



The Impact Of Political Stability On The Relationship Between The Fiscal Policy, Fiscal Deficit, And Economic Growth In South Asian Economies: An Empirical Analysis

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Abstract

The aim of this study to investigate the influence of political stability on the relationship between the fiscal policy, fiscal deficit, and economic growth in South Asian countries. This study used the panel data from 2001 to 2018 and used pooled mean group approach for estimation. Results indicated that political stability and human capital had a positive effect on the economic growth. Moreover, the gross capital formation, labor force, and government expenditure had a positive, whereas inward FDI and fiscal deficit had negative effects on economic growth. These findings support the Keynesian view on the fiscal policy and the neoclassical theory on fiscal deficit in the presence of political stability. The study suggested that the expansionary fiscal policy, reduction in fiscal deficit, and political stability can enhance the economic growth in South Asian economies. The findings have significant implications for policy makers and can contribute to the existing literature.

Keywords: government expenditures; fiscal deficit; political stability; the pooled mean group approach; South Asian economies

Introduction

The long-term economic well-being of the people in a country is often closely tied to its economic growth, which is influenced by various macroeconomic indicators such as trade, price stability, and employment (Arpaia & Turrini, 2007; Carter et al., 2013; Mahmood et al., 2011; Rehman et al., 2020). The Solow and

Endogenous growth models demonstrate how factors such as technological progress, population growth, and resource allocation can affect a country's growth and improve living standards (Kapunda & Topera, 2013). There is no guaranteed magic pill", however, for achieving rapid economic growth, as evidenced by the limitations of these theories (Gratzer, 2013; Mankiw, 2003). As a result, researchers have begun to explore hybrid versions of the Solow and Endogenous growth models through empirical testing (e.g., Petrakos et al., 2007) to better understand the complex relationships that drive the economic growth.

The fiscal policy is crucial for boosting the GDP growth, as noted by Chugunov and Pasichnyi (2018). In the short term, the counter-cyclical fiscal expenditures can stimulate the aggregate demand and economic growth during the recession, a highlighted by Alesina (2012). Conversely, the fiscal contraction can have a detrimental effect on the economy, particularly in situations where there is rising unsustainability, as pointed by Abdon et al. (2015). Government expenditures on infrastructure projects such as power plants, ports, and roads can impact firms and industries' productivity, as well as the wider economy (Chugunov & Pasichnyi, 2018). Similarly, investment in education can enhance the human capital, which is essential for the long-term growth, as suggested by Arpaia and Turrini (2007). However, compared to developed countries, Asian nations have limited experience in using the fiscal policy for counter-cyclical purposes (Abdon et al., 2014; Navaratnam & Mayandy, 2016).

The relationship between government expenditures and the economic growth has been a topic of extensive debate among researchers, both in empirical and theoretical contexts (Kapunda & Topera, 2013). While some governments have attempted to promote the economic growth through increased spending, others have not followed this pattern (Bojanic, 2013; Laech & Lechthaler, 2013). To understand the fiscal policy, it is essential to consider the two main aspects, as highlighted by Arpaia and Turrini (2007). Additionally, their study contributes to establishing a benchmark for assessing the spending and overall fiscal policies. Despite government expenditures constituting a significant share of the national income, it has often been considered a double-edged sword (Ahmad & Loganathan, 2015; Rehman et al., 2020). While the Keynesian theory suggests that an increase in government expenditures will result in the economic growth, the Wagnerian law posits that an increase in the economic growth will lead to an increase in government expenditures.

In contrast to the previously mentioned theories, Ahmad and Loganathan (2015), and Odhiambo (2015) argued that there exists a bidirectional relationship between government expenditures and the economic growth, meaning that an increase in one will lead to an increase in the other and vice versa. Achieving higher levels of economic growth requires both efficiency and awareness of expenditure, as highlighted by Angelopoulos et al. (2008). The government efficiency is often considered when analyzing the relationship between government expenditures and the economic growth (Angelopoulos et al., 2008; Avkiran, 2006; Kimaro et al., 2017; Mandl et al., 2008; Rahmayanti & Horn, 2010).

The relationship between the fiscal deficit and economic growth is a contentious issue in both theoretical and empirical literature (Bhari et al., 2020). The neoclassical economists argued that the fiscal deficit has a detrimental effect on the long-term GDP growth by reducing savings and crowding out private investment (Carter et al., 2013). In contrast, the Keynesian economists contended that the fiscal deficit is a short-term phenomenon that can stimulate government expenditures and accelerate the GDP growth. The Ricardian equivalence theory stated that the fiscal deficit has no effect on the current consumption or economic growth but may have negative consequences for future growth and the consumption pattern of future generations (Alshahrani & Alsadiq, 2014; Umaru & Gatawa, 2014).

Empirical research on the topic has produced conflicting results. Some studies have found that an increase in the fiscal deficit leads to a decline in the economic growth (Ezeabasili et al., 2012; Mohanty, 2012; Navaratnam & Mayandy, 2016), while others suggest that it can stimulate the economic growth (Nayab, 2015; Umaru & Gatawa, 2014). Moreover, they also skip the importance of political stability, because the political stability is important for to enhance the relationship between fiscal policy and economic growth (Cox & Weingast, 2018; Shabbir et al., 2016). Therefore, there is a need to examine the effect of government expenditures and the fiscal deficit on the economic growth in the context of political stability to test the Keynesian view that an increase in government expenditures and the fiscal deficit can promote the economic growth.

