DOES FOREIGN INFLOWS CONTRIBUTE TO ECONOMIC GROWTH IN BANGLADESH: AN ARDL BOUND TESTING

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ABSTRACT

This article features an examination of the relationship between foreign inflows (FDI, External Debt, Remittances and Foreign Aid) and the Economic Growth of Bangladesh for the period 1991-2019. The data used for the study has been taken from World Development Indicators. The data has been analysed by employing the ADF test, PP test and ARDL model. The results reveal that a long-run relationship exists between foreign inflows and economic growth in Bangladesh. The coefficients of short-run & long-run results suggest that in the long run remittances, foreign aid and FDI have a positive impact on economic growth. In the long-run and short-run, external debt harms economic growth. The policies suggest that Bangladesh should focus on FDI, foreign aid and remittances for the development of the economy. External Debt is a burden for the economy as it has a negative impact in the long run.

Keywords: *Foreign Inflows, Foreignaid, Remittances, External debt, ARDL, Economic Growth, FDI.*

Introduction

Foreign inflows help the host counties to fill the saving-investment gap, technology transfer, knowledge spillovers, efficiency in production and transfer of managerial, human and technical skills, etc (Ehigiamusoe & Lean, 2019).As the domestic capital alone cannot accelerate investment, foreign inflows are needed. It helps the developing countries to achieve their targeted growth rate. Foreign inflows are an important source of foreign reserves as they help to enable technology transfer & progress foreign exchange reserve of a country (Mowlai, 2018).Foreign inflows play a drastic role in strengthening the economic growth of developing countries. The reason behind the need for foreign inflows is the lack of adequate domestic capital in developing countries. That's why they need foreign capital to fulfil their development needs. The developing countries can also grow their economies, reduce poverty by attracting foreign capital inflows from developed countries (Tahir et.al. 2020). Foreign inflows help to fill the resources gap between a desired or targeted investment and locally mobilized savings. It also aids in meeting the specified foreign exchange requirements as well as those resulting from net export earnings. It also helps to fill the gap between targeted tax revenue and collect tax revenues. Foreign inflows significantly affect economic growth because it helps to raise the fund of the government and to invest it in infrastructure and income-generating project (Jena & Sethi, 2021).

Foreign capital inflows can be in different ways such as FDI, FPI, foreign aid, external debt and worker's remittances, etc. Each type of foreign inflow has a different influence on the economic growth of the hot countries due to different nature, political environment, etc.

When migrants send a percentage of their earnings home in the form of cash or goods to support their families, this is known as remittances (IMF, 2020). Remittances increase the foreign currency reserves in the home country and make the funds available to make payments of exports and other expenses. Remittances are the main source of foreign funds for developing countries (Khan et.al., 2019). For the economic development of developing countries, worker's remittances have been considered as a major source of foreign inflows. It impacts the overall economic growth of the recipient countries.

Foreign aid is aimed to support the financial prosperity and well-being of developing nations and can be supplied bilaterally is referred to as bilateral aid (OECD report, 2020). Foreign aid plays a vital role in helping recipient countries prosper economically. Foreign aid helps to boost financial expansion in major developing countries. In the countries having less domestic capital, foreign aid contributes to promoting human capital, adopting new technologies,etc. (Balde, 2011).

For many developing countries, foreign aid has been a significant source of income.

