The Impact of Foreign Direct Investment on Unemployment and Poverty in Pakistan

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Submitted to the
Institute of Graduate Studies and Research
in partial fulfillment of the requirements for the degree of

Master of Arts in Marketing Management

Eastern Mediterranean University February 2017 Gazimağusa, North Cyprus

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ABSTRACT

This thesis research covers the topic 'The Impact of Foreign Direct Investment (FDI)

on Unemployment and Poverty in Pakistan'. The study is a comprehensive analysis

which discusses Pakistan's economy in detail to provide an overview on

unemployment and poverty of a struggling economy.

It further highlights the important political events and major FDI's made over years,

gauging its effect on the unemployment and poverty with a sector and country wise

breakdown of FDIs.

The research is a mix of qualitative and quantitative analysis showing enough

evidence that the FDI in Pakistan is not helping to remedy the existing issue of

increasing poverty and unemployment.

However, ironically a positive relationship is found between FDI and economic

growth in Pakistan where two variables correlate significantly. Although there is a

significant correlation between FDI and economic growth in Pakistan, the poverty

and unemployment in the country have not improved due to inefficiency of the

government.

Keywords: Foreign direct investment, Unemployment, Poverty, Economic growth

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ÖZ

Bu tezaraştırmakonusu "Doğrudan Yabancı Yatırımların (DDY) Pakistan' daişsizlik

veyok sulluğaetkisini" kapsamaktadır. Bu çalışmaPakistan'ınekonomisini, işsizlik

veyok sullukolgularının DDY' daetkileşi mlerinianali zetmektedir.

Pakistan'da DDY ülkedekiyoksulluk, işsizlik sorunlarınıç özmekiçinyar dımcıolmadı

ğınıkanıtlamıştır. Araştırmad anicelvenite lanalizler kullanılmıştır. Ancak Pakistan'

da DDY ileekonomik büyümearas ındaanlam lıbirkorelasy onbulunmuştur.

Araştırmanıniçeriğinde, ekonomikbüyüme, işsizlikve yoksullukar asındaoluşturulan

bağlantıdet aylıbirşekildean latılmıştır. Aynızamanda buaraştırmalar Pakistan'

dahükümet inuygulamada yetersizvever imsizolduğunu, makroek onomikçözüm

lereldeet medebaşarısı zolduğun ugöster mektedir. DDY ileGSY' ninarasındakigü

çlükorelasyon, Pakistan' dayoksulluğuveiş sizliğiazaltmakiç inetkisiolmamıştır.

AnahtarKelimeler: Yabancıdoğrudanyatırım, işsizlik, yoksulluk, ekonomikbüyüme

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To My Father

Mr. Shahid Dar, whose wisdom and knowledge has always inspired me.

ACKNOWLEDGMENT

I would specially like to thank Assoc. Prof. Dr. Şule Aker who initiated the concept for this thesis and supervised it with the utmost efficiency and commitment beside her busy schedule. It is certainly true that I was very lucky to have had a supervisor of her stature.

The diversity of her knowledge and cooperation was remarkable. Her accuracy of assigning work and sophistication is truly amazing; this certainly is an experience that I have never had before in my educational or professional career to say the least.

I owe a lot to my parents and family for their never ending support and trust that they have expressed over so many years. No matter how hard I try I can never express my gratitude for them and my efforts to give them something back in return still continues.

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Chapter 1

INTRODUCTION

The research hereby attempts to conclude the impact of Foreign Direct Investment (FDI) in Pakistan keeping under consideration a practical approach backed up by economic derivations and a discussion of extenuating factors that can flourish or sabotage an economy, as a result of which how a country follows some patterns triggered by FDI.

The gaps in the research however are gauging of FDI in terms of its effectiveness with respect to encountering poverty and unemployment that will be gauged with a yearly trend analysis with all three variables under consideration.

FDI is the investment from outside geographic boundaries to a host country. Poverty on the other end describes a state where a certain percentage of the population cannot meet the basic necessities of life. Unemployment refers to the percentage of people willing and able to work but yet jobless within a country. Lastly economic growth is the increase in production of goods and services within a country or increase in Gross Domestic Production (GDP).

All these concepts will be used in the basic discussions and the thesis attempts to impact of independent variable on the dependent ones.

The review provides us information from several researches all concluded comprehensively to interpret economic factors like GDP, unemployment and poverty with respect to FDI. Most of these were concluded by several universities in Pakistan and several on an international scale, with a diversified set of information and comprehensive approach.

However what must be kept under consideration is that Pakistan's economy cannot be compared to that of Europe, China, Japan or Turkey since the economic structure of Pakistan is heavily influenced by extenuating factors like corruption, terrorism and energy crises. Pakistan has not been following a much disciplined economic cycle since decades, as a result of which the economic picture of Pakistan looks much different than the countries mentioned in the literature review.

To attain a conclusion for this research, firstly statistics for two decades of poverty, three decades of unemployment, three decades of GDP and three decades of FDI are obtained. This is then followed by a simple regression technique to measure the relationship of these variables as FDI being the independent variable and unemployment, poverty and economic growth being the dependent variables.

The focal point however was the impact of these FDIs with respect to macroeconomic concerns (poverty and unemployment). The purpose is hence for the readers to highlight the above mentioned forces and their influences with respect to FDI that will further reflect its impact on Pakistan's economy.

