

The Impact of Foreign Aid on the Economic Growth of Afghanistan

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Abstract: Afghanistan is a war-affected and developing country and it is mostly dependent on foreign aid from the international communities to fulfill its developmental and non-developmental expenditures. Afghanistan has been the recipient of substantial foreign funding from several global financial institutions during the past two decades. This thesis explores the relationship between foreign aid and economic growth in Afghanistan. Additionally, it investigates the impact of control variables such as remittances, gross domestic investment, and labor force participation on economic growth. Time series data from 2001 to 2020 are used in the study. To check if the data is stationary, the Augmented Dickey-Fuller test is used. The Autoregressive Distributive Lag (ARDL) model is used to see if there is a cointegration link between the factors being studied. The findings validate a persistent correlation between foreign aid, economic growth, remittances, employment rate, gross domestic investment, and terrorism. The findings demonstrate that foreign aid exerts a substantial and beneficial influence on Afghanistan's economic growth. Conversely, domestic investment and employment levels have a favorable but negligible impact on economic growth, both in the short-term and the long-term. Moreover, terrorism exhibits a detrimental and highly substantial correlation with the economic advancement of Afghanistan during the analyzed timeframe.

Keywords: Foreign Aid, Economic Growth, Afghanistan

1. Introduction

To attain an enhanced quality of life, global economies, regardless of their development status, must establish a stable economic framework. This necessitates the implementation of good economic policies by the respective governments. A lot of countries can't meet their development and non-development spending obligations because they don't have enough money in their budgets. Because of this, they depend on money from outside sources, like loans, grants, and foreign aid from the ADB, WB, IMF and other countries that are part of the Development Assistance Committee. Afghanistan, situated in Central Asia, is a landlocked nation. The area possesses an abundance of human and natural resources. As per the National Statistics and Information Authority (NSIA, 2019), 27.5 million individuals, or 63.7%, of the nation's populace is classified as youthful. As a consequence of the ongoing political instability and military conflict, the nation is unable to effectively employ these resources. At the present time, Afghanistan is confronted with the challenges of attaining economic expansion, mitigating destitution, and curbing unemployment. Afghanistan's agricultural sector employs approximately 61.6% of the labor force and provides sustenance for approximately 70% of the population (Muradi and Boz, 2018). The country is classified as a low-income nation and faces significant obstacles, including but not limited to political instability, insufficient industrial development, ineffective governance and law enforcement, high crime rates, corruption, and insecurity (Nijssen, 2010). In the aftermath of the September 11th attacks on the World Trade Center, an offensive was initiated by the United States and its allies against Afghanistan, which ultimately led to the Taliban regime being overthrown. This marked the beginning of a process to rebuild Afghanistan, with the support and financial aid from the international community. Various sectors of the economy received technical assistance and foreign aid to facilitate this rehabilitation. Following a period of forty years of devastating conflict, Afghanistan has become reliant on

foreign aid. In order to facilitate its reconstruction, the country has received a substantial amount of financial assistance from international financial institutions and donor countries associated with the Development Assistance Committees. According to OECD data, Afghanistan was listed as the highest beneficiary of Official Development Assistance (ODA) in the world in 2011, receiving 5% of the total global ODA. Since 2002, the United States has been the main source of economic growth and reconstruction aid for Afghanistan, contributing one-third of the overall assistance. Additional notable contributors comprise Japan, the United Kingdom, the European Commission, Germany, the World Bank, and Canada (Fayez, 2012).

Regrettably, Despite receiving foreign aid and economic help from several donor countries for over two decades, Afghanistan continues to depend on foreign aid. Approximately 40% of government expenditures are currently funded by these foreign nations. Simultaneously, the provision of foreign aid and economic support facilitated the growth of several sectors within the Afghan economy, resulting in a significant increase in GDP per capita from \$100 in 2001 to \$750 in 2012. Based on the 2014 report from the ministry of finance, the percentage of multidimensional poverty declined from 93.2 percent in 2007 to 77.1 percent in 2012. In order to sustain its official services, the Afghan government currently need 40% of international assistance annually (Cooper, 2018).

Problem Statement

Comprehensive research examining the relationship between, Economic development and foreign aid moreover the factors that influence economic growth, including remittances and domestic investment, is scarce in Afghanistan, relative to other nations. Determining the characteristics, significance, cointegration, and immediate correlation between foreign aid and Afghanistan's economic development using time-series data spanning 2001 to 2020, this study seeks to fill this research void.

Objectives of the Study

The research aims to achieve four principal objectives. The principal aim of this study is to examine the correlation between foreign aid and Afghanistan's economic development, taking into account the dynamics of the short and long term. Furthermore, the aim of this study is to analyze the attributes, significance, immediate and long-term correlations, and reciprocal associations between the expansion of the Afghan economy and the elements that contribute to it, including domestic investment, remittances, and employment rates. Moreover, the objective of this research is to clarify the impact that terrorism has had on the economic progress of Afghanistan.

1.3 Hypothesis

H01: There is no evidence of a long-term relationship between foreign aid and the economic progress of Afghanistan.

H02: There is no evidence of a long-term relationship between remittances and the economic progress of Afghanistan.

H03: There is no evidence of a long-term relationship between domestic investment and the economic growth of Afghanistan.

H04: There is no evidence of a long-term relationship between the employment level and economic growth of Afghanistan.

H05: The impact of terrorism on the economic growth of Afghanistan is negligible.

