

IMPACT OF TRADE OPENESS AND FINANCIAL INCLUSION ON ECONOMIC GROWTH IN PAKISTAN

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***ABSTRACT-**The objective of this study is to analyze the Impact of trade openness and financial inclusion on Economic growth in Pakistan. This study is a kind of quantitative research in which secondary data has been used. The data was collected from the databases of World Development Indicators of World Bank, IMF, Pakistan Economic Survey and State Bank of Pakistan. The period of study was 1967-2017. ARDL method was used to ascertain relationship between variables in the short run and long run. The variables include Financial Inclusion, Trade Openness, Credit Market, Broad Money, Labour Force participation, Gross capital formation, FDI and Economic growth. Our results show that Broad money is the main proxy variable that has negative impact on economic growth in contrast to FDI, which has positive impact on economic growth. On the other hand, Trade Openness, Credit Market, and Gross capital formation and labour force participation have positive impact on economic growth. We also found that financial inclusion and Trade Openness have positive impact on Economic Growth of Pakistan.*

Key Words: Financial Inclusion, Trade Openness, FDI, Credit Market, Economic Growth.

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1. INTRODUCTION:

Almost all the countries of the world that are developing and are developed are accessing international markets of the world through bilateral and multilateral trade agreements. Under these agreements trade openness is essential for promotion of trade in the era of globalization. Financial linkages are more vigorous than ever due to integration of economies. Trade venues and opening has become the site of interest and attraction for investors as well. The current literature has revealed that trade openness as well as economic growth influence each other significantly. It has been noticed that efficient trade can result in economic growth and enable integration of global markets in a proper way. The intermediate goods and import of capital goods has substantial impact on growth process because it enhances the economic productivity. Goods as well as services upgrade due to trade that is an effective tool in bringing technological advances by diffusing its impact on global level (Haq et al., 2015). The investment stream realignment has influence on economic growth and global economy. Most of the countries in Asia have made inclusive growth. Individuals' participation is encouraged in the process of growth to allow access to economic opportunities. It has been evident that reduction in poverty is the result of financial inclusion. International Monetary Fund (IMF) has introduced Financial Inclusion separately as the categorical and organized efforts of targeting availability of fiscal services for those people who are deprived and poor. The target of Financial Inclusion is based on provision of financial services to underprivileged and it has gained popularity due to its emphasizes on reasonable approach to opportunities. According to Park & Mylenko (2015; pp. 1), "The most important constituent of inclusive growth is ultimately inclusive financial system and it usually enhances financial services for the poor. Actually the matter of fact is that the

finance empowers poor to safeguard themselves”. It has been investigated that knowledge based economy is actually empowered by some key factors that include economic performance, research, human capital and technology (OECD, 1996).

1.1 Financial Inclusion:

Financial inclusion can be used to eliminate poverty and it can do by increasing the financial venues and leading to increase employment and education (Aghion & Bolton, 1997). The second way is the access of underprivileged to financial services for the purpose of allocation of resources in a manageable way. Deficiency of the financial resources always discourage economic growth along with increased inequality of income in the society Kakwani and Pernia (2000).

Banking reforms were introduced in Pakistani banking sector during the year of 1990 and the purpose of launching these reforms by the government was privatization of commercial banks and strengthening financial sector. It was also aimed at making financial industry transparent and competitive. Before 1990 the financial sector was under state control. The interest rates were negative and direct allocation of credit was used to set by monetary policy. It was noted during the mid of year 1980 the financial sector institutions accounted for 93.8 percent of overall total financial assets (SBP Source; Khan and Qayyum, 2007). The government of Pakistan has set various criteria to eradicate distortions to enhance economic growth. Financial reforms were introduced to: (A) implementation and fostering of competition by privatizing public sector banks, (B) making State bank of Pakistan autonomous, (C) provision of credit for SMEs,(D) strict implementation of

corporate governance, (E) liberalization of foreign exchange market, and (F) upgrading technology by launching ATMs and e-banking. Financial inclusion can be achieved via indicators that are Currency/M2 ratio and Currency/GDP, which show the currency in use and monetization level in the economy. M_3 is also a parameter used to analyze performance of intermediaries of finance and the ratio of M_3 /GDP.

