



The Commitment of Foreign Direct Investment and Foreign Portfolio Investment on the Monetary Development of Pakistan

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Abstract: Foreign direct investment has played an essential role in the economic growth of developing countries. The flow of foreign capital in the capital takes place mostly in the form of loans, foreign direct investment (FDI) and foreign portfolio investment (FPI). The FDI could influence higher consumption and Investment in short-term and reflect destructively on long-term growth. However, an increase in FDI may decrease FPI volatility because it enhances the confidence of foreign investors and brings more investment in the home country. The Pakistan growth rate was witnessed from 2001-2016, which was descending due to various macroeconomic variables which influence the foreign direct investment of Pakistan. The FDI affects positively in the development process and economic progress as it supplies capital for developing nations for investment purpose. A few investigations have been directed on contact between FDI, FPI and large-scale manufacturing. Because of this plausibility, FDI impacts monetary extension, and thus, financial solidness impact FDI inflow, the connection among FDI and the development of the economy are likely unique. Also, the remote venture may impact monetary progression legitimately and in a roundabout way. In this manner, it is recommended in reliance hypothesis that FDI stream would not impact long haul practical limit in creating economies. Henceforth the progression of remote capital in a nation happens for the most part as credits, FDI and FPI. Likewise, the determinants of FPI incorporates factors which increment interest for outside trade and urges remote speculators to contribute their capital over the creating scene. Hence, therefore, this paper highlights the importance of FDI and FPI on the growth of developing countries.

Keywords: Foreign direct investment, Foreign Portfolio Investment, Mass production, Economic growth

1. Prologue to Foreign Direct Investment in Developing Economies

The noteworthy component of the worldwide economy is global exchanges. The most significant parts of such exchanges are Foreign Direct Investment (FDI). The progression of FDI is basic in both created just as creating nations. The building up country's objective is to draw in FDI into their economies, as they expect the long-haul financial advancement from extra stable assets in host economies. There as some fundamental reasons that help the engaging quality of FDI, for example, trend-setting innovation abilities, commitment in global exchange joining, innovative work exercises. These elusive resources would be valuable for host nations to energize proficiency and commercial development. FDI likewise gets to foreign markets when the host nations utilize the fare window to circulate items in the locales. Subsequently, FDI seems to offer great attributes, for example, a high level of steadiness, development in money related assets, positive efficiency and access to the outside market.

The progression of remote capital in a nation happens for the most part as advances, outside direct venture and remote portfolio speculation. The determinants of FPI incorporate components which increment interest for remote trade and factors which urges outside financial specialists to put their capital in creating nations.

International Institute for sustainable development recognized the role of FDI in the development of an economy (Mann et.al. 2005). Due to the possibility, FDI influences economic growth and in turn, economic growth influence FDI inflow, the relationship between FDI and economic growth are likely dynamic. As indicated by the dependency theory developed by Amin (1974) and Frank (1979), FDI stream would not impact long-term economic growth in developing economies. However, the foreign direct investment could impact higher utilization and investment in the short-term and reflect negatively on long-haul development. (Bunchier 1980, O'Hearn 1990, Stoneman, 1975).

Foreign Investment may impact financial development in two different ways immediate and indirect. The immediate impact influences on a remote venture to expands creation, work, esteem included, and trade. These components straightforwardly increment GDP; e.g., business increment a person's pay and pay augmentation are legitimately determined in GDP. Similarly, it is for esteem included and send out. However, remote venture increment GDP in a roundabout way too; e.g., change in innovation, learning, work preparing. Additionally, innovation overflow, human capital arrangement, proficiency, and efficiency are the elements which by implication increment GDP in financial development. (Chakrabarti 2001 and Borensztein, et al 1998).

