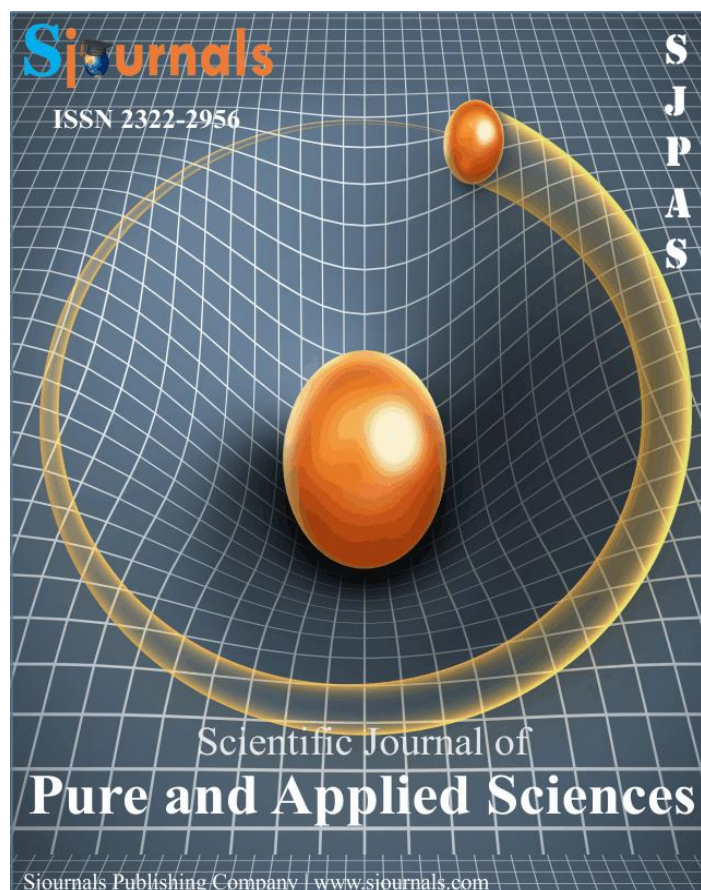


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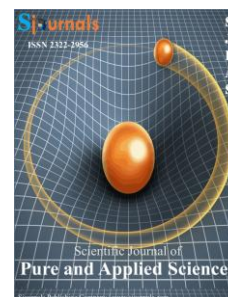
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Review article

Impact of terrorism, gas shortage and political instability on FDI inflows in Pakistan

Khakan Najaf*, Shumraiz Ashraf

Department of Accounting & Finance, University of Lahore, Islamabad Campus, Pakistan.

*Corresponding author; Department of Accounting & Finance, University of Lahore, Islamabad Campus, Pakistan.

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ABSTRACT

In the paper the prime objective of this study is to verify that foreign direct investment has crucial role in the progress of developing and under developing country. This paper is trying to expose that foreign direct investment is the reason of remove unemployment, bridging the gap between both saving and investment, latest technology, GDP of all the nations. We have applied annual time series dataset to prove it empirically. In this study we have taken data from 1981 to 2011 and applied the OLS and ARMA techniques. In the main paper in which we have analyzed the impact of gas shortage, political instability, terrorism on the foreign direct investment in Pakistan. As anticipated, this study has proves that there is negative relationship between political instability and terrorism whereas gas generation has positive with FDI inflows in Pakistan. There is positive relationship between control variables and FDI inflows in Pakistan, in the other side exchange and interest rate have negative relationship between FDI inflows.

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1. Introduction

From the last decades, there are the numerous researchers regarding the promote role of FDI and its contribution in the progress of all developing and under developing country. For making the much needed

