

# Foreign Capital, Political Instability and Financial Performance of Pakistan

Muhammad Jawad-ul-Hassan

Federal Urdu University of Arts, Science & Technology, Islamabad (Department of Business Administration)

## Abstract

Political Instability is one of the most important factor in the development of the country. To check the development of the country one must check the political instability of that country. I defined political instability is somehow the “the prosperity of government clash”. While going through different literature done on the political instability. Study showed that political instability and growth goes hand in hand. They both affect each other respectively. This study showed that investors are attracted only when there is stable environment for the business market. One variable is directed for future research that is corruption. In concluding the article it is concluded that political inability leads towards low growth of the country and similarly vice versa.

## Introduction

Political Instability is regarded as one of the most important factor which affects the Economic position of the country. Similarly Burdens of borrowing also affect one’s country badly which not only affects the people but makes country weak internally that growing up can be difficult. Political Instability and Economic Growth both are interconnected with each other. As Pakistan is facing serious issues of Political Instability and numerous research has been done on this topic in which many researchers agreed that his leads to the financial destruction of the country. (Alesina & Perotti, 1996) Show that “socio-political instability generates an uncertain politico-economic environment, raising risks and reducing investment”. “Political instability also leads to higher inflation” as shown in (Aisen & Veiga, 2006). (Alesina, Ozler, Roubini, & Swagel, 1996) “used data on 113 countries from 1950 to 1982 to show that GDP growth is significantly lower in countries and time periods with a high propensity of government collapse”.

## Objective

The main objective of selecting this topic is to assess the work done on the political instability and foreign debts with concern to Pakistan and less developed countries. As refreshing political situation of Pakistan is affecting Economy badly so that’s why this topic is selected that how much Pakistan’s economy is being affected by this Political Instability. Aim and Objective is to withdraw the important points through which we can get rid of this issue of political Instability. So this is the serious issue which needs to be addressed as (Michael, 1971) quoted that "Political Instability can be regarded as important to maintain peace, harmony, enduring constitutional contentment’s, maintenance of government institutions and possession of civic order”

## Methodology

To address the topic which is the impact of Pakistan’s Political Instability I collected the Research material from different websites like J-STOR, Facebook Literature Survey Groups and specially EMERALED. Journals from which articles are downloaded are National Bureau of Economic Research, British Journal of Arts and Social Sciences, The Lahore Journal of Economics, Sci. Int. Lahore and from IMF Working Papers & World Bank Reports etc. By providing links into the groups on facebook from different articles I found the articles and after going through the article all the work is arranged accordingly to address & generalize the topic.

## Literature Review

Numerous work has been done about why Pakistan is failed to attract the foreign investors and one factor of this is political instability. Due to this important investors hesitate to invest in developing countries like Pakistan. (Baumol, 1990), (Murphy, Shleifer, & Vishny, 1993), (Acemoglu, 1995), (Mauro, 1995), (Baumol, 2004) Suggests that poor economic conditions are often associated with bad governance and poor country’s institution work which results rent seeking and corruption therefore effecting the economic conditions of the country. (Khawaja & Khan, 2009) also note that bad governance and poor institutional quality will affect the country’s economic development. Another study done by (Zakaria & Fida, 2010) finds indirect effects of democracy on economic growth. Pakistan’s Economic Growth is keep fluctuating from time to time. Pakistan’s Economic Growth GDP was strong in 1991 which was 7.57% and this rate was further decreased to 2.1% in 2000. However further increased over the time by 8.96% in 2003 and 2004 a study done by (Zaidi, 2005) (Iqbal, Shaikh, & Shar, 2010). However Pakistan’s overall GDP kept on decreasing in the era of 2007 to 2011 just due to the political instability and the corruption which kept increasing in these years. This political instability also leads towards security threats and also to the business environment of the Pakistan. Similarly, all this political

instability caused the inflation rate 13.8% in 2011 which was 3.6% in 2001. The overall economic growth of the Pakistan was decreasing in 2007 due to the natural flood's and Political Parties rivalry issues, all this lead Pakistan more at the bottom position in the history of Pakistan. Political Stability is one of the most important aspect of the development of the country and especially for the business environment of the country said by (Husain, 2009)

If the country's Political Stability conditions are not good, in this regard foreign visitors hesitate to invest in that country until the environment of the country is well according to the fruitful profitable environment (Brada, Kutan, & Yigit, 2005), (World Bank Report, 2011), (UNCTAD, 2011). While in the Pakistan's case, it is categorically mentioned in in the World Bank Report which was published in 2011 that the investments in the private sector is low due to the political instability and lots of corruption.

