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### IMPACT OF POLITICAL STABILITY ON ECONOMIC GROWTH IN PAKISTAN

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#### Abstract

This paper of research has been investigated to realize the impact of stable politics on the economy. A time series analysis has been done from the era (1996-2020) utilizing data from secondary sources in research report. Political Stability (estimates), Regulatory Quality (estimates) and Voice and Accountability (estimates) are explanatory variables and dependent variable GDP are the variables used in this research. The results signify that regulatory quality has a negative relation with GDP whereas political stability and voice and accountability have a positive relationship with GDP.

#### Keywords

Political unrest, GDP, Political stability



#### 1. Introduction

Economic growth and political stability go hand in hand so that foreign and domestic investors increase investment in a safe environment. This in return increases savings, investment, consumption, and opportunities of earning for people in Pakistan. Due to political stability unemployment and inflation is reduced to great extent as high unemployment and inflation causes rise in political instability which leads to political unrest, strikes against government policies. Political stability is achieved through political rest and good economic performance and by being prominent in the eyes of the public by gaining

their vote. Since the creation of Pakistan, the political scenario of the country has been unstable. In first era of economic planning's witnessed efforts of the government to keep on its toes. As soon after independence Prime Minister Liaquat Ali Khan was assassinated that led to instability. In 1960 according to Akbar Zaidi economic policy is highlighted due to its economic and political effects. From 1960 onwards in Ayub Khan's era major development in the economy too place such as in the agriculture sector land reforms were introduced by Ayub to apply ceiling on land, this helped farmers to measure their land in produce index in units (PIUs). Yahiya Khan imposed martial law in the country. This caused

political disturbance and strong opposition amongst the political parties that increased political instability. Soon after Ayyub's government ended Bhutto became the prime minister and during his reign corruption in the economy reduced. There was currency depreciation under floating exchange rate and devaluation of rupee under fixed exchange rate in Zulfikar Ali Bhutto rule as well as unequal wealth distribution. There was high investment in public sector that led to rapid development in industry. An increase in remittance inflow led to second economic revolution. Pakistan faced a period of recession in Bhutto's era. In Bhutto's government East Pakistan was separated from West Pakistan that led to huge economic loss as many goods were made in East Pakistan that received foreign exchange. Bhutto's policy formation and government had severely negative and permanent consequences for Pakistan's economy. After judicial murder of Z.A Bhutto Zia ul Haq came in to power. Zia ul Haq brought the economy to market in a positive manner. He introduced policy shifts regarding privatization that led to budget surplus, deregulation. This resulted in economic recovery, prosperity and stable prices which made the Zia period a good political stability in history. Pakistan received aid from US as it catered Afghan Refugees due to Soviet Union invasion that led to high population growth. Loans from IMF increased burdening the repayment of previous and current loans. Zia's rule imposed martial law that led to deep damage to society and promoted violence. After end of Zia government Musharraf came into power through martial law. During his reign the war of Kargil was fought. There was military dictatorship in the country. He improved employment by

openness of media, jobs for women increased. After Musharraf, later the PPP ruled the country where economic analysis leading to a regime of Benazir where she was elected as first Muslim women prime minister but soon was assassinated. Zardari came into power to rule the country, inflation was at rise during his rule as well as there was power generation, soon he exchanged frequent government with Nawaz Sharif. Whereas Nawaz Sharif, he strengthened ties with Saudi Arabia, Turkey, China. He took many loans from China and utilized them for infrastructure improvement especially in Punjab District. Nawaz introduced foreign policy schedule that promoted trade liberalization. Nawaz went to exile, his government came to an end as in the next elections PTI Imran Khan's party won elections, PTI took the oath for office of prime minister. Major contribution was made to Pakistan Economy. Relations with Afghanistan, Russia and Iran improved significantly. Imran put the foundation of CPEC China Pakistan Economic Corridor that created massive employment and investment opportunities. Inflation during Imran's rule was at highest in history. In 2022 despite favor of public his government came to an end due to vote of no confidence, sooner, Shahbaz Sharif became Prime minister of Pakistan.

### *1.1 Impact of Political Stability on Economic Growth in Pakistan:*

Pakistan has faced fluctuation in growth rate from 1971 when political turmoil led to a war that had disastrous effects on loss of money. Political instability interferes in economic activity macroeconomic variables. Another cause of political instability is terrorism. High rate of political stability

is unwanted mostly as it shortens time limit for policy making process Pakistani society is categorized into poor, elite and middle class. In ethnically diverse society the exclusion of minority group during decision making leads to mistrust in society, lack of cooperation caused by elites of society for self-centered purpose fulfillment. In Pakistan's economy the development is unstable as there is a large difference in underdeveloped and developed areas foreign help in development forecasts in monetary as well as fiscal policies were typical and less changes were made.