investment its supplies capital to nations' for the development of economy, It is also sources for improvement of managerial skills and beneficial for creating the jobs opportunities. FDI inflows is supportive to update latest technology, which is reason of the improvement in the economic development and growth. Now a day's many economies are facing the challenges regarding to attract overseas investment. Different procedures are being implemented to attract the overseas investors. After these procedures most of countries succeed whereas some countries failed. It results are exploring the evaluate strategies being design for the attracting of FDI inflows. In many developing countries there are huge gap between saving and investment, for the improvement of this GAP there is need of FDI inflows, which is beneficial for rising production level, latest technology, creating of best employment opportunity and also beneficial for improving the competition. For the achievement of economic development FDI inflows are considered the crucial element. Now a day's Pakistan is facing the problem of shortfall of gas. This problem is at the peak in the Pakistan; due to load shedding of gas the economy of Pakistan is going to decline position. In year 2011 the loading shed of gas was at huge level and Pakistan government did a lot of promises to lessen it as soon as possible but still this problem is common in Pakistan. The issues of load shedding of gas have badly effect on local and foreign investors .Many business units have shutdown due to gas shortfall. Most of the investors are relocating for the investment in the business units of Pakistan, because without the availability of gas it is impossible to run business units. From a last few years the FDI condition has seen incredible. During the year of 1980, the FDI inflows were 6.7%, in 2003 it was mounted to about 24%. From the last couple of years Pakistan has been in the condition to attract a lot of investors towards Pakistan investment policies. In 1970 the rate of FDI inflows increased from 24 million to 65 million (Khan, 2007). In 2004, the FDI inflows had significantly increased till 5.6 billion, in 2007 it was only 2.7%. FDI is known as the telecommunication sector of Pakistan. For analyzing the FDI impact of the Pakistan economy. They have utilize the regression analysis from the period of 2000-2007.the variables which have included in this test is per capita income market, market size, foreign trade. All results have shown that these variables had significant impact on the telecommunication. Khan et al., in 2011 analyzed that impact of political instability on the FDI in Pakistan from period of 1972-2005 by utilization the least square method. In this paper they have found the correlation between human capital and FDI inflows, while the correlation between political instability and FDI. Mohamed et al., in 2010 studied that macroeconomic variables and FDI inflows by using the OLS techniques. He found that macroeconomic variables and FDI had positive relationship. Mughal and Akram (2011), studied that impact of FDI inflows on the market size of Pakistan 1976-2009 by using the ECM econometric techniques.

Naeem and Azam (2005) Analyzed the impact of economic policy on the FDI inflows in seven south Asian countries including Pakistan. They had taken data from the period of 1997 -2008. The authors demonstrated that mracoecomic variables had positive impact on the FDI inflows. Presently, it is seen that political instability has negative influence on the FDI inflows. War against the terrorism has very bad impact on the Pakistan s economy. From the last five years it is appearing at very huge level. The economy of Pakistan is facing such a vicious depression. Since year 2000 Pakistan has been facing such economic and social terms due to this war. Different researchers have shown that political stability is necessary for the economy. But in Pakistan there is poor political stability, which is reason of the deciding the investment decision. Aqeel et al., (2004) has described that due to instable political environment are losing the investors' confidence. Foreign direct investment has a crucial role in the international economic system. For a economic development, it acts as a catalyst. Investor has seen that developing and emerging countries are facing the problem of the losing the investors Due to critical issues. Different scholars are trying to explore that improvement in the FDI inflows will create the competition in the market. It is most potent tool for the sustainable development.

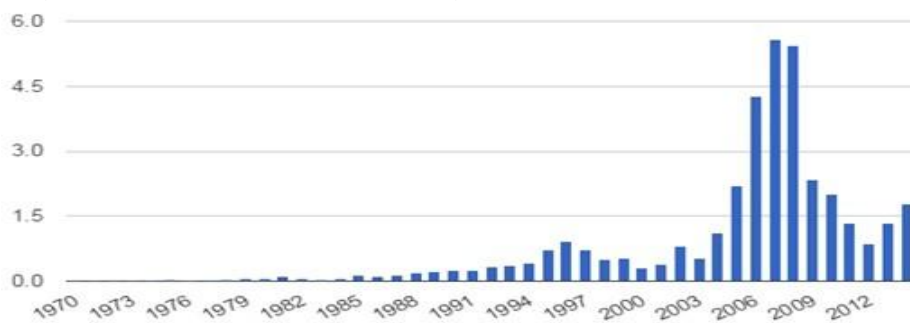


Fig. 1. Pakistan foreign direct investment in dollars(source: TheGlobalEconomy.com The World Bank).

Table 1

Foreign investment inflows in Pakistan (\$ Million).

Year	Greenfield Investment	Privatisation proceeds	Total FDI	Private Portfolio Investment
2001-02	356.00	129.00	486.00	-20.00
2002-03	623.00	177.00	799.00	23.00
2003-04	751.00	198.00	948.00	-29.00
2004-05	1,162.00	364.00	1,525.00	154.00
2005-06	1,982.00	1,541.00	3,522.00	352.00
2006-07	4,874.20	267.40	5,138.60	1,821.00
2007-08	5,277.60	134.20	5,408.80	19.40
2008-09	3,718.90	0.00	3,718.90	-510.40
2009-10	2,151.80	0.00	2,151.80	587.80
2010-11	1,574.6	0.00	1,738.40	344.6
2011-12 (Dec.)	531.4	0.00	386.5	-143.3
Total	22,996.4	2,805.61	25,823.2	2,606.3

Note: Pakistan’s Fiscal Year runs from 1st July till 30th June, Source: Board of Investment Pakistan (Awan et al., 2010).