1.2 Trade Openness:

Pakistan has chosen an approach that has diversity to reach economic development and has followed some of the most unique industrialization policies as a substitution of import. All policies focused on strengthening of domestic industry, achieving a level of sustainability in industry, providing the power of autonomy to chief industries, protection and safeguard of newly born industry. The government made liberalized policies for encouragement of private sector in different periods. The overall trade to GDP ratios was increased from 26.6% in 1970s to 37.6% in 2005 (Iqbal, 2008) but the ratio was started to decline from 35.6% in 2008 to 25.8% in 2017 (World Bank, 2017). This insight reflects trade integration at higher level. The imposed limitations on inflow and outflow of capital were removed steadily to encourage foreign direct investment. The investors are provided the opportunity to purchase equity up to 100% in industrial firms. The nonresidents were given rights to remit of dividend and permission granted them to disinvest and took sale proceed to their country without prior approval from SBP. The Pak Rupee was set free and its value was determined by market forces.

1.3 Main Research Problem:

The main research problem of this study is to measure the impact of trade openness and financial inclusion on economic growth of Pakistan during 1967-2017

1.4 Objectives of the study:

The objectives of this study are stated as under: -

- To explore relationship between financial Inclusion and economic growth.
- To explore short-run and long run relationship between trade openness, financial inclusion and its impact on economic growth.

1.5 Scope of the Study:

The scope of this study is wide and its results will be helpful for policy makers to frame policies regarding trade openness and financial inclusion. Similarly, the results of this study will be beneficial for the researchers and academicians as well.

2.LITERATURE REVIEW:

Kakar and khilji (2011) ascertained relation between exchange rate and foreign direct investment and its effect on financial development. The study period 30 years, from 1980-2010. Their results show that foreign direct investment is the key factor for financial development.

Atique et al (2004) examined the impacts of exchange rate on the Foreign Direct Investment and financial development. They utilized time series data over the period of 1970-2001. They found financial development had significant on Exports. They had discovered Pakistanis ability to advance

on financial improvement would rely upon attracting Foreign Direct Investment.

Rousseau and Wachtel (2011) saw the impact of monetary Deepening on Economic Growth and for that reason they just took data from 1960-1989. In their research they had discovered that money related emergencies is identified with hosing of impact of budgetary extending on development and inordinate monetary developing or too rapid expansion of credit may had encouraged together swelling and harmed budgetary structures which in this way resulted in financial crisis.

Baltagi et al (2007) revealed that exchange and money related transparency is factually significant determinants of budget deficit improvement across the nations since 1980. They found that opening of both exchange rate and capital accounts may have a positive effect on financial development.

3: THEORETICAL FRAMEWORK:

3.1 Definitions of Financial Inclusion:

It is defined as the proportion of individuals and firms that use financial services. The lack of usage of financial services doesn't necessarily means to lack the access to financial services as some people might have access to financial services at affordable cost but they didn't chose to use financial services. On the other hand, many people lack the access in the sense that the costs of these financial services are considerable high or might be that services doesn't available in their areas due to regulatory barriers, legal hurdles or cultural reasons. Around the world, nearly 50% of the adults have one or more bank accounts. In 2011, adults who were having bank accounts included the 9% of those who received loans and 22% those who saved through financial

institutions. Moreover, financial inclusion varies widely across the world. For example, the share of adults with a formal banking institution in developed countries is nearly more than twice than in developing countries. Globally, 44% of adults use a bank account on regular basis. However, 40% of income earners in developing countries out of which only 23% use bank account regularly, which is half the participation rate among the rest of the population in these countries (the corresponding participation rates in developed economies are 81% and 88% respectively). It is also troublesome that disparities in financial inclusion are large particularly in the people who are poor, young, unemployed, out of labor force or less educated the one who lives in rural areas are much less likely to have an account. Financial inclusion products comprise of Micro loans, Micro insurance, Money transfer, Micro pensions, Saving Products. These products are marketed by financial institutions like Micro Finance Institutions, Cooperatives Societies, Micro Insurance brokers and commercial and investment Banks.

