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THE IMPACT OF DEFICIT FINANCING ON ECONOMIC GROWTH: A COMPARATIVE STUDY OF PAKISTAN AND MALAYSIAN ECONOMIES

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Abstract

The objective of this study is to investigate the impact of deficit-financing on economic growth of these two countries, using time series data from 1990 to 2020. Economic growth was taken as dependent variable and budget deficit, broad money growth, exports as percentage of GDP and FDI were chosen as independent variables. ARDL approach was applied to analyze the relationship between dependent and independent variables in the long run and short run. The findings of the study reveals that there is a strong positive relationship between deficit financing and economic growth in Pakistan but is weak Malaysia, while broad money growth, exports in both countries have positive association with economic growth. FDI also has positive effect on growth in Malaysia but negative effect on growth in Pakistan.

Key words: Deficit Financing; Broad Money growth; FDI; Exports; GDP growth.
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1: Introduction

It is common practice that most of the countries resort to deficit-financing to bridge gap between revenue and expenditures and it is carried out either through borrowing or through printing of money. Pakistan emerged on the globe on 14th 1947 as an Agriculture-based economy with a lot of problems like poverty, unemployment, illiteracy, poor infrastructure, poor trade performance and nonfunctional industrial sector and many more. The main endowment factor of the Pakistan is fertile land with largest irrigation system. It is also rich in minerals containing large reserves of gas, coals and uranium, etc. However, Pakistan has failed to exploit these natural resources due to financial constraints. It has low tax base (about 9% tax-to-GDP ratio), low total exports (about US$31 billion per annum) and low FDI. In contrast, it is fifth largest populous country of the world for which it has to import more than US$7 billion food items every year. Moreover, it has to spend major portion of its revenue on its armed forces because it has fought four wars with its neighboring country, India. There is a wide gap between its revenue and expenditures and in order to bridge this gap it has to borrow loans from world donors and friendly countries as well as meet its budget deficit through deficit-financing. The net result is that its national debt burden is increasing year after year and now its debt-to-GDP ratio has exceeded 70%. Pakistan has made remarkable progress in the field of education as the adult literacy rate has reached 70%, Manufacturing sector particularly textile industry is contributing 60% in exports and provides employment to 7 million labour. But its ranking in Human Development Index is at 154, which is

very low. It has also been facing severe threat of climate change and in recent devastating flood it has incurred about US$28 billion loss. The World Bank estimated that poverty rate in Pakistan was 39.3 % in 2020-21 which was decreased to 37.9% in 2022-23.

Malaysia is also a developing country located in the Southeast Asia. It is an investment hub and its locations open the gate way of trade with other countries. Major exports of Malaysia are electric goods (secondary exports) which gives the country better terms of trade. It also has skilled labor which has attraction for the foreign investors. GDP per capita of Malaysia is around US$ 12,500 far higher than Pakistan's $1,798. Literacy rate in Malaysia is 94.3% against Pakistan 70% adult literacy rate. These statistics prove that Malaysia is performing much better than Pakistan.

1.2 Socio-Economic indicators of Malaysia and Pakistan

In order to understand the current economic condition of Pakistan and Malaysia we just glance at macroeconomic indicators of two countries which are shown in the following table.

Table 1.

Socio-economic indicators of Malaysia and Pakistan

Indicators	Pakistan	Malaysia
National Debt as % of GDP	83.42%	65%
Inflation rate	11%	-1.14%
Unemployment rate	4.45%	4.3
Poverty rate	39.3%	Below 5%
Economic growth rate	0.47%	5.64%
Current account deficit % of GDP	-60%	-2%

HDI ranking	154	62
Infant mortality rate	56.8	5.4
Population growth rate	2%	1.3%
Exchange rate against dollar	1$=170 Pak Rupee	1$=4.19 Ringgit
Adult Literacy rate	70%	95%
Foreign currency reserves	US $14 billion	US$116.3 billion
Per Capita income	$ 1,798	$ 12,500
Dependency (primary sector)	23.13%	8.19%

1.2.1 Quality of education in Malaysia and Pakistan

Pakistan has achieved remarkable growth in the field of education as its adult literacy rate has reached 70%. Pakistan has spent billions of rupees to provide education to its male and female population. Government has spent a lot of money to build schools, universities and colleges, besides providing transportation facilities so that students should have access to the education but still Pakistan has to make more efforts to achieve 100% literacy rate. The quality of education is also questionable in Pakistan as the teachers in mostly government schools are not well qualified and are mostly found absent from their jobs. Old curriculum is being taught in the schools with outdated setup as a result student are degree holder but have no knowledgeable.

As for Malaysia is concerned the literacy rate is higher than Pakistan (95% adult literacy rate). the reason is that Malaysia has focused on the human development resources with sincerity and strong commitment. Corruption is also very lower in Malaysia so the funds allocated for education are properly utilized, Moreover, quality of

education is better and more focus is given on technical education against Pakistan where all focus is on general education. The expenditure of health as % of GDP in 2021 was 5%in Malaysia as compared to 1.2 percent % of GDP in Pakistan. Malaysia meets World Health Organization benchmark of 5% allocation of GDP for health sector. Poverty in Malaysia is below five percent while in Pakistan it is around 39.3%. It means 40% population in Pakistan is facing the miseries of poverty.

