Globalization Challenges and Opportunities: An Empirical Analysis of Pakistan

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Abstract

The prime goal of this study is to evaluate the association between poverty, economic globalization and income disparity in the context of Pakistan. The pragmatic work is based on the Auto Regressive Distributed Lag (ARDL) for long run relationship and Error Correction Mechanism (ECM) approach for short run relationship testing span from 1973 to 2013. The study shows that there is long-term and short run association between Real GDP and GLOB. This study identifies the globalization's impact over inequalities in income and poverty in the context of Pakistan. The paper provides some useful and doable policy recommendations to reap maximum benefits and make globalization successful, acceptable and fruitful for Pakistan.

Keywords: globalization, growth, income inequality and poverty.

1. Introduction

Globalization has diversified impact in the developing as well as in the developed countries. The developed countries enjoy greater gains and benefits as compared to the developing countries. The drivers of globalization postulate the potential gains and the real cost borne by the developing countries. All over the world, there have been wide ranging debate and discussions relating to the pros and cons of globalization. To address a few of the issues and challenges related to it, the paper attempts encompass some of them which are essential for the growth of the developing countries.

What does globalization mean? Does this mean that all countries have equal opportunities? Does it mean the integration of economic, political, and cultural systems in the global village? Whether it will reduce the empowerment of individual countries to take decisions on their behalf? All these multidimensional and multifaceted phenomena have both positive and negative implications on the economy. If these are the realities of globalization, what kinds of impacts will it have on the way we live?

Globalization broadly refers to the expansion of global linkages, coordination between economic and cultural subsystems among countries, hence to the consolidation of world society. It is beneficial and favorable for the growth and progress of the economy.

Globalization is conflicting because of the economic and social benefits and costs associated with it. There are different outcomes related to globalization in various countries in term of growth, poverty and income inequalities. The benefits of globalization are more visible where the government policies, growth in population, institutional framework proved to be a powerful force as compared to the countries where all these are absent.

Measuring globalization is a complicated process due to its multidimensional nature. Oftena composite indicator is used to explain these phenomena. The purpose of this paper is to focus the relationship of economic and socioeconomic variables with globalization.

The objective of this study is to examine the relationship among globalization, poverty, inequality and economic growth by using ARDL and ECM model span from 1973 to 2013 in the context of Pakistan.

The paper comprises of 4 sections. Section A explains introduction, Section 2 dilated upon review of the literature, Section 3 is methodology and examines the association between poverty, inequality and globalization. Section 4 is conclusion and policy recommendations.

2. Review of Literature

Advocates of globalization propose that it encounters the needs of the developing countries and bring a paradigm shift from internally oriented to externally orient growth strategies. However, Zedillo (2007) emphasizes that the gains are associated only with the rich and developed countries like USA, Canada, Australia and Europe among others, etc. In (2004) Whiteford and Clair explain that organizations ought to rationalize production to become effective and efficient to compete with the outside world. Whiteford and Clair (2004) Conservatives are of the opinion that, globalization leads to the cultural pollution. Joseph (2003) exhibits that social and political manipulations are on the rise to control the poor and developing countries which are unethical and manipulative. Robert and Lajtha (2002) explore that the multinational companies hire cheap labor from the developing countries and provide poor working conditions, lower labor standards along with negligible up gradation of knowledge. Richardson (2002) explores that the rich and developed countries controls not only the political leaders, but also the social and economic strategies in the developing economies. It is noteworthy to mention that the developing countries are exploited by the rich and powerful countries to the extent that they are not supposed to spend the aid on their desired projects. IMF Report (2000) on globalization elucidates that globalization intensify the different dimensions of inequalities. The dominant position is enjoyed by the rich and powerful countries by exploiting and influencing the government policies of the developing countries.

The pessimists believe that it badly hit the vulnerable segments of the population in the poorestcountries, while the optimists argue that it is one of the vital key in poverty reduction strategies. The gains of globalization are very prominent in the caseof East Asian countries, where income per person accelerated by eight times by bringing the millions of people out of poverty.

In the case of China, the gains from foreign direct investment (FDI), has been enormous. While in other countries like Korea, little improvement is seen. However, some areas of Latin American economies show that the SAPs have discouraging economic outlooks.