2. Literature Review

2.1 Foreign Aid and Economic Growth:

The relationship between foreign aid, investment, and economic growth was investigated in six of the poorest African nations. The study's conclusions showed that there was cointegration—a positive and statistically significant relationship—between these factors. With the exception of Niger, the connection was discovered to be negligible in the near term (Mallik, 2008). Similarly, ARDL and ECM methods were used in a Nigerian study to look into the connection between foreign aid and economic growth. Positive and statistically significant cointegration between the two variables was discovered by the study (Babalola et al., 2019). A study conducted in Nepal looked at the cointegration of economic growth and foreign aid. Due to the result, which were supported by favorable policy environments, foreign aid was shown to be highly beneficial when these variables were statistically significant and positively correlated (B. P. Bhattarai, 2009). A study that used the cointegration approach together with aid-growth and aid-fiscal models looked at how foreign aid influences economic expansion in Bangladesh. The analysis found that, in contrast to grants, which showed no such

relationship, loans from ODA were directly and significantly associated with economic development. The study also discovered that loans supported public investment projects and the development of human capital, which increased output, while grants were utilized to fund ineffective civil activities (Quazi, 2005). Using cointegration and ECM methods, a Tanzanian study found that foreign aid inflows enhanced productive investment, which in turn produced a positive rise in supply (Nyoni, 1998). ODA and economic growth have a favorable and statistically significant association, according to another Tanzanian study (Rotarou and Ueta, 2009). Studies carried out in emerging nations revealed a statistically significant and affirmative correlation between foreign assistance and economic expansion. Numerous facets of economic growth were assessed, such as the contribution of agriculture, value addition, economic conversion, infant mortality rate, social welfare indicators, human and physical capital, and poverty reduction. According to the study's findings, foreign aid significantly influenced structural changes, enhanced economic growth, decreased poverty, and improved social indicators in developing nations over the last 40 years (Arndt, Jones, and Tarp, 2015). A study conducted in 2006 in developing nations also discovered a statistically significant and positive correlation between economic growth and foreign help. Specifically, an increase of one percent in foreign aid was found to result in a 14 to 26 percent rise in the per capita growth rate.

Using production theory and the efficiency index, a thorough investigation into the relationship between foreign help and economic growth in sixty nations looked at the effectiveness of the aid. Due to the finding, Pakistan, India, and Indonesia had the lowest efficiency values among the sixty countries, while China and Nigeria showed the highest levels of efficiency. Additionally, the study discovered a favorable correlation between the degree of production or efficiency and capital-intensive nations. **Bad Connection Relationship between Economic Growth and Foreign Aid**

Foreign aid and economic growth in Cambodia have a negative cointegration connection (Sothan, 2018). In a similar vein, study conducted in Ethiopia also found a strong and negative correlation between foreign aid and economic growth. To examine this link, researchers employed ARDL and ECM (Belay Asfaw and Girma Gezmu, 2021). Similarly, a study conducted in Morocco to determine the cointegration and short-run correlation between foreign aid and economic growth came to the conclusion that there is a negative cointegration association between ODA and economic growth and that foreign aid promotes economic growth because it raises the government's level of consumption (Aghoutane and Karim, 2017). In a similar vein, foreign aid in Nigeria has a long-term, substantial negative correlation with both economic growth and HDI. Additionally, research indicates that foreign aid has a notable and positive impact on Nigeria's economic growth in the short term (Offiong et al., 2020).

According to a study conducted in African nations, foreign aid is inefficient both in the long and short terms, suggesting that it doesn't support the economic development of these nations (Yahyaoui and Bouchoucha, 2020). Similar to the previous study, which looked at the relationship between economic growth and foreign aid in Sri Lanka and India, this one found that although foreign aid has no significant correlation with economic growth in Sri Lanka, it is cointegrated with domestic investment, trade, and economic growth in India (Sethi, Bhujabal, Das, and Sucharita, 2019). Additionally, a study conducted in 95 developing countries discovered a strong and negative correlation between official development assistance and economic growth (Yiew and Lau, 2018).

Remittance & Economic Growth

A study indicated that remittances have a statistically significant and favorable effect on economic growth in thirty-six African countries. According to studies, remittances can help developing economies overcome their cash constraints and provide an alternative source of funding for investments (Fayissa and Nsiah, 2010).

In a similar vein, research carried out in seven CEE nations found a positive and significant correlation between FDI and remittances and the economic growth of these countries (Comes, Bunduchi, Vasile, and Stefan, 2018).

In addition, a different study examined how remittances affected four South Asian nations. It was found that there is a negative correlation between remittances and economic growth in Pakistan, Bangladesh, and Sri Lanka. Remittances were discovered to be statistically significant and favorably correlated with economic growth in India, however. Furthermore, the combined results show that remittances have a negligible and unfavorable relationship with the overall economic growth of these four South Asian nations (Sutradhar, 2020).

Domestic Investment and Economic Growth

A research study conducted in Pakistan revealed a strong positive and statistically significant cointegration between domestic investment and economic growth (Rahman and Ferdaus, 2021). In a similar vein, research conducted in Vietnam revealed a strong correlation between domestic investment and economic growth (Tran and Hoang, 2019). Emeka, Odo, Idenyi, and Nweze (2017) conducted a study to further explore this link and found cointegration and a substantial correlation between domestic investment and economic development. Growth in the Economy and Employment Level

A study looked at the connection between Bangladesh's economic growth and labor force participation. The study found that there is a substantial long-term correlation between these variables, showing that they are favorably and considerably cointegrated. Furthermore, the research discovered evidence of a correlation between economic growth and labor force participation in the near term (Haque, Kibria, Selim, and Smrity, 2019).

3. Research Methodology

Theoretical framework is utilized in this section to examine the link among variables of the investigation. The paper provides a concise description of the diagrammatical representation, empirical model, data sources, variables, and estimation methodologies used.

3.1 Theoretical Framework

According to the research, there are two types of relationships observed between foreign aid and economic growth in emerging and established economies, particularly in nations located in South Asia, Africa, and Europe. Some research indicate a positive correlation between these characteristics, while others show a negative association.