1.2.2 Dependency of Pakistan and Malaysia on primary sector:

Pakistan is an agriculture economy which contributes 23.13% to the GDP. The industrial sector is also depended on agriculture sector for raw material. The whole Textile and Sugar sectors depend upon cotton and sugar produced by agriculture sector. As Pakistan's factor endowment is fertile land with full of minerals and having world largest irrigation system and four seasons which further strengthen agriculture sector. But Pakistan is not fully exploiting the potential of agriculture sector as the per acre yield is very low in Pakistan as compared to Japan, USA and other developed countries. Being an agrarian economy Pakistan has to import food items from other countries to feed its growing population. Pakistan is producing primary agriculture products and has so far not moved toward full value addition. This is the reason the quality of products is poor and wages in agriculture sector are very low.

1.2.3 Foreign Currency Reserves of Pakistan and Malaysia

The economic performance of Malaysia is much better than that of Pakistan as Malaysia is having more foreign currency reserves about

US$ 116.3 billion than Pakistan's US$14 billion in 2022. This shows that Malaysian economy is stronger than Pakistan from financial and economic point of view. Ample foreign currency reserves provide strength to Malaysian currency against UD dollar, British pound and Euro. It stabilizes the economy as well as inflation rate. But Pakistan's currency is highly volatile, besides high inflation rate.

1.2.3 Exchange rate in Pakistan and Malaysia

If we compare the exchange rate of US dollar with rupees the situation of Pak Rupee is very bleak and Pakistan is facing continuous depreciation. Dollar is becoming stronger and the international debt burden is also increasing rapidly, creating balance of payment crisis. Pakistan has opted free float exchange rate regime with less reserves in hand provided no cushion against any economic shock. Having huge and accumulating balance of payments deficit and poor government planning are the key elements for the persistent continuous devaluation of Pak rupee. In contrast, Malaysian currency, ringgit, is stable against US dollar and other world currencies due to political and economic stability. Malaysia has no balance of payment problem at all as compared to Pakistan which is at the edge of sovereign default.

1.2.5 Inflation rate in Malaysia and Pakistan

Inflation rate is higher in Pakistan due to various reasons. One of the main reasons is that Pakistan is highly indebted and as per the requirement of the IMF Structural Adjustment program, Pakistan has to increase taxes, prices of electricity and petroleum products continuously, leading the inflation rate to 37.5% in May 2023. Similarly, under IMF conditionalities Pakistan has been withdrawn subsidies from

different sector, results increase in the cost of production consecutively. Pakistan energy sector depends upon imported furnace oil for electricity generation and due to high prices of oil in international market, the government has to increase energy prices which ultimately fuel the inflation. In contrast, the inflation rate is normal in Malaysia due to stable prices.

1.2.6 Unemployment rate in Malaysia and Pakistan

Unemployment rate is higher in Pakistan as compared to the Malaysia due to various reasons. Economic growth in Pakistan and job creation is very low and as such unemployment rate is very high. As population is increasing rapidly it adding number of workers in total labor force every year, making employment situation worse. A high level of disguised unemployment is existing in Agriculture sector due to use of outdated framing techniques. Similarly, structural unemployment is also increasing in Pakistan due to depletion of natural resources like water, gas, oil and other minerals. Thousands of CNG Gas stations providing employment to million of people have been closed due to unavailability of natural gas. Contrary to Pakistan, Malaysia is not much dependent on the agriculture sector and its industrial sector is developed and creating required number of jobs. The business environment for new entrepreneurs is also better.in Malaysia.

1.2.7 Share of exports as % of GDP in Pakistan and Malaysia

Total exports of Malaysia in 2021 were **$256.76 billion** and its share in total GDP was more than 68.84%. Its highest share in GDP was 119.81% in 2000. However, it remained above 60% during 1990 and 2020. In contrast, total exports of Pakistan in 2021 were USD 31.58

billion and its share in GDP was only 9.%.and its highest share in GDP was 17. 27% in 1992 and since then the share of exports in Pakistan's GDP is declining. In contrast, the share of exports in Malaysian GDP is increasing continuously since 1990 as is seen in the Figure 1 and 2.

Fig 1 Malaysia's total exports" shares as % GDP.

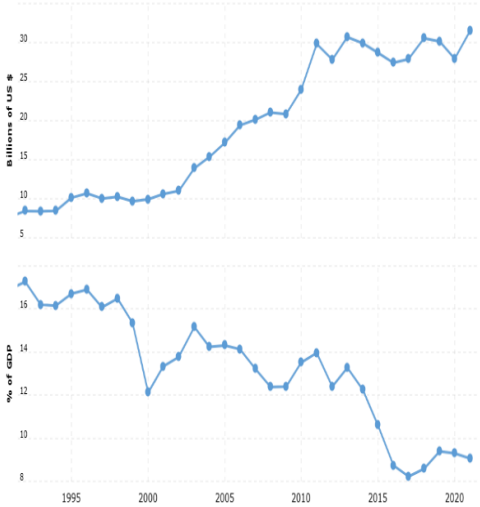
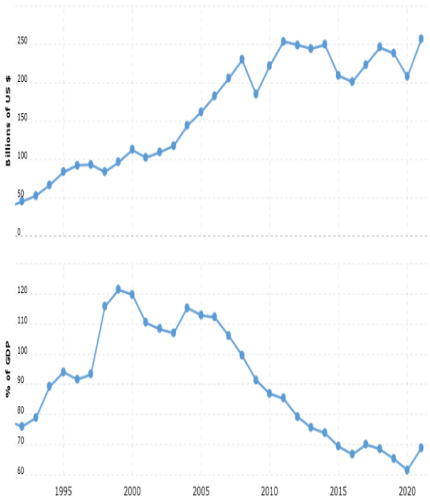


Fig 2: Pakistan total exports" share as % GDP



Source: https://www.macrotrends.net/countries/exports.

