, 2017).

In the viewpoint of above literature, it is clear that capital flow plays very important role in the growing of emerging countries. The emerging nations are full of resources, but lack of capital resource, this unconditional capital inflow assists the economy which is lacking in the emerging economy. Ankita and Gupta (2004 & 2013) states, Capital inflow does not mean only the flow of currency notes, it means the mobilization of the skilled labor, technology and machinery and all other resources which are unavailable in the developing economy to assist the growing process. One the other hand, the conditional capital inflow like the IMF or World Bank with strong terms and conditions reduce the speed of growth.

III. Theoretical Framework &Data

Theoretical Framework

Keynes (1936) was the foremost economist who offered thoughtfulness regarding the presence of a free venture choice in the economy. He saw that speculation relies upon the forthcoming negligible productivity of capital with respect to some loan cost that mirrors the open-door cost of contributed assets. The Harrod and Domar model, which introduced by Harrod and Domar in 1940 to explain the connection between development and capital requirements, which is extensive use in the emerging countries.

The one of the hypotheses of the model is that yield of the monetary unit, firm and industry impacted by the capital, which is put resources into that firm. Whenever yield Z and capital stock S, at that point yield can be identified with a capital stock by $Z = S/s$ where S is a constant, called the capital output ratio. For an economy the elementary Harrod - Domar relationship is $T = C/s$, while 'T' is the stock generated by the asset in plant and equipment is the chief factor in the development and it is the reserve fund by individual and organization that makes the speculation conceivable Maclolm (1987).FPI are decidedly connected with monetary development is arranged, in development hypothesis that accentuates the role of enhanced innovation, effectiveness and efficiency in advancing development Lim (2001).

The possible participation of FPI with progress, which based firmly on the situations in receiving nations. The capital arrangement gets from the investment funds collection. It positively affects the private reserve fund amassing as the increment in capital development will prompt more investment fund. At that point, when the reserve fund gathers, it will prompt an expansion in gross local speculation and the payment made in light of the endeavor ventures consequently, thus prompt GDP development Uremadu (2006). Here investigation uses the model 02, which is utilized by the Mba, Peter in 2011 in his exploration.

Data

Every year State Bank of Pakistan announces statistical data under the head of Handbook of statistics. This study employs the time series data which is comprises on 1964 to 2017. All the data is collected from the World Development Indicators and Handbook of Statistics.