A summary of the literature

The relationship between government outflow and GDP growth has been investigated in various studies, producing different results. For instance, Iqbal and Zahid (1998) used a multiple regression model to examine the impact of macroeconomic variables on GDP growth in Pakistan from fiscal year 1959-60 to 1996-97. They found that primary education and the stock of physical capital were significant components that influenced economic growth. They also observed that trade openness promoted economic growth, while budget deficits had a negative association with output growth variables. Similarly, Hasnul (2015) showed that external debt had a negative association with economic growth and suggested that relying on domestic resources to finance government expenditure was a better option. However, Aoyagi and Ganelli (2015) argued that growth-oriented policies played an important role in sustaining output growth in the long run. The global financial crisis affected India's economy in multiple ways, including exchange rates, trade flows, and financial markets (Kumar & Vashisht, 2009). Capital inflows decreased, leading to a credit crisis in local markets and a decline in demand for exports, which resulted in a more than 2% decrease in GDP in the FY 2008-09. To counteract the effects of the crisis, the central bank and government in India implemented countercyclical measures, including easing monetary policy and introducing fiscal incentives to boost local demand. However, Kumar and Vashisht (2009) noted that there were limitations to the effectiveness of these measures due to limited fiscal variability and inadequate control of monetary policy.

Rehman et al. (2010) conducted a study to examine the causality between the components of government spending and national income in Pakistan, using data from 1971 to 2006. They applied the Toda-Yamamoto causality test to analyze the nature and direction of causality. Their findings supported Wagner's Law, as they found a unidirectional causality running from GDP to public spending. They also found that administrative expenditure was caused by GDP, while GDP had no causality with defense expenditure, debt servicing, and development expenditure (Rehman et al., 2010). These results oppose the Keynesian hypothesis, both at the disaggregate and aggregate levels, which suggests that government expenditure is caused by economic growth.

Adams et al. (2010) found that countercyclical expansionary fiscal policies implemented in Asia were relatively well-designed before the crisis, indicating that fiscal policy played a vital role in promoting sustainability. However, they also found that fiscal space was limited in the medium run, which could impact inclusive growth (Adams et al., 2010).

Saqib et al. (2014) conducted a study to examine the impact of taxation on output growth in Pakistan from 1973 to 2010 using the ARDL technique. Their findings suggest that tax-to-GDP, income tax, and sales tax have negative effects on economic growth. In a separate study, Abdon et al. (2015) focused on the effect of fiscal policy on output growth in developing countries in Asia. They analyzed the impact of the composition of public expenditure and taxes on GDP growth and found that different types of public spending and taxes have varying consequences on GDP growth. Based on theoretical background, they concluded that property taxes are more effective than corporate and personal income taxes in promoting GDP growth in Asian developing countries. The authors also recommended increasing spending on education as it has a significant impact on GDP growth. Finally, they suggested that Asian developing countries should focus on the composition of tax revenue and expenditure to increase the contribution of fiscal policy to economic growth (Abdullah et al., 2020).

Hasnul (2015) examined the relationship between government spending and output growth in Malaysia using data from 1970 to 2014 and employing OLS techniques to analyze the data. The author divided government expenditure into developmental and operating expenditure and found a negative association between output growth and public expenditure. Specifically, developmental and housing sector expenditure had an adverse effect on economic growth, while operating expenditure, healthcare expenditure, defense spending, and education expenditure had statistically insignificant consequences on GDP growth in Malaysia. The authors of a later study (Abdullah et al., 2020) recommended that the Malaysian government review its fiscal policy implications in light of these findings.

Aoyagi and Ganelli (2015) analyzed a cross-country dataset and proposed that structural reforms aimed at increasing productivity, reducing unemployment, and stimulating trades, as well as monetary policy focused on macroeconomic stability and fiscal redistribution, are significant determinants of inclusive growth. They suggested that implementing such policies in Asia could better achieve economic growth with shared prosperity.

The authors further suggested that increasing fiscal redistribution could have a large effect on promoting inclusive economic growth in emerging Asia.

Nursini (2017) examined the impact of trade openness and fiscal policy on GDP growth in Indonesia from 1990 to 2015. Fiscal policy was measured by public expenditure on routine expenditure, human resources, and infrastructure, as well as foreign loans and tax revenue as financing sources. The study found that public expenditure on human resources and infrastructure had a significant and positive effect on output growth when funded by tax revenue, but not when funded by foreign debt. Regular public expenditure had a negative and insignificant effect on GDP growth, regardless of funding sources. Trade openness was also found to have a significant and positive effect on output growth (Nursini, 2017).

In another study, Hasanov et al. (2018) investigated the impact of fiscal policy in Azerbaijan over a long period. Their results indicated that fiscal policy had a significant and positive effect on the non-oil sector. They recommended that policymakers in Azerbaijan take measures to compensate for the decreasing share of oil revenue in the total public revenues, such as phasing out less effective infrastructure and social projects and optimizing government expenditure. The authors cautioned against increasing exports and imports fees, tariffs, energy prices, and tax rates as quick remedies for the budget deficit, as these measures may harm economic growth.

Abdullah et al. (2019) conducted a study on the impact of fiscal policy on output growth in ASEAN-5 countries, considering the issues of fiscal policy dependency, domestic economy vulnerabilities, fragile financial support, and small fiscal multiplier. The study used data from 1970 to 2016 and analyzed it using the ARDL technique. The results showed that government spending, used as a proxy for fiscal policy, had a significant impact on GDP growth in ASEAN-5 countries except in the case of Indonesia. The study also found that the government spending had a significant impact on GDP growth in the long run after the implementation of non-tax policies, except for Indonesia. However, tax and non-tax policies were significant in Singapore, Thailand, and the Philippines, while public debt was significant in Thailand and Indonesia.

Munir and Riaz (2019) conducted a study on the relationship between macroeconomic stability and fiscal policy in South Asian countries. They examined the impact of different channels of fiscal policy, including discretionary fiscal policy, cyclical fiscal policy, and the automatic stabilizer role, on macroeconomic

stability. Their study was based on Keynesian theory, which suggested that an increase in aggregate demand (AD) would reduce the gap between expenditure and taxes. The authors analyzed data from four Southern Asian countries, namely Sri Lanka, Pakistan, India, and Bangladesh, for the period of 1990 to 2015. They employed both IVLS and pooled OLS techniques to estimate the data. The results indicated that cyclical fiscal policy and automatic stabilizers destabilized the developing economies, whereas discretionary fiscal policy played a significant role in stabilization and efficient government in the Southern Asian economies.