Keeping in view the background of study, the main objective of this study is to investigate the impact of deficit-financing on economic growth of Pakistan and Malaysia and also to examine the low economic performance of Pakistan vis-à-vis Malaysia in terms of low tax-to-GDP ratio, high external debt, high unemployment, high inflation rate and volatile currency. As both are Asian countries, both have Muslim majority population and both have close bilateral relations. They have identical size of GDP but large differences in per capita GDP. The comparison of the economies of Pakistan and Malaysia will be very

interesting and its findings will have much value for researchers, policy makers and academicians. Being a new study, it will contribute into body of knowledge and literature and provide an insight to the policy makers because one country is far ahead economically while the other one is far behind. Is it due to endowment of natural resources or wrong policies? This is the main question of this research study. It also highlights the large scope of this study. The findings of this study will open the door for further research on different macroeconomic variables of Malaysia and Pakistan

The study contributes into the existing body of literature in many ways. For example, it will introduce a cohesive framework for comparing and contrasting the economic dynamics of Malaysia and Pakistan. By combining insights from various studies focused on different economic factors, it will provide a comprehensive perspective on the strengths, challenges, and intricacies of both nations. Moreover, by investigating into the interaction of fiscal, monetary, and trade policies, this research offers a granular understanding of how these policies influence economic growth in the respective countries. Such an analysis helps policymakers in both Malaysia and Pakistan to refine their strategies, drawing lessons from each other's experiences. This study will also bridge gaps, ranging from direct economic comparisons to exploring the impacts of macroeconomic policy interactions and in this way, this study will contribute to filling crucial knowledge voids. This can guide future research directions and provide a foundational basis for further inquiries. The comparative analysis not only serves academic purposes but also offers actionable insights for policymakers

in both countries. By understanding what worked and what didn't in similar regional contexts, governments can tailor their economic strategies more effectively. Additionally, by evaluating Malaysia's trajectory towards becoming a high-income economy and understanding the disruptions caused by the pandemic, this study contributes predictions about future economic developments. These predictions can be vital for stakeholders ranging from investors to international organizations.

2 Literature Review

The relationship between economic factors and growth varies significantly based on the region and the specific variables being considered. This review seeks to contrast the economies of Malaysia and Pakistan in light of the selected studies.

2.1. Pakistan's Economic Dynamics

Montiel (1991) appreciates Pakistan’s macro-economic performance despite its deficit financing and high external debt. However, he highlights the trade-off between reducing government expenditure and negative impacts on economic growth. Ahmed and Bukhari (2016) reveal a negative relationship between interest rates and Pakistan’s economic growth, suggesting that higher interest rates could possibly discourage investments. This is further substantiated by Javid (2014), who finds a positive relationship between inflation and interest rates in Pakistan. Trade and Exports: Faridi (2012) makes a surprising revelation about agricultural exports exerting a negative impact on Pakistan’s economic growth, with higher domestic prices nullifying growth benefits. Debt Dynamics: Malik (2010) sheds light on

the adverse relationship between external debt and growth in Pakistan. Countries grappling with high external debt can experience suppressed growth if a significant portion of their revenue is channeled towards debt servicing. FDI and Growth: Falki (2009) could not find a beneficial correlation between FDI and economic growth in Pakistan. The primary attribution for this is the direction of FDI towards speculative ventures rather than growth-promoting industries. Fiscal Policy and Economic Indicators: Chowdhury (2005) did not find a significant link between fiscal policy and interest rates in Pakistan, but discerned regional variations in the price effects.

2. 2. Malaysia's Economic Landscape

Structural Changes and Growth: Chee Peng, Lim (1982) observes significant structural changes in Malaysia's economy, particularly in the manufacturing sector. The shift from focusing on substitution manufacturing industries for local demand to manufacturing for exportation is highlighted. Policies promoting industrialization and exports are credited for the exceptional growth in Malaysia's manufacturing sector. According to The World Bank (2021), Malaysia is poised to transition to a high-income economy between 2024 and 2028. Public policies over the past two decades and a per capita GNI of US$11,200 underline this potential. Nevertheless, the COVID-19 pandemic has momentarily halted this fast-paced progress, as it did for economies worldwide.

Pakistan and Malaysia, while geographically close, exhibit divergent economic dynamics. Pakistan's economy, from the selected studies, presents a complex interplay between debt, interest rates, and

fiscal policies. Malaysia, on the other hand, exhibits the potential of structured policies and economic shifts, particularly in manufacturing and export-oriented strategies, which have propelled its growth trajectory. The unique challenges and strengths of each country underscore the importance of region-specific approaches in economic research and policymaking.