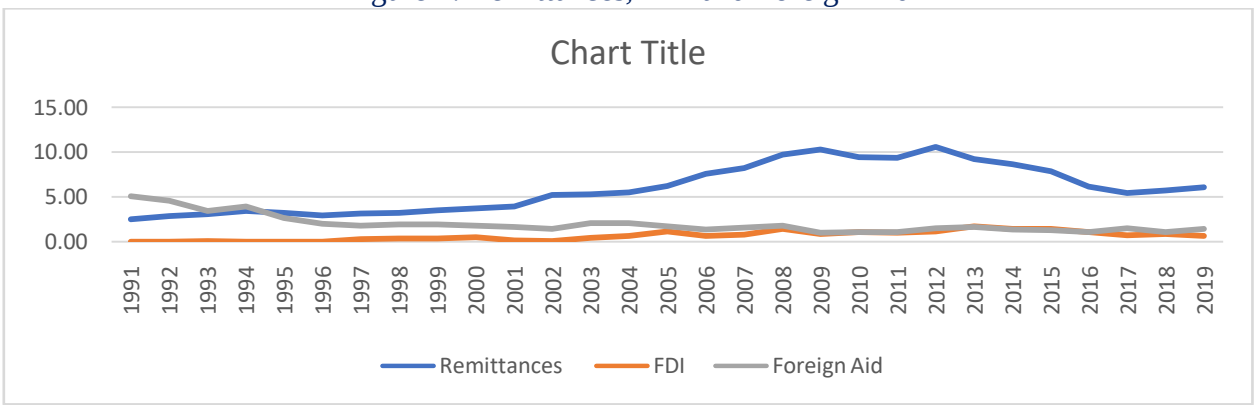
External debt is a composition of long-term debt, short-term debt owed by the country and loans taken by the country from IMF. External debt is an important part of the debt structure in developing countries (Atique & Malik, 2012). As it helps the developing countries to finance capital formation, increase investment and reduce poverty (Ijirshar & Godoo, 2016).

FDI is described as an investment that entails a long-term relationship and implies a resident of one economy's long-term interest and ownership in a company based in a different economy (UNCTAD report, 2020). FDI helps to generate more employment opportunities in host countries. FDI affects sectoral growth, promoting development, promote industrial growth, capital accumulation.

The neoclassical theories and endogenous growth theories stressed two important factors for economic growth which are: capital accumulation and technological progress. These theories also suggested that foreign capital inflows help to provide funds for the economic growth in capital deficient countries (Solow, 1956).

The remainder of the paper is laid out as follows. A review of the literature is discussed in section 2. Then, the data & methodology are dealt with in section 3. Empirical results are discussed in section 4. Conclusion, summary and policy suggestions are discussed in the last section.

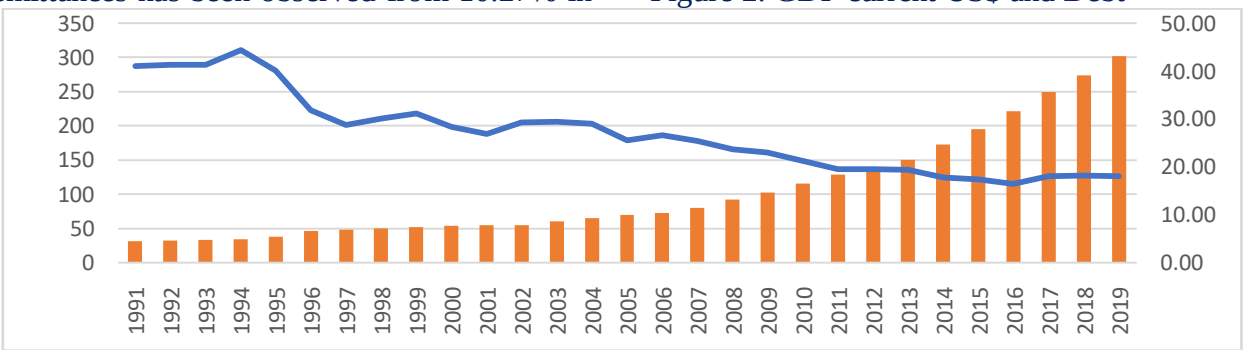
Figure 1. Remittances, FDI and Foreign Aid



Source: World Bank

Figure 1 shows the trend of remittances, FDI and foreign Aid in India for the period 1991-2019. An increasing trend can be observed in remittances until 2009. It is due to increasing migration from developing countries to developed countries, transfer of technology and ease in transferring money from one country to another country.In 2009, a sudden decrease in remittances has been observed from 10.27% in 2009 to 9.41 % in 2010. This decrease might be attributed to the financial crisis in 2008 in the US, which adversely affected remittances in Bangladesh. Further, the inflows of external funds and foreign aidalso decreased during the financial crisis of 2008. The inflows of foreign aid decreased to 141.85 % of GNI in 2010 from 149.44 % of GNI in 2009.