Empirical studies indicate that foreign aid has a significant and favorable effect on the economic growth of Nigeria (Offiong et al., 2020). Furthermore, a distinct investigation carried out in South Asian nations unveiled a favorable and statistically substantial association between economic expansion and foreign assistance in these economies (Jena and Sethi, 2020). In his study, Husein (2019) discovered that foreign aid has a positive and statistically significant impact on the economic growth of Jordan. Furthermore, a further investigation revealed a significant and favorable association between Economic Growth and foreign aid in forty-seven African nations (Adedokun, 2017).

Arndt, Jones, and Tarp (2015) discovered a robust and positive association between foreign aid and economic growth in impoverished countries. Furthermore, foreign aid plays a crucial role in fostering Structural Changes and effectively reducing poverty in the long run. Anyieni (2014) conducted a study in Kenya that revealed a notable and straightforward relationship between foreign aid and economic growth. A study conducted by Museru, Toerien, and Gossel (2014) discovered a statistically significant and positive correlation between the amount of foreign aid received by twenty-six Sub-Saharan economies and their level of economic growth.

The study investigated the existence of a statistically significant and positive cointegration relationship between foreign aid and economic growth. Foreign assistance has a greater effect when there is a conducive policy framework (B. P. Bhattarai, 2009). Similarly, African countries exhibit a cointegration between economic growth and foreign investment, with a positive and statistically significant association (Mallik, 2008).

As to the findings of Belay Asfaw and Girma Gezmu (2021), the literature suggests a strong negative correlation between foreign aid and economic growth in Ethiopia. Babalola, Mohd, Ehigiamusoe, and Onikola (2019) did a study which revealed that foreign aid had a significant and negative effect on the economic growth of sixteen western economies. In their study, Aghoutane and Karim (2017) discovered that in Morocco, there exists a cointegration and short-term relationship between Foreign-aid and Economic growth. Furthermore, it was found that the correlation between ODA and economic growth is negative and has a high level of statistical significance.

Furthermore, in Vietnam, there exists a statistically substantial and unfavorable correlation between foreign assistance and economic growth. Furthermore, there is compelling evidence indicating that aid has been utilized in an inefficient manner and that corruption is prevalent within the government (N. Quy, 2016). According to Abd El Hamid's 2013 research In Egypt, there exist both short-term and cointegration phenomena. The relationship between foreign aid and economic growth exhibits a negative and statistically significant correlation. The scholarly literature, namely the research conducted by Yahyaoui and Bouchoucha (2020), presents empirical evidence indicating that foreign aid does not have any noticeable impact on the economic advancement of African nations, neither in the immediate nor in the extended period. While there is no evident correlation between foreign aid and economic growth in Sri Lanka, a study conducted by Sethi, Bhujabal, Das,

and Sucharita (2019) discovered that foreign aid, domestic investment, and economic growth are cointegrated in India. Furthermore, empirical research indicates a statistically significant and positive relationship between remittances and economic growth in India. Conversely, there is a negative link between remittances and growth in Bangladesh, Sri Lanka, and Pakistan. Similarly, the research carried out by Comes, Bunduchi, Vasile, and Stefan (2018) uncovered a robust and statistically significant correlation between remittances and economic expansion in the Central and Eastern European regions. Rahman and Ferdaus (2021) have discovered additional evidence indicating a robust and statistically significant correlation between domestic investment and economic growth. Tran and Hoang (2019) have said that there is a positive correlation between Vietnam's economic growth and domestic investment. In 2019, Haque, Kibria, Selim, and Smrity conducted a study which revealed a robust and statistically significant correlation between the labor force and economic growth in Bangladesh. This association holds true in both the short term and the long term.

in equation 1.

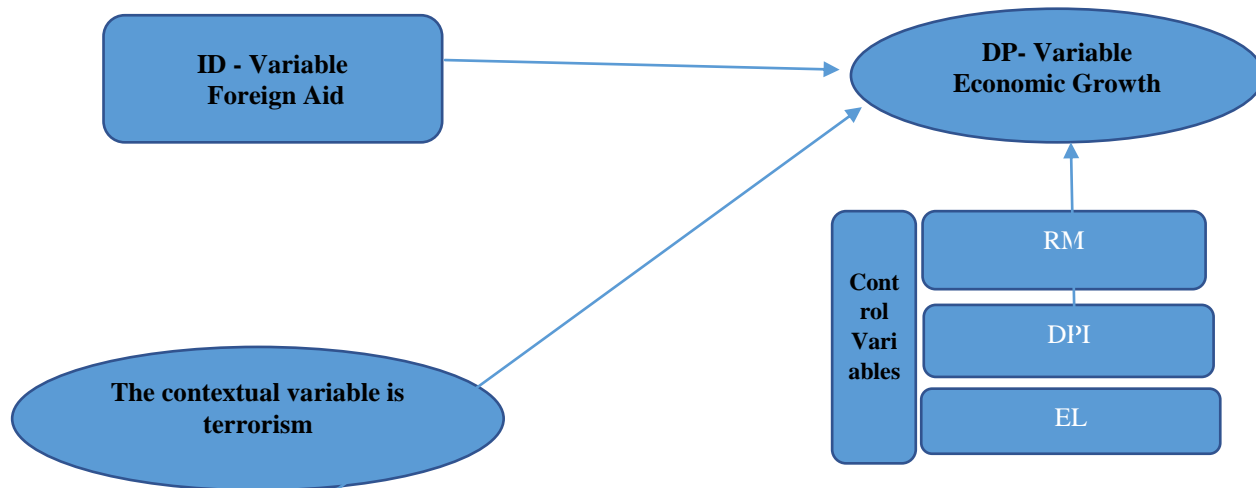
GDP Growth Rate

$$= f(\text{Foreign Aid, Remittances, Labor force Particapation, Domestic Investment, Terrorism}) \dots (1)$$

The GDP growth rate is the dependent variable in equation (1), and the control variables are domestic investment, labor force participation, remittances, and foreign aid. Conversely, terrorism is employed as a contextual variable. Although they are not the primary subject of the study, control variables are included in the equation since they may have an impact on the results. To determine how these variables affect the dependent variable, they are controlled. Terrorism is one example of a contextual variable that sheds light on the social and cultural context of the relationship under study. They aid in offering a more thorough comprehension of the setting in which the variables function.