One noticeable research gap is the absence of a direct comparison between the economic dynamics of Malaysia and Pakistan in the selected studies. While both countries are mentioned separately, there is a lack of studies that explicitly examine and contrast their economic performances, despite their geographic proximity and similar historical backgrounds. While the literature discusses various economic factors affecting growth in both countries, there is limited research that delves into the comprehensive evaluation of the effectiveness of macroeconomic policies in Pakistan and Malaysia. Specifically, there is a gap in understanding how fiscal, monetary, and trade policies interact and influence economic growth in these two nations. This study offers a novel perspective by comparing the economic dynamics of Malaysia and Pakistan in a single framework. This approach can provide valuable insights into the similarities, differences, and potential lessons that can be learned from these two nations' economic experiences. Thus, the novelty of the study lies in its endeavor to bridge these gaps, offering fresh insights into the economic dynamics of these two nations and the policy landscape that shapes their growth trajectories.

3. Data and Methodology

This is a quantitative study in which quantitative data and research methods have been used. Thirty years data from 1990 to 2020 relating to selected variables of Pakistan and Malaysian economies were collected from World Development Indicators, International Monetary Fund, Central Banks of Pakistan and Malaysia. The dependent variable for both countries was economic growth while independent variables included: Broad money growth, Budget deficit as % of GDP, Foreign Direct Investment as % of GDP and exports as % of GDP. Budget deficit is representing Fiscal policy and the broad money growth represents monetary policy, whereas the FDI and exports as % of GDP represents international trade for both economies. The econometric model developed for this study is given in the following mathematical equation:

$$Y=\beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \mu$$

Where:

Y = Economic growth.

X_1= Broad Money as % of GDP.

X_2 =Budget deficit as % of GDP.

X_3= Exports as % of GDP.

X_4= FDI as % of GDP.

The same model is used for both Pakistan and Malaysia. The hypotheses of this study are the followings: -

H_0 = Deficit financing does not have any significant and positive impact on economic growth in Pakistan and Malaysia.

H_1 = Deficit financing does have significant and positive impact on

economic growth in Pakistan and Malaysia.

Different statistical techniques were applied to analyze the data. For example, ADF's unit root test was applied to check stationarity among variables while correlation matrix was applied to determine strength of correlation between pair of variables. ARDL Model was used to check short run and long run association between dependent and independent variables. LM was used to check multicollinearity while Breusch-Pagan-Godfrey test was applied to check Heteroskedasticity problem. Finally Custom stability tests applied to check the stability of model during the study period.

4. Results

4.1 Analysis of Pakistan's economy

First, we apply ARDL approach to determine long run relationship between dependent and independent variables. The results of ARDL model for Pakistan are shown in the following table.

Table 2:

Results of ARDL Model for Pakistan

Variable	Coefficient	Std. Error	t-Statistic	Prob.
FDI_GDP	-0.729499	0.249390	-2.925135	0.0118
BMG__	0.274022	0.048664	5.630885	0.0001
B_D__GDP	0.338456	0.070944	4.770745	0.0004
X___GDP	-0.371888	0.057876	-6.425617	0.0000
C	7.254372	0.785616	9.233988	0.0000

Variables such as BMG (broad money growth), FDI (Foreign direct investment), and X (Exports as % GDP) are significant. Budge deficit has positive coefficient value which confirms that if one unit increases

in government expenditure for education, health and infrastructure development economic growth will be likely to be increased by 33% in the long run. FDI and Exports have negative coefficient values which confirm strong negative impact on the economic growth of Pakistan. Results show that if one unit increases in FDI it will likely to decrease GDP by 72%. Similarly, if one unit increases in exports it will likely to decrease GDP by 37.18% in the long run. The reason of the negative effect of GDP and Exports is that FDI mostly invested in speculative activities for short term and it does not make any contribution in fixed capital formation. Similarly, Pakistan's exports are consisted of primary products which fetch very low value in international market. Moreover, it is highly subsidized sector that consumes fiscal incentives but its performance is very low. For example, in the fiscal year of 2023 Pakistan's total exports were around US$ 31 billions against total imports of US$ 81 billion. However, broad money has positive association with GDP growth in Pakistan as one unit increases in the volume of broad money will likely to increase GDP by 27%. Similarly, one unit increases in budget deficit will likely to increase GDP by 33% in the long run.

Now we confirm this relationship through Bound test.

Null Hypothesis states that there are no long-run relationships between variables. The results of Bound Test are shown in the table below.

Table 3.

