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Searching for Hills among Plateaus, Mountains and Plains; Understanding Determinants of Economic Growth in Pakistan

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Abstract

This article mentioned the effect of macroeconomic variables on the Pakistan's economic climate. This objective of this study to explore the determinants of the economic growth affected such as inflation, Government spending, oil prices, FDI, Exports, Real interest rate. These variables would increase actual outcome for Pakistan. For this purpose data is used for the period of 2001 to 2010.Fixed Effect Model is used in this study. The result of this study shows that these macroeconomic variables have a significant impact on the economy of Pakistan .The increase in the international oil prices has affected negatively on the economy in the shape of balance of payment and budgetary position. FDI and Exports positively correlate with the economic growth whereas real interest rate is negatively affected the economy.

Keywords: Real interest Rate, FDI, Crude oil, Exports, Government Spending

Introduction

The countries which are economically developed are able to achieve the political stability, decrease their poverty level in the economy and the quality of life. Economic growth is positively related with the fiscal performance and negatively correlated with the inflation in the long run.(Stanley, 1993). Oil costs are always controversial and stay an essential varying in identifying the business activities of any nation.

The nation is beginning to improve from its past of problems mainly because of a persistence to make the best possible use of its earnings from the development of its large oil resources.

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The permitting of oil earnings is usually important in the development of a country.(Carey, 1999).The high saving rate will lead to high investment in the economy and high investment and foreign direct investment is highly correlated with the economic growth whereas inflation is negatively correlated with economic growth.(M.Shahbaz, 2008).

“There has been an ongoing improve in the power intake in Pakistan since 1996-97. The prices of oil gas have a significant role in the development of an economy with the proper utilization of its resources. (Kiani, 2008).Oil has made possible our modern society. It has modified farming and market and has totally changed the means of transportation. The regional submission of proved helpful oil sources in regards to the tremendous need, mainly from the 'advanced' nations, has created community business of remarkable amount, value and importance. The growing cost of energy in the globe had short-term repercussions of both financial and social personality.(Francis, 1981).There is plenty of information available on the success of international development of raw oil, but less has been done so far to elucidate the concern how successful international improving and industry are now and what the long run has in shop for that industry of the industry(Newton, 1959).

Significance of the study

The study aims at finding out the effect on these macroeconomic variables on the economic growth in Pakistan. Every year government declares to improve in costs of fuel and diesel fuel, which straight impacts the market, transport and consumer goods. Economic Growth of a country can be affected by many macroeconomic factors but in this study 7 factors (independent variables) are taken to see the impact of these factors on the economic growth either positively or negatively. For these purpose five hypotheses has been created.

H0: There is no Significant Impact of macroeconomic variables on the economic growth.
H1: There is an impact of Real Interest rate on economic growth
H2: There is an impact of FDI on economic growth
H3: There is an impact of Exports on economic growth
H4: There is animpact of Government spending on economic growth
H5: There is an impact of oil prices on economic growth

This study used the data from World Bank for 10 year (2001-2010) therefore future researchers can conduct study with same variables for more than 10 year by taking also previous years. And this study is limited to 10 years of data of Pakistan.

Literature Review

H-Kazim (2007) examined that Pakistan's daily raw oil growth has stayed considerably low as opposed to need. To assist in growth of alternative types of, the create nations are irritating to maintain raw oil costs above 50 a barrel. However, the liability OPEC for rising raw oil costs. Saleem (2007) Observes that the oil prices and expenditure were not enhance during the previous 19 weeks to preserve the economy from further issues of the economy although increasing the prices in worldwide expenditure.

Low Inflation rate, trade openness, and foreign direct investment is important for the development of the economy Moreover the technological development is also need for the economic development .Many other factors are important for the development of the economy like agriculture development, industrial development and better infrastructure so these are the factors through which foreign direct investment is attractive and FDI will leads to economic growth(Hussein, 2001). Increase in oil costs is the dangerous top quality on oil and is continuous, as provide by some main manufacturers is considered as volatile.This pattern in growing costs has become a severe issue for the creating financial systems like Pakistanbecause if this problem carries on, can result in inflationary demands in the financial climate, improving funds lack and stability of payment problems and recession in the financial growth.

Bashar (2008) The basic problem for the increase in prices are the demand of worldwide as well as purchasing the needs of the future so that why basher give statement against the Khan and says that there are few main rules and significant factors which increase the prices of oil. The geo governmental circumstances in different areas also frustrated the situation. However, the reason of growing oil costs was devaluation of different foreign exchange such as money and exchange rate. Fazal-e-Haider (2007) Baluchistan is the main source of oil producing area and this area has potential and sources to produce oil.

There are many strong arguments are given by the researchers for the support of foreign remittances and economic growth they are believe that foreign remittances can increase economic growth.

Lopez and Olmedo (2005) believe that foreign remittances is important source for poverty reduction and education which also leads to economic growth whereas the exports instability has no effect investment and negative impact on the imports and economic growth in Pakistan.