The results show that FDI and economic growth is significantly correlating positively and supporting the economic notion. On the other end there is no significant impact of FDI on poverty and a slightly positive relationship with unemployment which exposes the current failure of Pakistan in terms of its fulfillment of macro-economic objectives.

Moreover, an underutilization of natural resources, corruption and weak internal and external policies provide a detailed image of the country's existing situation. Chapter 2 further shows the details of how the FDIs were not fruitful to address a better employment and poverty rate.

The research attempts to benefit the Government of Pakistan, enhance the knowledge of students and create a statistical understanding for business investors (both foreign and domestic) and also comes up with recommendations that will prove helpful in order to have a better system in place.

Chapter 2

LITERATURE REVIEW

This review entails the findings of the impact of Foreign Direct Investment (FDI) on poverty, unemployment, and economic growth based on quantitative data along with any qualitative factors that ultimately play when analyzing the dependent variables in Pakistan. The researchers previously have already applied time series, econometrics and statistical analysis based on formulas and economic interpretations.

There is no previous research on FDI's impact on poverty and unemployment in Pakistan. So this thesis will be the first research based on the following variables in Pakistan; FDI being the independent variable, whereas economic growth, unemployment and poverty are the dependent variables.

To begin with the most interesting and detailed research conducted to measure the impact of FDI on poverty using time series analysis and other qualitative measures. After taking data from sixty developing countries the research explained that FDI does not have a significant relationship with poverty reduction in most developing countries. This was due to a high income inequality and an incompetent system to restore equalization of wealth by utilizing state revenue effectively [56].

As a compliment to the previously mentioned research at a domestic level, another research concluded that there is no significant impact of FDI on Pakistan's poverty [4]. The argument therefore becomes stronger focusing on how effectively Pakistan is utilizing its FDIs. Pakistan (as discussed) is a country that employees most of its population in the primary sector, another evidence using statistical analysis based on yearly trends elaborates how poverty is the most common amongst agriculture and construction sectors [29]. On the other side, it is argued with the help of time series analysis that reduction in poverty and income gains at a decent percentage were attained by Pakistan in 1972-73 and 1990-91 [31]. Elaborating the focus mentioned above, this with the help of yearly trends and analysis, it was concluded that main reason behind poverty in rural areas of Pakistan is due to agriculture sector being ignored [40].

To understand the macroeconomic perspective of a stronger economy, results compiled were perfectly aligned with the economic theory. The research in China using FDI statistics and employment trends came to a conclusion that there was indeed an increase in home employment triggered by FDI [55].

Further with another comparative analysis of Pakistan and Turkey concluded that Pakistan and Turkey both heavily rely on the primary sector for exporting whereas the reason for Turkey getting better results in the primary sector is because it has a better business environment. It further brings into attention similar problems that a country can face due to its unsuitable business climate and to lack of FDIs despite the rich lands they are gifted with for agriculture [57]. Moreover, discussing the balance of payment account and dependability of a country's economy, it is also argued that

the FDIs in tertiary sector are not being beneficial in the long run for Pakistan due to its income outflows [21]. This concludes lack of confidence in local spending.

From a developed country's perspective, another piece of work clears the picture by laying emphasis on business confidence and implementation in the right areas in order to restore economic footings and maintain a decent balance of payment account

at the same time [20]. Similar results of FDIs being focused on business acquisitions

and land purchases in Turkey that did not result as beneficial as expected [41].

The most common link researchers worked upon is FDI and economic growth. Some researchers formed an opinion suggesting that the inflows from FDI in Pakistan are not very much related to its economic growth. While other Asian countries mainly China and Japan did attract a lot of foreign investors for meaningful investments, this helped them capitalize their economy and encounter problems like unemployment and poverty to guarantee mutual gains[1][2]. A very interesting research by further highlights how telecom sector was the focal point of all investments made in Pakistan, this gave a boost to one particular industry and created employment for a specific segment [6].

A recent research using a detailed statistical drill down and time series in the Chinese Economic Review is a comprehensive argument favoring the idea of FDI adversely affecting the regional equality of income levels, which can be encountered by the government and mobility of human resources. Therefore this opens a possibility of negative impact of FDI, since equalization of wealth is one of the primary objectives of countries which certainly require a decent rate of employment and poverty. Further elaborating the economy of India and China, the research explores some of

the areas struck by inequalities that can hamper employment and worsen poverty crisis [7].

The perfect contrast on a domestic level was drawn that supported the link of FDI with political stability in order to ensure reduction of poverty in the country, hence concluding that there is no relationship between FDI and poverty reduction in Pakistan [3]. The idea supported with yearly trends of poverty concluded the importance of better management of resources, with emphasis on water management and agriculture in order to curtail poverty [40]. The concentration as a result is in the rural areas where most of the cultivation is practiced.

As a compliment to the research mentioned above, another prolific finding concluded under the Second World Conference of Economic Management states that FDI can curtail poverty indirectly; given that economic and technological factors are used efficiently to increase the rate of employment and most importantly increase economic growth. This gives an idea that economic growth plays a vital role in a nation, given that the right economic system is in place [5].

Bringing forward the findings based on statistics from the European Union (EU) it can be understood that the EU strongly believes in attracting FDI, as it is a great help to encounter poverty and unemployment. As a result of which the EU includes policies to attract FDI in order to strengthen their economic footings in the long run [54].

The idea mentioned above can is a prefect analysis of how a stronger economy can ensure a very positive impact of FDI due to its implementation, this is further discussed in detail with data gathered from several developing countries including China. This brings into attention the effectiveness of implementation that lead China to benefit its economy by FDI injections [55].