Empirically, a plethora of studies indicates that economic globalization encourages economic growth; lessen the burden of poverty by providing employment chances (Cuadros et al. 2004). In the nutshell, the implications of globalization differ among the countries due to economic, social and labor policies.
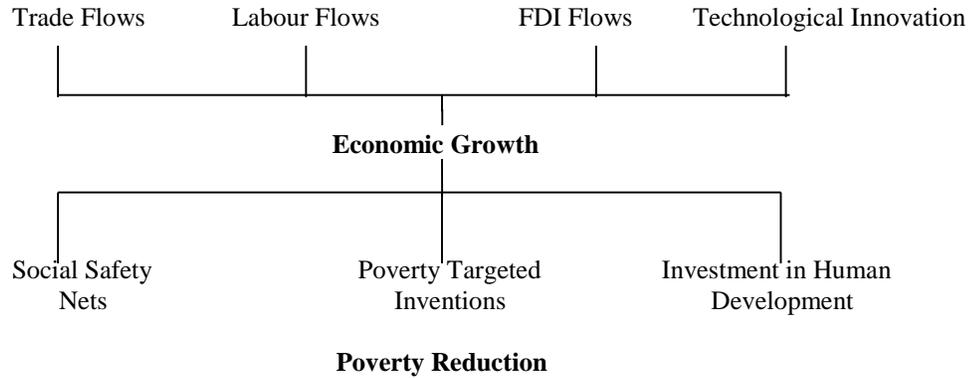
2.1 Globalization Poverty and Inequality

As the multidimensional nature of globalization, the studyinvestigates that how a reduction inpoverty and inequalities are linked with globalization in case of Pakistan. Conclusion of empirical work will help to understand this association.

Chaudhry and Anwar (2001) investigate that despite continuous attempts to attract foreign investors by providing numerous incentives in the form of tax holidays etc. FDI has remained low in Pakistan. In 1990's, empirical work showed that globalization had no significant effect and trade performance had depressed in spite of trade liberalization. The study also finds that permanence in policies stays for a short period due to instability in institutions along with frequent adjustments and transformations in policies that disturbs the stability and its drive. By constantly attempting to stabilize the economy along with trade liberalization move the economy to a vicious circle. Lower tariff rates create the situation of stagnant GDP ratio, which increases loss in government revenues leads to cut the development expenditures to reduce the budget deficit. All this results in lowering GDP growth, increase in indebtedness, higher unemployment and thus increase poverty and inequalities.

Some empirical work on foreign remittances and trade liberalization shows that lowering the tariff rates without reducing foreign remittances contracts urban and rural poverty.The gains in this context in urban areas are larger than rural areas. Further, the reduction in tariff rates along with decrease in foreign remittances decreases rural poverty larger than urban poverty. In short gain by urban households is larger when trade liberalization occurs without a decline in foreign remittances. And gain by rural households is larger in the presence of trade liberalization with the decrease in foreign remittances.

Orden (2006) exhibits the impact of global cotton prices in Pakistan. The study identifies that household who earned income by producing cotton will be benefited when the global price of cotton increases. The study estimated that 20% increase in prices would reduce all cotton producing households' poverty from 40% to 28%.

The mechanism of how globalization affects poverty reduction give rise to the answer of our research hypothesis that does globalization reduce poverty in Pakistan? Mechanism works through two channels. Firstly globalization pushes economic growth. Secondly sustained economic growth helps in minimizing the poverty as shown in figure 1 below.

Trade Flows   Labour Flows   FDI Flows   Technological Innovation

Economic Growth

Social Safety   Poverty Targeted   Investment in Human
Nets   Inventions   Development

Poverty Reduction

Figure 1: Globalization and Poverty Reduction

3. Methodology

In this section methodology and empirical will be discussed.

3.1 Unit Root Test

The essential state for the cointegration among these variables is their stationary levels in the ARDL Bound Testing for Cointegration. Variables are tested for stationary employing the Augmented Dickey-Fuller (ADF) (Dickey and Fuller, 1984).

3.2 ARDL Bound Testing For Cointegration

Pesaran and Shin (1998) develop the ARDL approach to Cointegration to test the long run association.Different from other cointegration methods; the ARDL approach does not oblige a restraining assumption that the entire variables under study should be stationary at the same order. ARDL approach may be used irrespective of whether all variables are integrated at I(0) or I(1) or jointly stationary Pesaran et al. (1999). The ARDL approach is appropriate still if the sample size of data is small; in difference to other cointegration methods that are sensitive to the sample size of data. Moreover, it takes enough quantity of lags to confine the data generating process in a general to specific modeling structure. Fourthly, it eliminates problems associated with absent variables and autocorrelations; gives balanced and competent estimates Narayan (2004). Procedurally, ARDL approach involves two distinguishing steps. The primary step entails the establishment of long run association through the ARDL model.

The variables of the study have been described earlier. To create a long run association, joint significance test of Co-integration shows that all long run coefficients are equal to zero. The F-statistic, which has an irregular distribution, is considered on the numbers lags of variables in determining whether co-integration among the variables exists or not. In this regards, two bounds which are LCB (lower critical bound) and UCB (upper critical bound) of critical values are generated. The LCB defined as I(0) variables, though the UCB defined as I(1) variables. In relation to the bound test, long run association exists if the calculated F value greater than the UCB. If computed F value is in between the UCB and LCB, no decision about long run association, however other method of cointegration can be applied. Finally, if the F value is lower than the LCB, it entails no cointegration.