Figure 2. GDP current US$ and Debt

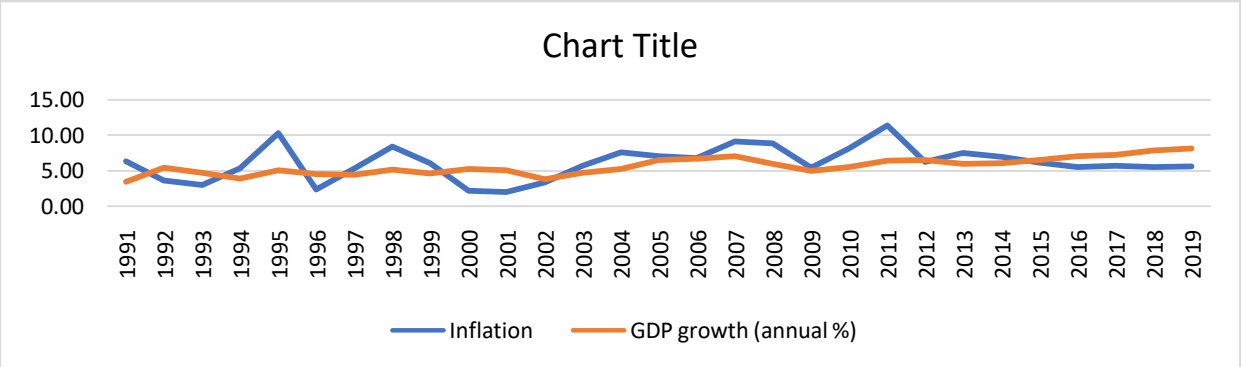


Source: World Bank

GDP (Current US$) is continuously increasing at a high rate. External debt is continuously decreasing. Some slight increases can be seen in foreign debt inflows in Bangladesh. A trend

can be observed in GDP. The two main reasons for the increasing GDP of Bangladesh are as follows: first, is the increasing exports of readymade garments which constitute more than 80% part of its overall exports. The second is increasing investments and worker's remittances inflows in Bangladesh (figure 2).

Figure 3: Inflation and GDP growth



Source: World Bank

Many fluctuations can be observed in the case of inflation in Bangladesh. Due to the global financial crisis of the year 2008, a significant decrease at can be observed in inflation and GDP growth rate. Large variations can be observed in inflation. GDP growth is increasing continuously.The reason behind the increasing GDP growth is the growth of the garments industry, service sector and more remunerative agriculture, etc. After the independence of Bangladesh in 1971, it focused on policymaking and implications related to trade, investment, increase production, etc. for promoting economic growth. After the year 1991, the economy of Bangladesh accelerated sharply due to openness of trade and the renovation of democracy (Islam, 2001). In the last three decades, the economy of Bangladesh was characterized by the fruitfulgrowth of the export-oriented readymade garment industry and green revolution implementation which resulted in a substantial increase in agriculture yield, the introduction of various high yield grains and the use of various pesticides to boost the production of rice (Manni & Afzal, 2012).

Literature Review

External Debt and Economic Growth

Some light on the association of external debt and economic growth in Nigeria during the period of 1981-2014 by applying various econometric tests has been shed. The study concluded that the economic growth of Nigeria has been positively affected by external debt (Ijirshar & Godoo 2016). A negative association between foreign debt& economic growth in Vietnam for the period 1987-2016 has been reported (Nguyen, 2018). Also, the negative effect of external debt on Pakistan's economic growth for the period 1970-2010 has been revealed by (Ali & Mustafa, 2012). A negative influence of foreign debt on economic growth in emergentnations for the period 1990-2016has been testified (Atique & Malik, 2012). Whereasno influence of foreign debt on pecuniary growth in Mauritania during the period 1975-2005has been concluded (Mahmoud, 2015).

Table 1.Relationship Between External Debt & Economic Growth

Author	Data Period	Economies Included	Empirical Findings
Ijirshar & Godoo (2016)	1981-2014	Nigeria	Positive
Nguyen (2018)	1987-2016	Vietnam	Negative
Ali & Mustafa (2012)	1970-2010	Pakistan	Negative
Atique & Malik (2012)	1980-2010	Pakistan	Negative
Mahmoud (2015)	1975-2005	Mauritania	No effect

Source: Author's compilation

Remittances and Economic Growth

Some light on the association of remittances, aid & savings in SSA during the period of 1980-2004 by applying two econometric models has been shed. The study concluded that a significant positive influence of

remittances, aid has been found on savings in SSA (Balde, 2011).A positive association among remittances & economic growth in 4 ASEAN countries for the period 1976-2012 has been found (Azam 2014).A positive association between remittances & economic growth has been revealed (Mowlaei, 2018; Das & Sethi, 2019). While a negative affiliation amid remittances & economic growth in Pakistan for the period 1975-2009 has been considered (Jawaid & Raza 2016).Whereasno relationship between remittances and economic growth has been reported in Nigeria for the time frame 1981-2017 (Anetor 2019).