3.2 Diagrammatical Representation

The relationship between Afghanistan's economic expansion and foreign aid from donor nations and international financial institutions, including the World Bank, International Monetary Fund, European Union, and others, is depicted in Figure 3.1. Control variables in the study include labor force participation rate, domestic investment or investment in capital goods, and remittances. Furthermore, it is thought that terrorism is a context-specific variable that is very important to comprehend in order to comprehend its influence on Afghanistan's economic development.



Diagrammatical Representation (Figure 3.1)

3.3 Empirical Models

Equation 1 shows the link between the primary independent variable, foreign aid, and the dependent variable, GDP growth rate. As additional control variables, there are remittances, gross domestic investment, and employment level. In addition, the study takes into account terrorism in Afghanistan as a contextual variable.

$$GDPR_t = \alpha_0 + \alpha_1 FA_t + \alpha_2 RM_t + \alpha_3 GDI_t + \alpha_4 EL + \alpha_5 TM_t + \epsilon_t \dots \dots \dots (1)$$

Table 3.2:

| Variables Symbols utilized for the study's factors | Symbols |
|-----------------------------------------------------------|----------------|
| The GDP growth rate, or gross domestic product | GDPR |
| Foreign AID | FA |
| Percentage of remittances to GDP | RM |
| Investing domestically and in capital assets or goods | DI |
| Employment Level | EL |
| Terrorism | |

3.5 Sources of Data and Variables

Series of time data covering the years 2001 to 2020 have been used to investigate the nature and relevance of the relationship between foreign aid and Afghanistan's economic growth. This association has been estimated using time series analysis. The WDI (world development indicator) database included the information for the dependent variable (economic growth), independent variable (foreign aid), control variables, and contextual variables for the year 2020.

3.5.1 Economic Growth (GDP GR)

The GDP growth rate is used as a metric to measure economic growth in order to investigate the relationship between economic growth and foreign aid. Economic growth, according to McConnell Brue (1996), is the gradual rise in real GDP. Similar to this, Awan and Moeen-ud-Din (2015) point out that GDP is frequently employed to gauge a nation's revenue and output at the national level.

3.5.2 Foreign Aid (FA)

The term "foreign aid" describes the monetary resources given to recipient countries by foreign governments, businesses, or people. It can come in many forms, including grants of different kinds, project support, technical assistance, commodities assistance, and food aid. Further classified as forms of aid that support a nation's economic development include capital flow assistance and humanitarian aid (Pohwani, Khoso, & Ahmed, 2019). The goals of these various aid programs are to promote and strengthen the recipient countries' economic development.

3.5.3 RM: Remittances

The money transmission from foreign workers to their family members back home is known as remittances. They represent a considerable financial transfer from developed to poor countries. Remittances are defined by the International Monetary Fund (IMF) as the money that overseas workers who have been living abroad for more than a year send home. These transactions are tracked in the Balance of Payments (BOP). Likewise, research by Alfieri, Havinga, and Hvidsten (2005) indicates that remittances are viewed as a reliable source of income for households in poor nations and play a critical role in providing that income.

3.5.4 DI: Domestic Investment

The fundamental aim of all economies, regardless of their development status, is to achieve stable and sustainable economic growth in the production of goods and services. This objective can be realized through investments made by private entities, domestic entities, and the government within an economy. Investment can be understood as the foregone consumption or an increase in the capital stock, as described by Andrew B and Ben S (2011).

3.5.5 EL: Employment Level

due to the definition provided by the International Labor Organization, the labor force in an economy consists of people who are employed as well as those who are not. The percentage of persons who are actively employed in an economy indicates the amount of employment in that sector. According to research by Sodipe and Ogunrinola (2011), employment in Nigeria and economic growth have a positive and significant association. Nevertheless, they also discover a negative correlation between the nation's GDP growth rate and employment growth rate.

3.6 Estimation Techniques

Two commonly applied techniques for finding cointegration and short-run relationships are the Johansen Cointegration technique and the Autoregressive Distributed Lag (ARDL) model with Error Correction Mechanism (ECM). The Johansen Cointegration technique is employed when all variables in the model exhibit

stationarity at the same level. This technique is suitable for analyzing relationships among variables that share the same order of integration. On the other hand, the ARDL model with ECM is utilized when the variables in the model are integrated at different levels. This approach allows for the analysis of relationships between variables that exhibit different orders of integration. The choice between these techniques depends on the stationarity characteristics of the variables involved in the analysis, ensuring that the appropriate method is selected to accurately capture the relationships of interest.

3.6.1 The Augmented Dickey-Fuller Test of Stationarity:

An often-used test to address non-stationarity in time-series data is the Augmented Dickey-Fuller (ADF) test. One typical issue that compromises the validity of regression results in time-series analysis is non-stationarity. By comparing the null hypothesis with the alternative hypothesis of stationarity, the ADF test assists in determining whether a variable is non-stationary. The Autoregressive Distributed Lag (ARDL) technique is used when the ADF test indicates a mixed order of stationarity, meaning that some variables are stationary at the level and others at the difference. The ARDL model is suitable for analyzing relationships between variables exhibiting different orders of integration, allowing for a more accurate analysis in such cases. By utilizing the ADF test to identify stationarity characteristics, researchers can determine whether to utilize the ARDL technique to account for mixed order stationarity in their analysis.