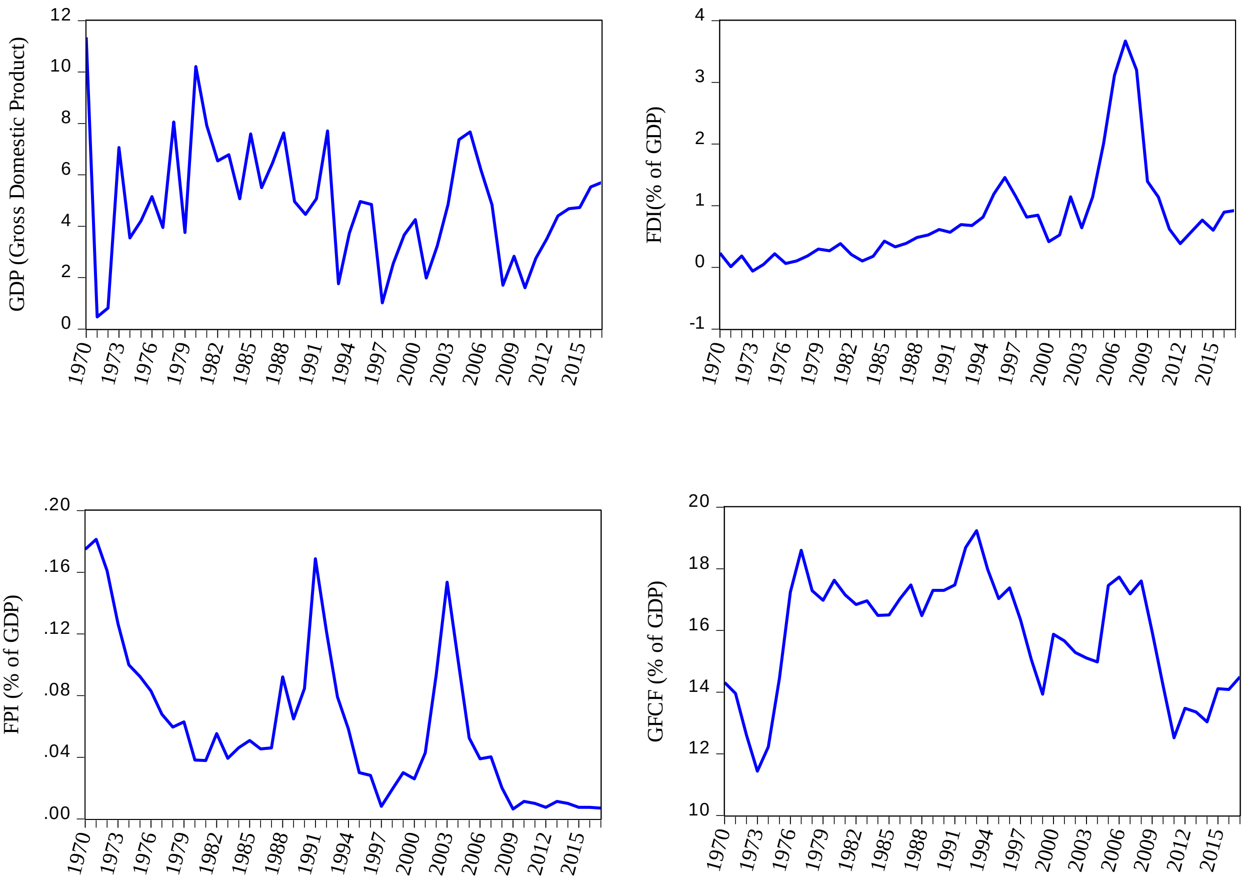
IV. Results and Discussions

To investigate the expressive overview of the gross domestic product, foreign private investment, foreign direct investment and the gross fixed capital formation, the study employs the descriptive analysis. This test elaborates that the average values of GDP (1.42), FPI (-3.22), FDI (-0.72) and GFCF (2.76) lie between the minimum (-0.75, -5.06, -4.66 and 2.50) and the maximum value (2.42, -1.70, 1.29 and 2.95 respectively). Well, the trend of the variable is denoted in the Figure 01.

Table 1 Descriptive Analysis

Variable	Mean	Median	Maximum	Minimum	Std. Dev.	Skewness	Jarq-Bera
LN GDP	1.42	1.57	2.42	-0.75	0.64	-1.35	22.74
Ln FPI	-3.22	-3.07	-1.70	-5.06	0.97	-0.43	2.76
Ln FDI	-0.72	-0.55	1.29	-4.66	1.11	-0.99	16.15
Ln GFCF	2.76	2.80	2.95	2.50	0.11	-0.56	3.57

Source: Author(s) calculation



Source: Author(s) calculation

Fig1. Trend of the Data

First of all, the study finds out the stationery which is the per-requisite of the time series, stationery means zero mean and constant variance. If, the study moves without checking the stationery, the results will be spurious and non-reliable. So, it is important to make the data, stationery before estimation. The results are mentioned in the Table 02.

Table 2ADF and PP Results

Variables	ADF test	P-values	Integration Order	PP test	P-values
GDP	-5.42	0.00	I(0)	-5.54	0.00
FPI	-2.82	0.06	I(0)	-6.57	0.00
GFCF	2.93	0.04	I(0)	-4.72	0.00
FDI	-6.57	0.00	I(1)	2.95	0.04

Source: Author(s) calculation

The outcome demonstrates that three variables are stationery at I(0) and one is at I(1), which states that all the variables stationery. However, to determine the structural break in the data, ZA test was employed, whom results are shown are in Table 03.

Table 3 ZA Results

Variables	**Structural Break**	**t-statistics**
GDP	1993	-6.35
FDI	2009	4.65
FPI	2008	5.03
GFCF	2010	5.02

Source: Author(s) calculation critical values, 1%, 5% & 10%, -5.34, -4.93 & -4.58 respectively.

The results state that GDP has structural break in 1993, FDI in the 2009, FPI in the 2008 and the GFCF has data break in the year of 2010. The results of the ADF and PP set the course of the research towards the Johansen test of co-integration to find out the long-term association between the variables. The co-integration test comprises of two parts, trace and the maxi-Eigen values, whom results are mentioned in Table 04 and 05.