2. Foreign direct investment in Pakistan

According to World Bank report in 2014, the foreign direct investment in Pakistan was 0.73. it is the known as the both long and short terms capital. This cart is the indicator of GDP rate in Pakistan.

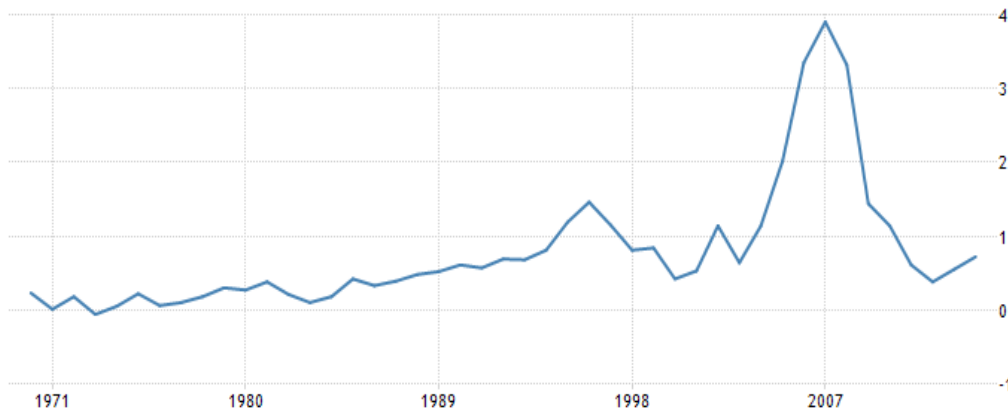


Fig. 2.

3. Objective of the study

Consequently, it has shown that there is strong association between FDI and political instability. The purpose of the study is to show the relationship between political instability and some macroeconomic variables and overseas investors .The paper is based on the following parts research literature, research methodology and results and discussion.

4. Problem statement

For the stimulating the development of economic FDI has a curial role. However, all the developing and under developing country do not get the equal benefit for the FDI inflows. While some countries are not able to attract the investors and some countries are able to attract the foreign and local investors. Here, some questions have risen that which determinates affect the inflows of FDI. Obadan (1982) argued that in Nigeria the main determinants are the market size, trade prices. Accorderding to Ajakaiye (1995) has proved that high interest rate is also reason of discouraging of FDI inflows.

5. Scope of the study

The scope of this study is to work on the main determinates of FDI in Pakistan. In this research paper has explained the reason of low investment ratio. Pakistan is facing which types of problems due to political instability, how these factors are influencing the economy of Pakistan.

6. Literature review

There have been conducted various studies related to inflows of FDI in Pakistan. All the literature has given that empirical evidence that which factors are affecting on the FDI inflows. Numerous studies had been evaluated form this purpose. For instance, Azam and Rehman (2009) studied that impact of different factors on the FDI in Kenya for this purpose he has used the OLS and Johansen co integration techniques applies. This study has approved that human capital had significant relationship with Kenya stock exchange for a short time. Hakro and Ghumro (2005) has examined the FDI inflows in the Bangladesh for periods of 1970 to 2008 and analyzed the results that political instability had negative impact on the stock exchange of Bangladesh. Jafari et al (2011) studied the determents of FDI in Malaysia by using the ARDL framework. The study has proved that there is positive relationship between GDP growth rate and FDI inflows. Khan et al (2010) by using the panel data of 71 countries analyzed the determents of FDI. They had found that GDP had significant on the FDI inflow. The researcher had applied VECM framework to analysis the determinates of FDI for the time period of 1971-2004. They found that there is market size has positive relation with FDI inflows.

The paper studied that in the Nigeria determinates of FDI and their impact on the inflation, stock market capitalization. The prime aim of this study is to explain such policies which are helpful to promote the FDI inflows in Nigeria. For this purpose they have used different tests like ECM. Resuts have shown that these variables and FDI have a significant relationship with them. The recommendation of this paper is that there is need to improve the economic planning, which will be increase the confidence level of the investors.