### *1.2 Impact of Regulatory Quality on Economic Growth:*

Regulatory Quality helps in the improvement of the economic situation of a country. It means to implement and make effective government policies aiding in promotion of private sector development. A better regulatory quality in the country reduces corruption and gives new opportunities for business incentives and increases public service quality. A better regulatory Quality in Pakistan will help to increase productivity. Regulation of government institutions is much less, and local authorities do not care much in following the rules and policies made by government in the case of Pakistan. Thus, effective policies should be made and to make sure these policies are used a monthly follow up or report should be given to ensure policy analysis and its effects in Pakistan.

### *1.3 Impact of Voice and Accountability on Economic Growth:*

It refers to the rate of participation of the public in giving their votes and selection of a government. Accountability means to use media for expression of

freedom and association. Transparency leads to achieving accountability. Good accountability aids in achieving economic development. Lack of transparency surely reduces investment and funding in the country due to lack of confidence and mistrust. Voice and accountability are essential for removal of malpractices taking place in the society and to hold culprit accountable. In the case of Pakistan, voice and accountability is practiced, where each citizen has freedom of speech, vote, and expression.

### *1.4 Pakistan's Current Political Landscape:*

The political landscape indicates a weaker foundation; this would ensure slow economic development leading to less investment in the country. The present situation in Pakistan leads to political turmoil as opposition of political parties have united one side and PTI is on the other side. The PTI government may receive short term advantage of the political system, but the long-term result may be reduction in polls in 2023 for next government selection. The public has a free will to support the government of their choice to establish political peace. Signs of erosion of unity and understanding between military and PTI have weakened Imran's relation with ISI and ISPR. Imran Khan's strengthening ties with Afghanistan, protests from non-supporting political parties, rising inflation, are a few major reasons that dismissed Imran Khan's government in no confidence vote. Pakistan is currently facing a political turmoil in the country leading to political instability as Imran Khan's rule has been limited to 4 years.

### *1.5 Economic growth:*

Rise in human capital, goods, technology, and workforce leads to economic growth in a

country. It describes the increase in quality and quantity of goods and services that rise in an economy. Economic growth is important for fiscal stabilization and for raising the standards of living. GDP is the money value of commodities and services manufactured inside a country in some time. It increases the size of the economy of a nation and growth rate. Rise in per capita income may improve the standards of living. It measures the market worth of goods and services.

## 2. Literature Review

Jan, Ahmed, Tahir, Hussain, Khan (2021) examined the relation between political risk on GDP from time (1996- 2018). A Time series data was collected and analyzed to determine dependency of independent variable on the dependent variable. The results show that political issues were the reason for poor economic growth. Government crises also political regime transitions have a significant effect on economic development. Ali, Ahmed, Shahid (2020) analyzed the effect of political stability on growth in the economy of Pakistan since (1984 -2018). Time series analysis was done as data was collected from World Bank and Pakistan Bureau of statistics. Autoregressive distributed lagged model was used. The findings and results implied that political stability has a good impact on economic growth. Better policies should be used for better political stability in the country and a sustainable political system should be established for enhanced economic growth. Phul, Rahpoto, Ghulam, Mangnejo paper (2020) estimated impact of political stability on economic growth from (1988 -2018) in a time series analysis. In this paper independent variables were inflation, capital, political stability, and the

dependent variable was GDP. The data of these variables was collected from OECD, WB National accounts data and from worldwide governance indicators. The outcomes of all variables have shown that all independent variables have positive and significant impact on GDP whereas Political stability has a small effect on growth in the long run.

## 3. Methodology

### 3.1 Data Collection:

The data has been obtained from indicators of the World Bank from various indices and series of different variables. Data on voice and accountability, regulatory quality and political stability has been measured in estimates. The time period of research is from 1996-2020. The research has been based on data obtained from secondary resources. Stata software version (11) has been used to check the stationary and long-term relationship between variables.

### 3.2 Model Specification:

The variables included in the models are Regulatory Quality, Political Stability, Voice and Accountability are independent variables whereas their impact is focused on Economic growth (GDP) which is a dependent variable.

$$Y_t = f(PS, RQ, VAC)$$

$$Y = \alpha_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \mu$$

Where,

$\alpha_0$  = Intercept

$Y$  = Economic Growth (GDP per capita growth annual %)

$X_1$  = Political Stability (Estimates)

$X_2$  = Regulatory Quality (Estimates)

$X_3$  = Voice and Accountability (Estimates)

$\mu$  = Error term

$Y$  represents the predicted value of GDP per capita

annual growth rate (%). The intercept shows that if all independent variables are zero then  $\alpha_0$  is the value of economic growth rate. The term E contains all other explanatory variables which are neither explained in

### 3.3 Augmented Dicky Fuller Test:

Augmented Dicky Fuller test is used to check stationarity of the model, Augmented Dicky Fuller test further contains three models:

- 1: Random Walk Model the equation used to check stationarity without trend and intercept
2. Random walk model with drift and intercept. The equation is used to check stationarity with trend and intercept.
- 3: Random walk model with drift and intercept. The equation is used to check stationarity with trend and intercept.