As reviewed, the gist of researches mentioned above is that a poor utilization of FDI might harm the interests of masses in a nation and a corrupt or inefficient political system can worsen the situation; Pakistan is suffering due to a corrupt and weak government as another setback apart from a high percentage of poverty and unemployment. The conclusion therefore driven from the researches illustrated above is that FDI can have a noticeable impact on poverty and unemployment, given that it is firstly infused in the right sectors and secondly utilized effectively.

The case for Pakistan however might not be a perfect representation of an ideal economic scenario but based on the economic derivations it is possible to pin point any irregularities in Pakistan's economic system or factors related to it.

In theory, economics states that attracting FDI should be one of the basic macroeconomic aims of a host country. A perfect case for FDI includes an effective utilization of resources, increased home employment, and better capital account in balance of payment account, increased competition, economic growth, international exposure and above all revenue generation for the government [20].

With such a change, the government can also change its country's dynamics by investing in the infrastructure and forming favorable monetary and fiscal policies. As a result, a country can at least move towards more stable international relations, provided it is politically sound which will help it to maintain its roots in order to have a say on international forums and succeed with a global understanding.

Moreover, this economic theory in a perfect world is definitely applicable. There are however some prerequisites to insure gains, primarily which includes a stable and just governance as a politically sound country is economically stable one.

As we move forward, an economy therefore managed by a responsible government should lead to better results. These results (if derived from a substantial increase in FDI) will result in economic growth, increase in employment and reduction in poverty. This is because more investment means more operations in the host country, this will automatically trigger more employment opportunities increasing the possibility to subside poverty and stabilize the distribution of wealth.

On a broader scale employment helps the government to collect more taxes and generate revenue to spend in all its essential endeavors. This usually includes a percentage of unearned income and pensions in developed countries, where a greater percentage of poverty is eliminated because of a very effective and timely implementation process.

Hence, the economic assumption is that; FDI has a positive relationship with economic growth and negative with poverty and unemployment.

Since we have to develop a detailed understanding of the Pakistani economy, we will have to take real statistics for evaluation.

2.1 FDI Inflows in Pakistan



Figure 1: Yearly FDI in Pakistan, and its taken from Jaffri. A. A. et al. (2012), Breoder Business and economy (2014)

Figure 1 above shows the statistics of FDI in Pakistan from 1980 to 2014. The data generated above shows continuous fluctuations with noticeable jumps in 1995-96 and 2005-2008.

The basic investments made in Pakistan were majorly made initially in the power sector, for industrialization and production support. The basic inflows during the early decades were from UK and USA followed by Gulf Countries and above all China and Iran.

US generally prefer catering the tertiary sector of Pakistan, which includes food and beverages. It also assists Pakistan for the exploration of natural resources such as oil, gas and agriculture. UK had similar interests as the US, but was more inclined towards the power sector [48].

China on the other end invests in a variety of industries ranging from agriculture, manufacturing (automobile, textile etc.) to now even in the energy plants in order to encounter the power crises which is one of the main problem for all businessmen in Pakistan today. Japan and China somehow follow the same pattern of investment as the two countries are archrivals in terms of competition, mainly in cellular and automobile industry [49].

In the housing and construction sector, Singapore, China and Japan all have a considerable amount of inflows which is very consistent since the projects are long-term.

Secondly the United Arab Emirates (UAE) mainly focuses on livestock, agricultural sector and recently the telecom sector in Pakistan. The most interesting trend in recent years for a substantial amount of investment is coming in from Turkey in the transportation sector, the country also invested in waste management and intends to invest further for the years to come [50][51].

Moreover, intitally this trend of investing in the power sector was under certain checks and measures initially. In 1984, an industrial policy was made giving equal significance to the public and private sectors. Before this almost all powerful industries or monopolies were nationalized leaving less power in the hands of individuals and more to the government.

In the 90's however, many restrictions imposed for the protection of home industry were lifted except for a very few which were subjected to sensitivity for example alcohol, ammunition, security goods, etc.

Further in 1995 an even more flexible policy was introduced which reduced duties and, as a result another increase in FDI was triggered that can be observed in Figure 1. This was then followed by another opening, this time in the agricultural and service sectors. Food chains, restaurants and shopping malls were hence a new charm for cities like Lahore, Islamabad and Karachi.

In 1997, all foreign countries' local market was open to any investments in the primary and tertiary sectors of Pakistan. The impact of which was yet to be witnessed since Pakistan back then was not a worthy contender compared to other economies [53].

In 2005, Etihad Etisalat (located in Riyadh, Saudi Arabia) bought PTCL as a result of which Pakistan's only telephone line was now owned by an external party, diversifying it into a broadband internet and telephone line service [52].

The trend however was the investments in the communication industry which also required a substantial input in the services sector and as a result companies like Mobilink were established [36]. Thus some investments in the Financial Sector were made by UAE and Saudi Arabia in 2006-2007 as entrants to the communication and financial industry which gradually decreased because the investments that followed were now only operational investments.

To make matters worse on 24th of September 2006, there was a complete blackout in Pakistan resulting from lack of electricity to which Water and Power Development Authority (WAPDA) had no explanation.

It was publicly declared after this event however that Pakistan did not have enough electricity for its residential or commercial activities. This gave foreign investors an image that Pakistan lacks the ability to manage its publicly owned firms efficiently that solely work for the country's infrastructure facilities [23].