3.2 Financial inclusion in Pakistan:

In Pakistan a lot of insurance and investment companies came under the definition of financial inclusion which is: Jubilee insurance, Adamjee Insurance, EFU insurance, Jazz cash, Easy Paisa, Tameer Bank, U bank, Mobilink micro finance Bank, etc

3.2.1 Key Measures of Financial inclusion:

3.2.2. Ownership of Accounts:

Account is one of the vital tools which could be used to measure the financial inclusion because all the financial activities are connected with an

account. In developed countries, 89% of adults have accounts at formal financial institutions however; this percentage is 24% in developing countries.

3.2.3 Payments:

Now a days noncash mode of payments is becoming common day by day but still this method lagged behind the cash mode of payments. Debit and credit cards accounts for a large part of non-cash retail transactions. Only a small proportion of adults are making transactions through the medium of online payments.

3.2.4 Savings:

Saving is also one of the main instruments of measuring the financial inclusion internationally. In developed countries this ratio is 58 percent while developing countries it is just 30 percent. Across the globe, 22% of adults report they used to save at a bank, credit unions or microfinance institutions (MFI) in 2011. Network based reserve funds techniques, like as, investment funds Clubs are generally utilized far and wide as a substitute to sparing at formal credit. But these penetration formal savings behaviors also vary by country category or by individual characteristics within countries (Demirguc-Kunt and Klapper 2012). For instance, 43 percent of account holders worldwide saved at a formal institution. The reason for this includes high cost of using the account, such as (a) Balance, (b) Withdrawal fees as well as (c) Costs associated with physical distance. So, Policy makers and commercial bankers should introduce innovative products and methods to encourage exiting account holders to save in formal financial institutions.

3.2.5 Insurance:

In developing countries, 17 percent of adults used to pay for their health insurance. However, this percentage ranges from 3 to 5 percent in Sub

Saharan African, Europe, Central Asia and south Asia. This percentage for East Asia and the Pacific is 38 percent which is driven by China where 47 percent of adults' report used to pay for health insurance. People who use to work in farming, forestry or fishing are critically vulnerable to severe weather and other catastrophic events. However, only 6 % of such people used to purchase crop, rainfall or livestock insurance. In Europe and central Asia only 4 percent purchase such insurance.

3.2.6 Credit:

Universally, 9 % of adults used to take loans from a formal institution. But this percentage is 3 times more in developing countries as adults are likely to borrow from family and friends. Credit card is one the innovative mode of taking short term credit. So the demand of short term loans is greatly affected by arrival of credit cards. In developed countries, 50% of the adult population has a credit card. Despite a surge in recent years, the proportion of credit card holders in developing countries still far behind than that of developed countries; as in developing countries, only 7 percent of adults have a credit card. As a result of extensive increase in demand of credit cards, the demand of short term loans from formal financial institutions has fallen tremendously. Indeed, if the adults in developed countries own a credit card are included in the share of those adults who borrowed from a formal financial institution, the share rises from 14 percent to 54 percent.

3.2.6 Types of Money:

3.2.6.1 M-1:

It Consists of Currency, Travelers' Checks, Demand Deposits, Other Checkable Deposits, NOW and ATS.

3.2.6.2 M-2:

It includes components of M-1 plus small denomination time deposits with banking institutions. Moreover, they include: Overnight Purchases agreements between commercial banks, Overnight Eurodollars held by U.S. residents other than banks at Caribbean branches of member banks, Money market Mutual funds, Money market deposit accounts (MMDA's).

3.2.6.3 M-3:

This includes M-2 plus large denomination time deposits at all financial institutions and term repurchase agreements between commercial bank and savings and loans associations. It also includes large term Call Deposit Certificate of Deposit on which no checks can be written.