Sriyalatha and Torii (2019) investigated the impact of fiscal variables on long-term output growth in Sri Lanka and Singapore. They utilized time series data from 1972 to 2017 and applied the autoregressive distributed lag (ARDL) and error correction model (ECM) techniques to estimate the data. Their findings indicated that government investment, revenue, and expenditure had a statistically significant and positive effect on long-term output growth in both Sri Lanka and Singapore. Their results strongly supported the Keynesian theory. Additionally, the results indicated bidirectional causality between output growth and inflation in Singapore and between output growth and expenditure on investment in Sri Lanka.

Abdullah et al. (2020) examined the association between institutions, fiscal policy, and output growth in Asian countries using data from 1982-2001. They employed Padroni's cointegration technique to estimate the data and scrutinized the long-run effect of fiscal policy and institutions on output growth in two ways. First, they used aggregate public expenditure and other fiscal variables along with institutional variables to influence economic growth, and secondly, they determined the institutional effect on economic growth. Results revealed a long-run connection between fiscal policy, institutions, and real per capita GDP. Public expenditure, other fiscal variables, and institutional factors had a statistically significant and positive impact on GDP growth. The study also confirmed that institutions have a significant role in influencing economic growth. Some studies have concluded that an increase in government expenditure promotes economic growth (Beraldo et al., 2009; Bojanic, 2013; Kapunda & Topera, 2013; Kimaro et al., 2017; Wang, 2011), while others have concluded that an increase in government expenditure reduces economic growth (Carter et al., 2013; Chang et al., 2011; Ghura & Hadjimichael, 1996; Kweka & Morrissey, 2000; Ndambiri et al., 2012; Nurudeen & Usman, 2010). Some studies have found that an increase in government expenditure has no effect on economic growth (Kollias et al., 2004; Sáez et al., 2017; Sinha, 1998). Rehman et al. (2020) found that government expenditure on research and

development, education, subsidies, and compensation to employees have a positive effect on economic growth, while interest payments and military expenditure have a negative effect on economic growth, and strongly support the validity of the Keynesian hypotheses in Pakistan.

Kimaro et al. (2017) concluded that government efficiency has no effect on economic growth, while government expenditure has a positive effect on economic growth with or without efficiency. The relationship between government expenditures and the economic growth has been a topic of extensive debate among researchers, both in empirical and theoretical contexts (Kapunda & Topera, 2013). The Keynesian theory suggests that an increase in government expenditures will result in the economic growth, while, the Wagnerian law posits that an increase in the economic growth will lead to an increase in government expenditures (Ahmad & Loganathan, 2015; Rehman et al., 2020).

The relationship between the fiscal deficit and economic growth is a contentious issue in both theoretical and empirical literature (Bhari et al., 2020). The neoclassical economists argued that the fiscal deficit has a detrimental effect on the long-term growth (Carter et al., 2013). While, the Keynesian economists contended that the fiscal deficit is a short-term phenomenon. The Ricardian equivalence theory stated that the fiscal deficit has no effect on economic growth (Alshahrani & Alsadiq, 2014; Umaru & Gatawa, 2014). Empirical research on the topic has produced conflicting results. Some studies have found that an increase in the fiscal deficit leads to a decline in the economic growth (Ezeabasili et al., 2012; Mohanty, 2012; Navaratnam & Mayandy, 2016), while others suggest that it can stimulate the economic growth (Nayab, 2015; Umaru & Gatawa, 2014). Moreover, they also skip the importance of political stability, because the political stability is important for to enhance the relationship between fiscal policy and economic growth (Cox & Weingast, 2018; Shabbir et al., 2016). The inconsistent and inconclusive results of different studies suggest that the relationship between government expenditure and economic growth requires further investigation.

Methodology

This study aimed to investigate the impact of political stability on the relationship between fiscal policy, and fiscal deficit on economic growth in six Southern Asian countries: Sri Lanka, Pakistan, Nepal, Iran, Bhutan, and Bangladesh. Annual panel data covering the period from 2001 to 2018 were utilized. Political stability data were obtained from the Global Economy website in 2020, while all other variables were collected from the

Model specification

Several previous studies have incorporated fiscal policy as an independent variable within the Solow growth model, such as Gupta et al. (2005), Aliyev and Mikayilov (2016), Loto (2011), Mudaki and Masaviru (2012), Ahmad and Wajid (2013), Akpan (2005), Tsoukis and Miller (2003), and Le and Suruga (2005). Similarly, in this study, the Solow growth model has been utilized with modifications that include the addition of political stability and other control variables.

$$GDPP = (LF, GCF, HK, GE, PS, IFDI, FD) \quad (1)$$

$$GDPP_{it} = \beta_0 + \beta_1 LF_{it} + \beta_2 GCF_{it} + \beta_3 HK_{it} + \beta_4 GE_{it} + \beta_5 PS_{it} + \beta_6 IFDI_{it} + \beta_7 FD_{it} + \mu_{it} \quad (2)$$

In this study, several variables were used to examine their relationship with economic growth. Specifically, GDPP was used to measure economic growth, LF represented the labor force, GCF represented physical capital, HK represented human capital, GE represented government expenditure (as a proxy for fiscal policy), PS represented political stability, IFDI represented FDI inflow, and FD represented fiscal deficit.