Table 4 Trace Statistics

Null Hypothesis	Alternative Hypothesis	genvalue	Trace Statistic	5% Critical Value	ob.	Hypothesized . of CE(s)
f = 0	f≤ 1	0.62	67.73	29.79	0.00	None *
f = 1	f ≤ 2	0.33	23.31	15.49	0.00	At most 1 *
f = 2	f ≤ 3	0.10	4.79	3.84	0.02	At most 2 *

Source: Author(s) calculation

Table 5 Max-Eigen Statistics

Null Hypothesis	Alternative Hypothesis	Eigen value	Trace Statistic	5%Critical Value	Prob.	Hypothesized No. of CE(s)
N_0: f = 0	N_1: f ≤ 1	0.62	44.42	21.13	0.00	None *
N_0: f = 1	N_1: f ≤ 2	0.33	18.52	14.26	0.01	At most 1*
N_0: f = 2	N_1: f ≤ 3	0.10	4.79	3.84	0.02	At most 2**

Source: Author(s) calculations

The projected outputs of Trace and Max-Eigen values, at 5%, trace value is greater than the critical value at every step none, at most 1 and at most 2 respectively. Hence, all three null hypotheses are rejected with respect to their alternative hypotheses (Table 2). However, the max-Eigen value at 5 % level of confidence at most 1, 2 and none positions and exploring the rejection of all respective null hypothesis. The trace value and the maxi-eigenvalue show the presence of a co-integration equation, which confirms the long-term association between the variables.

The Vector Error Correction is utilized, to measure the short-term connection among the variables. This method is the driven technique, which is utilized to imprisonment the influence of one series on the other time series. This technique also elaborates the speed of convergences towards equilibrium. The results are expressed in the Table 6.

Table 6 Vector Error Correction Estimations

Error Correction:	D(GDP)	D(FDI)	D(FPI)	D(GFCF)
CointEq1	-0.043185	0.230242	-0.118612	0.057779
	(0.11187)	(0.11372)	(0.10614)	(0.00914)
	[-0.38601]	[2.02473]	[-1.11754]	[6.31856]

Source: Author(s) calculations

The result specifies the speed of convergence of GDP towards equilibrium is very fast, while FPI shows the adjustments towards the equilibrium and GFCF indicates the sharp adjustment towards equilibrium meaning that it will be converging towards equilibrium sharply. However, to analyze the validation of the VECM, wald test has been employed. The results of the wlad test were described in the Table 7.

Table 7 Wald Result

Test Statistics	Value	df	Prob.
F-statistic	5.24	(3,38)	0.00
Chi-square	15.73	(3)	0.00

Source: Author(s)calculations

The results show that the explanatory variables in the model are significant and also having the cumulative influence on the dependent variable.

However, to analyze the stability and the reliability of the model a number of diagnostic techniques are utilized which are mentioned in Table 6. The results of different diagnostic tests are presented in the Table 8.

Table8 Diagnostic Tests

Heteroskedastic: Breusch- Pagan- Godfrey Test		
$X^2 - Statistics$	Degree of Freedom	Prob
	1	0.19
Breusch- Godfrey serial Correlation LM Test		
$X^2 - Statistics$	Degree of Freedom	Prob
	1	0.23
Jarque-Bera Test		
$F - Statistics$	Degree of Freedom	Prob
1.32	(2.34)	0.19
Ramsey RESET Test		
$F - Statistics$	Degree of Freedom	Prob
15.6	(1,39)	0.25

Source: Author(s) calculation

The autoregressive conditional heteroskedasticity (1982)and Breusch–Godfrey shows that the error term is free from the problem of autocorrelation and serial correlation. Whereas, Ramsey Reset test (1969) describes the misspecification of the model. While, Jarque-Bera (1987) states that model is normally distributed.