3.3 THEORIES OF FINANCIAL INCLUSION:**3.3.1 Classical Economics Theories:**

In his book, "Wealth of Nations" Adam Smith called invisible hands to those forces (of demand and supply) which take the economy to equilibrium state. According to Adam Smith classical theory is based on the concept of Laissez Fair Economy. Bagehot (1873) pointed out the vital role of banking system in the growth of economy and highlighted circumstances when banks could bring innovation in future growth by productive investments.

Schumpeter (1912) was of the view that the banker was not so much important middleman in the commodity "purchasing power" as a producer of this commodity. He was of the view that the services provided by financial intermediaries such as mobilizing, savings, evaluating projects, managing risks, monitoring managers and facilitating transactions are essential for economy grow.

King, Levine (1993) presented empirical evidence consistent with Schumpeter's view that financial system can get economic growth while using data of 80 countries of the period 1960-89. He also explored various tools to measure financial development has relation with real GDP growth, rate of physical capital accumulation and improvement in efficiency in which economies engaged physical capital.

3.3.2 Keynesian Theories:

Keynes (1930) was of the view that bankers provide the way which could transport the production and productive powers of the society that could be deployed fully. Similarly, Robinson (1952) argued that financial development follows growth. In Keynesian theory, financial inclusion occurred by expansion of government expenditure and to attain full employment, the government might infuse the money in economy by increasing its expenditure. Well-functioning financial institutions gave invitation to all entrepreneurs to make their investments in productive ways and hence could be one of the causes to boost growth, improving income growth and reduce poverty.

Keynes (1936) was of the view that government could directly manage the investment. As an increase in Government spending increases the aggregate demand and income and hence the demand for money will increase. There will be then instability in the market which would be set on by reduction in private investment from higher interest rates. As higher interest rates reject the private investment and increase in government spending promote investments and might be one of the causes to cut down private investment (Dornbusch and Fischer 1978). Hence, it will be necessary to design

government policies that could remove drawbacks and make the markets efficient.

4: RESEARCH METHODOLOGY:

4.1 Nature of Study:

This study is based on the time series data, which was collected from World Development Indicators, World Bank, IMF, Pakistan Economic Survey and State Bank of Pakistan for the period from 1967 to 2017.

4.2. Selected variables:

The selected variables of this study are the followings: -

4.2.1 Independent variables:

1. Trade Openness.
2. Financial inclusion.
3. Foreign Direct Investment.
4. Labour participation rate.
5. Gross Capital formation.
6. Broad Money.
7. Credit Market.

4.2.2 Dependent variable:

8. Gross Domestic product.

4.3 Research Hypotheses

H₀: Financial inclusion and Trade openness have no positive effect on economic growth.

H₁: Financial inclusion and Trade openness have positive effect on economic growth.

4.4 ANALYTICAL TECHNIQUES:

We have used the following statistical techniques to analyze data:-

1. ADF Test to check stationarity.
2. Correlation analysis to check correlation between variables.
3. ARDL Model and Bound Test to determine long run relationship between variables.
4. Error Correction Model to check short run relationship between variables.

4.5. Specification of Model:

The Bounds test is used on three bases: First, Pearson et al. (2001) advocated use of ARDL model for the estimation of relationships between variables and suggests that once the order of the ARDL has been recognized, the relationship can be estimated by OLS. Second, the Bounds test allows a mixture of I (1) and I (0) variables as regressor, that is, the order of integration of appropriate variables may not necessarily be the same. Therefore, ARDL technique has the advantage of not requiring a specific identification of the order of the underlying data. Third, this technique is suitable for small sample size (Pearson et al., 2001).