3.3 Error Correction Model

The error correction mechanism (ECM) was used by Sargan and later adopted by Engle and Granger (1969) corrects for disequilibrium. An important theorem, known as the Granger representation theorem, describes that if variables are co-integrated, then the relationship between them can be expressed as ECM.

3.4 Globalization and Growth

In this section of the paper, we construct the relationship between globalization and growth. We use ARDL and ECM approach for finding the research hypothesis that are there existinglong run and short run association between said variables. We used RGDP and GLOB index for analysis.

Table 1: Autoregressive Distributed Lag Estimates ARDL

Regressor		Coefficient		Standard Error		T-Ratio		Prob
RGDP(-1)		0.76104		0.11275		6.7498		[0.000]
GLOB		-38178.9		30090.8		-1.2688		[0.219]
GLOB(-1)		-16779.9		33775.7		-0.4968		[0.625]
GLOB(-2)		75538.2		27960.6		2.7016		[0.014]
Constant		-147452.2		582465.9		-0.25315		[0.803]
Trend		23832.6		51359.3		0.46404		[0.648]
R^2	0.99095	Adj R^2	0.98868	DW	2.0152	F-stat	437.782	[0.000]
Serial Correlation		0.00356	[0.953]	Functional Form		1.9527		[0.178]
Normality (χ^2)		17.8251	[0.000]	Heteroscedasticity		1.68E-05		[0.997]

Source: Author's Estimation

According to ARDL method there is long run cointegration exist between RGDP and Glob. There is a problem like serial correlation, normality, functional form and heteroscedasticity on the basis of another F-value, Chi-square and probability.

Table 2: Error Correction Model ARDL

Regressor		Coefficient		Standard Error		T-Ratio		Prob
DGLOB		-38178.9		30090.8		-1.2688		[0.219]
DGLOB(-1)		-75538.2		27960.6		-2.7016		[0.013]
DConstant		-147452.2		582465.9		-0.25315		[0.803]
Dtrend		23832.6		51359.3		0.46404		[0.648]
ECM(-1)		-0.23896		0.11275		-2.1194		[0.046]
R^2	0.41816	Adj R^2	0.2727	DW	2.0152	F-stat	3.5935	[0.022]

Source: Author's Estimation

According to Error Correction Model (ECM) ARDL approach, there is short run cointegration exist between RGDP and Glob. Lag of Error correction term has negative sign which shows the convergence from short run equilibrium path to long run equilibrium path. ECT is also statistically significant at the 5%.

4. Conclusion and Policy Recommendations

Trade and openness have been considered an important engine of growth and development of the developing countries. United Nation Report (2004), reports that the most LDCs took initiative steps to globalize their economies in the 1990s. Liberalization along with enhanced market access is essential, however not a statistically satisfactory condition for minimizing poverty and inequality. In order to counter the negative influence of globalization the developing countries should unite and adopt sound economic and labor policies that serve the genuine cause of reducing poverty and income inequalities.

The prime goal of this study is to evaluate the association between poverty, economic globalization and income disparity in the context of Pakistan. The pragmatic work is based on the ARDL for long run relationship and ECM approach for short run relationship testing. The study shows that there is long-term and short run association between RGDP and GLOB. The study concludes that globalization minimizes poverty in the long-term, provides job opportunities but increase inequalities. It is stated that trade liberalization is an essential but not the prime requirement for improving social and economic indicators. There is a dire need of integration between economic and cultural subsystems as globalization demands more interaction and integration in terms of production, exports, imports, investment in human development indicators along with appropriate social safety inventions.

The gist of the study is that the true gains and potential benefits of globalization are not enjoyed in the case of Pakistan. In order, to translate the real benefits and reduce poverty, the government has to take certain harsh and hard measures. The following are the policy recommendations to upgrade and uplift the economy.

- ➢ The government must develop a carefully planned the framework with constant resource endowments to reap the maximum gains from globalization.
- ➢ The government must invest in quality control and working conditions of labors.
- ➢ The government must formulate Social Safety Net policies which are pro poor in nature and the existing funds for social security to be disbursed to the desirable segment of the population.
- ➢ The government needs to promote export culture by involving the Export Processing Zones.

It is, therefore, concluded that the benefits gather from economic globalization depends upon economic, labor and social policies, market composition, quality of institutions and last but notless politicalwill to bring the contributory environment.

The limitation of the study is that the scope of the study is narrow and it can be broad by including more variable(s) like for example foreign direct investment, trade openness etc. It can be further broader if we add more South Asian countries and covert the time series data into panel data.

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