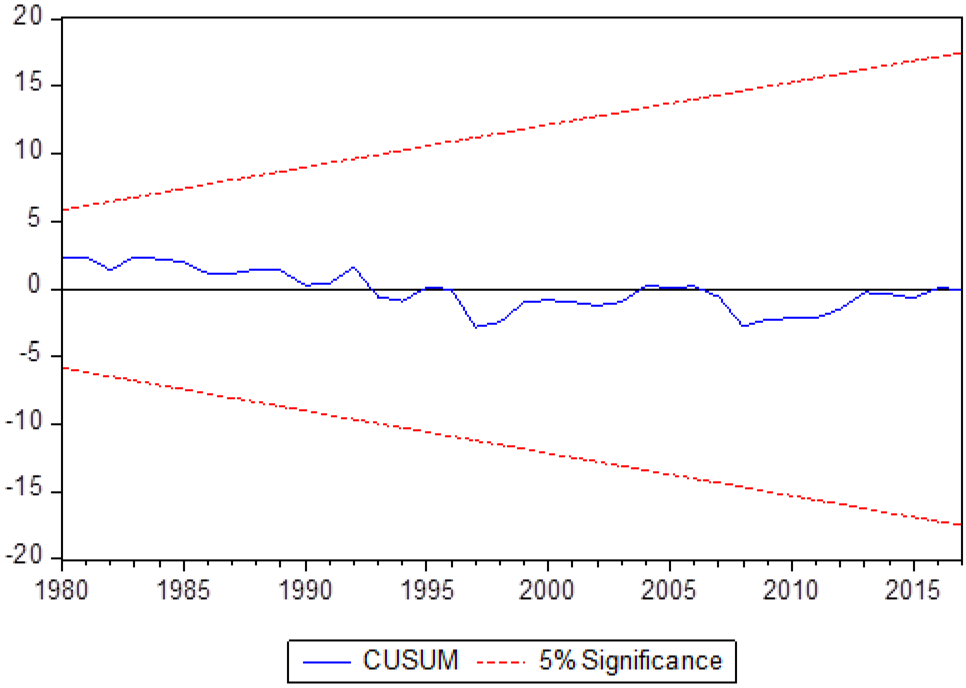


Fig 2. CUSUM

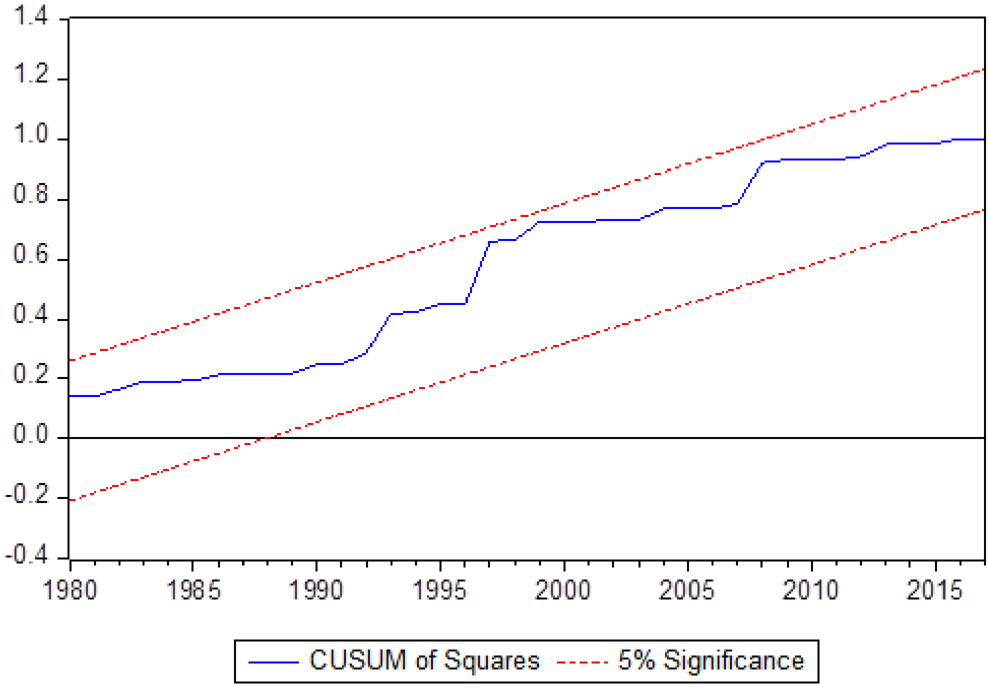


Fig 3. CUSUM Q

The CUSUM and the CUSUM Q test were employed to check the stability of the parameters respectively. The 5% level of significance is represented by the straight line. The null hypothesis of stable parameters is accepted against the alternative hypothesis of unstable parameters as the plots of CUSUM and CUSUMSQ statistic fall within the 5% significance level.