In 2008, 800000 acres of farmland was acquired by Abraaj Capital and some other companies located in UAE. This was then followed by another investment of \$40 million in order to acquire 16187 hectares of land. 'Qatar meat and livestock' is a major investor in Sharakpur, Larkana and Sukkur which are considered to be rich areas in terms of farming and livestock [24].

Following was an overall property boom in 2006-2007 which resulted in a large cap property purchase that was unfortunately not liquefied. Once the bubble did burst, it left its impact later in 2009-2010. There were ample schemes for land purchasing in Pakistan but once the money was held up due to land purchases, the reselling of lands became difficult which slowed the circulation of money. As a result, the demand for local and foreign commodities reduced drastically.

On the other end, as a result of an unforeseen event known as the 9/11 resulted as US-Afghan friction, following which Pakistan received a phenomenal support from the US in order to curtail terrorism.

Certainly, US did creep in the roots of Pakistan's political and economic agenda having a say in almost every major decision the country had or still has to make on a domestic or an international scale as a result of weak governance.

2.2 Unemployment with Respect to Demographics

The second part of the chapter analyzes the trend of unemployment in Pakistan. The country has almost half of its employment in the primary sector with a literacy rate of 60% (recorded in 2013) and relies on aid to groom its agricultural industry [25].

As the smallest province, Sind has a very high rate (50.3%) of unemployment with Karachi being the main attraction of revenue generation and employing a decent percentage of human resources. Whereas Baluchistan, being the largest piece of land as a province in Pakistan is still being highly underutilized has a percentage of 49.7% of the labor force that is unemployed.

Punjab, to date is the most developed province and yet it fails to guarantee employment with 52% of its population unemployed and the rate is still increasing. Lastly KPK, the most troubled area and a province in Pakistan has a rate of 40.6% unemployment rate which exhibits a decent rate of reduction given the challenges it faces [26].

The problem however is that Punjab (as per statistics) has the highest literacy rate of slightly more than 70%, with education promotion becoming a profit oriented industry the percentage of skilled labor force is drastically decreasing.

Whereas the basic literacy rate in Sind, KPK and Baluchistan are 69, 60 and 50% (last recorded in 2012/13) respectively. With a limited number of schools and universities currently present in these areas a large percentage of people is deteriorating and being exposed to challenges like poverty and corruption [27].

2.3 FDI and Unemployment

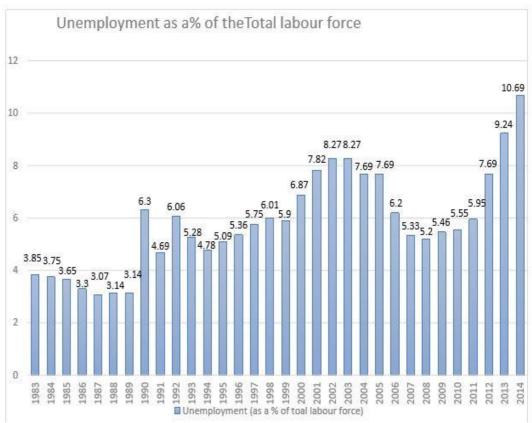


Figure 2: Yearly Unemployment as a percentage of the total labor force in Pakistan, Trading economics and unemployment rate (1985-2015)

As discussed earlier, the assumption is that there is a positive relationship between employment and FDI. We can initially observe the trend of employment, it is matching the simple economic equation as the level is gradually decreasing with an increase with FDI.

Some major inflows in 1996-97 didn't reduce the rate of unemployment due to factors like an increased population, political uncertainty and lack of accountability. Moreover, a proof for a better political accountability can be further seen, as an increased FDI in 2006-07 was utilized rightfully to a certain extent if to say the least. As a result of which the unemployment rate was curtailed for the following years.

Moving forward, unemployment rate elevated to a great extent in the following years presenting the aftermath of the previous years of reduced FDI. So the impact of a fall in FDI in 2010 was a disaster for the years to come which lead to cyclical unemployment, which is the most threatening since it's more difficult to encounter.

Given the literacy rate and underutilization of natural resources the country failed to employ its labor force in the primary sector; as a result the industrial sector did not grow reducing the chances for further employment. As the only sector that could cater uneducated and rural residents was the primary sector which is the basic strength of Pakistan's economy. However once the incentive to produce was not given in the primary sector, the industrial sector automatically didn't find enough raw materials to convert into finished products leading to a bigger disadvantage.

As a comparison, the foreign countries that did employ a large percentage of people in Pakistan were badly influenced by political corruption and increasing crime rate. Seasonal unemployment was further another problem Pakistan faced, it failed to switch its production depending on seasonal trends due to a poor mobility of factors of production (FOP).

2.4 FDI and Poverty

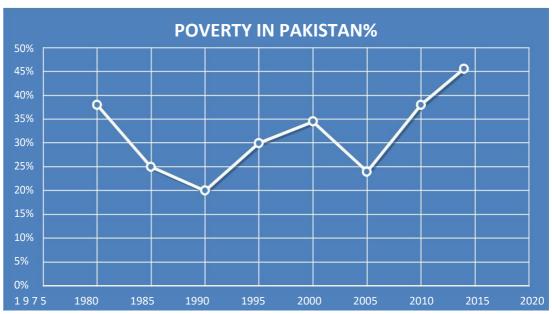


Figure 3: Yearly Poverty stats as a percentage to the whole population of Pakistan to the nearest percentage, source: Jan et al. (2009), Trading economic, Poverty gap at national poverty line (2015), Goheer N. A et al. (1999)

Surprisingly, the constitution of Pakistan does state a section for rural development with the purpose of encountering poverty in the country. The problem however comes majorly because of land holdings and lack of incentives for agricultural sectors where most of the population is unemployed and hence deprived of any government assistance.