$$\Delta GDPP_{it} = \beta_{0t} + \phi_i GDPP_{it-1} + \beta_1 GCF_{it} + \beta_2 LF_{it} + \beta_3 HK_{it} + \beta_4 PS_{it} + \beta_5 IFDI_{it} + \beta_6 FD_{it} + \beta_7 GE_{it} + \sum_{i=1}^n \gamma_{ij} \Delta GDPP_{it} + \sum_{i=1}^n P_{1j} \Delta GCF_{it} + \sum_{i=1}^n P_{2j} \Delta LF_{it} + \sum_{i=1}^n P_{3j} \Delta HK_{it} + \sum_{i=1}^n P_{4j} \Delta PS_{it} + \sum_{i=1}^n P_{5j} \Delta IFDI_{it} + \sum_{i=1}^n P_{6j} \Delta FD_{it} + \sum_{i=1}^n P_{7j} \Delta GE_{it} + \omega_{it} \dots \dots \dots (3)$$

Where

$$\phi_i = - \left(1 - \sum_{i=1}^p \gamma_{ij} \right), \beta_i = \sum_{i=1}^p P_{ij},$$

$$\gamma_{ij} = - \sum_{m=j+1}^p, j = 1, 2, \dots, p-1 \text{ and } P_{ij} = - \sum_{m=j+1}^p, j = 1, 2, \dots, q-1, i = 1, 2, \dots, n$$

where

$i = 0, 1, 2, \dots, n$, ϕ_i is the correction term from the short run to long run equilibrium.

This study employed a modified Solow growth model that included several control variables, excluding political stability.

$$GDPP = (LF, GCF, HK, GE, IFDI, FD) \quad (4)$$

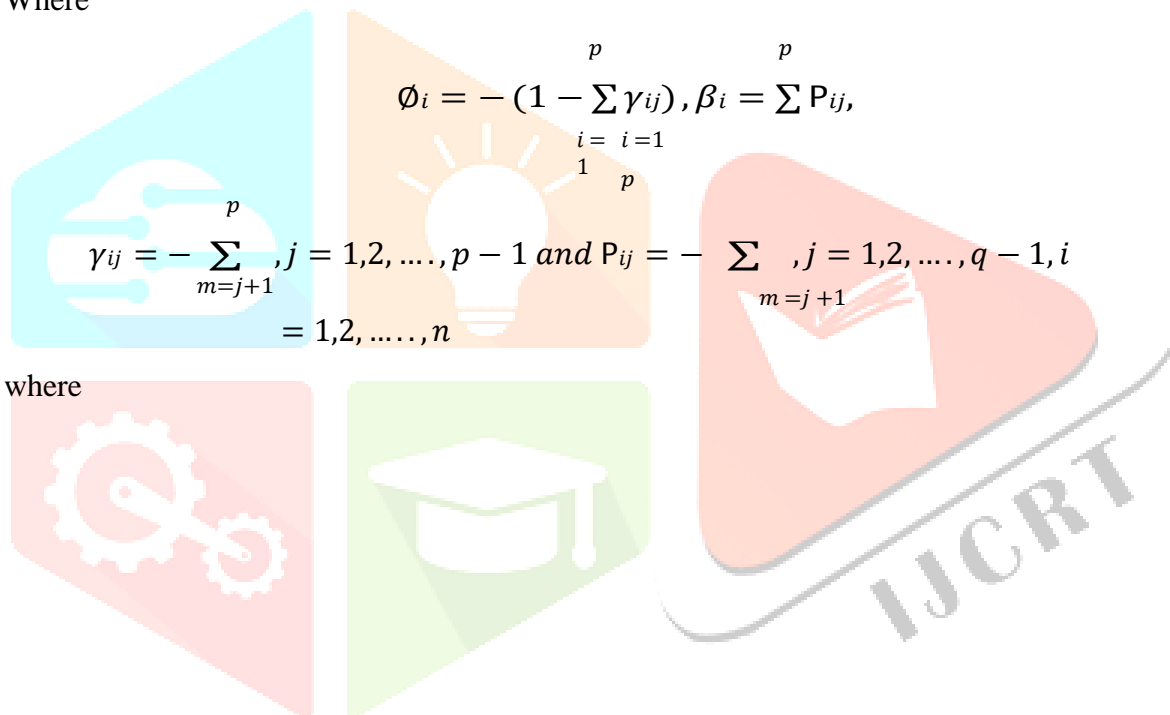
$$GDPP_{it} = \beta_0 + \beta_1 LF_{it} + \beta_2 GCF_{it} + \beta_3 HK_{it} + \beta_4 GE_{it} + \beta_5 IFDI_{it} + \beta_6 FD_{it} + \mu_{it} \quad (5)$$

Where, GDPP used for economic growth, LF for labor force, GCF for physical capital, HK for human capital, GE for government expenditure represent, fiscal policy, IFDI for FDI inflow, and FD for fiscal deficit.

$$\Delta GDPP_{it} = \beta_{0t} + \phi_i GDPP_{it-1} + \beta_1 GCF_{it} + \beta_2 LF_{it} + \beta_3 HK_{it} + \beta_4 IFDI_{it} + \beta_5 FD_{it} + \beta_6 GE_{it} + \sum_{i=1}^n \gamma_{ij} \Delta GDPP_{it} + \sum_{i=1}^n P_{1j} \Delta GCF_{it} + \sum_{i=1}^n P_{2j} \Delta LF_{it} + \sum_{i=1}^n P_{3j} \Delta HK_{it} + \sum_{i=1}^n P_{4j} \Delta IFDI_{it} + \sum_{i=1}^n P_{5j} \Delta FD_{it} + \sum_{i=1}^n P_{6j} \Delta GE_{it} + \omega_{it} \quad (6)$$

Where

$$\phi_i = - \left(1 - \sum_{j=1}^p \gamma_{ij} \right), \beta_i = \sum_{j=1}^p P_{ij},$$

$$\gamma_{ij} = - \sum_{m=j+1}^p, j = 1, 2, \dots, p-1 \text{ and } P_{ij} = - \sum_{m=j+1}^p, j = 1, 2, \dots, q-1, i = 1, 2, \dots, n$$


where

$i = 0, 1, 2, \dots, n$, ϕ_i is the correction term from the short run to long run equilibrium.