Table 2.Relationship Between Remittances & Economic Growth

Author	Data Period	Economies Included	Empirical Findings
Azam (2014)	1976-2012	Bangladesh, India, Pakistan & Sri Lanka	Positive
Balde (2011)	1980-2004	Sub-Saharan Africa	Positive
Mowlaei (2018)	1992-2016	African countries	Positive
Das & Sethi (2019)	1980-2016	India & Sri Lanka	Positive
Jawaid & Raza (2016)	1975-2009	Pakistan, India, Bangladesh & Sri Lanka	Negative
Anetor (2019)	1981-2017	Nigeria	No significant impact

Source: Author's compilation

Foreign Aid and Economic Growth

By applying the unit root test and ARDL model for the period 1960-2018, a positive association has been found between foreign aid and economic growth in Sri Lanka (Aslam & Samsudeen, 2021).A positive association between foreign aid and economic growth in South Asian countries for the period 1985-2015 has been determined (Ehigiamusoe & Lean (2019). The positive influence of foreign aid has been foundon South Asian countries' economic growth for the time frame 1996-2017 (Jena & Sethi, 2020).A positive relationship between aid & economic growth in Cambodia, Lao PDR, Myanmar & Vietnam has been revealed during the period 1997-2014 (Moolio & Kong, 2016).

Table 3.Relationship Between Foreign Aid & Economic Growth

Author	Data Period	Economies Included	Empirical Findings
Aslan &Samsudeen (2021)	1960-2018	Sri Lanka	Positive
Ehigiamusoe & Lean (2019)	1985-2015	Nigeria	Positive
Jena & Sethi (2020)	1996-2017	8 South Asian countries	Positive
Moolio & Kong (2016)	1997-2014	Cambodia, Lao PDR, Myanmar & Vietnam	Positive

Source: Author's compilation

FDI and Economic Growth

A positive relationship between FDI and economic growth in developing countries has been reported during the period 1970-2009 by applying the GMM model (Nwaogu & Ryan 2015). An inverse association between FDI & economic growth has been found in lower-middle-income countries (Alvarado et.al., 2017). Whereas no direct influence of FDI on Nigeria's economic growthhas been found for the period 1989-2013 (Olagbaju & Akinlo, 2018).

Table 4.Relationship Between FDI& Economic Growth

Author	Data Period	Economies Included	Empirical Findings
Nwaogu & Ryan (2015)	1970-2009	Africa, Latin America & the Caribbean	Positive
Alvarado et.al. (2017)	1980-2014	Latin America	Negative
Olagbaju & Akinlo (2018)	1989-2013	Sub-Saharan Africa	No impact

Source: Author's compilation

However, no consensus has been found among the researchers on the relationship between economic growth and foreign inflows. The experimental findings are not homogeneous. Some studies reported a positive association between external debt and economic growth(Ali & Mustafa, 2012) while some revealed a negative association amid external

debt & economic growth (Atique & Malik, 2012). A positive connotation amid foreign aid & economic growth has been found (Aslam & Samsudeen, 2021) while Appiah Konadu et.al. (2016) revealed a negative impact of aid on the economic growth of Ghana. Moreover, Sethi et.al.(2019) found no significant impact of foreign aid on economic growth. Das & Sethi (2019) reported a affirmative connotation amid FDI &growth of the economy. Jawaid & Saleem (2017) revealed the negative association amid FDI and economic development. Datta & Sarkar (2014), Husain & Anjum (2014) revealed an optimistic on notation amid remittances & growth of the economy whereas Bird& Choi (2019) reported a negative impact of remittances on economic growth.