Examined that the rapid leap in the oil prices has been hit by the world financial environment. Financial uncertainty is main reason for increasing the prices of oil and international increase the demand for oil has greatly affected the economy. Bowing up rate and the oil prices are positively related which disturbs the balance of the government and for the public due to increase in prices of oil. Every country need to be control their oil demand or they would have to produce and generate the sources of oil production to fulfilled the demand of oil of the economy.

Mohammad Wasi Khan observed that increase in petrol prices worldwide are due to many factor of the economy and major significant impact by the decrease in the money in the many countries because this statement shows that there are many factors which affected the oil prices in the economy but they need to be find out(Bashar, 2007).Basically huge quantity of oil is used by the transportations companies, owners, and heavy machinery in less developed countries like Pakistan which affect the peoples adversely through the increase in oil prices.

Limitation of the Study

Many other variables like Foreign remittance, imports, agriculture and industrial sector development , exchange rate, political instability,per capita income, Foreign aid,are also affect the economy and these variables are not consider in this study and time period is limited to only 10 years. So future researchers can further study by taking all these variables.

Data and Methodology

The time period of survey is of 10 years (2001-2010) and data was collected from IFS, Pakistan Economic Survey and Energy Year Book. The real crude oil price is taken in Rs per barrel.

The real government spending and revenues is measured in millions.The multiple Regressionsare used in this study and fixed effect model is used for this purpose because this model give more reliable results. The macroeconomic model in order to see the impact of oil price increase in Pakistan can be expressed asY = y(X1, X2, X3, X4, X5, X6)

Explanation of Variables

Y = Real GDP in millions
X1 = the real crude oil prices $/barrel.
X2 = Exports
X3 = Inflation rate
X4 = Foreign direct investment
X5 = the real government spending
X6 = the real interest rate.

The dependent variable is real GDP while explanatory variablesinclude the real crude oil prices, FDI, exports, real interest rate, the real government spending, and the real government revenues. The Model is GDP = β_0 + β_1Oil Prices + β_2Exports + β_3 Inflation + β_4 FDI + β_5 Gov Spending + β_6 Real Interest Rate

Results

Dependent Variable: GDP				
Method: Least Squares				
Sample: 2001 2010				
Included observations: 10				
	Coefficient	Std. Error	t-Statistic	Prob.
C	0.6691	36.76091	0.018204	0.0471
GREVENUE	0.02	0.00288	1.069296	0.0369
GSPENDINGS	-0.0143	0.000028	-0.074825	0.0272
INFLATION	1.395963	0.702509	1.987112	0.0153
INTEREST_RATE	-1.257832	1.286528	-0.977695	0.4313
OILPRICES	0.05094	0.003005	1.694977	0.0322
EXPORTS	2.647626	2.178837	1.215156	0.00483
FDI	2.154564	1.92	2.751811	0.01106
R-squared	0.929522	Mean dependent var		120.9885
Adjusted R-squared	0.915282	S.D. dependent var		39.30863
S.E. of regression	2.700015	Akaike info criterion		4.814953
Sum squared resid	14.58016	Schwarz criterion		5.057022
Log likelihood	-16.07477	Hannan-Quinn criter.		4.549405

Interpretation

We have estimated the macroeconomic model include the data for Pakistan during years (2001-2010). The Estimated model is GDP = 0.6691 + 0.050Oil Prices + 2.64Exports + 1.39 Inflation + 2.15 FDI -0.0143Gov Spending-1.25 Real

Interest Rate

The dependent variable isreal GDP while independent variables involve the real interest rate, the real government spending, FDI, the real government revenues, Inflation rate and the real crude oil prices. Results shows that most of the explanatory variables have a positive impact on GDP.

The exports shows that one unit change will change in GDP is 2.64 and Crude oilshows that that 1 percent change in oil price will change the real GDP by less than 1 percent (0.050) i.e. less elastic price response of crude oil. F test shows that the model is good and significant. The significance of the individual variables is less than 5 percent except the interest rate. The value of durbon Watson is 2.6 which show that there is no problem of hetroscadastictiy.

Conclusion

Every country is continually trying toimprove their economy by different methods but many economic variables are effect the economy so In this study 6 variables are taken for analyzing the impact of these variables on the GDP. Ten years data are taken (2001-2010) for this purpose. Interest rate and government spending has a negative impact on the economic growth. Oil prices affect the economy adversely and actual outcomes. Results shows that these factors have a significant impact on the GDP but these are not enough for the economic development many other factor factors like proper financial plan, investing decisions, controlling on corruption and through proper making governance rules. Literature shows that trade openness also have the positive impact on the economic growth.

It is really need of time to reduce the blowing up and have the reduced investment costs of everyday use; govt should provide the financial aid to the farm owners for power intake and diesel petrol use in towns, and also some assistance to transporters for petrol in places.Fianacial sectors of the economy plays important role so that’s why main focus should give for the improvement of this sector. Oil prices are negatively affect the economy because every consumer good is related with the crude oil prices which leads to inflation. The Government should regulate techniques for guaranteeing performance in use and growth, capability and stability of provide.

Unless suitable actions are taken this pattern of oil costs will further get worse has an effect on the economic climate.

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