Table 1

Description of variables

No.	Variable	Units	Sources	Mark
1	Gross Domestic Product per capita growth (annual percentage) used as proxy for economic growth.	Percentage	World Development Indicators, (2020)	GDPP
2	Labor Force as a percentage of total population	Percentage	World Development Indicators, (2020)	LF
3	Gross capital formation as percentage of GDP	Percentage	World Development Indicators, (2020)	GCF
4	Secondary school enrollment as percentage of gross enrollment used as proxy for human capital	Percentage	World Development Indicators, (2020)	HK
5	Political Stability	Rank 1 to 100 (weak to strong)	The global economy website, 2020	PS
6	Inward Foreign Direct Investment as a percentage of GDP	Percentage	World Development Indicators, (2020)	IFDI
7	Fiscal Deficit as a percentage of GDP	Percentage	World Development Indicators, (2020)	FD
8	Gross National Expenditure as a percentage of GDP	Percentage	World Development Indicators, (2020)	GE

Estimation techniques

This study used the correlation among the variables and descriptive statistics to check the status of each variable. Furthermore, this study employed three panel unit root tests to identify the presence of unit roots in the data, specifically the Levin, Lin and Chu t test (2002), Im, Pesaran and Shin W -test (2003), and ADF Fisher Chi-square test developed by Maddala and Wu (1999). The Pooled Mean Group (PMG) method developed by Pesaran, Shin, and Smith (1999) was utilized to estimate the short run and long run coefficients for the full panel and short run coefficients for individual countries. In addition, the panel cointegration test developed by Kao (1999) was applied to the data to examine the long run relationship between the independent variables and the dependent variable.

Results

Table 2 presents the descriptive statistics and correlation matrix for all variables. The results show that all variables, except GDP per capita, have positive skewness, while GDP per capita has negative skewness. The kurtosis values indicate that all variables have heavy tails. In terms of correlation, GDP per capita is positively correlated with gross capital formation, labor force, human capital, government expenditure, political stability, and inward FDI, while it is negatively correlated with fiscal deficit.

Table 2

Descriptive statistics and correlation

	GDPP _{it}	GCF _{it}	LF _{it}	HK _{it}	GE _{it}	PS _{it}	IFDI _{it}	FD _{it}
<i>Mean</i>	3.620	33.340	40.943	60.083	109.406	31.037	0.990	132.145
<i>Median</i>	3.547	30.334	40.598	57.745	107.114	27.500	0.830	120.109
<i>Maximum</i>	15.397	61.702	57.585	99.627	133.790	76.000	6.175	290.350
<i>Minimum</i>	-8.609	15.805	28.165	20.000	89.894	1.000	-0.655	11.819
<i>Std. Dev.</i>	2.937	12.307	7.295	22.138	10.434	20.503	0.921	72.422
<i>Skewness</i>	-0.024	0.706	0.365	0.005	0.486	0.675	2.682	0.446
<i>Kurtosis</i>	7.194	2.572	2.178	1.960	2.527	2.680	13.765	2.363
GDPP _{it}	1							
GCF _{it}	0.339	1						
LF _{it}	0.252	0.358	1					
HK _{it}	0.147	0.215	0.028	1				
GE _{it}	0.137	0.415	0.786	-0.161	1			
PS _{it}	0.292	0.885	0.321	0.233	0.419	1		
IFDI _{it}	0.109	0.076	-0.224	-0.038	-0.144	0.069	1	
FD _{it}	0.016	0.134	0.412	-0.085	0.554	0.049	-0.180	1

Table 3 presents the results of panel unit root tests, indicating that GDP per capita, labor force, and inward FDI were stationary at the level and have a zero order of integration, while gross capital formation, human capital, government expenditure, political stability, and fiscal deficit were stationary at the first difference and have a first order of integration. The order of integration of the variables is mixed.

Table 3

Panel unit root tests

Variable	LLC Test		IPMW Test		ADF- χ^2 Test		Order of Integration
	At I(0)	At I(1)	At I(0)	At I(1)	At I(0)	At I(1)	
GDPPit	-2.017** (0.0219)	---	-3.5174* (0.0002)	---	34.0115* (0.0007)	---	I(0)
GCFit	-0.8499 (0.1977)	-5.4199* (0.0000)	-0.4148 (0.3392)	-5.5941* (0.0000)	16.5368 (0.1679)	52.903* (0.0000)	I(1)
LFit	-3.5769* (0.0002)	---	-2.4307* (0.0075)	---	25.8062** (0.0114)	---	I(0)
HKit	-0.3769 (0.3531)	-2.7232* (0.0032)	1.0764 (0.8591)	-4.9272* (0.0000)	5.7157 (0.9297)	45.8364* (0.0000)	I(1)
GEit	-1.1679 (0.1214)	-6.0408* (0.0000)	-0.8889 (0.1870)	-5.3384* (0.0000)	17.0255 (0.1486)	49.5192* (0.0000)	I(1)
PSit	0.0513 (0.5205)	-2.9037* (0.0018)	0.0635 (0.5253)	-3.1371* (0.0009)	11.9320 (0.4512)	30.1986* (0.0026)	I(1)
IFDIit	-1.851** (0.0321)	---	-1.833** (0.0334)	---	22.7236** (0.0302)	---	I(0)
FDit	2.4539 (0.9929)	-2.3908* (0.0084)	4.6056 (1.0000)	-4.3473* (0.0000)	0.5646 (1.0000)	40.7409* (0.0001)	I(1)

N.B.: * and ** indicated significant at 1% and 5% respectively and p-value inside the (--).

Table 4 presents the results of the long run relationship and short run coefficients of the variables in the presence of political stability. The findings indicate that gross capital formation (GCF) and labor force (LF) have a positive and significant effect on economic growth in the long term but have no effect in the short run. Similarly, human capital (HK) and political stability (PS) have significant and positive effects on economic growth both in the long and short term. The government expenditure (GE) has a positive and significant effect on economic growth in the long run, where a 1% increase in GE leads to a 0.06 increase in GDP per capita in the long term.