That's why the study is an attempt to test the association between foreign inflows and Bangladesh's growth. The majority of earlier research related to this area absorbed specific aspects offoreign inflows into poor countries. However, this study differs from prior studies in that it examines the influence of 4 types of foreign capital inflows on Bangladesh's economic growth: FDI,aid, debt and worker's remittances. The study has been useddata from 1991-2019 to test the impact of foreign inflows on economic growth. This time frame is chosen as Bangladesh liberalized its economy in the 1990s. Another reason for choosing Bangladesh is that no previous study on Bangladesh has been found examining all the components of foreign inflows and economic growth together.

The study found conflicting results for the relationship of economic growth and foreign inflows. The usage of various econometric models, proxies for evaluating theforeign inflows, period and data set used by the studycontributed to the inconsistent conclusions obtained in prior results. Furthermore, the effect of foreign inflows on growth of the economy is dependent on the characteristics of the given country such as technological advancements, macroeconomic stability, development of financial system and development of human capital. This study is unique for the academic purpose because best of author acquaintance, no study is available on Bangladesh except (Tahir et.al., 2018) which have conducted the study for a very short period 2008-2015.This study is an attempt to test the association between foreign inflows & growth of Bangladesh for the time set from 1991 to 2019. This data also includes the period when Bangladesh liberalized its economy and opened its door for foreign investment.

Based on past studies, it can be concluded that very few studies have been found which are related to the contributory relationship between inflows of foreign capital& economic growth. Many studies employed cointegration approaches such as Engle and Granger's (1987) cointegration test or Johansen and Johansen and Juselius' maximum probability test (1990). If the sample size is small, these cointegration techniques are not appropriate. The current study tests the causal relationship between foreign inflows and the economic growth of Bangladesh by implementing the newly developed ARDL bound testing approach.

Data and Methodology

Foreign inflows play an important part in promoting the economic growth of a country. As a result, the emphasis on the importance of foreign inflows (foreign aid, external debt, FDI& worker's remittances) in Bangladesh's economic growth has been shed. The research relies on secondary data. The study used many variables to understand the possible impact of foreign inflows on economic growth. Two additional variables inflation and employment have been used as control variables. Testing the stationarity of a time series is an important task. If the series are non-stationary, results will be unreliable. That's why ADF and PP test has been employed to check the stationarity property of theseries at the level and first difference. The study tests the cointegration association between foreign inflows& economic growth in Bangladesh using the Autoregressive Distributed Lagged (ARDL) model. This method is chosen because it can handle the variables in the model when the variables are unified in a different order. Even the sample size is small, this model gives more robust and reliable results. The data set used in the study covers the period 1991-2019 sourced from the World Bank.

Table5.Explanation of Variables

Variables	Measurement	Source
Economic Growth	GDP Annual Growth (%)	World Development Indicators
Personal Remittances Inflows	% Of GDP	World Development Indicators
Foreign Aid(ODA)	% Of GNI	World Development Indicators
Foreign Direct Investment inflows	% Of GDP	World Development Indicators
Employment (control variable)	No. of People Employed (millions)	PWT
External Debt	External Debt Stocks (% of GNI)	World Development Indicators
Inflation (control variable)	Consumer Price Index	World Development Indicators

Source: Author's compilation

Table 6.Preliminary Analysis

	GDP	FDI	EMP	DEBT	AID	INF	REM
Mean	5.67649	0.6617	47.81986	27.0019	1.94898	6.126375	5.925843
Median	5.44269	0.63566	46.27964	26.5717	1.651	6.106696	5.504373
Maximum	8.15269	1.73542	65.53407	44.4818	5.09897	11.39517	10.58794
Minimum	3.48523	0.00449	32.12558	16.4302	0.97896	2.007174	2.485233
Std. Dev.	1.20048	0.51987	10.32522	8.30556	1.0472	2.317632	2.629764
Skewness	0.2013	0.30854	0.160953	0.64036	1.79913	0.121873	0.341446
Kurtosis	2.31249	2.00769	1.748934	2.40756	5.38129	2.795361	1.723056
Jarque-Bera	0.76701	1.64994	2.016453	2.40608	22.4967	0.122391	2.533787
Probability	0.68147	0.43825	0.364865	0.30028	1.3E-05	0.94064	0.281705
Sum	164.618	19.1893	1386.776	783.054	56.5205	177.6649	171.8494
Sum Sq. Dev.	40.3525	7.56744	2985.085	1931.5	30.7058	150.3997	193.6384

Source: The author's calculations

The summary of preliminary statistics for data has been shown in terms of mean, median, standard deviation, kurtosis and Jarque-Berastatistics. The skewness value for each series is small but positive for all variables, indicating that the distribution's upper tail is thicker.The results of Jarque-Bera indicate that data is normally distributed because the p-value of Jarque-Bera statistics is more than the significance level. The value of kurtosis is less than 3 in all the series except aid which indicates that the distribution is platykurtic. The distribution of series aid is leptokurtic as its kurtosis value is more than 3.