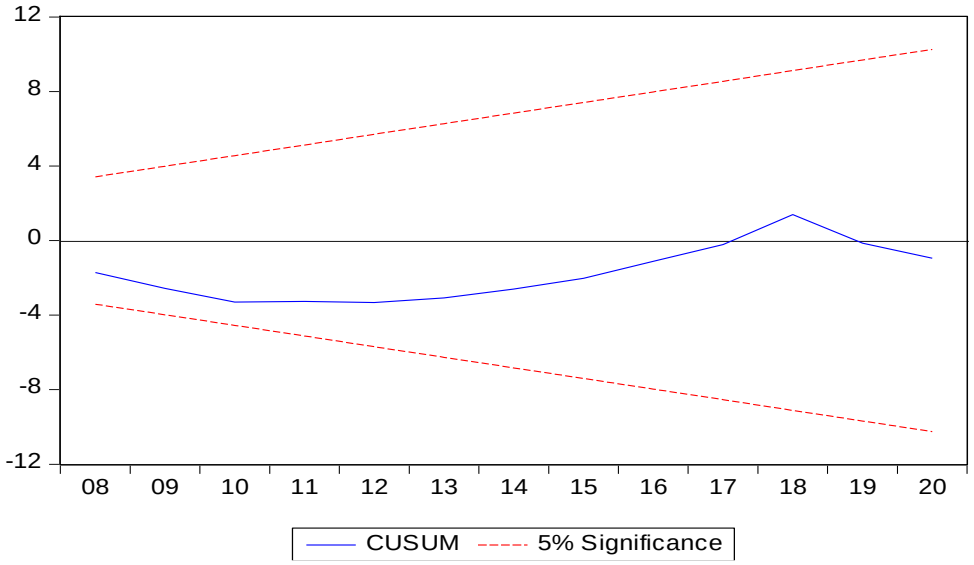
Bound test results for Pakistan

Significance	I0 Bound	I1 Bound
10%	2.456	3.523
5%	2.867	4.012
2.5%	3.259	4.495
1%	3.741	5.065
F-statistic value = 14.27728		

The results in Table .3 reveal that the value of F statistics does not fall in the lower and the upper bound so the long run relationship between variables were confirmed and Null hypothesis is rejected and alternate hypothesis is accepted. The alternate hypothesis stated that broad money growth, budget deficit, exports and FDI have positive relationship with economic growth in the long run.

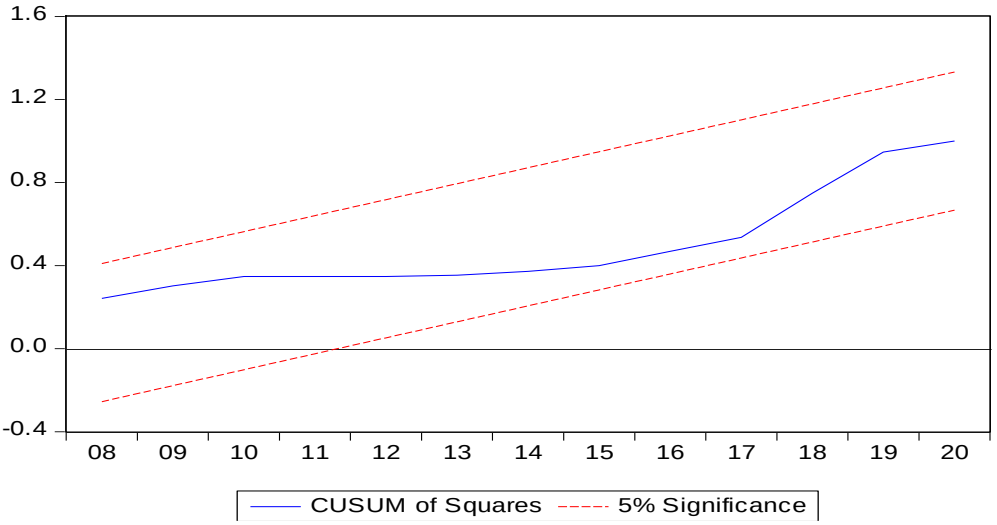
Two diagnostic tests such as CUSUM TEST and CUSUM of SQUARE are used to check stability of model during the study period. The results of CUSUM test for Pakistan are shown in the following figure.

Fig 3: CUSUM Test for Pakistan



In Figure 4.1 blue line predicts the stability of data. The blue line is in between upper and lower red lines, which is good and it shows that there is stability in the model. If blue lines cross the upper and lower red lines, then there would have been the problem of instability in the model of the study. The CUSUM of square test is also used to check stability of model. Similar rule of thumb is applied as in CUSUM test that if blue line is in between the red lines, it means that there is stability. CUSUM test predicts stability then there is chance that CUSUM of SQURE will also predict and show stability of the model during study period as is shown in the figure below**.**

Fig 4.: CUSUM of Square Test for Pakistan



Results of both the CUSUM and CUSUM Square are significant as shown in the above figures because the blue line is in between the boundaries and is not close to red lines. It means the model is stable.

4.2 Analysis of Malaysian Economy

First, we apply ARDL model to determine relationship between dependent and independent variables in the long run in Malaysia.

Table 4.:

ARDL Long Run Results Malaysia

Long Run Coefficients				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
FDI	0.140394	1.630175	3.766708	0.0197
BMG__	0.876022	0.236494	3.704200	0.0208
B_D_GDP	0.539109	0.378301	1.425078	0.2273
X___GDP	0.156775	0.033655	4.658246	0.0096
C	-21.640622	7.396812	-2.925669	0.0430

From the above results of ARDL model, we can see that all independent variables have positive relationship with dependent variables in Malaysia. For example, the coefficient value of FDI has positive association with economic growth it means if one-unit creases in the FDI it will likely to increase GDP around 14 percent in the long run. The reason positive impact of FDI in Malaysia is that all foreign investment is made fixed assets and it will increase capital formation that leads to increase in GDP growth rate. The second variable, broad money (BMG) has also had strong positive relationship with economic growth and if one unit increases in broad money growth it will likely to expand GDP by 87.60%. Budget deficit also have positive association with economic growth and if one unit increases in budget deficit it will likely to increase GDP by 53.91%. The variable, Exports also have positive association with economic growth and if one unit increase in Exports it will likely to have positive impact on Malaysian GDP by 15.67% in the long run. Now the above results of ARDL model are confirmed from Bound test through hypotheses testing. Null hypothesis states that there is not long run relationship between dependent and independent variables in the long run while alternate hypothesis states there are significant positive relationship between independent and dependent variables.