3.6.2 Autoregressive Distributive Lags Model

The ARDL model is used to examine both long and short-term relationships between variables, particularly when there are differences in the order of integration or stationarity among the variables. In this study, certain variables exhibit stationarity at the first difference while others are stationary at the level.

3.6.3 ARDL Cointegration Bound Test

The presence of cointegration between the variables in the model is ascertained using the ARDL bounds test. When the F-statistics value above the upper critical bound value (IO), it signifies cointegration between the variables. The outcome is not conclusive if the F-statistics value lies between the upper and lower critical boundaries. Conversely, if the F-statistics value is less than the lower critical constraint, it implies that the variables are not cointegrated. Based on these crucial bound values, the ARDL bounds test aids researchers in evaluating the cointegration connection between the variables.

3.6.4 Serial Correlation Test

A serial correlation test is used to determine if the error term and associated lag values exhibit autocorrelation. The null hypothesis is rejected if the likelihood related to the F-statistics is less than the five percent significance level. This suggests that autocorrelation among the variables is present and supports the alternative hypothesis of autocorrelation. On the other hand, the null hypothesis of autocorrelation among the variables is accepted, indicating no substantial autocorrelation, if the probability associated with the F-statistics is greater than the 5 percent significance level. Researchers can assess if autocorrelation is present and how it affects the model's output by using the serial correlation test.

3.6.5 Test for Normality

The normality of residuals is evaluated using the Jarque-Bera test. The null hypothesis is rejected if the Jarque-Bera probability is less than the five percent significance level, assuming that the residuals are normally distributed. The alternative hypothesis is accepted in this instance, suggesting that the residual distribution is not normal. On the other hand, the null hypothesis is accepted, indicating that the residuals have a normal distribution, if the Jarque-Bera probability exceeds the five percent significance level. If the residuals in the model satisfy the normalcy assumption, it can be ascertained using the Jarque-Bera test.

3.6.6 Heteroskedasticity Test

Heteroskedasticity tests are conducted to examine the variance and covariance between the residuals and explanatory variables in a model. If the variance of the residuals is constant and there is no covariance, then there is no issue of heteroskedasticity in the variable. Conversely, if the variance of the residuals is not constant and the covariance is not zero, it indicates the presence of heteroskedasticity in the data. Heteroskedasticity tests help identify whether there are variations in the error term that violate the assumption of constant variance in the model.

3.6.7 The model's Stability Test

Two tests, namely the CUMSUM test and the CUMSUM of squares test, are conducted to assess the stability of the used model. These tests compare the alternative hypothesis, which suggests instability, against the null hypothesis, which assumes that the model is stable. By analyzing the results of these tests, researchers can determine whether the model exhibits stability or not.

4. Discussion & Results

This section provides a concise overview of the projected outcomes of the study's model. The estimate process encompasses the description and stationarity analysis of the data, examination of correlations among the variables in the study, estimating of results, doing cointegration bound tests, analyzing short and long-term relationships, assessing stability, and performing diagnostic tests.

4.2 The Table show Descriptive Statistics, Table 4.1 The Table show Descriptive Statistics

| | GDP Growth Rate | Foreign Aid | Employment Level | Remittance Percentage | GDI | TM |
|--------------------|------------------------|--------------------|-------------------------|------------------------------|------------|-----------|
| Mean | 8.813 | 137.441 | 47.123 | 2.135 | 17.806 | 8.033 |
| Median | 3.912 | 112.624 | 48.160 | 2.184 | 17.809 | 8.250 |
| Maximum | 76.000 | 311.871 | 47.600 | 3.637 | 26.408 | 9.600 |
| Minimum | -6.800 | 7.43 | 47.060 | 0.886 | 12.557 | 5.700 |
| Std. Dev. | 15.945 | 73.622 | 0.425 | 0.868 | 3.180 | 1.393 |
| Skewness | 2.867 | -0.071 | -0.326 | -0.003 | 0.672 | -0.415 |
| Kurtosis | 11.826 | 2.301 | 3.323 | 1.612 | 4.235 | 1.707 |
| Jarque-Bera | 97.983 | 0.445 | 0.466 | 1.682 | 2.918 | 2.066 |
| Probability | 0.000 | 0.801 | 0.791 | 0.432 | 0.231 | 0.355 |

The GDP growth rate in Table 4.1 above has a mean value of 8.813, a maximum value of 76.00, and a lowest value of -6.800. In a similar vein, the data on the economic growth rate exhibit a normal distribution with a Jarque-Bera value of 97.98 and a standard deviation of 15.945, both of which indicate a positively skewed and leptokurtic (Peaked Curve) distribution. Comparably, the average amount of foreign aid is 137.441, with standard deviation of 73.622 and minimum and maximum values of 7.43 and 311.871, respectively. Additionally, the data for this variable exhibits a negative platykurtic skewness (Jarque-Bera 0.446) and is not regularly distributed (Flatted Curve). Once more, the employment level or labor force participation rate has a mean value of 47.123, a maximum value of 48.90, and a lowest value of 47.06. In accordance, the data on employment level is not distributed regularly, as indicated by the correspondingly high standard deviation of 0.425 and leptokurtic (Peaked Curve) value of 0.467 for the Jarque-Bera. Likewise, RM has a mean value of 2.135, a maximum and minimum value of 3.637 and 223.98, respectively, and a standard deviation of 0.868. It exhibits a negative skewness and is platykurtic (Flatted Curve). Jarque-Bera 1.683 indicates that the data distribution for this variable is not normally distributed. In a similar vein, the gross domestic investment mean value is 17.806, with a standard deviation of 3.180 and minimum and highest values of 12.557 and 26.408, respectively. It is platykurtic and positively skewed; the Jarque-Bera value of 2.919 indicates that it is not normally distributed. The independent variable TM has a mean value of 8.033, a maximum value of 9.60, a minimum value of 5.700, and a standard deviation of 1.393. Moreover, the data of the Terrorism Index is not normally distributed, as indicated by the Jarque-Bera value of 2.067 and the fact that it is positively skewed and leptokurtic (Peaked Curve).