Results and Discussions

Table7.Results of Unit Root Test

ADF Test Results					
	Level		**Difference**		**Decision**
Variables	Constant	Constant & Trend	Constant	Constant & Trend	I(1)
GDP	-1.693	-3.4829	-6.41	-7.1053	I(1)
Inf	-3.8181	-4.0149	-7.1053	-7.07	I(0)
FDI	-1.8394	-2.1962	-6.2892	-6.3357	I(1)
Aid	-0.4262	-2.1873	-5.2211	-5.0216	I(1)
Rem	-1.41	-0.07	-3.4313	-3.5234	I(1)
Emp	-1.4107	-1.9368	-4.416	-4.4481	I(1)
Debt	3.3909	2.018	-1.8449	-3.9081	I(1)
PPTest Results					
	Level		**Difference**		**Decision**
Variables	Constant	Constant & Trend	Constant	Constant & Trend	

GDP	-1.693	-3.4829	-6.7393	-7.6885	I(1)
Inf	-4.1218	-4.1573	-9.3073	-10.0327	I(0)
FDI	-1.7233	-2.1969	-6.4366	-6.9552	I(1)
aid	-1.7782	-2.6067	-5.7859	-5.7022	I(1)
rem	-1.4432	-0.8515	-3.4258	-3.4793	I(1)
emp	1.1788	-2.0202	-4.4181	-4.4519	I(1)
debt	6.4797	10.7307	-1.7469	-2.4475	I(1)

Source: The author's calculations

If a series is found non-stationary, it can create spurious regression which can lead to unreliable results. To escape from these types of problems, it becomes essential to examination of the stationarity property of the time series. To examine the stationarity property of the time series, a unit root test has been used. This study has been applied ADF and PP test at the level and 1st difference to determine whether the time series data set is stationary or not. The results of the ADF and PP test indicate that all the variables are integrated at first difference except inflation. Inflation is integrated at the level. This mixed order of variables allows us to apply the Autoregressive Distributed Lag cointegration approach (Table 7).

Table8. Results of Bound Test

Response variable	**F-Value**	**Remarks**
F (GDP/Rem, Debt, FDI, Aid, Emp, Inf)	4.587222	Co-integrated
Critical Values	**Lower Bound**	**Upper Bound**
1 percent	2.88	3.99
5 percent	2.27	3.28
10 percent	1.99	2.94

Source: The author's calculations

The ARDL is a model that can manage variables that are not integrated into the same sequence. If certain variables are integrated at the level and others at the first difference, the ARDL model can be used to examine the long-term relationship between the variables. The presence of a long-run connection between the variables is assessed in the ARDL framework by comparing the estimated F-test result to the crucial values. We accept the long-run link among the variables if the anticipated F-test value is greater than the upper bound value.The results are inconclusive if the F-value lies between the lower and upper bound. If the estimated F-test value is smaller than the lower bound value, we rejectthe presence of a long-run connection between the variables.

Table 9.Results of Long-Run and Short-Run

Long Run Results			
Variables	Coefficient	Std. Error	t-Statistic
FDI	0.59805*	0.830937	-2.64242
EMPLOYMENT	0.050452	0.060528	0.833542
DEBT	-0.29948*	0.162468	-2.84329
AID	1.657923*	0.79059	2.09707
INFLATION	-0.28893*	0.137229	2.105423
REMITTANCES	0.265429*	0.153052	-2.73424
C	8.380984	5.6418	1.485516
Short Run Results			
ECT	-0.64576*	0.090452	-7.13927
GDP_GROWTH__ANNUAL___ (-1) *	0.645764*	0.187664	-3.44106
FDI**	0.386199*	0.572094	-2.67506
EMPLOYMENT**	0.03258	0.044134	0.738213
DEBT**	-0.19339*	0.079049	-2.44648
AID (-1)	0.070627*	0.368616	2.904454
INFLATION**	-0.18658*	0.059478	3.136916