Farmers in the main areas of Pakistan cannot grow crops in bulk due to lack of subsidy and technology. This leaves them to grow crops in smaller proportions and not experiencing any economies of scale, the traditional ways of growing crops is not only time taking but is also more costly which automatically causes cost push inflation (a higher cost leading to a higher price). Since the lands are rarely owned by these farmers, they are mostly in a weak position to bargain and they have to settle for lesser gains [33].

Before analyzing the given situation, it is important to assume the increasing rate of population in the country that automatically reduces the possibility of income maturity. Moreover the gap between the rich and poor classes within domestic boundaries was always a concern, since 1963, 20% of the richest population owned almost 45% of the income. Although, the distribution of wealth was a concern since the 1960's but was never stabilized.

Initially until 1990, the taxation system was better and the incidence of tax somehow did curtail the rate of poverty within the economy. As it can be clearly seen, FDI still has no significant increase or impact on the variable in the first decade.

In 1995, poverty rate reached 30% whereas at the same time there was a decent inflow of FDI as well. The trend is still increasing as in the year 2000; rate of poverty was around 35% since the businesses were yet at an establishing stage.

It can be seen in the coming years that poverty reduced at a decent rate until 2005. From this year onward however, there is a continuous increase in poverty despite the see large sums of FDI, very few of which were employed in useful causes (as discussed before).

2.5 Economic Growth as a Percentage of FDI

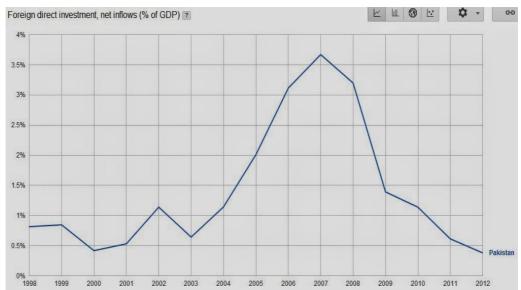


Figure 4: Economic Growth trends 1998-2012, data is taken from "declining Investment Hurting Pakistan Economic Growth" (May13,2014)

To maintain a brief understanding of the economic impact of FDI on economic growth, it is essential to analyze it as a percentage of GDP.

We can clearly understand the whole scenario as in the early 90"s there were more flexible policies announced in order to attract foreign investors. The threshold however was experienced in the coming years as a result of which the growth was more stable.

This was then followed by another event in 1997 where the investors were free to invest in the tertiary sector, initially which was a problem since Pakistan as a country was not known for its services industry.

We can clearly analyze, the local and foreign industries located within domestic boundaries struggled to work at their full capacities due to the energy crises. However, jump from 2003 till 2011 is a perfect demonstration of how FDI can enhance GDP per capita, what follows is even more interesting. From the data given, unemployment decreased to 5.2% in 2008 and poverty was below 25% which is to an extent quite remarkable.

What must be understood is that FDI has a delayed effect on GDP and it does take some time to reduce problems like unemployment and poverty even after the investment is made.

Since there was no consistency in the inflows of FDI, no noticeable effects can be witnessed in the reduction of poverty and unemployment.

Chapter 3

METHODOLOGY

The methodological framework includes secondary research to collect data that is a mix of qualitative and quantitative.

3.1 Data Collection Techniques and Measures

Time series data collection technique for all variables includes different sources including websites and research papers previously written on the subject. The most reliable and fruitful source considered is the Pakistan Institute of Development Economics since it is recognized by the government in terms of its reliability and validity. The statistics were also matched with several articles and newspaper publishing to check their accuracy.

On the other hand, the political events and trends of FDI in the Pakistan will include a sector wise breakdown that can be seen from previous research papers that have already been discussed in the literature review. Any amendments in the constitutions affecting the variables in this research were taken from Government of Pakistan's set of laws.

The bright side of this technique is that the data is being collected from multiple sources which will allow a room of crosschecking information. The research is connected to more than one tie, at one end it has the economic derivations whereas the other side relates political and external factors.

This will automatically highlight any gaps in the data collected since the impact of one aspect should be reflected upon the other.

3.2 Data Analysis

IBM SPSS version 14 is used to compile the results that include a simple regression, time series correlation and ordinary least square methods. FDI being the independent and unemployment, poverty and GDP being the dependent variables the analysis were made with the following formulas to support the findings:

1.
$$U = Cu + B1 FDI + e1$$
 (2. 1)

2.
$$P = Cp + B2 FDI + e2$$
 (2. 2)

3.
$$GDP = Cgdp + B3 FDI + e3$$
 (2. 3)

(2.1)

U = Unemployment as a percentage of the total labor force

Cu= Constant term for unemployment

B1 FDI= Coefficient for FDIs for equation 1

FDI in \$US billion

e1= Error term for equation 1

(2.2)

P= Poverty as a percentage of the total population

Cp= Constant term for poverty

B2 FDI= Coefficient for FDIs for equation 2

FDI in \$US billion

e2= Error term for equation 2

(2.3)

GDP= Gross Domestic Production in \$US billion

Cgdp= Constant term for gross domestic production

B3 FDI= Coefficient for FDIs for equation 3

FDI in \$US billion

e3= Error term for equation 3

To make the calculations possible and create a long term link between the variables, the data was collected as following:

- 1. FDI inflows (\$US billions) from 1983 to 2014
- 2. Unemployment as a percentage of the total labor force from 1983 to 2014
- 3. Poverty as a percentage of the total population from 1990 to 2014
- 4. Gross Domestic Production (\$US billions) from 1983 to 2014

3.3 Formation of Hypotheses

The hypotheses to be judged in the findings therefore are:

- 1. H1 : FDI and unemployment have a negative relationship
- 2. H2: FDI and poverty have a negative relationship
- 3. H3: FDI and GDP have a positive relationship

Chapter 4

PAKISTAN: THE ECONOMY

Amongst the most rapidly changing countries and with an ample potential for

development, Pakistan stands the sixth most populous country and the 36th largest in

terms of area size that is 796,095 km (sq.). With five seasons and four provinces, the

country has a rich climate for agriculture. With Punjab, Sind, KPK and Baluchistan

as the four provinces of Pakistan, it is a universally known fact that the cultural and

weather diversification in Pakistan is a unique element of this country, a variety of

race and tradition can therefore be witnessed, along with strong heritage

Geographically located in South of Asia, Pakistan shares its borders with India,

China, Afghanistan and Iran. With an underutilized abundant supply of water,

Pakistan has five rivers known as punjnat. The country ranges from deserts,

mountain ranges to plateaus and also has a shipping port in Karachi known as

Karachi Port Trust (KPT).

Standing as the 26th largest economy in the world and with the seventh largest

standing army, Pakistan is the first nuclear Islamic Republic. Many argue that the

country should have been in a much more stable position than it is at the given point

of time. In this thesis, we will look for reasons why Pakistan is not performing better

amid all its potential to encounter macro-economic issues [44].

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Pakistan today is a member of many associations on a global scale, the most noticeable of which are United Nations (UN) and The Commonwealth Nations.

4.1 Economy of Pakistan under the Political Influence

With a GDP of \$884.2 billion (recorded in 2014) [8] and an average recorded unemployment rate of 5.17% (recorded in 2014) [9], Pakistan is a developing country with most of its population being employed in the primary sector and thus its major exports consists of agricultural goods like cotton, wheat, fruits and vegetables. Whereas the industrial sector in Pakistan specializes mainly in textile, leather and cement industries with textile computing more than 60% of the total exports [10].

Moreover, it is no secret that tertiary sector of Pakistan mainly relies on food/beverages, communication and clothing/footwear markets contributing 53.3% of the total GDP. Subsequently the primary and secondary sectors are estimated to be 25.3 and 21.3% which is almost half of its GDP (recorded in 2014) [11].

4.1.1 Mismanagement of Nationalized Organizations and Corruption

At present, about 69 state owned organizations are being mismanaged by political leaders on purpose to be sold to their cronies and affiliated business groups. The height of corruption is that after the law being passed by the United Nations Organizations (UNO) to return stolen assets back to the deprived country, no effort was made to bring the culprits to justice because the court's decision of the deprived country is binding on the overseas government to return stolen assets to the host government while \$200 billion are just in the Swiss banks, owned by a handful of Pakistanis [42] [43].

4.1.2 Distribution of Income

The distribution of income in the country is fairly a big macro-economic issue, tax evasion and income in few hands is something the country has been facing since

decades. Nearly 60% of the population lives in villages and are low income earners. Poverty appears to be the greatest threat of all on a country wide scale [45].

4.1.3 Monetary and Fiscal Policy

Most of the capital inflows in Pakistan are aids from International Monetary Fund (IMF) or US aid (US) as a result of which Pakistan does not have the liberty to make its own fiscal or monetary policy. The state revenue collection strategy is failing partly because the country has failed to collect most of its taxes and due to the business groups ruling the country.

Furthermore the taxation policies made by the government is by and large based on indirect taxes rather than direct taxation, even duties on imports and exports are levied in accordance to their businesses to guarantee profits resulting in the expansion of their business empires. Hence the biggest social evil existing in Pakistan is governance in the hands of businessmen ensuring that even state run organizations like Pakistan International Airlines (PIA), Pakistan State Oil (PSO), steel mills, Oil and Gas Development Corporations (OGDC), National Bank of Pakistan (NBP) are first ones to be put into loss by bad governance and mismanagement which are then bought out by the same groups through privatization schemes.

4.1.4 Water and Electricity Crises

What must be understood about Pakistan is that the land is gifted with ample resources, based on which it can generate far better results if the focus is kept on the utilization of these resources by technological means.

The country is blessed with five seasons (an asset for farming and cultivation) [12] and a vast variety of natural resources including 3915 billion cu m of gas (recorded

in 2011) [13], rich forestry, 45 tons of uranium production (recorded in 2013) [14], copper and gold mines in Baluchistan province and seven rivers which (if managed properly) can give abundant supply of water for irrigation and consumption. The Himalayan Mountain range consists of world's third largest glaciers in the north with a length of 2400 km [15].

4.1.5 Balance of Payments deficit

Pakistan's balance of payments has been in deficit since decades. Since the country lacks the ability to convert its natural resources into finished products and hence losing a decent percentage of revenue generation. Also, large outflows in capital account are increasing the national debt, resulting as an increased deficit [46].

4.2 FDI, Unemployment and Poverty: An Overview

4.2.1 FDI and Revenue Generation

FDI in Pakistan shows a mixed trend which is not consistent, however a conclusion based on this cannot be drawn unless an in depth analysis is done.