The theory of portfolio investment, investors are concerned by the high-interest rate since it reduces the borrowing cost. Foreign portfolio investor will invest up until IR get alike everywhere thought out the world. Therefore, it is said that FPI is influenced by domestic interest rate, and not by domestic returns. Nevertheless, this theory structure is so immature when the risks, uncertainty, and volatility are introduced. Hence, we must reflect the risk factor regarding foreign investment volatility. The term volatility is focused on the international investors 'intention to invest for short-term advantages and they pull back their investment on uncertain terms. Therefore, volatility relates to uncertainty when it comes to the flow of FPI in the country. Numerous influences bring instability in foreign portfolio investment volatility. The fluctuation in the exchange rate increases the volatility in FPI. Hence, investors regularly monitor the exchange rate. Accordingly, Stock market execution is a pivotal factor in drawing in FPI (Bekaert and Harvey, 1998).

Portfolio investor considers the exchange rate and interest rate of the host country. The Devaluation of host country currency encourages foreigners to invest due to the high return. As indicated by Bleaney and Greenway, (2001), instability in the real exchange rate increase the volatility of the foreign investment. Besides, inflation additionally influences volatility in FPI. A decrease enhances volatility in FPI in return and an increase in inflation. The financial states of the nation likewise influence FPI emphatically. At the point when an expansion in speculation and sparing, innovation exchange to creating economies improves macroeconomics approaches and budgetary market advancement conveys more FPI to the nation of origin.

2. 2. Connection between Gdp with FDI Inflows and FPI

A few examinations have been led on foreign direct investment, foreign portfolio speculation, and monetary improvement. This area will feature work done by scientists on FDI, FPI and its effect on monetary improvement. FDI has become a significant resource of external capital for many economies. FDI flow to South Asia rose by 6 percent to \$54 billion. Even though the historically high number of announced greenfield projects in 2015, FDI flow to India was mainly flat at about \$44 billion in 2016, up to 1 percent in 2016. The defense behind this effort was that FDI positively affected the profitability of an economy by rousing innovation exchange and improving organizational ability. What is more, FDI improves business activity and its profitability and impact all things considered difficulties in an economy. Iqbal et al., (2013) referenced FDI streams demonstrate the advancement of worldwide exercises of Multinational Corporations. The business analyst accord is that FDI positively affects commercial development. The direct foreign speculation influences the advancement procedure and financial development as it supplies capital for creating countries for venture reason. Thus, the positive connection among FDI and monetary development spur numerous specialists to contemplate factors that are most proficient for drawing in FDI inflows (Bende-Nabende 2002, Alfaro 2004, Carkovic 2005 and Shahzad and Kaid Al-Swidi 2013).

As indicated by Gozgor and Erzurumlu, (2010) increase in direct foreign speculation may reduce foreign portfolio investment unpredictability since it upgrades the certainty of outside financial specialists and gets greater venture the nation of origin. Likewise, Iyer, Rambaldi, and Tang (2003) found that FDI cause FPI, while FPI does not cause FDI. Despite this, Ahmed and Malik (2012) reasoned that immediate speculation found to Granger cause by the portfolio interest in Pakistan directly because its budgetary market is encountering development and this factor will help in

understanding the distinctive venture situations. However, FPI was found to be non-consistent and non-persistent capital flow than FDI and other flows in crises times in some studies. Sarno & Taylor, (1999), Levchenko & Mauro, (2007) found a significant connection among FDI and foreign portfolio investment volatility. Darby, Hallett, Ireland, and Piscitelli (1999) mentioned that volatility in exchange rate had a significant effect on FPI.

Moreover, Carrieri, Errunza, and Majerbi (2006) argue that the real exchange rate should be considered than nominal exchange rate as real rate eradicate the effect of inflation and is a better indicator of FPI volatility. Hence, it is concluded that the real exchange rate and FPI flow changes over time Kodongo & Ojah, (2012). Farkas (2012) mentioned in his study the positive impact of FDI on the Pakistan economy. Similarly, Hameed and Bashir (2012) confirm that foreign direct investment leads to economic growth. Awan (2010) mentioned that the inflation rate has a significant impact on foreign direct investment inflow. Iamsiraroj (2016) investigated FDI economic growth nexus for 124 cross country data over the period 1971- 2010. His empirical outcomes demonstrated that global FDI influences positively in economic growth and the other way around. Likewise, a few determinants of FDI, for example, workforce, trade openness, and economic freedom stimulated economic growth. A wide range of studies considered GDP growth rate as an essential indicator of economic performance

