# Macroeconomic Factors and Economic Growth in Palestine

Subjects: Economics

Contributor: Mosab I. Tabash , Umar Farooq , Samir K. Safi , Muhammad Nouman Shafiq , Krzysztof Drachal

It is an immense need in the current age to sustain economic growth to ensure a better living standard for residents of a country. For this purpose, policy officials make strategies and focus on other economic indicators including trade, investment, borrowing, and inflation, etc., to escalate their country's economic growth. In this regard, many studies explore different factors affecting economic growth. The empirical outputs of these studies suggest the dynamic association between different macroeconomic factors and economic growth in different economies of the world. The emerging literature is silent on quantifying the dynamic effect of such factors on the economic growth of Palestine.

ARDL economic growth macroeconomic factors Palestine

## 1. Introduction

Among the others, some key factors that adhered to economic growth and dominantly determined economic health are debt volume, government expenditures, and government investment, etc., as suggested by prior studies. From a growth perspective, the volume of debt acquired by a country has a dynamic impact on the economic growth of a country. It can influence economic growth asymmetrically. In this regard, an empirical study conducted by Spilioti and Vamvoukas (2015) has vowed the positive effect of debt volume on the economic growth of Greece, implying the growth-promising role of debt that can be used in renovation or expansion of different development projects. Some other empirical studies have also supported this notion in alternative data specifications (Bal and Rath 2014; Ndoricimpa 2020; Makhoba et al. 2021). However, some studies have posited the adverse association of debt level with economic status (Daud and Podivinsky 2014; Kharusi and Ada 2018; Asteriou et al. 2021), suggesting the hampering role of debt in determining economic growth. Similar to debt, the literature has contradictory views regarding the role of other economic factors, e.g., inflation, government expenditures, etc., in determining economic growth. Such inconclusive outcomes of the literature argue to further arrange the more empirical studies that specify the dynamic influence of macroeconomic factors on the economic growth of a country.

Due to war and political instability in Palestine, the economy of Palestine is dwindling and has a slow growth rate. In this case, it is necessary to suggest some key factors that can play their vital role in improving economic growth. Given that, the current analysis unveils the role of various economic forces suggested by other studies in determining the economic growth of Palestine. The current empirical analysis tends to find out the dynamic impact of various macroeconomic factors on the growth of real GDP of Palestine. In the current analysis, the volume of

GDP is a dependent variable while government debt, total investment, government expenditures, and donations, etc., serve as explanatory variables. For regression analysis, researchers employ the quarterly data ranging from 2001Q1 to 2020Q4 and apply the *Autoregressive Distributed Lag* (ARDL) model to quantify the regression. The statistical findings imply that government debt, donations, government expenditures, and the unemployment rate have a negative impact whilst credit facilities, inflation, and total investment positively and significantly influence the economic growth of Palestine. Such dynamic impact of various macroeconomic factors depicts that government debt enhances the burden of interest payments and negatively impinges upon the real GDP. Similarly, the receipt of donations may hamper economic health by influencing the institutional efficiency and worsening the efficiency of policy officials due to greater dependence on donations. Government expenditures lead to a deterioration of real GDP for unmatured economies owing to the lower availability of funds to cover such expenditures and the improper management of funds due to high corruption rates. The negative influence of unemployment can be defined as high unemployment, leading to low per capita income and thus less economic activity. Concluding, the current empirical analysis highlights the asymmetric impact of various economic factors on economic growth of Palestine.

In contrast, the positive association of credit facilities with real GDP shows the favorable impact of private funds on the exploration of economic activities that further results in positive economic status. Similarly, the positive correlation of the inflation rate with economic growth suggests that the inflation rate may lead to more economic progress as it encourages the producers on voluminous production due to the price appreciation phenomenon. Lastly, the positive interaction of total investment with economic growth exemplifies the significance of government spending in expediting the attached economic activities. The findings of the study add new thoughts regarding the dynamic impact of various economic factors on the real GDP of Palestine. The analysis provides robustness to empirical findings of existing empirical studies arranged on other economies of the world and suggests focusing on these factors to achieve the objective of better economic status in Palestine. Researchers achieved an important research goal regarding the role of various economic forces that can boost or slow down the economic progress of Palestine. In addition, the current analysis can be marked as innovative as it supplements the innovative evidence by exploring the empirical impact of considered economic factors on Palestine’s economy. By employing the modern econometric technique, i.e., ARDL, the current study answers an important research question: what are the possible factors that can boost the economic growth of Palestine and vice versa? The policy officials should pay more attention to such factors that appeared to hamper economic growth and should develop some policy modifications to treat such factors. They should further escalate the other factors, e.g., private credit facilities and more investment to sustain the economic growth.