Punjab is the industrial hub and development sector mainly due to cities like Sialkot, Faisalabad, Lahore and Islamabad that attract a lot of FDI are not performing up to the mark because of external factors like power crises, lack of incentive and terrorism.

Karachi on the other end is the basic attraction of Sindh and contributes a great deal of development but is one of the most dangerous areas in Asia if to say the least because of political instability and terrorism.

The top cities in terms of GDP as recorded in 2010 generation therefore are Lahore and Karachi with \$13.2 and \$32 billion of nominal GDP respectively [16].

As a democratic state Pakistan has a few status quo parties (federal and provincial) that come in power and as a result manipulate a large majority by bringing in investments that have always been beneficial to the parties themselves rather serving the best interests of the country.

The best example is of Pakistan Noon League and Pakistan People's Parties who was in power for more than three times (one political span of 5 years) and yet failed to prove worthy. However due to lack of competition and rigging the parties have ruled for several years leaving the nation in horrific crisis.

The purpose of this thesis therefore will not only drill down the sectors in which these investments were made but also discuss how fatal can a corrupt system be to an economy specially when it comes down to serious economic issues like unemployment and poverty. The shortcomings can further hamper any sort of development for a country which can last for decades leaving generations to suffer its wrath.

4.2.2 Unemployment and Poverty

Pakistan suffers more than 50.3% unemployment in Sindh, 52% in Punjab, 40.6% in KPK and 49.7% in Baluchistan and still consistent (recorded in 2012/13) [17]. Pakistan is a nation that is currently under a huge foreign debt of more than 65 billion dollars. These statistics are also a result of substantial and periodic increases of foreign loans over time, especially in the time of world economic recession [47].

The type of unemployment Pakistan currently has is a combination of cyclical (a case where wage is above normal level which leaves a lesser percentage of the labor force employed) and structural (a case where there is a mismatch between the skills of

labor force and requirements of the job), these are definitely the most dangerous types and relatively difficult to encounter. Also with limited investments and high population, the unemployment trend is continuing to devastate the current condition of the economy.

Poverty, on the other end is another complicated equation since today 60.19% of the total population is below poverty line [18]. The issue therefore is not only in rural areas as it is also creeping at a dangerous rate in urban areas, this is mainly due to weak governance that has failed to establish an effective system of income distribution.

If we drill down further in poverty statistics, Baluchistan (a naturally rich province with 48% of the land of Pakistan) is the foremost victim with 70% households falling below 'severe' poverty line [19]. The government has also failed to accommodate this province in terms of employment; further development in this province is something that never took place and as a result a major percentage of the country's population was exposed to thirst and hunger.

Secondly, KPK (Khyber Pakhtoon Khawa) is stuck by the same virus with a high intensity particularly in some areas with a comparatively lower percentage of poverty than that of Baluchistan. It is obvious that any responsible government would use its tools to guarantee a minimized gap between rich and poor classes with respect to income levels which is clearly something Pakistan has failed to achieve. The turmoil however does not stop there as it gives a snow ball affect crippling a vast majority of stakeholders, leaving the economy weaker and weaker with each passing decade.

Chapter 5

FINDINGS

The findings of the thesis (based on stats in Appendix A) include all variables discussed in the methodology and are concluded as following:

5.1 FDI and Unemployment

Table 1: FDI when unemployment is the dependent variable derived from equation 2.1

	Beta	T-Value	R Square	Significance
FDI (\$US Billion)	0.201	1.127	0.041	0.269

Ironically, as it can be seen with the help values above there is a slight significance between unemployment and FDI since P < 0.05. To Pakistan's misfortune however, the relationship is positive. Hence we have enough evidence to reject H1 because the results show that there is no statistically significant negative relationship between of FDI on unemployment.

This means that with an increase in FDI a slight increase in unemployment is being experienced by the economy. The reason behind however is the privatization of public firms which are bought by foreign investors who then downsize them to fewer employees in order to reduce costs. As for the remaining major investments, these are mostly for the natural resources exploration and land holdings that cannot create a significant change in the current level of unemployment to improve it.

The analysis above is a direct agreement to researches that specifically laid emphasis on the employment in primary sectors in Pakistan and Turkey stating how important it is to get attention in agricultural sectors to curtail unemployment [56][7]. More evidence whereas consists of comprehensive analysis that elaborates the downside of FDI in terms of employment opportunities, which in this research highlights FDIs for business acquisitions and land purchases that will never create significant employment opportunities [41].

On the other end, there is a conflict clear between this research and the one concluded findings from developed economies [55][54], are the economic and political systems of Pakistan compared to that of China, Japan and the European Union, since the researchers did find a negative relationship as derived by the economic theory [1][2][55].

5.2 FDI and Poverty

Table 2: FDI when poverty is the dependent variable derived from equation 2.2

	Beta	T-Value	R Square	Significance
FDI (\$US Billion)	0.159	0.771	0.025	0.448

Based on the values mentioned in the table above it can be concluded that FDI and poverty have no significant relationship since P>0.05. Therefore, we reject H2 because the results show that there is no statistically significant impact of FDI on poverty.

Since it is already known and mentioned in the previous chapters that Pakistan is a country with a highly unequal distribution of income and faces provincial poverty which is now increasing, the government still fails to establish a system that can somehow curtail poverty with the help of FDI.