3. FDI Inflows and FPI has Significant Impact on the Economy of Pakistan

Qaiser (2011) watched Pakistan development rate from 2001-2011, which was moving to descend because of different macroeconomic factors which impact the outside direct venture of Pakistan. H. Younus et al (2014) examine the effect of FDI on the economic growth of Pakistan. The investigation applies data from 2000 - 2010. The findings of two-stage least squares technique of the simultaneous equation propose that the government should concentrate on policies to attract foreign direct investment and trade liberalization in Pakistan to increase foreign investment. The outcome reflects a positive relationship between FDI and GDP. Jawaid (2016) explored the relationship between the FDI and the economic growth of Pakistan over the period 1966-2014; he proposed that FDI significantly effect on the economic growth of Pakistan both in short run and long run.

Malik and Khola (2015) investigated the effect of FDI and exchange transparency on the financial development of Pakistan. By using time arrangement information from 2008-2013, the examiner reasoned that FDI, exchange receptiveness and household capital emphatically influence commercial development. The rise in FDI replaces absolute technology through advanced technology and educate the workforce of the nation. Likewise, it suggests that the administration should take stable estimates, for instance, balancing out the conversion standard to expand FDI in Pakistan.

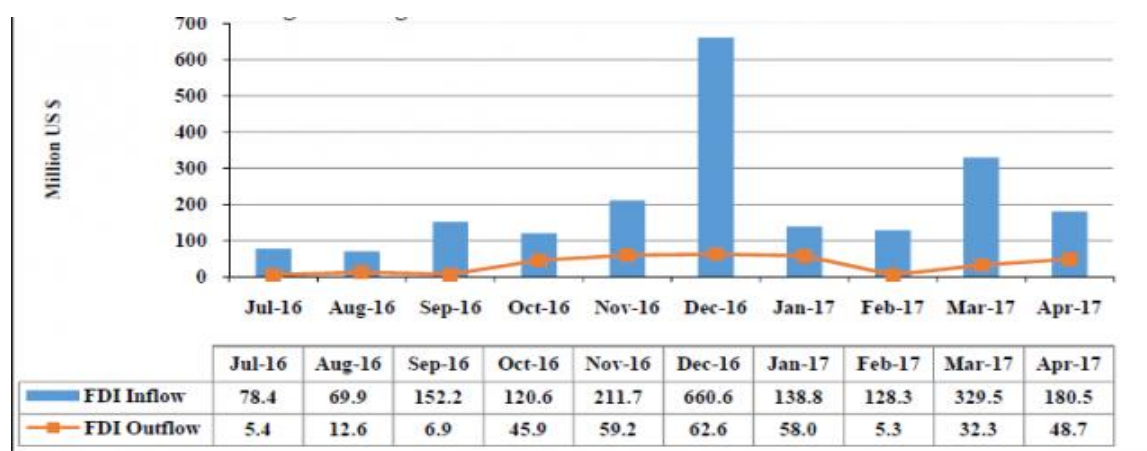


Figure 1: Foreign direct investment
Source: Pakistan Economic Survey 2016

Pakistan recorded growth in FDI in 2016-2017. Consistent with the Economic Survey of Pakistan, a 12.75% growth was enlisted in FDI as compared to 2015-2016. Since Pakistan’s FDI remained at Rs. 1.733 billion in 2016, however in 2015,

it remained at \$1.537 billion. Significant FDI inflows throughout the amount underneath review were from China (\$ 744.4 Million), Netherland (\$478.6 Million), France (\$171.0 Million), Turkey (\$137.7 Million), US (\$103.2 Million), U.A.E (\$ 48.4 Million), UK (\$47.6 Million), Italian Republic (\$ forty seven.4 Million), Japan (\$ forty two.1 Million) and Federal Republic of Germany (\$ forty.5 Million).