Inward FDI (IFDI) has a negative and significant effect on economic growth in the long run but has an insignificant effect in the short run. The fiscal deficit (FD) has a negative and significant effect on economic growth in the long term but has an insignificant effect in the short term. The error correction term value is -0.69 and significant at 1%, indicating that the speed of adjustment of these variables to the long run equilibrium is

69%. Furthermore, the Kao residual cointegration test value is -3.0743 and significant at the 1% level of significance, supporting the presence of cointegration among the variables in the long run.

Table 4

PMG long run and short run Results with political stability for full Panel

Variables	Coefficient	Standard Error	t-Statistic	Prob.*
<i>Long Run Coefficient</i>				
GCF _{it}	0.3459*	0.0220	15.7214	0.0000
LF _{it}	0.3528*	0.0595	5.9305	0.0000
HK _{it}	0.0607*	0.0128	4.7402	0.0000
GE _{it}	0.0603*	0.0090	6.7286	0.0000
PS _{it}	0.0840*	0.0107	7.8601	0.0000
IFDI _{it}	-0.6092*	0.0741	-8.2200	0.0000
FD _{it}	-0.0350*	0.0034	-10.2093	0.0000
<i>Short Run Coefficient</i>				
ECM	-0.6890*	0.2542	-2.7105	0.0093
Δ(GCF _{it})	0.2093	0.1479	1.4151	0.1636
Δ(LF _{it})	-0.1727	0.1967	-0.8777	0.3846
Δ(HK _{it})	0.1766*	0.0651	2.7126	0.0093
Δ(GE _{it})	-0.0428	0.0825	-0.5186	0.6065
Δ(PS _{it})	0.1203**	0.0475	2.5352	0.0146
Δ(IFDI _{it})	0.6813	0.5004	1.3614	0.1799
Δ(FD _{it})	-0.0048	0.0169	-0.2863	0.7759
C	-8.5331**	3.7418	-2.2805	0.0272
Kao Residual Cointegration Test			-3.0743	0.0011

N.B.: * and ** indicated significant at 1% and 5% respectively.

Table 5 presents the results of PMG short run coefficients and error correction for each country with political stability. The variables GCP, LF, and HK have a positive and significant effect on economic growth in all countries except Iran. The government expenditure has a positive and significant effect on economic growth in all countries in the short run. The inward FDI has a significant and encouraging effect on GDP per capita in Bangladesh, Bhutan, Pakistan, and Sri Lanka while having an insignificant effect in Iran and Nepal. The fiscal deficit has a positive and significant effect on GDP per capita in Bangladesh, Bhutan, Nepal, and Sri Lanka and has a negative and significant effect in Iran and Pakistan. The political stability has a positive and significant effect in all 5 countries except Iran in the short run. The error correction term coefficient values are negative and significant for all countries. The speed of adjustment to the long run equilibrium is 16% in Bangladesh, 87% in Bhutan, 25% in Iran, 49% in Nepal, 54% in Pakistan, and 83% in Sri Lanka.

Table 5

PMG short run country wise results with political stability

	Sections Bangladesh	Bhutan	Iran	Nepal	Pakistan	Sri Lanka
Variables						
ECM	-0.1622*	-0.8663*	-0.248**	-0.4903*	-0.5402*	-0.8270*
	[0.0031]	[0.0054]	[0.0501]	[0.0719]	[0.0175]	[0.0161]
	(0.0000)	(0.0000)	(0.0158)	(0.0064)	(0.0001)	(0.0000)
$\Delta(\text{GCF}_t)$	0.5276*	0.2310*	0.7190	0.1503*	0.1028*	0.1925*
	[0.0257]	[0.0021]	[0.3243]	[0.0169]	[0.0080]	[0.0242]
	(0.0003)	(0.0000)	(0.1134)	(0.0030)	(0.0010)	(0.0041)
$\Delta(\text{LF}_t)$	0.0503*	0.5588*	0.7138	0.4139*	0.3821*	1.4454***
	[0.0076]	[0.0075]	[1.2094]	[0.0695]	[0.0337]	[0.1595]
	(0.0071)	(0.0000)	(0.5966)	(0.0095)	(0.0015)	(0.0683)
$\Delta(\text{HK}_t)$	0.0490*	0.0462*	0.1199	0.3211*	0.3444*	0.2713*
	[0.0017]	[0.0006]	[0.2600]	[0.0132]	[0.0036]	[0.0066]
	(0.0001)	(0.0000)	(0.6760)	(0.0002)	(0.0000)	(0.0000)
$\Delta(\text{GE}_t)$	0.0663*	0.03581*	0.3643**	0.1518**	0.0691*	0.2209*
	[0.0106]	[0.0006]	[0.0740]	[0.0439]	[0.0062]	[0.0045]
	(0.0083)	(0.0000)	(0.0161)	(0.0407)	(0.0015)	(0.0000)
$\Delta(\text{IFDI}_t)$	1.1449***	0.0356**	-1.0562	0.8932	2.2333*	1.8368**
	[0.0616]	[0.0078]	[1.7032]	[1.4532]	[0.1071]	[0.4377]
	(0.1000)	(0.0195)	(0.5791)	(0.5823)	(0.0002)	(0.0247)
$\Delta(\text{FD}_t)$	0.0085*	0.0419*	-0.0822*	0.0005**	-0.0052*	0.0075*
	[0.0001]	[0.00003]	[0.0051]	[0.0001]	[0.0000]	[0.0007]
	(0.0000)	(0.0000)	(0.0005)	(0.0343)	(0.0000)	(0.0025)
$\Delta(\text{PS}_t)$	0.0348*	0.1242*	0.0938	0.0249**	0.3440*	0.1004*
	[0.0003]	[0.0020]	[0.0542]	[0.0046]	[0.0042]	[0.0011]
	(0.0000)	(0.0000)	(0.1821)	(0.0124)	(0.0000)	(0.0000)
C	1.5609**	-25.7854	-3.2100	-7.4778	-2.2974	10.867**
	[0.4242]	[20.7432]	[15.691]	[16.212]	[1.9280]	[3.157]
	(0.0348)	(0.3021)	(0.8510)	(0.6760)	(0.3191)	(0.0412)

Note: *, ** and *** indicated significant at 1%, 5% and 10% respectively and slandered error inside the [--], p-value inside the (--).