Following Pesaran et al. (2001), we engrave vector autoregression (VAR) of order p , denoted VAR (p), in following function:

$$Z_t = \mu + \sum_{i=1}^p \beta_i Z_{t-1} + \varepsilon_t \quad (1)$$

Where z_t is the vector of both x_t and y_t , where y_t is the dependent variable defined as economic growth (GDP), x_t is the vector matrix which represents a set of explanatory variables i.e., trade openness (TOP), financial Growth. Where z_t is the vector of both x_t and y_t , where y_t is the dependent variable defined as economic growth (GDP), x_t is the vector matrix which represents a set of explanatory variables i.e., trade openness (TOP), broad money (M2) and t is a time or trend variable. According to Pesaran et al. (2001), y_t must be

I (1) variable, but the regressor x_t can be either I(1) or 1(0). We further developed a vector error correction model (VECM) as follows:

$$\Delta z_t = \mu + \alpha t + \lambda z_{t-1} + \sum_{i=1}^p \gamma_i \Delta y_{t-1} + \sum_{i=1}^p \delta_i \Delta y_{t-1} + \varepsilon_t \quad (2)$$

Where Δ is the first difference operator. The long run multiplier matrix λ as:

$$\lambda = \begin{pmatrix} \lambda_{yy} & \lambda_{yx} \\ \lambda_{xy} & \lambda_{xx} \end{pmatrix}$$

The diagonal elements of the matrix are unrestricted, so the selected series can be either I (0) or I (1). If $\lambda_{yy} = 0$ then, Y is I (1). In contrast, if $\lambda_{yy} < 0$, then Y is I (0).

The VECM procedures described above are imperative in the testing co integrating vector between dependent variable y_t and a set of regressor x_t . To drive model, we followed the postulations made by Pesaran et al. (2001) in case III, that is, un restricted the intercepts and no trends. After imposing the restrictions $\lambda_{yy} = 0$ and $\alpha = 0$, the GIIE hypothesis function can be stated as the following unrestricted error correction model (UECM):

$$\Delta (GDP)_{t-1} = \beta_0 + \beta_1(GDP)_{t-1} + \beta_2(GDP)_{t-2} + \beta_3(M2)_{t-1} + \sum_{i=1}^p \beta_4 \Delta (GDP)_{t-1} + \sum_{i=0}^p \beta_5 \Delta (TOP)_{t-1} + \sum_{i=0}^r \beta_6 \Delta (M2)_{t-1} + \dots \dots (3)$$

Where Δ is the first difference operator and μ_t is white noise disturbance term.

GDP = Gross Domestic Product

TOP = Trade Openness (X+M/GDP)

M2 = Broad Money Supply as percentage of GDP

Equation (3) can be viewed as ARDL of order (p, q, r) . Equation (3) indicates that economic growth trend to be influenced and explained by its past values. The structural lags are established by using minimum Akaike's information criteria (AIC). From the estimation of UECMs, the long runs are the coefficients of one lagged explanatory variable (multiplied by negative sign)

divided by the coefficient of one lagged dependent variable (Bardsen, 1989. For example, in equation (3), the long run inequality, investment and growth elasticities are (β_2/β_1) and (β_3/β_1) respectively. The short run effects are captured by the coefficients of the first differenced variables in the equation (3).

5: DATA ANALYSIS:

5.1 Descriptive Statistics:

The results of descriptive statistics are shown in Table 1:

Table 1: Descriptive Statistics

Variable	GDP	Broad Money	Credit Market	TOP	FDI	GCF	LFP
Mean	4.142184	16.25685	22.80296	33.46815	1.149437	2.048621	51.52519
Medium	4.396457	16.53069	24.01000	32.99000	0.813610	3.047091	51.17000
Maximum	7.705898	45.53201	28.74000	38.91000	3.668323	18.49512	54.37000
Minimum	1.014396	4.314225	15.31000	25.31000	0.382827	-9.190904	49.19000
Std. Dev.	1.816035	7.679824	4.088682	3.445067	0.867507	6.494688	1.361205
Skewness	0.269795	2.056923	-0.494761	-0.375545	1.823085	0.241825	0.434808
Kurtosis	2.525390	9.194200	2.301464	2.712436	5.271853	3.063536	2.196031
Jarque Bera	0.580963	62.20332	1.650496	0.727684	20.76285	0.267698	1.577925
Probability	0.747903	0.000000	0.438126	0.695001	0.000031	0.874722	0.454316