## 4. Hypothesis Formulation

### 4.1 Overall Significance:

Ho: There is no significant effect of Voice and

the model nor is their impact on Economic growth, however they may or may not have a significant relationship with the dependent variable.

Accountability, Political Stability, Regulatory Quality on Economic Growth GDP

Ha: There is significant effect of Voice and Accountability, Political Stability, Regulatory Quality on Economic Growth GDP

## 5. Research Methodology:

### 5.1 Stationarity

If the value of t-stat < value of t critical Ho has to be rejected and conclude that the variable is stationary. The results show that the dependent and independent variable has different levels of integration shown in the table. Here, the best approach to use is the ARDL approach .After determining whether or not cointegration exists between variables.

**Table 1:** ARDL Approach

Variables	Level of Integration	Calculated Value	Critical value at 5%
GDP (%)	1	-3.028	-3.000
Political Stability (Estimates)	0	-3.666	-3.600
Regulatory Quality (Estimates)	0	-2.900	-1.950
Voice and Accountability	1	-3.661	-3.600

5.2 Regression Analysis:

When all the variables used in the model are stationary at level or at 1st difference" Auto Regressive Distributed Lag Model (ARDL) is used, which determines long run relationship among series of variables with different order of integration, along with short run dynamics of the variables. For more

accurate and accurate results some properties of ARDL should be considered. The tests are concluded to check if the assumptions were fulfilled. One advantage of ARDL is that it is not only based on that all variables should be integrated at order 1 but is still valid if some variables are integrated at 0 order.

5.3 Relation and Significance results

Table 2: Relation & Significance Results

Variables	Coefficients	P values	Interpretation
Regulatory Quality (Estimates)	-4.042813	0.203	Insignificant
Political Stability (Estimates)	4.513883	0.004	Significant
Voice and Accountability (Estimates)	13.95208	0.010	Significant

6. Discussion

This paper defines the impact of political stability on economic progress of Pakistan. The explanatory variable voice and accountability, regulatory quality, political stability is measured in estimates from weak to strong ranging from +2.5 to -2.5 and dependent variable GDP is measured in percentages also. According to the model, results are in accordance and relevance to our expected signs and significance to our past study. Time Series examination from the era (1996-2020) results prove that regulatory quality has a negative relationship with GDP whereas voice and accountability, political stability has a positive relationship with dependent variables. This coefficient voice and accountability and political stability reveals that a one percent rise in voice and accountability and political stability leads to an

increase in GDP keeping all other variables same. The p values 0.05 is greater than significance value so variable is significant. So, we accept the alternative Hypothesis and conclude that the relation between GDP and voice and accountability and political stability, is significant and it is positively associated to GDP. If there is a rise in better enforcement of policy, the economy prospers due to more freedom of expression and improvement in quality of institutions. Accountability leading to justice provision aids in creating more trust in the country and its institutions bringing more investment in the country. Numerical coefficient -4.042813 regulatory quality shows negative change as if regulatory quality increases by 1% then economic growth of country will fall by -4.042813 in numbers in long run. We accept Ho and conclude that

regulatory quality and GDP does have an insignificant relation as the p value is greater than 0.05 which is 0.203. Increase in regulatory quality may increase economic growth in short run in the case of Pakistan which is temporary but mostly is negative in the long run in the case of Pakistan that results in political instability and thus exists a robust relationship. This evaluation is supported by past trends of political instability where economic growth was highly volatile. No regulation in the country leads to uncertainty of investment, unemployment, and inflation. Further results have been done such as serial correlation, heteroskedasticity. Our results are consistent and in accordance to minimal studies done in Pakistan. The variable regulatory quality indicates poor quality of governance which prevail more in the long run leading to inefficiency of economy Deregulation of economy harmfully depletes economy due to political unrest. Increase in political stability may increase economic growth in the case of Pakistan. The variable political stability indicates absence and violence of terrorism. Terrorism and violence both prevail more in the long run leading to inefficiency of economy.

## 7. Conclusion

The objective of this study was to examine the relation of political stability and economic growth of Pakistan from the time period (1994-2020). Political Stability and Regulatory Quality is stationary at level whereas Voice and accountability is stationary at first difference whereas the results prove that there is an insignificant and negative relation existing between Regulatory Quality and economic growth and there is positive association of

Political Stability with GDP. The relation between Voice and accountability and economic growth is proven to be positive and significant. No signs of multicollinearity and heteroskedasticity or omitted variable were present in the model as the model is observed to be dynamically stable. Data of variables such as terrorism was missing so my research has been limited due to this variable.

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