REMITTANCES (-1)	0.171404	0.09325	-1.83813
D(AID)	0.560304	0.378963	1.478518
D(REMITTANCES)	0.124685	0.168021	0.742084

Notes: * Indicates the Significance Level,Source: The author's calculations

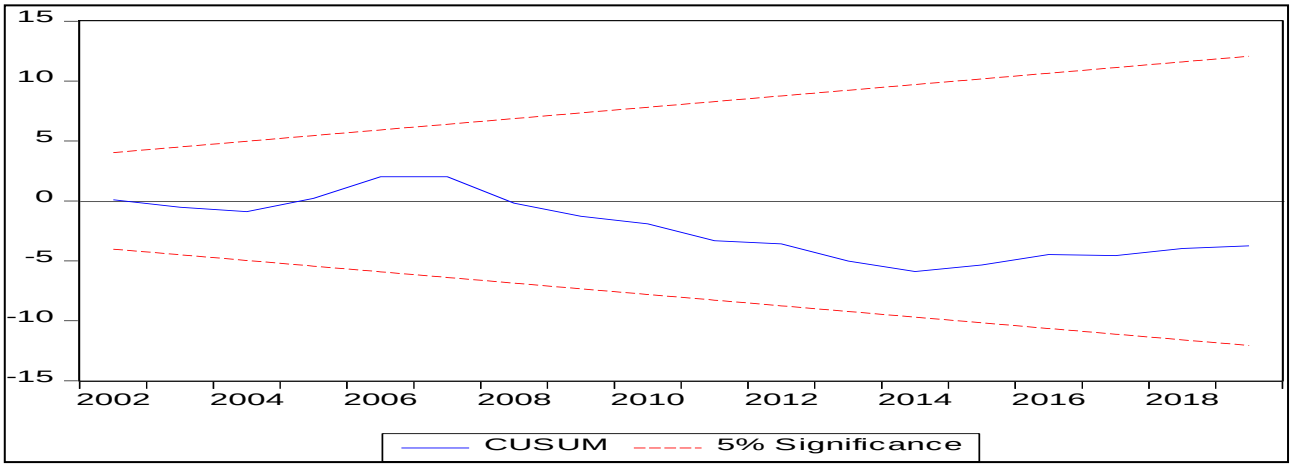
After determining that the variables are cointegrated, we must determine the long-run and short-run coefficients of the independent variables. The error correction term (ECT) is a measurement of how quickly a series adjusts from a short-run to long-run equilibrium. The table also includes the ECT term. Long-term results are displayed in the table's upper section.In the long run, the results reveal that foreign inflows i.e., remittances, aid, FDI have a positive and significant impact on the economic growth of Bangladesh in the long run. The country's external debt inflows have a major negative influence on economic growth similar to (Ijirshar & Godoo (2016), Nguyen (2018), Ali & Mustafa (2012), Atique & Malik (2012) and Mahmoud (2015).On the other hand, in the short run, FDI and foreign aid have a positive impact on economic growth in Bangladesh. Debt and inflation harm economic growth in Bangladesh inthe short run.