Source: Research Findings taken from Eviews

The Results in table 1 show that broad money which is used as a proxy variable for financial inclusion has a mean of 16.25685 with a minimum of 4.314225 and maximum of 45.53201 and skewness of 2.056923 and kurtosis of 9.194200. Hence, it is positively skewed, and data of broad money is highly peaked. Comparatively, GDP has a mean of 4.142184 with a minimum of 1.014396 and maximum of 7.705898 and skewness of 0.269795 and kurtosis of 2.525390. Its skewness, statistics showed that it is moderately skewed, however, kurtosis shows that it has flat peaked distribution. Trade Openness has a mean of 33.46815 with a minimum of 25.310 and maximum of 38.910 and skewness of -0.375 and kurtosis of 2.712. Its skewness statistics shows that it is approximately symmetrical and kurtosis figures showed it has normal distribution. On the other hand, Labor force participation has a mean of 51.525 with a minimum of 49.190 and maximum of 54.370 and skewness of 0.434 and kurtosis of 2.196. It is moderately skewed and has flat peaked distribution. Gross Savings Rate has a mean of 22.116 with a minimum of 16.887 and maximum of 27.951 and skewness of 0.447 and kurtosis of 2.556. It is approximately symmetrical and has flat peaked distribution. To the extent Jarque Bera test is concerned, it is ordinarieness test for integrity of fit. It gives the joint theory of skewness and kurtosis. As a typical dissemination has zero skewness and a kurtosis of three of estimation of Jarque Bera Test is very a long way from zero, it will at that point delineate that the information doesn't have ordinary circulation. As indicated by Jarque Bera Test, the residuals of practically all variables are regularly appropriated.

5.2 Results of ADF tests:

The results of ADF test are shown in Table 2:

Table 2: Results of Unit Root tests

Variables	Level		1st Difference		2nd Difference		Order of Integration
	Trend	Intercept	Trend	Intercept	Trend	Intercept	
GDP	-3.80	-3.69	-6.140	-6.058	-9.035	-8.888	I(0)
	0.009*	0.043*	0.000*	0.000*	0.000*	0.000*	
Broad Money	-4.170	-4.199	-6.250	-6.074	-5.588	-5.408	I(0)
	0.0034*	0.0141*	0.0006*	0.0003*	0.0002*	0.0013*	
Credit Market	-0.8251	-1.458	-3.977	-4.049	-7.051	-6.912	I(1)
	0.795*	0.8188*	0.0054*	0.0195*	0.000*	0.000*	
TOP	-1.544	-2.400	-6.352	-6.342	-9.469	-9.216	I(1)
	0.496*	0.3710*	0.000*	0.0001*	0.000*	0.000*	
FDI	-2.761	-2.671	-3.370	-3.327	-6.022	-5.891	I(1)
	0.077*	0.2549*	0.0217*	0.084*	0.000*	0.0003*	
GCF	-4.029	-3.98	-7.998	-7.868	-8.868	-7.878	I(0)
	0.004*	0.020*	0.000*	0.000*	0.000*	0.000*	
LFP	-0.522	-2.28	-4.96	-5.006	-6.586	-6.395	I(1)
	*	*	*	*	*	*	

Source: Results calculated through E-views software. * Indicate P-value

The data in Table 2 shows the Stationarity of the variable and their order of integration. GDP is stationer at Level and its coefficient Value is -3.80 where as it probability value is 0.009. However, Broad Money is also stationer at level as its coefficient Value is -4.170 and its probability value is 0.0034. On the other hand, Credit market is stationer at 1st difference with coefficient value of -3.977 and Probability value of 0.0054. Trade openness has also shown the same trend as being stationer at 1st difference with coefficient value of -6.352 and probability value of 0.000. Similarly, foreign direct investment

is stationer at 1st difference with having coefficient value of -3.370 and probability value of 0.0217. However, GCF is is stationer at 1st difference with coefficient value of -4.029 and probability value of 0.004. Labor Force Participation is stationer at level with having coefficient value -4.96 and probability value of 0.0005.