## 2. Influence Factors on Economic Development

Economic growth is a multifaceted factor that is affected by other factors including external borrowings, total investment, government spending, donations, and inflation rate, etc. In this regard, a number of studies emerged in the literature that tend to explain the impact of such factors on real GDP, commonly known as economic growth. For instance, Kharusi and Ada (2018) examined the correlation between external borrowings and the economic growth of Oman. They have found a negative relationship, implying that an increase in external debt can enhance

the burden of interest payments which further hampers economic growth. Supporting this, another study conducted by Abdelaziz et al. (2019) has specified the channel through which external debt deteriorated the economic growth. They have suggested that a higher volume of external debt impedes investment due to costly financing and hence leads to negative economic growth. Similarly, Razzaque et al. (2017) have documented the association between exchange rate volatility and economic growth. The empirical analysis of their study indicated that a 10% decline in the exchange rate may lead to a 3.2% increase in real output, indicating the favorable impact of a lower rate of exchange on economic expansion. The findings of their study appeal for re-considering the exchange rate policy for Bangladesh to achieve the objective of high economic development. Similar effects were also found by another study arranged by Habib et al. (2017) on some other developing economies. An appreciation in the rate of currency exchange (depreciation in the exchange rate) significantly reduced the real GDP (enhanced the real GDP). In view of such literature suggestions, the study rechecks the role of such factors on the economic growth of Palestine and provides robustness.

The receipt of donations is another factor that can affect the situation of economic prosperity. This effect is more obvious in poor countries or countries bearing the economic status of under-developed or aid intensive (Bayinah 2017). Donations are made in various forms including gifts, monetary help, or other consumable goods that may enhance human well beings in specific regions (Cappellari et al. 2011). In Islamic states, most donations are made in the form of *Zakat*1. Some studies have attempted to find its association with economic growth. For instance, Jedidia and Guerbouj (2021) have examined the effect of Zakat inflow on the economic expansion of eight Islamic states and found robust evidence of the favorable impacts of such inflow on real GDP. They have argued that the receipts of such funds can be used to fund investment and other government expenditures that can further augment economic growth. Similarly, another study arranged by Athoillah (2018) has suggested the positive influence of Zakat on economic development and its adverse effect on poverty. However, no specific study was found that explores the direct relationship between donations and economic development, particularly in Palestine.

Some other studies have apparently considered the availability of credit as an important factor to achieve economic expansion. ALZYADAT (2021) studied the impact of bank credit facilities on the non-oil economic growth of Saudi Arabia. The empirical analysis of his study reveals that credit facilities have a favorable influence on extending the economic activities that eventually lead to positive economic growth. Such credit facilities help in capital formation and financing development projects. Duican and Pop (2015) evaluated the impact of credit facilities on the economic growth of Romania and found the positive influence of such facilities in expanding economic activities. Additionally, the inflation rate has a dynamic impact on economic development. Some studies have argued a positive effect (López-Villavicencioa and Mignon 2011; Law and Singh 2014) while others supported a negative effect of inflation rate on the economic activity levels of an economy (Bick 2010; Bittencourt et al. 2015; Khan and Hanif 2020). The proponents of the inflation rate have argued a threshold point on which inflation may boost economic growth. Beyond this threshold point, inflation mostly impedes economic activities due to the inflationary effect of prices on the demand of consumers which turn the consumption rate to the lower end.

It is necessary for each country to spend a significant amount of funds to finance its running operations. Such types of spending have a dynamic association with the economic development of this country. Given that, Hamdi and

Sbia (2013) have found a vigorous relationship between government expenditures, oil revenues, and economic development in the economy of the Kingdom of Bahrain. The empirical analysis of their study suggested that oil revenues are a major source for financing the government spending that may have a negative impact if it exceeded this revenue. They have further conjectured that such spending may impede the economic expansion specifically for oil-dependent economies because such economies are more open to any economic shocks that can enhance the volatility of oil revenue. Another study, arranged by Onifade et al. (2020), has documented the negative impact of expenditures on economic development of Nigeria. Such negative effects of government spending on economic expansion can be supported by the view that spending can create financial stringency for developing countries and thus may reduce the growth of the economy (Ahuja and Pandit 2020).

Some other empirical studies further provide a quantitative assessment of the mixed influence of government investment and unemployment on economic development. For instance, Vedia-Jerez and Chasco (2016) estimated the positive effect of domestic investment on the economic growth of South American economies. They have suggested that economic growth was driven by physical investment in capital accumulation by the government. Nguyen and Trinh (2018) have also supported the similar effects for Vietnam and stated that both public and private investments have positive effects on both short-term and long-term economic growth. Irrespectively, the literature has illustrated the detrimental outcomes of unemployment for economic development. Ahuja and Pandit (2020) have confirmed the negative effect of unemployment on economic expansion in 59 economies from different areas of the globe. However, Sadiku et al. (2015) found robust evidence on the insignificant effect of unemployment on economic growth. Pasara and Garidzirai (2020) have also suggested the insignificant effect of unemployment on economic progress in the short run. Briefly, the literature argued the dynamic impact of various macroeconomic factors on economic growth for different countries of the globe.

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