Table 5

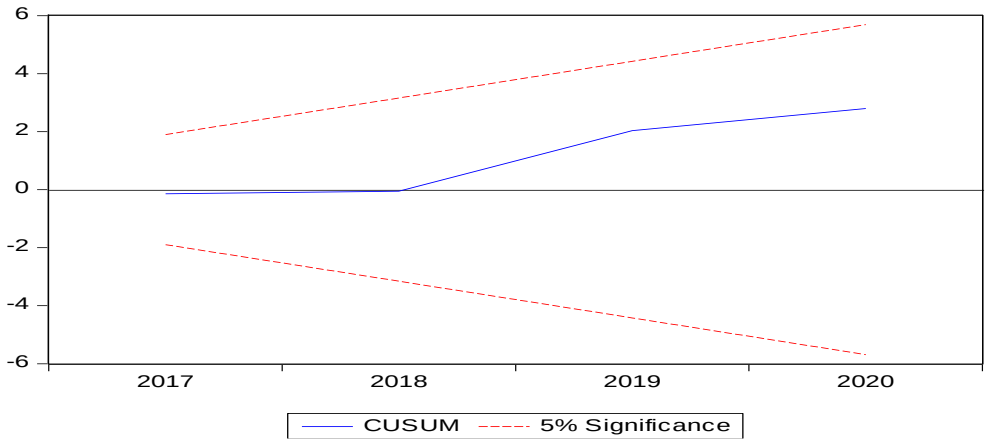
Results of Bound Test

Significance	I0 Bound	I1 Bound
10%	2.45	3.52
5%	2.86	4.01
2.5%	3.25	4.49
1%	3.74	5.06
F-statistic value = 12.09576		

The results in table 5 show that the value of F statistics does not fall in the lower and the upper bound so we can accept alternate hypothesis and reject Null hypothesis. It means that long run relationship exists between independent and dependent variables in the long run in Malaysia.

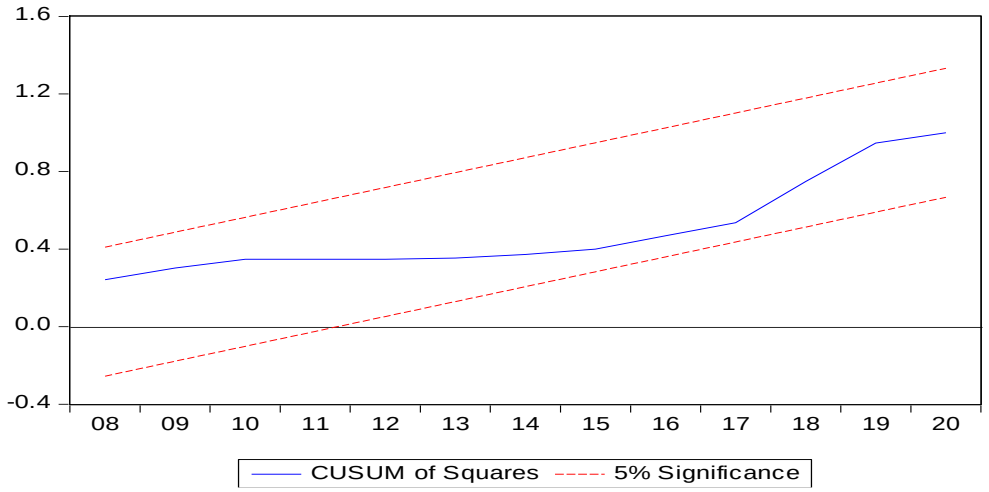
Now diagnostic tests are applied to check stability of the parameters of model during study period. For this purpose, mostly two tests, CUSUM TEST and CUSUM of SQUARE Test are applied. The results of stability diagnostic tests are shown in the following figures.

Fig 5 CUSUM Test Result



The results in Fig 5 show that blue line predicts the stability of parameters during 2017-2020. The blue line is in between upper and lower red lines, which is assumed to be good because it shows that there is stability in the model. If blue lines cross the upper and lower red lines, then there would have been the problem of instability in the data and the model.

Fig 6: CUSUM of Squares Test



The results of CUSUM of square test are also show stability of the parameters during study period. The rule of thumb is that if blue line is in between the red lines, it means that there is stability. CUSUM test predicts stability and there is a chance that CUSUM of SQURE will also predict and show stability between coefficient parameters. Results of both the CUSUM and CUSUM Square are significant, we can confirm from the graphs as the blue line is in between the boundaries and is not touching red lines.