5.3 Analysis of Correlation Matrix:

The results of correlation analysis are given in Table 3:

Table 3: Correlation Matrix

	GDP	Broad Money	Credit Market	TOP	FDI	GCF	LFP
GDP	1.0000	0.1407	-0.0460	0.1081	0.5031	0.1883	0.6052
Broad Money	0.1407	1.0000	0.2230	0.2985	0.3174	0.4590	0.1332
Credit Market	-0.0460	0.2230	1.0000	0.4915	0.5818	0.0070	-0.1937
TOP	0.1081	0.2985	0.4915	1.0000	0.1871	0.0716	-0.5004
FDI	0.5031	0.3174	0.5818	0.1871	1.0000	0.2728	0.2094
GCF	0.1883	0.4590	0.0070	0.0716	0.2728	1.0000	0.0357
LFP	0.6052	0.1332	-0.1937	-0.5004	0.2094	0.0357	1.0000

Source: Results calculated through E-views software

Correlation matrix estimates the strength of the relationship between the variables. In this table, we can see that all variables are positively correlated except credit market which is negatively correlation.

5.4 ARDL Model: Estimation of Long-run Relationship

Selected Model (2, 0, 0, 1, 1, 0, 1, 0), (GDP) is dependent variable

Table 4: Long run relationship between variables

Variables	Coefficient	Std. Error	T-Statistics	Probability
C	-29.383	16.781	-1.750	0.105
Broad Money	-0.014	0.029	-0.505	0.622
Credit Market	0.062	0.076	0.811	0.432
TOP	0.214	0.097	2.194	0.048
FDI	0.014	0.534	0.027	0.978
GCF	0.066	0.031	2.118	0.055
LFP	0.586	0.290	3.329	0.048

Source: Results calculated through E-views

ARDL model shows long run relationship between variables and the coefficient of Broad money has negative values which depicts that Broad money is negatively related with GDP in the long Run. However, all the other selected variables are positively related to GDP. TOP is positively related with GDP having coefficient value of 0.214, which shows that if trade openness increases by 1 unit, GDP (Dependent variable) will increase by 21% and, the probability value (0.048) shows its significance. LFP has positive relation with GDP and it shows if there is one-unit increase in LFP the GDP will increase by 58%. It indicates that there is significant relationship between labour force participation and GDP as the P-Value is less than 5%.

5.5 Bound Test:

In order to verify the results of ARDL model we applied Bound Test and its results are shown in Table 5:

Table 5: Bound Test Results

Test Statistic	Value	Significance	I(0)	I(1)
F-Statistic	3.70	10%	1.92	2.89
K	7	5%	2.17	3.21
		2.5%	2.43	3.51

Source: Results calculated through E –views software

Table 5 shows that the F Statistics is 3.7 which is more than upper bound value so there is long run relationship between variables.

5.6 ECM: Estimation of short run relationship:

Error Correction model is used to measure short run relationship between variable. Its results are shown in Table 6:

Table 6: Short run relationship between variables

Variables	Coefficients	Std. Error	T-Statistics	Probability
D(BRDMNY)	-0.021	0.284	-0.767	0.457
D(CRDTMRKT)	0.047	0.146	0.325	0.750
D(TOP)	1.422	0.115	3.521	0.004
D(FDI)	1.580	0.501	3.148	0.008
D(GCF)	0.111	0.030	3.690	0.003
D(LFP)	1.219	0.388	3.136	0.008
CointEq(-1)	-1.769	0.284	-6.210	0.000