Table 6 presents the PMG results of the long-term and short-term effects in the absence of political stability.

Gross capital formation has a significant and positive effect on economic growth in both the long run and short run. Labor force and human capital have a positive and significant impact on economic growth in the long run but have an insignificant effect in the short term. Government expenditure has a weak positive and significant impact on economic growth in both the short and long run. Inward FDI has an insignificant effect on economic growth. Fiscal deficit has a significant and negative effect on GDP per capita in the long run but has an insignificant effect in the short term. The error correction term value is -0.4408 and significant at the 5% level of significance, which means that these variables have a speed of adjustment of 44% to the long-run equilibrium. The Kao residual cointegration test value is -2.9956 and significant at the 1% level of significance, indicating that there exists cointegration among the variables in the long run.

Table 6

PMG long run and short run Results without political stability for full Panel

Variables	Coefficient	Standard Error	t-Statistic	Prob.*
<i>Long run coefficient</i>				
GCF _{it}	0.1938*	0.0549	3.5316	0.0009
LF _{it}	1.1668*	0.1685	6.9262	0.0000
HK _{it}	0.1982*	0.0439	4.5116	0.0000
GE _{it}	0.0544***	0.0319	1.7059	0.0938
IFDI _{it}	0.2207	0.2870	0.7690	0.4452
FD _{it}	-0.0304*	0.0112	-2.7300	0.0085
<i>Short run coefficient</i>				
ECM	-0.4408**	0.2063	-2.1361	0.0372
Δ (GCF _{it})	0.3346**	0.1547	2.1629	0.0350
Δ (LF _{it})	0.0367	0.2116	0.1735	0.8629
Δ (HK _{it})	0.0505	0.1806	0.2797	0.7808
Δ (GE _{it})	0.1882***	0.1059	1.7772	0.0812
Δ (IFDI _{it})	0.3754	0.2810	1.3357	0.1873
Δ (FD _{it})	-0.0159	0.0137	-1.1582	0.2519
C	-16.1540***	8.6565	-1.8661	0.0675
Kao Residual Cointegration Test			-2.9956	0.0014

Note:*,** and *** indicated significant at 1%, 5% and 10% respectively

In Table 7, the short-run results of the PMG model are presented for each country in the absence of political stability. The findings indicate that GCF, LF, and HK have a positive and significant effect on GDP per capita growth in all countries, except for gross capital formation in Pakistan and labor force in Sri Lanka, where the effect is insignificant. Government expenditure has a positive and significant impact on economic growth in all countries except Bhutan. Inward FDI has a positive and significant effect on per capita GDP in Bangladesh, but a negative and significant impact in Bhutan, and is insignificant in the other countries. The fiscal deficit has a positive and significant effect in Bangladesh and Sri Lanka, but a negative and significant effect in the other countries. The error correction term has a negative and significant impact in all countries, indicating a long-run equilibrium relationship between the variables. The speed of adjustment to the long-run equilibrium is 11% in Bangladesh, 56% in Bhutan, 86% in Iran, 9% in Nepal, 7% in Pakistan, and 58% in Sri Lanka.

Table 7

PMG

short run country wise results without political stability

Sections Variables	Bangladesh	Bhutan	Iran	Nepal	Pakistan	Sri Lanka
ECM	-0.1140* [0.0075] (0.0006)	-0.5567* [0.0198] (0.0001)	-0.8630* [0.0287] (0.0001)	-0.0922* [0.0064] (0.0007)	-0.0687* [0.0047] (0.0007)	-0.5778* [0.0175] (0.0001)
$\Delta(\text{GCF}_t)$	0.4642* [0.0359] (0.0010)	0.1105* [0.0075] (0.0007)	1.0362* [0.0938] (0.0016)	0.2468* [0.0158] (0.0006)	-0.0145 [0.0182] (0.4852)	0.1642** [0.0446] (0.0348)
$\Delta(\text{LF}_t)$	0.2398* [0.0084] (0.0001)	0.6246* [0.0858] (0.0054)	1.7908*** [0.2845] (0.0690)	0.3872** [0.0766] (0.0149)	0.3329* [0.0333] (0.0021)	0.1315 [0.2948] (0.6858)
$\Delta(\text{HK}_t)$	0.0479* [0.0022] (0.0002)	0.0678* [0.0062] (0.0017)	0.7974* [0.1100] (0.0054)	0.4549* [0.0082] (0.0000)	0.2245* [0.0088] (0.0001)	0.3053* [0.0137] (0.0002)
$\Delta(\text{GE}_t)$	0.0469** [0.0133] (0.0391)	0.0046 [0.0022] (0.1360)	-0.6556* [0.0286] (0.0002)	0.2388** [0.0451] (0.0131)	0.2389* [0.0078] (0.0001)	0.0469* [0.0053] (0.0030)
$\Delta(\text{IFDI}_t)$	0.5660* [0.0724] (0.0044)	-0.943* [0.0385] (0.0001)	0.3790 [0.6343] (0.5923)	0.8054 [1.6054] (0.6504)	1.0129* [0.1420] (0.0057)	0.4318 [0.5425] (0.4842)
$\Delta(\text{FD}_t)$	0.0130* [0.0001] (0.0000)	-0.0137* [0.0002] (0.0000)	-0.0816* [0.0015] (0.0000)	-0.0103* [0.0001] (0.0000)	-0.0048* [0.0001] (0.0000)	0.0021 [0.0014] (0.2347)
C	3.7621 [8.0380] (0.6717)	-55.25 [113.07] (0.6586)	-20.8844 [38.5542] (0.6257)	-5.5936 [18.1217] (0.7778)	-2.4065 [5.0516] (0.6663)	-16.5533 [20.169] (0.4719)

Note: *, **, and *** indicated significance at 1%, 5% and 10%, respectively; slandered error inside the [], and the p-value inside the ().