5. Discussion

The objectives of this study were to analyze the impact of deficit-financing on economic growth of Pakistan and Malaysia and also investigate the low economic performance of Pakistan vis-à-vis Malaysia in terms of low tax-to-GDP ratio, high external debt, high unemployment, high inflation rate and volatile currency. As both Pakistan and Malaysia are Asian countries, both have Muslim majority population and both have close bilateral relations. They have identical size of GDP but large differences in per capita GDP, size of population literacy rate. This prompted the authors to explore the question why Pakistan is poor and Malaysia is rich? Why Pakistan's economic growth is low and Malaysian economic growth is high? Why Pakistan's exchange rate is volatile and why Malaysian exchange rate is stable? Why Pakistan's per capita is low and Malaysia's per capita income is high? Now we explore the answers of the above questions by comparing empirical results of Pakistan and Malaysia.

The empirical analysis proves that the impact of foreign direct investment (FDI) on economic growth is positive and if one-unit

increases in FDI in Malaysia it will likely to have positive impact of GDP by more than 14 percent in the long run. The positive relationship between FDI and economic growth in Malaysia indicates that Government is stable in Malaysia that attracts foreign direct investment. Another point is that Malaysian government does not allow foreign firms to repatriate100% profit to their home countries. Moreover, Malaysian government also provide full legal protection to local industry and does not allow foreign firms to kick out local firms from the market. It has provided equal level playing field both for Malaysian and foreign investors. The availability of required human capital in Malaysia is another factor which attracts foreign companies to install high tech industries in Malaysia. World Bank has ranked Malaysia as 4th hot favorite country for investment. These findings are consistent with the study of Rahman, (2012) who found that there is a positive relationship between FDI and economic growth in Malaysia.

The analysis of ARDL model for Pakistan shows that foreign direct investment (FDI) has negative association with economic growth and if one unit increases in FDI in Pakistan it will likely to decrease GDP growth rate by 72%. The major cause of the negative impact of FDI on GDP growth in Pakistan is that most of foreign investment is made in speculative sector like Pakistan Stock Exchange or real estate for short term period due to political instability and fear of loss. Moreover, the government of Pakistan has allowed foreign investors to repatriate 100% profit. Pakistan's elite class maintain accounts in foreign banks abroad and they transfer their money to their foreign currency whenever political situation becomes worse. Even Pakistani investors

are reluctant to invest in fixed assets on long term basis and this is the reason that Pakistan has imported goods and services worth $81 billion against total exports of $31 billion in the fiscal year 2022-2023. The volume of FDI has been decreasing in Pakistan year after year due to high production cost, discontinuity of government policies, lack of skilled labor, threat of war and restrictive economic. The same results were drawn by Nuzhat Falki (2009) who also found negative relationship between FDI and economic growth in Pakistan. Broad money is a method of calculating money supply. It is a measure of the money supply in a national economy that includes both highly liquid "narrow money" and less liquid forms of money. Broad money growth (BMG) has positive and significant relationship with economic growth in Malaysia as empirical analysis of these two variables shows if one unit increase in broad money growth it will likely to increase GDP growth by 87 in Malaysia. It means Malaysian central banks wisely use this instrument of monetary policy to expedite economic growth. These findings are matched with the results of Ergin & Duhok (2018) who also found positive impact of broad monetary growth on Malaysian GDP.

Broad money growth **(**BMG) has also positive relationship with the economic growth in Pakistan in the long run because government is providing cheaper finance to the business firms to encourage business expansion and industrialization. According to the empirical analysis of the relationship between broad monetary growth and economic growth in Pakistan reveals if one unit increases in BMG it will likely to cause 27% increase GDP growth. However, its impact is less 60% in Pakistan as compared to Malaysia. It means Malaysian monetary policy is more

effective than Pakistan's monetary policy. These results are also confirmed by the study of Imran Sharif, (2012) who found moderate relationship between monetary policy, inflation and economic growth in Pakistan.

The budget deficit has significant positive relationship with economic growth in Malaysia as the analysis of ARDL model shows if one unit increases in budget deficit it will likely to cause increase in GDP growth by 53.91 % in the long run. The insignificant relationship between budget deficit and GDP growth rate indicates that Malaysian government is not spending extensively on the development and infrastructural development to speed up economic growth through money printing as such type of spending creates inflation in the economy. These results are also confirmed by Central Bank of Malaysia Report, (2011) which stated that deficit financial is made only for productive purpose to accelerate growth process. Budget deficit or deficit financing also has positive association with GDP growth rate in Pakistan buts its impact on growth is less 20% as compared to Malaysia. The ARDL analysis show if one-unit changes in budget deficit it will likely to expand GDP growth by 33.84%. The reason for low impact is that deficit financing is carried out in Pakistan to bridge gap between revenue and expenditures and very low portion of such financing is made on social sector like health, education and infrastructure. These results support the findings of Gupta et al. (2005) who found a positive relationship between budget deficit and economic growth both in the short and long terms. They also find that productive and nonproductive expenditures both have positive impact. Bose,

Haque and Osborn (2007) also found similar results and proved that, if the budget deficit is due to productive spending, its impact on economic growth would be positive.