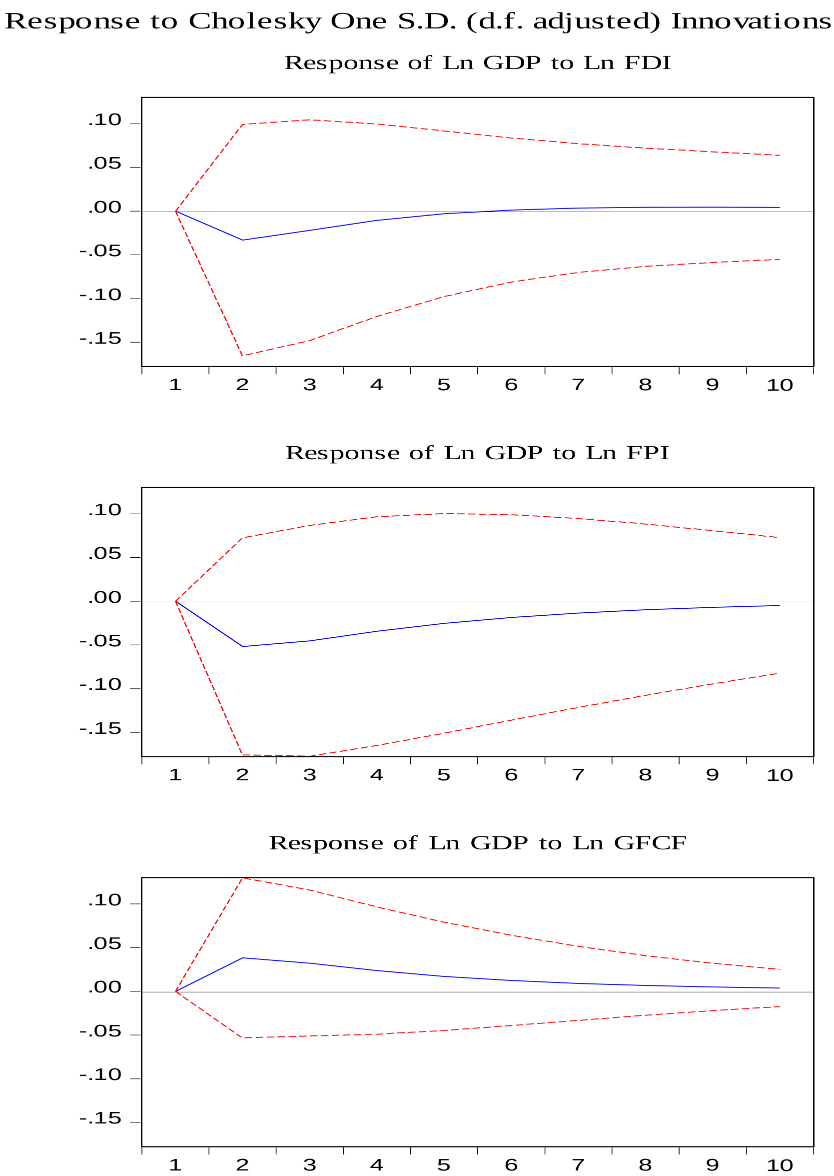
Finally, we performed the VAR test because it deals all the variables on the same ground there is no endogenous and the exogenous variable in the model. The result of the VAR test is presented in the Table 09.

Table 9 VAR Result

Variables	Ln GDP	Ln FDI	Ln FPI	Ln GFCF
Ln GDP (-1)	0.3438	-0.423	-0.017	0.050
	(0.164)	(0.193)	(0.119)	(0.013)
	[2.095]	[-2.191]	[-0.144]	[3.609]

Source: Author(s) calculation

The results of VAR elaborate that the factors are cointegrated in the long term, we are well aware about the VAR that we cannot elaborates the results of VAR lonely, we have to take the assistance of the impulse response function (hereafter IRF) to predict the behavior of the variables in the future, which are presented in the figure 0



Source: Author(s) calculation

Fig.4 Impulse Response Function

The results of IRF elaborate that when a shock of standard deviation of FDI is given to the GDP, initially GDP would respond positively, then starts to move negatively till third period after that the GDP starts to move towards the equilibrium and attain the equilibrium in the sixth period and after that GDP moves along the equilibrium position. Simply we can say that the change in the level of the FDI would change the response of the GDP initially negatively, but after some time GDP increases with an increasing rate.