Decision making is considered a art in which difficult situation is tackle. It is also known as cognitive process in which we have chosen a suitable decision. The result can or cannot be vision. For fair decision making there is need of proper planning. Decision making is known as a art in which we have taken decision between the various choices. Mangers who has skills to take good decision they can compete in the business market. It is very important discussion that for competitive the world there is need of proper decision making. In addition to this, all the investors have different vision and they are different from each others. Some investors behave more risky while others believe in less risky investment and return.

In this paper the scholars had determined the data from 1998 to 2009. The prime object of this study is to determine the FDI inflows on the macroeconomic variables on the Nigeria stock exchange. For this purpose they have utilized the different techniques like unit root. Cointegration, and ECM. Their results have shown that all the marcoecominc variables have significant impact on the FDI Nigeria. In this study also concluded that there is long run relationship between them. They have recommendation that government should focus on the economic policy. This is a best way to attract the investors towards FDI.

In this study they had utilized the Ganger causality and error correction model to investigate the determinates of foreign direct investment of Indian during the period of 1971 to 2008. For this purpose they had utilized that error correction model and taken the results that there is significant relationship between determinates of FDI and government policy of India. In the light of these results, government should focus on the facial policy. Shah and Ahmed (2003) have determined the FDI in Pakistan by using the data and they have utilized the Phillips-parson test. Their study has proved that FDI has positive impact with the market size and their results have shown that there is need of proper policy for the maintained of FDI level in Pakistan.

Aqeel and Nishat (2004) have proved in their studies that financial policies have impact of the FDI of Pakistan. They have taken the data from the 1961 to 3003 and applied co. Integation and error techniques. Their results have shown that there is significant relationship between FDI and marcoecomoc variables.

Shah and Masood (2003) has analyzed the determinants of FDI in various countries. They have applied the Phillips-parson and unit root test. Their results have proved that market size has impact of the FDI determents.

Awan et al. (2010) has analyzed the impact of FDI on the economy of Pakistan. For this purpose he has utilized the annual data for the period of 1971-2009. Fe has run a regression and taken the results that there is strong relationship between FDI and economy of Pakistan.

Khan (2011) has analyzed that impact of international polices of the FDI level of Pakistan. He has utilized the Autoregressive Distributed lag bounds test and taken the results that there is negative relationship between FDI inflows and international polices. According to this policy government should give attraction towards international policies.

Azam (2010) has examined the impact of economic factore on the FDI on Pakistan for this purpose he has utilized the linear regression model and also applied the least square method. His result has shown that the management of Pakistan needs to enhance the inflow of FDI for the proper development.

Zamanet al. (2006) has explained about the impact of economic factors on the FDI of Pakistan for this purpose he has used Augmented Dickey Fuller test and error correction model. He has taken the result that FDI is not going to promote in Pakistan.

Ahmed (2011) in his paper he has analyzed the why FDI level is low in paksiatn. For this purpose he has utilized the primary data and taken the results that there is no any policy in Pakistan related to these issues. Pakistani authorities should take note of issues in Pakistan.

Nonnemberg and Mendonca (2005) have used the determine of the FDI in developing countries. For this purpose they had used the panel date and used the OLS techniques for this purpose. They analyzed that FDI correlated with the macroeconomic variables.

Khan and Nawaz (2010) have analyzed that FDI in Pakistan linkage with price index and growth rate. They have found run the regression analysis and taken the results that Pakistan s government need proper improvement in growth rate and price index.

6.1. Gaps in literature

- 1) Prior studies have not found out the solution to improve FDI level in Pakistan.
- 2) In the previous study did not explain properly what government should do to overcome such types of issues.
- 3) In the last studies did not work on the emerging country.
- 4) Previous studies have not discuses about the how can attract foreign and local investors towards investment in the emerging country.

7. Materials and methods

We have taken the data from 1981 to 2010 and collected from state bank of Pakistan s' reports, world bank. IMF and statistical division database. At the first level we have applied the for checking the stationary we have used the ADF unit root test .at the second level least square regression model has applied. The prime target of this study to analysis the relationship between political instability, terrorism, gas shortage, inflation, GDP etc.

Equation:

$$\text{LnFDI} = p_0 + p_1\text{Pol} + p_2\text{LnTerror} + p_3\text{LnGas} + p_4\text{Inf} + p_5\text{GDP} + p_6\text{Trade} + p_7\text{Exch} + p_8\text{Incen} + U_t$$

Where:

- LnFDI = FDI inflows in million rupees
Pol = Value of 1 for military and 0 for civilian rule
LnTerror= Cost of war against terrorism in million rupees
LnGas = Gas production in million cubic feet
Inf = Annual inflation rate expressed as %
GDP = GDP deflator
Trade = Ratio of exports to imports
Exch = Growth rate in exchange rate of Rupee / \$

Table 2
ADF Stationarity Unit Root Test for Variables.