The exports have positive association with economic growth in Malaysia as the empirical analysis proves if one unit increases in the exports it will likely to speed up economic growth by 15.17%. These results are also consistent with theory of comparative advantage. skilled and cheaper labor along with friendly government policies help firms to become competitive in international market as a result export are increased and helped to achieve desired economic growth. Exports of Malaysia are mainly based on finished or semi-finished goods which fetch premium price in international market. Malaysia total exports in 2021 were $256.76 billion and its share in total GDP was more than 70%. It indicates surplus production of goods and services for exports. The same results were noted. by Baharumshah and Rashid (2022) who found that there is a close relationship between exports, imports and economic growth in Malaysia.

When we analyze the role of exports in economic growth, we find disappointing results because Pakistan total exports in 2021 was USD. 31.58 billion and its share in GDP was only 9. The empirical results of ARDL model about Pakistan's exports show if one unit increases in total exports it will likely to cause decrease in GDP by 37.8%. In this way, the exports and GDP growth rate have negative relationship. The reason is that the government provides generous subsidies to this sector since long in the shape of concessionary finance, electricity, gas, infrastructure and working capital. These subsidies are given out of tax

revenue and in this way this sector is actually rent-seeker and doing business on national exchequer. Its share in GDP was declined from 14.79% in 1990 to 9.6% in 2021. Major share in the Exports is from agriculture sector, so when exports increase the availability of products reduces in the local markets which leads to increase in prices and inflation, hence, causes negative growth.

6. Conclusions and policy implications

Pakistan's low economic performance compared to Malaysia can be attributed to several factors such as a low tax-to-GDP ratio, high external debt, high unemployment, high inflation rate, and a volatile currency. These factors have hindered Pakistan's economic growth and contributed to its lower per capita income. Foreign direct investment (FDI) has a positive impact on economic growth in Malaysia, indicating a stable government, attractive investment policies, legal protection for local industries, and the availability of skilled labor. In contrast, FDI has a negative association with economic growth in Pakistan, mainly due to political instability, short-term speculative investments, and the repatriation of profits by foreign investors. Pakistan should focus on political stability and the provision of legal protection to local industries to attract foreign direct investment. The policy makers should implement policies to encourage long-term investments in productive sectors, rather than speculative sectors like the stock exchange and real estate. They should encourage local investors to invest in fixed assets on a long-term basis to reduce reliance on foreign investment. The policy

makers should also address issues such as high production costs, discontinuity of government policies, lack of skilled labor, and geopolitical threats to create a favorable environment for investment. Broad money growth (BMG) has a positive relationship with economic growth in both Malaysia and Pakistan, but its impact is more significant in Malaysia. This suggests that Malaysia's monetary policy is more effective in stimulating economic growth. In Pakistan, cheaper finance provided by the government encourages business expansion and industrialization, but its impact on GDP growth is relatively lower. State Bank of Pakistan should strive to improve the effectiveness of its monetary policy to achieve higher GDP growth rates. There is need for strengthen the coordination between fiscal and monetary policies to ensure their combined effectiveness in promoting economic growth.

The budget deficit has a positive relationship with economic growth in both Malaysia and Pakistan, although its impact on growth is higher in Malaysia. This indicates that deficit financing can be used for productive purposes to expedite economic growth, but the allocation of funds and the nature of expenditures matter. Malaysia's approach of using deficit financing for productive purposes should be emulated, focusing on development and infrastructure projects rather than excessive spending that can lead to inflation. In Pakistan, a greater portion of deficit financing should be directed towards social sectors like health, education, and infrastructure to promote inclusive and sustainable growth. Exports have a positive association with economic growth in Malaysia, driven by factors such as skilled and cheaper labor, friendly government policies, and the production of finished or semi-finished goods. However, in Pakistan, exports have a negative

relationship with GDP growth due to generous subsidies provided by the government, which are not sustainable and lead to rent-seeking behavior. Pakistan should reevaluate its subsidies to the export sector and ensure they are targeted towards sustainable and productive activities. There is need to promote diversification of exports and explore opportunities to add value to agricultural products to increase competitiveness in international markets by Implementing policies that balance the growth of exports with the availability of products in local markets to mitigate inflationary pressures. Thus, findings of this study suggest that Pakistan can learn from Malaysia's experiences in attracting foreign investment, implementing effective monetary and fiscal policies, and promoting exports. Addressing the identified issues and implementing the suggested policy implications can help Pakistan improve its economic performance and achieve higher levels of economic growth and development.

7. Limitations and suggestions for further research:

The study focuses on the comparison between Pakistan and Malaysia, which may limit the generalizability of the findings to other countries with different economic contexts and characteristics. The study relies on empirical analysis and does not consider qualitative factors or case studies that could provide a more comprehensive understanding of the issues discussed. The study does not delve deeply into the specific policy recommendations or implementation strategies for addressing the identified issues. Further research and analysis would be needed to develop detailed and actionable policy implications. The study does not consider the impact of external

factors, such as global economic trends, geopolitical dynamics, or regional trade agreements, which could influence the economic performance of both countries. The study's findings are based on the available data and analysis methods used, which may have inherent limitations and potential biases. It is important to consider these limitations when interpreting the findings of the study and formulating policy recommendations based on its conclusions. Further research and analysis are encouraged to provide a more robust understanding of the economic challenges and potential solutions for Pakistan's economic development.

Data statement

The data that supports the findings of this study will be made available by corresponding author on strong request.

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