4.3 Correlation

The strength of the association between two variables is measured by this standardized form of covariance, which has a value range of -1.0 to + 1.0. fully positive and fully negative correlations are shown by the values + 1.0 and -1.0, respectively. If there is no linear relationship between the variables, the correlation value is 0.0. Table 4.2: Matrix of Ordinary Correlation

| Correlation | GDP Growth Rate | Foreign AID | Emplment Level | Remittance | GDI | TM |
|------------------------|------------------------|--------------------|-----------------------|-------------------|------------|-----------|
| <i>GDP Growth Rate</i> | 1.100 | | | | | |
| Foreign AID | 0.054 | 1.000 | | | | |

| | | | | | | |
|--------------------|--------|--------|--------|--------|-------|-------|
| Empolymen Level | 0.037 | -0.173 | 1.000 | | | |
| RM | 0.335 | -0.046 | -0.211 | 1.000 | | |
| GDI | -0.228 | 0.316 | 0.244 | 0.023 | 1.000 | |
| TM | -0.342 | 0.488 | 0.177 | -0.725 | 0.235 | 1.000 |

The ordinary correlation between the study's variables is shown in table 4.2 above. The GDP growth rate and foreign aid have a positive association, indicating that increased foreign aid also contributes to higher rates of economic growth. Current research indicates a negative relationship between GDP growth rate, terrorism, and gross domestic investment. In a similar vein, remittances, employment, and economic growth are all positively correlated.

Additionally, extant literature indicates a negative correlation between foreign aid, employment level, and remittances, but a favorable correlation between foreign aid and domestic investment. Existing research indicates a negative correlation between employment level and remittances, but a positive correlation between employment level, gross domestic investment, and terrorism. There is a positive and negative association, respectively, between remittances and gross domestic investment and terrorism. Contrary to previous research, there is a positive correlation between gross domestic investment and terrorism.

4.4 Testing of Stationarity Table 4.3 Test for Stationarity

| Variables | ADF Test | | | | | | Order of integration |
|------------|------------|---------------------|--------------------------|-------------------------------|---------------------|--------------------------|----------------------|
| | At level | | | At 1 st difference | | | |
| | Intercepts | Trends & Intercepts | No trends, No intercepts | Intercepts | Trends & Intercepts | No trends, No intercepts | |
| GDPR | -4.024*** | -5.412*** | -3.519*** | -12.132 | -11.726 | -11.518 | I (0) |
| Foreign A | -2.531 | -1.125 | -0.0712 | -1.495 | -4.755*** | -1.701 | I (1) |
| EmploymL | -3.132** | -2.641 | -0.351 | -0.557 | -0.364 | -1.020 | I (0) |
| Remittance | -1.732 | -3.316 | -1.244 | 5.629*** | 5.612*** | -5.559*** | I (1) |
| GDI | -3.558** | -3.558 | 0.0075 | 3.568*** | 3.403*** | -3.671*** | I (1) |
| TM | -3.321** | -0.035 | 1.564 | -2.161 | 4.476*** | -2.122** | I (1) |

Note: ***, ** & * show level of significance at 1, 5, and 10 percent, respectively.

4.5 Estimation Results

The Augmented Dickey-Fuller test results are presented in Table 4.4 above. It functions to ascertain the stationarity of the variables under investigation. Terrorism, foreign aid, remittances, and gross domestic investment are initial stationarities; however, the level of employment and the rate of GDP growth are constant stationarities. Certain variables are stationar at the first difference, whereas others are stationar at the level, as demonstrated by the ADF's conclusion. The Autoregressive Distributive Lag model will be utilized in lieu of the conventional Johnson cointegration test for this thesis due to the ambiguity surrounding the order of stationarity.

4.5.1 The Criteria for Model Selection Table 4.4 VAR Lag Order Selection Criteria

| Lags | LogL | LR | FPE | AIC | SIC | HIC |
|------|-----------|-----------|-----------|-----------|-----------|-----------|
| 0 | -180.8410 | NA | 713019.5 | 18.28410 | 18.38367 | 18.3054 |
| 1 | -181.4878 | 31.90036* | 185885.8* | 18.74878* | 17.04750* | 18.80710* |

The VAR model's results are displayed in table 4.4 above, and it is these data that will be used to determine the ideal lag length for the model. The least value serves as the criterion for the ideal model. The aforementioned table indicates that AIC has a minimum value, is chosen by EVIEWS as a model selection criterion automatically, and recommends a maximum of 1 lag for the model.

4.5.2 ARDL Bound Test for Cointegration Table 4.5 ARDL Bound Test

| T- Statistics | Value | No of Parameters (K) |
|------------------------------|----------|----------------------|
| F-Statistic | 9.420845 | 5 |
| Critical Value of Bound Test | | |
| Significance Level | I0 Bound | I1 Bound |
| 10 % | 2.36 | 3.25 |
| 5 % | 2.72 | 3.69 |
| 2.5 % | 2.86 | 4.28 |
| 1 % | 3.11 | 4.78 |

The F statistic's estimated value, 9.420845, is shown in Table 4.6 above. This result is higher than the upper bound's critical values at the One, Five, and Ten percent significance levels, indicating that the cointegration of Afghanistan's economic growth and foreign aid is approved.

