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Trade Openness, Institutions and Industrial Growth in Pakistan: An Application of Bayer and Hanck Cointegration Test

Abdul Farooq
COMSATS University Islamabad, Lahore Campus
A.R. Chaudhary
Dean School of Social Sciences at NCBA&E, Lahore
Ahmad Nawaz
COMSATS University Islamabad, Lahore Campus

Abstract
Per Capita Income and productivity of industrial sector are very low in developing nations including Pakistan as compared to developed nations. Three reasons have been mentioned in the literature for this difference; geographical differences, role of international trade and the quality of institutions. This study examines the short run and long run impacts of trade openness, and quality of institutions, on the growth of industrial sector of Pakistan, using time series data over the period of 1984-2013.The Cobb- Douglas production function has been augmented by adding quality of institutions, trade openness, and financial development variables to probe their impacts on the industrial growth. The most recently developed combined cointegration technique by Bayer and Hanck (2013) has been used to check the cointegration among the variables. Long run empirical results show that trade openness, and quality of institutions positively contributes to the growth of industrial sector. These results suggest that better quality and well-functioning of the institutions is a pre requisites to boost the foreign trade, and the growth of industrial sector of Pakistan.
Keywords: Trade Openness, Institutions, Industrial Growth, Pakistan

The per capita GDP and the productivity of industrial sector are very low in Pakistan as compared to the developed countries. Pakistan has a per capita GDP of $1200, compared to Luxembourg's $50061(WDI,2015). In the numerous literatures on this topic three aspects have been mentioned for this enormous difference; geographical differences, role of international trade, and the quality of institutions (Rodrik et al.,2004). This study focuses on the last two aspects. It is also worth mentioning that relationships between the quality of institutions, trade openness and economic growth have been the topic of intense debate among the development economists in these days. The endogenous growth theories have deliberated trade openness as the key driver of economic growth through the channel of technological spillover (Romer,1990).Similarly numerous studies have also pointed only to trade openness as one of the mechanisms to promote economic growth (Krueger, 1997; Grossman and Helpman,1990; Lucas,1988;Romer,1990; Young,1991; Wacziarg,2001;Kaufmann et al.,2002;Yanikkaya, 2003; Greenaway et al., 2002; Foster, 2008;Chang and Ying,2008;Das and Paul,2011;Squalli and Wilson,2011).In contrast to the above empirical findings, few studies have revealed that trade openness hampers economic growth (Batra, 1992; Batra and Slottje, 1993; Vamvakidis, 2002);Parilti and Tunc,2018).

Pakistan has gradually liberalized its economy after accepting the first IMF Structural Adjustment Program in 1988 and joining the World Trade Organization in 1995.But the fruits of trade openness has not been realized in terms of economic growth Chaudhary and Ahmed, (2004). It might be due to the poor quality of the institutions. Institutional quality has been deliberated a new driver of economic growth (Stiglitz,1998,2000; Frankel and Romer,1999; Dollar and Kraay,2003;Rodrik et