The research with respect to the poverty of a Pakistan hence draws an agreement with some domestic researches since there was no significant impact of FDI found on poverty due to the political weaknesses that restricts the two variables to bridge [4][3][5][56][29]. Whereas the importance of agriculture for Pakistan is another compliment to this research [57].

On the contrary, strong economies like China, Japan and Europe argue that FDI does impact poverty [1][2][54][55].

5.3 FDI and GDP

Table 3: FDI when GDP is the dependent variable derived from equation 2.3

	Beta	T-Value	R Square	Significance
FDI (\$US Billion)	0.593	4.034	0.352	.000

Based on the level of significance mentioned in Table 3 i.e. P < 0.05 it can be deduced that there is strong significance between both variables and proves that FDI has a positive relationship with economic growth. As a result, we accept H3 because the results show that there is statistically significant impact of FDI on GDP. This supports of the notion of privatizations leading to more efficiency in terms of production and hence better utilization of resources.

Further with technological advancement (mainly in the agriculture sector) in recent years it is not a surprise to see the scale of GDP increasing with FDI since Pakistan mainly relies on the primary sector as mentioned in the previous chapters.

As a comparison to other researches mentioned before, these findings are similar to researches showing that FDI has an important role in the economic growth of Pakistan [54] [5]. On the contrary the research partially disagrees with the findings that found no significant relationship of FDI with economic growth (an increase in GDP) [1]. However, this further provides details related to the factors that cause the economic demise of Pakistan despite a positive relationship between FDI and GDP which may not be the case in other economies.

Chapter 6

CONCLUSION AND RECOMMENDATIONS

The link found between FDI and unemployment is a positive relationship, since the rate of unemployment increases with an increase in FDI, poverty whereas has no significant relationship with FDI since no correlation was found between the two variables.

Interestingly enough, the link between FDI and GDP suggests that economic growth did take place with an increase in FDI suggesting a very strong correlation.

It is therefore obvious that Pakistan lacks the right system to curtail poverty and unemployment and does not promote the right sectors for foreign investment. Although economic growth takes place with an increase in FDI but it is not being used efficiently to address macroeconomic problems like unemployment and poverty.

The sector and country wise major FDI's analysis shows that most of the investments made were not inclined towards production or business formations, hence FDI (throughout the years) remained a very low percentage of economic growth. Moreover, other external factors that include corruption, unequal distribution of income, deficit balance of payments and lack of incentive provide a detailed image of the country's existing situation that directly affects the economy.

Pakistan should therefore primarily improve the system for taxation to generate revenue in order to counter poverty from the state revenue, concentrating aids in areas like Baluchistan. Further, policies should be made to grasp attention from people who intend to open business endeavors rather privatize firms or purchase property. This should then be followed by introducing better incentives in the primary sector, since majority of the population is employed there.

A better accountability and a disciplined chain of command are definitely needed in order to vanish or reduce corruption from the country which is becoming a very dangerous hurdle to its economic stability.

However, the limitation of this research is that there is no primary research which makes it difficult to discuss the current economic scenario with a government official who presumably must be currently very aware of the adverse effects of negative FDIs.

The stakeholders who will be benefited from this research primarily include the Government of Pakistan and foreign and local investors since it proffers a long term analysis and recommendations based on which a further predictions or remedies can be made.

It will also assist other researchers since it includes three variables that were not included in any of the domestic researches before, making it possible to contrast a relationship between variables in a new research by using this research as a reference.

Last but not the least, students from both foreign and domestic universities and students can learn a lot about Pakistan's economy to develop an understanding based on statistical data and analysis.

However, it must be known that the research is not applicable to all economies as it can be clearly seen that some researches mentioned before from developed economies contradict with this research. The findings as a result cannot be generalized.

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APPENDIX

Appendix A: Yearly Statistics for FDI, Unemployment, poverty and GDP.

Year	Foreign Direct Investment (\$ millions)	Unemployment (as a% of total labour force)	Poverty (as a% of the total population	GDP (\$US billions)	
1983	29	3.85		26.7	
1984	56	3.75		31.2	
1985	131	3.65		31.1	
1986	106	3.3		33.4	
1987	129	3.07		36.1	
1988	186	3.14		38.5	
1989	211	3.14		40.2	
1990	245	6.3	20	40	
1991	258	4.69	33.4	45.5	
1992	336	6.06	26.8	48.6	
1993	349	5.28	42	51.5	
1994	421	4.78	34	51.9	
1995	723	5.09	41	60.6	
1996	922	5.36	29.8	63.3	
1997	716	5.75	30.2*	62.4	
1998	506	6.01	30.6	62.2	
1999	532	5.9	37	62.9	
2000	308	6.87	34.5	73.9	
2001	383	7.82	35.9	72.3	
2002	823	8.27	33.9*	72.3	
2003	534	8.27	32	83.2	
2004	1118	7.69	23.9	97.9	
2005	2201	7.69	22.3	109.5	
2006	5590	6.2	37.25	137.3	
2007	5438	5.33	29.9	152.4	
2008	4273	5.2	36.1	170.1	
2009	2788	5.46	55.1	167.9	
2010	2016	5.55	38	177.2	
2011	1327	5.95	43	213.6	
2012	852	7.69	21	224.4	
2013	1566	9.24	33.5	232.3	
2014	1630	10.69	46	246.9	
*: average of next and previous year					

Yearly stats for all variables [28][29][30][31][32][33][34]

Sources: Sarhad Journal, Trading economics, Pakistan Development Review (2005) and Government of Pakistan Review (2015), Trading Economics and World Bank