4.5.3 Long-Run Results Table 4.5 Long-Run Coefficients

| Variables | Long Run Coefficients | | | |
|------------------|-----------------------|-----------------|-----------------|---------------|
| | Coefficients | Standard Error | t-Statistics | Probabilities |
| Foreign AID | 0.454510 | 0.148855 | 2.131650 | 0.0597 |
| Remittance | -34.168430 | 17.461922 | -1.804917 | 0.0759 |
| GDI | 4.122392 | 2.574136 | 1.404184 | 0.1534 |
| Employment level | 4.372540 | 7.364109 | 0.499206 | 0.4624 |
| TM | -31.029266 | 12.702764 | -2.137431 | 0.0515 |
| C | 27.722199 | 356.358634 | 0.088399 | 0.8391 |

The long-run relationship finding, the variable coefficients, and the corresponding standard errors, t-statistics, and probabilities are shown in table 4.5 above. The results show a favorable and significant long-term relationship between foreign aid and Afghanistan's economic growth. The coefficient of FA is 0.454510, meaning that for every 1% rise in foreign aid, Afghanistan's economic development will increase by 0.35 percent. Similarly, there is a positive and strong correlation between foreign aid and economic growth, according to the results above. The fact that during this time, infrastructure was developed, the majority of people were employed, investment increased, and more than five million people returned to Afghanistan with new skills is what accounts for the positive and significant relationship between the aid given and the country's economic growth.

The findings of Babalola et al. (2019), who also looked at the statistically significant and positive cointegration between foreign aid and economic growth in Nigeria, are consistent with this empirical outcome. In a similar vein, there is a positive but negligible relationship between employment level, GDP, and economic growth. The null hypothesis of an insignificant association is accepted in light of the aforementioned outcome. The coefficients for GDI and EL are 4.122392 and 4.372540, respectively, showing that a one percent rise in GDI and EL employment levels will result in increases in Afghanistan's economic growth of 4.02 percent and 4.47 percent, respectively.

The aforementioned weak correlation between employment, domestic investment, and economic growth results from Afghanistan's underwhelming domestic investment and covert unemployment, which forces people to work in unskilled positions such as managers despite having graduated from medical school and agriculture schools. There is a favorable correlation between Bangladesh's economic growth and (Haque et al., 2019). Similarly, domestic investment in Pakistan and Vietnam has a good long-term relationship with the economies of both countries, according to Rahman and Ferdous (2021) and Tran and Hoang (2019).

Remittances also bear a weak and unfavorable correlation with Afghanistan's economic expansion. The reason for the aforementioned link is because remittances are not adequately utilized in Afghanistan and are instead spent for consumption; they would be more successful if they were used for small businesses that generate revenue. The aforementioned outcome is consistent with the findings of Sutradhar (2020), who found that remittances had a negligible and insignificant relationship with economic growth in both Pakistan and Sri Lanka.

The findings above indicate a negative and substantial relationship between terrorism and economic growth. The coefficient of terrorism is -32.02, meaning that a one percent increase in TM will eventually result in a 32.02 percent decline in Afghanistan's economic growth. Without a question, during the past forty years, terrorism has had a significant negative impact on Afghanistan. It has changed investment patterns and

redirected governmental and private resources from beneficial endeavors to defensive measures. Put simply, terrorism diminishes Afghanistan's economic potential and destroys capital. The outcome is consistent with the findings of Saleem et al. (2020), who discovered a statistically significant negative relationship between economic growth and terrorism in South Asian nations. Likewise, (Zakaria et al., 2019) discovered a long-term, substantial, and adverse relationship between terrorism and economic expansion.

4.5.4 Short-Run Relationship Table 4.7 Cointegrating form, selected ARDL model (2, 4)

| Variables | Cointegration Form | | | |
|-------------|--------------------|----------------|--------------|---------------|
| | Coefficients | Standard Error | t-Statistics | Probabilities |
| D(FA) | 0.379802 | 0.088679 | 3.456241 | 0.0062 |
| D(RM) | -7.397407 | 4.651922 | -1.435675 | 0.1656 |
| D(GDI) | 1.197811 | 1.286445 | 0.756732 | 0.5117 |
| D(EL) | 3.430017 | 5.808811 | 0.497416 | 0.5535 |
| D(TM) | -112.369037 | 23.684120 | -4.247162 | 0.0020 |
| CointEq(-1) | -0.889265 | 0.217186 | -3.709446 | 0.0034 |

The short-run correlation result between foreign aid and Afghanistan's economic growth is shown in Table 4.7 above. The standard errors, probabilities, t-statistics, and variable coefficients are shown in the above table. The coefficient of foreign aid is 0.379, meaning that a one percent increase in foreign aid will result in a 0.379 percent short-term rise in Afghanistan's economic development.

The fact that during this time, infrastructure was developed, the majority of people were employed, investment increased in comparison to previous years, and more than five million people returned to Afghanistan with new skills is what accounts for the positive and significant relationship between the aid given and the country's economic growth. This finding is consistent with that of Jena and Sethi (2020), who also discovered a short-term positive correlation between foreign aid and the economic expansion of South Asian nations.

Moreover, there is a positive but negligible relationship between employment level, GDP, and GDP growth. The coefficients for GDI and EL show that increases of one percent in each will result in increases of 1.18 and 3.53 percent, respectively, in Afghanistan's economic growth. The aforementioned tenuous correlation among employment, domestic investment, and economic growth can be attributed to Afghanistan's low level of domestic investment and covert unemployment, which forces people to work in occupations unrelated to their areas of expertise, such as managers despite having degrees in agriculture and medicine. The outcome is consistent with the findings of Haque et al. (2019), who found that employment levels and economic growth in Bangladesh had a favorable short-term relationship. There is a weak and negative correlation between remittances and Afghanistan's economic growth. The coefficient of remittance is -7.29, meaning that if remittances rise by 1% in the near term, economic growth will fall by 7.296 percent. Remittances and economic growth have a negative link since they are incorrectly used in Afghanistan and are consumed there rather than being used for revenue-generating activities like small businesses, which would be more beneficial.

