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# The impacts of tourism, energy consumption and political instability on economic growth in the MENA countries

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## HIGHLIGHTS

- Tourism and energy consumption have positive impacts on GDP growth.
- GDP reacts negatively to political instability.
- Energy-led growth and tourism-led growth hypotheses are validated in MENA countries.
- Supporting tourism, energy use and political stability will enhance economic growth.

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## ABSTRACT

Using panel data of 24 countries in the Middle East and North African (MENA) region from 2001 to 2009, the purpose of this study is to examine the impacts of tourism, energy consumption and political instability on economic growth within the neoclassical growth framework. To address the objective of this study, we utilise both the static panel data approach as well as the dynamic generalised method of moments (GMM) estimator to examine the impact of candidate variables. Our results show that energy consumption and tourism significantly contribute to the economic growth of countries in the MENA region. Hence, our study lends some support to the existence of the tourism-led growth and energy-led growth hypotheses in the region. In line with our expectation, our estimation results also reveal that political instability impedes the process of economic growth and development in the MENA region. Therefore, macroeconomic policies to promote expansion in tourism and energy consumption will directly stimulate economic growth. Additionally, efforts to help the region overcome its history of political instability would attract more international tourist arrivals and further invigorate economic growth.

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## 1. Introduction

Economic growth is one of the most important elements in macroeconomic analysis. Therefore, confirming the actual catalysts of growth is essential to the formulation of effective policy instruments that will promote long-term economic growth. Theoretically, tourism and energy play an important role in stimulating economic growth. Tourism is one of the largest and fastest growing services sector in the world. It may contribute to the economic growth of a country by creating more employment opportunity, increasing investment in new infrastructure, and augmenting a country's tax revenues and foreign exchange earnings. Moreover, Stern, (2011) noted that energy influences economic growth through its impact on production activities.

Nevertheless, the existing empirical literature reveals that the impacts of tourism and energy consumption on economic growth remain a puzzle. Some of the empirical studies found that tourism and/or energy consumption would effectively promote economic growth (e.g. Tang, 2008; Tang and Abosedra, 2012; Tang and Tan, 2013a, 2013b; Tang, 2013; Apergis and Tang, 2013), whereas others empirical studies argued that economic growth is not the result of tourism or energy consumption (e.g. Oh, 2005; Katircioğlu, 2009a; Payne and Mervar, 2010; Shahbaz and Feridun, 2012). Apart from that proposition, we also find that most studies ignore the role of institutional factors such as political instability on economic growth. According to Aisen and Veiga (2013), political instability is likely to create volatility and frequent change in policies. This tension would be harmful to the macroeconomic performance of any country (see also Campos and Nugent, 2002). Moreover, a recent study conducted by Ingram et al. (2013) found that political instability is likely to jeopardise the peace and security of a country, which in turn has a negative impact on tourism.

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Fletcher and Morakabati (2008) have also highlighted similar outcomes in Fiji and Kenya. Therefore, political instability is another important factor in determining the economic growth of a country.

The purpose of this study is to investigate empirically the role of tourism, energy consumption and political instability in the economic growth of 24 countries in the MENA region via panel data estimation. Within the neoclassical growth framework, our motivation in this study goes beyond examining the validity of the tourism-led growth and energy-led growth hypotheses. This study also attempts to compare the impact of tourism, energy consumption, capital, and political instability in the process of economic growth of these countries. Therefore, more useful and reliable information can be provided to the policymakers to formulate effective policies to promote long-term economic growth for the MENA region. This region was chosen as the focus of this study because empirical analysis of countries in this region is relatively scarce. In addition, the characteristics of the countries in the MENA region are very suitable to the case of the present study, for example, its abundance in oil and natural resources. More specifically, World Bank (2012) showed that the MENA region covered approximately 57 per cent of the world oil reserves and approximately 41 per cent of natural gas resources. In terms of tourism, MENA has been named as a *tourist paradise*, owing to the rich history of its ancient civilisations, its unique cultural heritage and many religious sites. Bell et al. (2012) noted that in the MENA region nearly 4.5 per cent of GDP is contributed by the tourism sector and 6.8 per cent of total employment is in the tourism sector. In addition, Al-mulali (2011) claimed that the economy of the MENA region is likely to be influenced by fluctuations in oil price and political instability. In 2011, the tourism sector in the MENA region suffered a decline in tourist arrivals owing to the Arab Spring revolution and the on-going political instability in the region (UNWTO, 2012). Specifically, international tourist arrivals to the Middle East dropped by 8.4 per cent and those to North Africa declined by 6.5 per cent. Therefore, it is of utmost importance to analyse the role of tourism, energy consumption and political instability in the economic growth of countries in the MENA region.