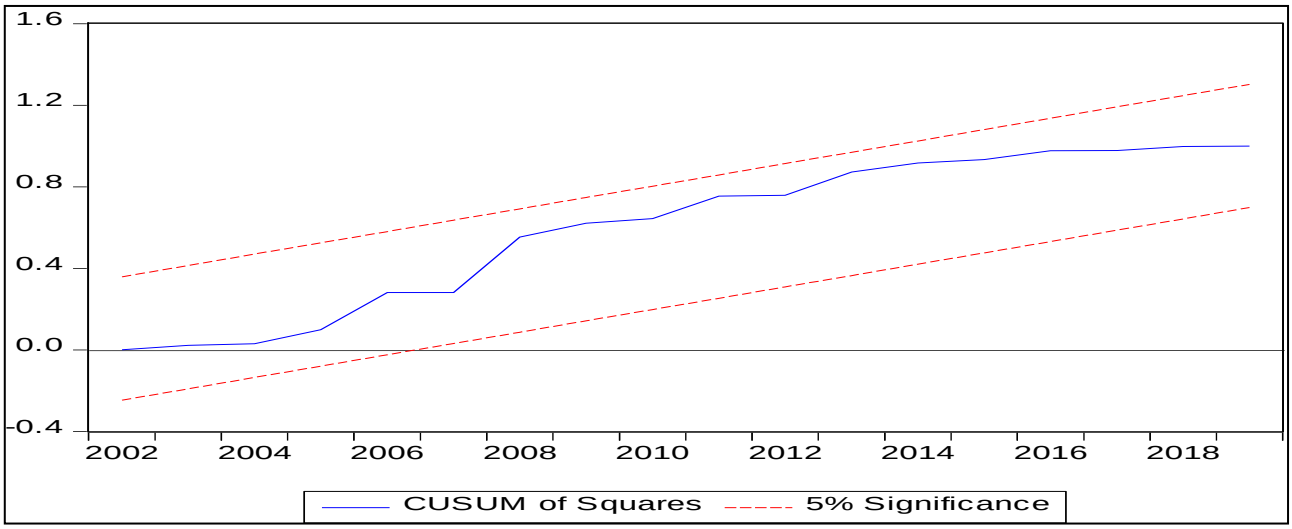
Table10. Diagnostic Testing

Diagnostic Tests	**F-Test**
Serial Correlation	0.446202 (0.6478)
Heteroscedasticity	1.314917 (0.2959)
Normality	0.460155 (0.7944)
Functional Form	0.145953 (0.8653)

Source: The author's calculations

Various diagnostic tests have been used in this section to ensure that the assessed models were free of somewhat econometric problems. The estimated models must be devoid of serial correlation, heteroscedasticity, and functional form problems to be used in ARDL modeling. Similarly, in the ARDL framework, the normalcy assumption must not be violated to produce valid results. All of the aforementioned tests are completed, and the outcomes are shown (Table 10). The statistics and p-values have proven that there are no severe econometric concerns. The findings show that the stated model has no serial correlation problems, as the p value of LM test is more than the significance value. Similarly, the White test (1980) ruled out heteroscedasticity in the estimated model. The data normality is demonstrated by the Jarque–Bera statistic and its probability value. When it comes to ARDL modeling, residual stability is crucial. The CUSUM and CUSUM square tests were used to accomplish this.The graphs for both experiments are displayed in Figures 5 and 6, respectively. Both assessed lines lies between the critical lines at the 5% level of significance, according to the graphs. As a result, it is possible to conclude that the previously stated results are dependable and stable, and hence could be used to formulate policy.





Source:The author's calculations

Conclusion

This paper is an attempt to test the association between economic growth & foreign inflows of Bangladesh.The long-run association among the variables has been tested by employing the ARDL model for the period 1991-2019.To test the short-run dynamics, error correction modeling has been carried out. To avoid various econometric issues, appropriate diagnostic tests have been applied. The attained outcomes are much fascinating. The inflows coming to Bangladesh particular for the study have played an important part in boosting Bangladesh's economic growth. A long-run association has been found between foreign inflows & Bangladesh's economic growth.The short-run and long-run coefficients imply that FDI, remittances, and aid have a large and favorable impact on Bangladesh's economic growth in the long run. Debt, on the other hand, harms economic growth in the short run and long run.Therefore, the outcomes of the study are eye-opening for policy-makers. This is suggested to the policymakers that Bangladesh should focus on FDI, aid, remittances for the development of the economy. Debt is a burden for the economy as it has a negative impact in the longrun. Moreover, as the outcomes reveal that external debt has a deleterious effect on economic growth in Bangladesh, the economy needs to take major steps to reduce the foreign debt inflows in the country. This is significant because external debt inflows result in a bigger external debt load and higher debt service obligations, both of which are detrimental to Bangladesh's economic growth.The results indicate a need foran effective management strategy for domestic and external debt. Bangladesh's government should devise new strategies for the management of debt. So that debt can be utilized profitably, add value to the economy and more future income can be generated. Bangladesh should focus to make more friendly relations with neighbouring countries, reducing trade barriers with mutual consent so that exports of production can be increased and inflows of foreign exchange can be increased and dependency of the economy on debt can decrease.

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