Discussion

The findings of the study indicate that gross capital formation (GCF) and labor force (LF) have a positive and significant effect on economic growth in the long term but have no effect in the short run. Similarly, human capital (HK) and political stability (PS) have significant and positive effects on economic growth with the presences of political stability. The government expenditure (GE) has a positive and significant effect on economic growth, while, Inward FDI (IFDI) and fiscal deficit has a negative and significant effect on economic growth in the long run but has an insignificant effect in the short run in the presence of Political stability. These results are consistent with the findings of Abdullah, Yien, and Azam (2019), Beraldo et al. (2009), Bojanic (2013), Kapunda and Topera (2013), Kimaro et al. (2017), and Wang (2011) but contradict the

findings of Carter et al. (2013), Chang et al. (2011), Ghura and Hadjimichael (1996), Kweka and Morrissey (2000), Ndambiri et al. (2012), Nurudeen and Usman (2010). Similarly, Gross capital formation has a significant and positive effect on economic growth, while, Fiscal deficit, labor force and human capital have a positive and significant impact on economic growth in the long run but have an insignificant effect in the short term. Government expenditure has a weak positive and significant impact on economic growth in the absence of political stability. Inward FDI has an insignificant effect on economic growth. This finding is consistent with the findings of Rehman et al. (2018), Azam (2019), and Azam et al. (2020). These results are consistent with the findings of Coccia (2017), Fischer (1993), and Nazari, Asadi, and Imanian (2019) but contradict the findings of Bhari, Lau, Aslam, and Yip (2020). Therefore, this political stability is promoted and strengthen the relationship between fiscal policy, fiscal debt and economic growth in the south Asian countries.

On the basis of above findings, it can be concluded that government expenditure has a positive and significant impact on the long-term economic growth in all countries except Bhutan. In the short run, gross capital formation and government expenditure have a positive and significant effect on economic growth, while inward foreign direct investment has an insignificant effect. In the absence of political stability, gross capital formation, labor force, human capital, and government expenditure have a positive and significant impact on long-term economic growth, while fiscal deficit has a negative and significant effect. Additionally, government expenditure has a positive and significant impact on economic growth in all countries except Bhutan, while fiscal deficit has a positive and significant effect on GDP per capita in Bangladesh and Sri Lanka but a negative and significant effect in other countries in the short run.

This study supports the Keynesian view that an increase in government expenditure significantly promotes economic growth, similar results were given by (Beraldo, Montolio, & Turati, 2009; Bojanic, 2013; Kapunda & Topera, 2013; Kimaro et al., 2017; Wang, 2011), while dissimilar results were given by (Carter, Craigwell, & Lowe, 2013; Chang, Huang, & Yang, 2011; Ghura & Hadjimichael, 1996; Kweka & Morrissey, 2000; Ndambiri et al., 2012; Nurudeen & Usman, 2010), while support neoclassical theory that an increase in fiscal deficit has an adverse effect on economic growth, the results is line with (Ezeabasili, Tsegba, & Ezi- Herbert, 2012; Mohanty, 2012; Navaratnam & Mayandy, 2016) while opposite conclusion were given by (Nayab, 2015; Umaru & Gatawa, 2014). Political stability also plays a crucial role in the influence of economic growth. The results show that without political stability, the

significance level of government expenditure is weak, and the effect of inward foreign direct investment is insignificant (Mercado, 2019; Yakubu et al., 2020).

Limitations:

This study is focus on the impact of political stability on the relationship among the fiscal policy, fiscal debt and economic growth in the South Asian Countries to take the longer period of data to revealed the robust and authentic results to generalized. But this study used the short period of data because the data of majority of variable included in the model especially political stability were not available for long period. Similarly, this study is only limited to five South Asian countries due to non-availability of the data.

Conclusion

The main aim of this study was to examine the relationship between the fiscal policy, fiscal deficit, and economic growth, as well as the role of political stability in Southern Asian countries using panel data from 2001 to 2018. The nature of the data suggested that the pooled mean group model is the most appropriate method to estimate the data. The results revealed that political stability, gross capital formation, human capital, labor force, and government expenditures have a positive and significant impact on the long-term economic growth, while the inward foreign direct investment and the fiscal deficit have a negative and significant effect. Additionally, the human capital and political stability exhibit a positive and significant effect on the economic growth in the short run.

Recommendations:

Based on these findings, this study recommends:

- 1) By implementing an expansionary government expenditure will increase economic growth
By following certain measurements like infrastructure spending, social welfare programs, subsidies to businesses and other initiatives can increase government spending. This approach should be used during the times of economic downturns when private investment and consumer spending are low and the economy needs a boost.
- 2) By minimizing fiscal deficit will accelerate economic growth
Fiscal deficit can be minimized by cutting unnecessary expenditures, reducing subsidies and welfare

programs and optimizing the use of resources to achieve efficiency in public spending. The government should also reduce the size of bureaucracy and eliminate duplication of services to reduce the overall cost of running a government. Government requires to have a balanced approach that takes into account the economic and social impact of fiscal policies.

3) By ensuring strong political stability will accelerate economic growth.

Uncertainties about politics are one of the issues that the industrialists and businessmen complain about the most. Because to see the front of the businessman who wants to invest is the main condition for a country to achieve a stable economic growth is a strong and stable political structure. The strong political stability will should be prioritized by the leadership by making and implementing strong policies.

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