The rest of this study will be organised as follows. The subsequent section will provide the literature review pertaining to the tourism-led growth hypothesis, energy-led growth hypothesis and the impact of political instability on economic growth. We describe the empirical model and the source of data in Section 3. The econometric techniques used in this study will be reported in Section 4. Then, Section 5 will discuss the empirical results of this study. Ultimately, the conclusions and policy implications are presented in Section 6.

## 2. Literature review

Over the last few decades, the question of whether tourism, energy consumption and political instability influence the rate of economic growth has formed an important query among economists and policymakers. Such interest stems primarily from the important policy implications in relation to the desired actions that can accelerate economic growth and prosperity. Empirical studies on this issue have provided conflicting results, which have been reported in the literature. There is no consensus among economists and policymakers about the nature of the relationship of such variables in economic growth. Various econometric techniques have been used to examine the topic. In the following sub-sections, we provide a brief review of studies that have addressed the nexus of tourism, energy consumption and political instability with economic growth.

### 2.1. Tourism

In this sub-section, we present the literature review of tourism-growth nexus. From our reading, the role of tourism in the process of economic growth has long been debated in the economics literature. Studies have been conducted in a country-specific and/or multi-country framework using various methodologies and models. However, it remains unclear whether or not tourism expansion could effectively stimulate economic growth. Using the cointegration and Granger causality tests, Balaguer and Cantavella-Jordá (2002) for Spain, Gunduz and Hatemi-J (2005) for Turkey, Belloumi (2010) for Tunisia, Akinboade and Braimoh (2010) for South Africa, Brida et al. (2010) for Uruguay, Katircioğlu (2010) for Singapore, Lean and Tang (2010) for Malaysia, Tang and Abosedra (2012) for Lebanon, and Tang (2013) for Malaysia have observed that tourism and economic growth are likely to be cointegrated and tourism Granger-cause economic growth. Recently, Tang and Tan (2013a) further confirmed that the tourism-led growth hypothesis in Malaysia is not only valid, but it is also stable from 1995 to 2009. On the other hand, there are also studies which found that economic expansion is not the result of tourism expansion. In the case of South Korea, Oh (2005) found that economic growth Granger-cause tourism rather than the other way around. Other studies such as Katircioğlu (2009b) and Payne and Mervar (2010) also found similar outcomes. Against the conventional wisdom of at least one way of causality between tourism and economic growth, Katircioğlu (2009a) found that tourism and economic growth are not related at all, particularly in the long-run because they are likely not to be cointegrated.

Apart from that, some other studies also estimated the impact of tourism on economic growth. Most studies found that tourism has a positive impact on economic growth but the size of the impact tends to be less than 1 per cent (i.e. inelastic). For example, Modeste (1995) analysed the impact of tourism on economic growth in three Caribbean countries (i.e. Barbados, Antigua and Barbuda and Anguilla) using pooled OLS estimation. The study showed that only 0.25 per cent of economic growth in the three Caribbean countries is contributed by 1 per cent change in tourism. Gökovali and Bahar (2006) conducted a study to examine the contribution of tourism on economic growth in the Mediterranean countries via panel data estimation. They found that tourism only contributes approximately 0.1 per cent of Mediterranean countries' economic growth for every 1 per cent increase in tourism. In the case of Turkey, Kaplan and Çelik (2008) also showed that a 1 per cent increase in tourism, in the long-run, causes economic growth to increase by only 0.3 per cent. Likewise, Katircioğlu (2010) found that the impact of tourism (0.23) on economic growth in Singapore is also about same as Kaplan and Çelik (2008) found in Turkey.

### 2.2. Energy consumption

Since the influential work of Kraft and Kraft (1978), the relationship between energy consumption and economic growth has been widely studied and debated among economists, environmentalists and policymakers in the world. Undoubtedly, many empirical studies have been published on this topic, but we are unable to review all studies within the limited space of this study. In light of this limitation, we only review articles that are relevant to the present study. Although many believe that energy is an input of production, empirical studies still fail to find strong evidence to support the view that energy use leads to economic growth. Apergis and Tang (2013) articulated that the variations of causality results among studies are highly due to the choice of model specification and the stage of economic development (see also Ozturk, 2010). Specifically, they found that energy

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