The aforementioned result supports the findings of (Awad & Sirag, 2018), who determined that there is no substantial negative relationship between remittances and economic growth in Sudan. It also implies that international remittances will be more effective if they are channeled appropriately. Additionally, (Sutradhar, 2020) found that remittances from Pakistan and Sri Lanka had a short-term negative impact on economic growth.

Comparably, the coefficient of terrorism is -102.36, indicating that TM has a negative and substantial impact on Afghanistan's economic expansion. Terrorism has had a significant negative impact on Afghanistan during the past forty years. It has changed investment patterns and redirected public and private resources from constructive endeavors to defensive measures. Put simply, terrorism both short- and long-term destroys capital and diminishes Afghanistan's economic potential. Saleem et al. (2020) found a negative and significant short-term relationship between economic growth and terrorism in SACs, which lends validity to these findings. CoinEq (-1) has a negative and highly significant coefficient of -0.789265. This demonstrates that any short-term shock will eventually adjust at a rate of 78%.

4.6 Residual Diagnostic Tests

For reliability of the results, we use the following diagnostic tests.4.6.1Serial Correlation TestTable 4.8 Breusch Godfrey Test of Correlation

| Result of Breusch Godfrey Test | | | |
|--------------------------------|----------|----------------------------------|--------|
| F-Statistics | 0.778293 | Prob. F(2,7) | 0.4912 |
| Obs*R-squared | 3.225017 | Probability Chi-Square(2) | 0.2096 |

The outcome of the Breusch-Godfrey autocorrelation test is shown in table 4.7 above. The outcome demonstrates that there is no autocorrelation among the study's variables, with the probability of the F-statistics and Chi-Square being greater than the 0.05 significance level.

4.6.2 Normality Test:

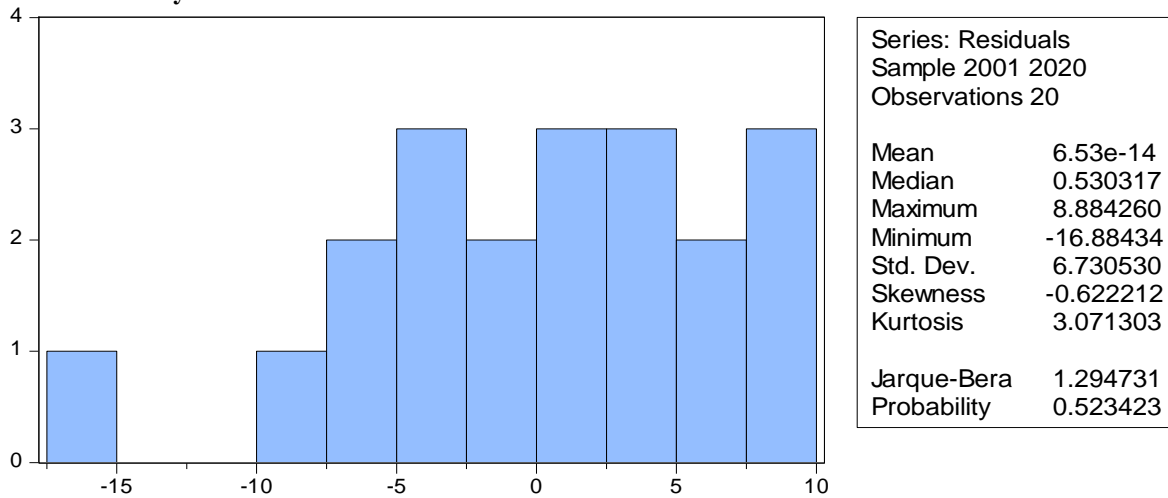


Figure 4.1 Histogram Normality Test

The graphical representation in Figure 4.1 is the outcome of the Jarque-Bera test. The probability of the Jarque-Bera test is 0.523, which exceeds the significance level of 5% and provides confirmation that the data do not follow a normal distribution.4.6.3 The Heteroskedasticity TestTable 4.9 Breusch Pagan Godfrey Heteroskedasticity Test

| | | | |
|-----------------------------|-----------------|------------------------------|---------------|
| F-statistics Values | 0.350922 | Probability of F(7,9) | 0.8150 |
| Obs*R-squared Values | 3.462983 | Prob. Chi-Square(7) | 0.9285 |
| Scaled explained SS | 1.125579 | Probability of Chi-Square(7) | 0.8923 |

Typically, one uses the Breusch-Pagan Godfrey test to examine the heteroskedasticity issue. The criteria for heteroskedasticity states that there is a heteroskedasticity problem in the data if the probability of the F-statistics is less than the 5 percent level of significance; otherwise, there is no heteroskedasticity in the data and the data will be homoscedastic. The results of Breusch Godfrey's test of heteroskedasticity are displayed in Table 4.9 above. They demonstrate that there is no heteroskedasticity in the data because the F-statistics value is greater than the 0.05 significant level.

5. Conclusion

The primary goal of the study is to determine whether foreign aid and Afghanistan's economic growth are cointegrated. In addition, various control variables, such as employment level, remittances, and gross domestic investment, have been looked into. It has been determined that terrorism is a contextual component that significantly affects Afghanistan's economic growth. Annual time-series data from 2000 to 2020 has been included for this purpose.The outcome validates the relationship between foreign assistance and Afghanistan's economic expansion. Both in the short and long term, the coefficient of foreign aid is positive and considerable. In a similar vein, Afghanistan's economic growth is favorably and marginally correlated with gross domestic investment and employment level. However, there is a weak and negative correlation between Afghanistan's economic growth and remittances. Similarly, the outcome demonstrates that terrorism, a contextual variable in

the case of Afghanistan, has a negative and very significant impact on Afghanistan's economic growth **over the long and short terms**

Future Research Work

This study examined the relation between foreign aid and Afghanistan's economic growth; consequently, future research will examine the relation between foreign aid and Afghanistan's economic development.

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