The IRF also elaborates that when the fluctuation in the level of the foreign private investment (FPI) creates the shock and hit the GDP, then GDP initially respond positively, and then declines negatively till second period after that increase with an increasing rate till 6th period and moves very closely to the equilibrium position. While on the other hand, when the standard deviation shock of the gross fix capital formation (GFCF) is given to the GDP, then the GDP would respond positively and moves upward till second period after that starts to move towards the equilibrium line. In such a way that with every passing year the gap between the equilibrium line and the movements become closer and closer. Simply we can say that increase in the level of GFCF it will positively stimulate the GDP of the economy.

To capture the cumulative influence of all the variables on the GDP, the Block exogeneity test was applied, whom the result is presented in the Table 10.

Table 10 Block Exogeneity Test

Dependent Variables: Ln GDP

Excluded	Chi-sq	Df	Prob.*
Ln FDI	6.68	1	0.00
Ln FPI	9.03	1	0.00
Ln GFCF	13.02	1	0.00

Source: Author(s) calculation

The results of the block exogeneity reveal that FDI, FPI and GFCF are strongly influencing the GDP cumulative as well as individually. The finding of this study is on the line with the findings of the Rogmans and Ebbers (2013), Omri and Kahouli (2014), Khan and Reinhart (1990), Azam and Daubree (1997), Uremadu, 2006, Adam and Tweneboah (2009), Orji and MBA (2011), Bertaut et al, (2012), Fratzscher (2012), Forbes (2014), Jones and Temouri (2016), Najeh Bouchoucha and Walid Ali (2019).

V. Conclusion& Suggestions

Capital inflow plays pivotal role in the emerging as well as in developed economies. The availability of capital encourages an economy to boost up its development projects quickly. One of the most hurdle in the way of propriety in developing economies like Pakistan, is the lack of capital and unconditional capital flow in term of machinery, business administers (Capital Formation). If make a bird's eye view of the Pakistan history, come to know when capital was available in that era GDP growth rate was remarkable, the economy is flourishing with full speed which in turn encourages all the sectors of the economy. The foreign private investment and foreign direct investment are accepted to make other critical commitments to development and improvement. In the first place, it can raise/change income, make work and open new markets for fares. By and by, however, execution in these territories does not constantly meet desires. Poor and creating nations regularly contend to offer duty occasions as an approach to draw in speculation. Business may really be lost, if non-natives purchase and re-structure wasteful existing ventures, frequently claimed by the state.

The FPI and FDI help to mobilize the management skills and expertise, technology and efficiency in the production which increases the productivity of the economy. That's why this study is conducted to investigate the capital inflow which influence the Pakistan economy and found that FPI, FDI, GFCF and GDP are affiliated with each other in the short run as well as in the long-term. The capital inflow (foreign investment) not only increases the availability of the funds, but also improves the economy at the management level, enhance the technology, increases the efficiency in the production and in management, which in turn promotes the domestic performance, either it is the private sector or the government one. And also, the government has more opportunity to complete its productive projects which assist to attain prosperity in the long run. The parametric and diagnostic tests are in the favor of the study, they find out that the model is normal, no chance of misspecification, heterogeneity and serial correlation are also absent while parameters are lies in the significance range (5% significant). Moreover, the IRF elaborates that the shock wave generated by the FDI, FPI and the GFCF would be positively influenced the economic growth of Pakistan. It is also depicted by the block exogeneity that all the variables individually affect the growth rate and they also cumulative influencing the economic growth of Pakistan. Some suggestions would be as follows.

When foreign investment is increasing, then government should not create the situation of crowding out. The excess of the capital for the private sector should be easy and in favor of both either it is finance or receiver. The government itself should control over borrowings which in turn increases the interest rate.

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