### Critical Assessment

In the past researches researcher worked on the political stability affections on the performance of Pakistan. Sufficient work has been done in this regards. "Political instability leads to higher inflation" as shown in (Aisen & Veiga, 2006). The point is political instability is a vast field but political instability must be presented separately. All the issues must be addressed like (Alesina, Ozler, Roubini, & Swagel, 1996) "used data on 113 countries from 1950 to 1982 to show that GDP growth is significantly lower in countries and time periods with a high propensity of government collapse". The main issue in the previous researches is that they not highlighted the point of corruption which leads toward the political instability as said by (Haider, 2013). But from many years and recently some other factors are also now the part of political Instability which are affecting the performance of Pakistan. Like, recently two Pakistani Political Parties Pakistan Tehreek e Insaf and Pakistan Awami Tehreek decided to start the Long March from Lahore to Islamabad in respect of meeting some demands like resignation of Prime Minister of Pakistan. As Long March started towards Islamabad. Stock Exchange performance at once came down at low (World Development Report 2014). When they reached Islamabad. All the business Market's and stock exchange was very low in performance. It is all due to political instability. A Big Multinational Mitsubishi Electronics transferred its business from Pakistan to other country in the days of Long March. This point is missing in previous research. Not much work done on this point. This issue must be addressed properly that these strikes are also impacting the economy of the country badly. Otherwise it will be very difficult to attract foreign investors. IMF stopped its funding to Pakistan due to the instability in the environment due to which Pakistan suffered from increasing in the prices of daily use (Daily Times Report) (INP, 2014).

### Conclusion

This study mainly focused the impact of political instability on the economic position of the country. In concluding and going through all the literature which was available on this topic. It is further concluded that political situation is one of the most important part which play its vital role in the development of the country. If the political situation of the country is well stabled then a country can be strong economically similarly on the other side if there is instability in the political environment of the country then country's economic progress will be very low.

### References

- Acemoglu, D. (1995). Reward Structures and the Allocation of Talent. *European Economic Review*, 39: 17 – 33.
- Aisen, A., & Veiga, F. (2006). Does Political Instability Lead to Higher Inflation? A Panel Data Analysis. *Journal of Money, Credit and Banking* 38(5), 1379–1389.
- Alesina, A., & Perotti, R. (1996). Income distribution, political instability, and investment. *European Economic Review* 40, 1203- 1228.
- Baumol, W. (1990). Entrepreneurship: Productive, Unproductive, and Destructive. *Journal of Political Economy*, 98: 893 – 921.
- Baumol, W. (2004). Entrepreneurship, Growth and Rent-seeking: Henry George Updated. *The American Economist*, 48: 9 – 16.
- Brada, J. C., Kutan, A. M., & Yigit, T. M. (2005). The effects of transition and political instability on foreign direct investment in ECE emerging market. *Paper presented at the United Nations Economic Commission for Europe (UNECE) Spring Seminar*.
- Husain, I. (2009). The Role of Politics in Pakistan's Economy. *Journal of International Affairs*, 63(1), 1-18.
- INP. (2014, December 10). *Long-march, sit-ins affect economy of Pakistan: WB*. Retrieved from Daily Times: <http://www.dailytimes.com.pk/national/10-Dec-2014/long-march-sit-ins-affect-economy-of-pakistan-wb>
- Iqbal, M. S., Shaikh, F. M., & Shar, A. H. (2010). Causality Relationship between Foreign Direct Investment, Trade and Economic Growth in Pakistan. *Asian Social Science*, 6(9), 82.

- Khawaja, M. I., & Khan, S. (2009). Reforming institutions: Where to Begin? *Pakistan Development Review*, 48: 241 – 267.
- Mauro, P. (1995). Corruption and Growth. *The Quarterly Journal of Economics*, 110: 681 – 710.
- Michael, S. (1971). Federal Political System in Federal societies. In Peter Meckison Canadian Federation (Toronto). pp.119-120.
- Murphy, K. M., Shleifer, A., & Vishny, R. (1993). Why is Rent-Seeking so Costly to Growth? *American Economic Review*, 83: 409 – 414.
- UNCTAD. (2011). *World Investment Report. United Nations*. New York.
- World Bank Report. (2011). United State, New York.
- Zaidi, S. A. (2005). Issues in Pakistan's Economy 2nd Edition. *Oxford University Press: USA*.
- Zakaria, M., & Fida, B. A. (2010). Democratic Institutions and Variability of Economic Growth in Pakistan: Some Evidence from the Time-series Analysis. *Pakistan Development Review*, 48: 269 – 289.