4. 4. Effects of FPI is Positive or Negative toward the Economic Growth of Pakistan

Prior research ponders found a positive connection between monetary development and FPI (Santis and Luhrmann 2009, Ferreira and Laux 2009, Ghura and Goodwin 2010, Easterlyetal 2001 and Abdelhafidh 2013). Foreign Portfolio investment is factually huge and has adversely connected with the financial development of Pakistan. Tahir et al (2015) investigated the connection among foreign remittances, FDI, imports and financial development by utilizing time series econometrics methods covering the information over the time 1977 to 2013. The investigation revealed that foreign remittances and FDI have a significant essential role in the financial development procedure of Pakistan. Saqib et al, (2013) give differentiating proof of FDI and its effect on the monetary development of Pakistan. Information was taken from 1981 - 2010. The factors utilized in the investigation were Inflation, obligation, local speculation, and FDI. The strategy used to break down information were the Augmented Dickey-Fuller test and square technique. The investigation reasons that Pakistan economy negatively affects FDI, though residential speculation profited its economy.

N. Zeb et al (2014) talked about the role of FDI and its effect on Pakistan's economy. The data used from 1972 to 2012 and the variable used in the article were trade openness, foreign direct investment, terrorist attack, and political instability. The system used to break down the information was the least square strategy and finding of the investigation propose that FDI has a positive and huge impact on Pakistan economy. Turkey. B et al (2011) examine the impact of FDI on the economic growth of Jordan. Factors in the study utilized were foreign direct investment, domestic investment, trade liberalization, and GDP. The data were analyzed from 1990-2009. Cointegration and error correction methods were used to analyze data. The examination infers that FDI, domestic investment and exchange progression positively affects the financial development of Jordan. The foreign portfolio investment (FPI) happened as one of the significant options as it has the fundamental property of effective hazard sharing and income. The FPI makes a noteworthy effect on the advancement of the local capital market. As indicated by Guerin (2006), portfolio venture outflow is related to FDI and is very delicate to change in GDP per capita. The creator referenced that if there is negative yield stun, FPI stream will be more unpredictable than outside direct venture

5. Conclusion

This paper has asserted that the significance of FDI and FPI inflows significantly affects the economy of Pakistan. So also, the advancement rate from 2001-2011, which was moving to drop due to various macroeconomic components which impact the growth of Pakistan. Moreover, foreign portfolio investment is factually huge and has adversely connected with the financial development of Pakistan. However, FDI influences the advancement procedure and financial development as it supplies capital for creating countries for venture reason.

Additionally, the increase in FDI may diminish outside portfolio venture unpredictability since it upgrades the certainty of outside financial specialists and gets more considerable venture the nation of origin. Equity capital flows are often taken as an indication of the number of new investments related to FDI. Nevertheless, economic growth could itself cause an increase in FDI inflows. The FDI could influence higher consumption and Investment in short-term and reflect destructively on long-term growth. Additionally, an increase in FDI may decrease FPI volatility because it enhances the confidence of foreign investors and brings more investment in the home country. The Pakistan growth rate was witnessed from 2001-2016, which was descending due to various macroeconomic variables which influence the foreign direct investment of Pakistan. Likewise, FDI affects positively in the development process and economic progress as well it supplies capital for developing nation for investment purpose. A few investigations have been directed on contact between FDI, FPI and large-scale manufacturing. Because of this plausibility, FDI impacts monetary extension and thus, financial solidness impact FDI inflow, the connection among FDI and the development of the economy are likely unique. The foreign remittances and FDI play a vital and constructive role in the financial development procedure of Pakistan. It is demonstrated by Jawaid (2016) the connection between the FDI and the commercial development of Pakistan over the

period 1966-2014 and proposed that FDI significantly affects the financial development of Pakistan equally in short run and long run.

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