Var.	T-ADF Stat.	Critical Values	Decision
LnFDI	-4.844 (0.004)	1%level= -4.45 5%level= -3.585 10%level=-3.234	Stat. at level
LnTerror	-5.445 (0.000)	1%level=-3.678 5% level=-2.968 10%level=-2.623	Stat. at 1st difference
LnGas	-4.489 (0.002)	1%level=-3.671 5%level=-2.964 10%level=-2.622	Stat. at level
GDP	-4.033 (0.005)	1%level=-3.671 5%level=-2.964 10%level=-2.622	Stat. at level
Trade	-5.424 (0.000)	1%level=-3.678 5%level=-2.968 10%level=-2.623	Stat. at 1st difference
Exch	-4.114 (0.004)	1%level=-3.671 5%level=-2.964 10%level=-2.622	Stat. at level
Inf	-3.754 (0.008)	1%level=-3.712 5%level=-2.982 10%level=-2.628	Stat. at level

Table 3

Variable	Co efficient	Std. Error	t-Stat.	Prob.
POL	-0.772	0.264	2.928	0.008*
LNTEROR	-0.038	0.027	1.418	0.07***
LNGAS	5.742	0.576	9.984	0.000*
INF	-0.012	0.022	-0.545	0.592
GDP	0.018	0.006	-3.032	0.007*
TRADE	0.038	0.024	1.702	0.08***
EXCH	0.011	0.008	1.206	0.25
INCEN	0.878	0.342	2.569	0.03**
C	-68.09	7.387	-9.219	0.00

8. Interpretation of results

The stationary data are describing that inflation and interest rate, GDP and gas generation are stationary at level, while other variables are stationery at the first difference. After this we have applied OLS regression techniques and shown that there is positive relationship between market size and FDI inflows, results are similar in (Mohamed et al., 2010; Rehman et al., 2011).

For checking the stationary in both dependent and independent variables we have applied the unit root test. Which is explained in the table no 1. The OLS regression model has shown that adjusted r square is 0.99 which has proved that 99% variation in the FDI inflows in Pakistan. Durbin waston value is 1.98 which explained that there is autocorrelation between the explanatory variables. The AIC value of 0.39 shows that model is fyi it is considered in the proficient making inferences. These results have shown that terrorism is important variable and there is

negative relationship with the inflows in Pakistan. This study has shown that terrorism is the main reason of destroyed the FDI level in Pakistan. This study has also shown that political instability has been affecting the FDI inflows. According to different research foreign investors are only willing in that country which is free from terrorism. There is positive relationship between gas generation and FDI inflows in Pakistan. Furthermore, our result has shown that there is negative association between FDI and inflation rate.

9. Analysis

I have read a lot of papers related to FDI in Pakistan before making this research. In this article we have used the most important variables. According to different theories with an increase in the GDP the FDI level will also increase. There is found positive relationship between FDI and inflows of Pakistan.

10. Conclusion

Many studies have proved that FDI inflows act as a traversing economic. However, all the countries did not get the equally benefit for FDI inflows. For the development of economic there is need of FDI inflows. All the developing and under developing country need a equally benefit from the FDI inflows. It is important to promote the determinates of FDI inflows. The main conclusion of this study is that Pakistan has to need focus on the polices that will helpful to promote FDI inflows. To this extent these target can be achieve by the proming the economic planning. Due to lack of resources there is FDI level in Pakistan is poor. Conclusion:

The prime objective of this study is to find out the various determinants of FDI in Pakistan but utilization the time series data from period of 1981 to 2011. The result of these variables have shown that some variables have positive association with FDI inflows whereas inflation and exchange rate have negative association with FDI inflows. The results have proved that these variables have influence on the FDI inflows of Pakistan. Therefore; this study is showing that government should need to give attention on these variables for the attracting of more FDI inflows.

Suggestions

- 1) Pakistan has need more attracting of FDI for the development of country.
- 2) With honest government efforts Pakistan can be improve the economy position.
- 3) For achieving the target there is need the support of all developing countries.
- 4) There is urgent need to improve the gas shortfall for the industries development.
- 5) Pakistan authorizes need to improve the GDP rate then local and foreign investors will invest in the business units.
- 6) Finally, auothoreis should provide more and more incentives for the attraction of FDI.

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