Source: Results drawn through E-views software

$$\text{CointEq} = \text{GDP} - (-0.0147 * \text{BRDMNY} + 0.0622 * \text{CRDTMRKT} + 0.2146 * \text{TOP} + 0.0144 * \text{FDI} + 0.0667 * \text{GCF} + 0.386 * \text{LFP} - 29.38$$

R-Square	= 0.7878	D.W Stat	= 2.07
Adj. R-Square	= 0.5757	F-Stat	= 3.71
Akaike info Criterion	= 3.5481	Prob (F-Stat)	= 0.01

Table 6 shows the short run relationship between dependent and independent variables. If one unit increases in Broad money there will decrease in GDP by 2%, but this is not statistically significant. Similarly, when one-unit increase in Credit market it will likely to increase GDP by 4%, but this is not statistically significant. If trade openness, increases by one unit the GDP (Economic Growth) will increase by 14% and this is statistically significant in the short run. However, if FDI increases by one unit GDP will increase by 58%, and their relation is statistically significant in the short run. Similarly, if GCF increases by one unit GDP (Economic Growth) will increase by 11% and their relation is statistically significant in the short run. Similarly, If LFP increase by one unit GDP (Economic Growth) will increase by 21% and their relation is statistically significant in the short run.

6: FINDINGS OF STUDY:

The value of R-Square is 0.78 that implies there is 78 percent change in the dependent variable due to variation in independent variables. The calculated value of DW is 2.07 which means there is no auto connection. Likelihood of F-measurement is critical with estimation of 0.01. In this way, the broad money supply and Foreign direct investment have positive effect on financial development in Pakistan. We found that labour force participation, foreign direct investment and gross capital formation have significant positive effect on GDP of Pakistan during our study period. Foreign direct investment and gross capital formation enhance productive capacity and in turn increase in international trade and development of human capital. It also promotes financial development in the country and accelerate economic activities. Gross capital formation means expansion of capital stock which enhances productive

capacity of the country and enable it to produce surplus goods and services. Our findings show that only broad money supply has negative effect on GDP growth in the short run and long run because it gears nominal GDP rather than real GDP.

7 CONCLUSION:

From the above findings we draw conclusion that trade openness, financial development, foreign direct investment, gross capital formation and labour force participation have significant positive relationship with GDP in Pakistan while broad money supply has negative relationship with GDP. So the credit expansion, increase in foreign direct investment and acceleration in the gross capital formation and trade openness have plus sign for Pakistan economy and Pakistan must focus on improvement of these variables. Whereas money supply must be controlled as it increases in inflation rate and price level of goods and services in the country and domestic and foreign consumers are reluctant to purchase goods and services at higher prices. These results also pinpoint the fact that Pakistan should focus on production of goods and services to reduce inflation and poverty. If the quantity of goods and services are available in sufficient amount it will enable consumers to purchase them easily. Thus, productive capacity of country must increase in order to increase Pakistan's share in international trade and investment in speculative assets must be discouraged.

8. POLICY RECOMMENDATIONS:

In the light of the above conclusion we would like to make the following policy recommendations: -

► A regulatory framework should be created by the government to encourage financial inclusion which is already in practice by adaptation of Mobile

Telecom (Like Easy Paisa, U-Paisa, Jazz Cash etc.) to operate money transfer without having to comply with SBP regulations. In order to make financial services accessible to a number of people, such activities should be encouraged.

▶ A vast section of disadvantaged and low income groups are facilitated with banking services at economical rates due to financial inclusion. Setting up new branches in rural areas might involve a huge finance by banks and other financial institutions to increase their rural areas branch network.

▶ As phone banking and banking applications have eased the transfer of funds from one person to other. So, these initiatives should be promoted in the light of growing financial needs of the people.

▶ Financial resources must be invested in productive activities rather than in speculative activities in order to increase productive capacity of the country.

5. Loans on low interest rate should be provided to poor segment of the society to enable it to meet its urgent need and to start small business activities. It will not only increase their income but also reduce poverty level in the country.

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CONTRIBUTION OF AUTHORS AND CONFLICT OF INTEREST

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