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Assessing the Dynamic Economic Impact of Tourism for OIC Members

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Abstract: The purpose of this study is to investigate the relationship between tourism expansion and economic growth in OIC countries by using a panel data method and GMM model over the period of 1995-2010. The results show that tourism significantly contributes to the economic growth of Islamic countries. Also, the result of GMM method shows that the tourism-growth nexus is a dynamic phenomenon. The Johanson co-integration analysis indicates that there is a long-run relationship between tourism expansion and economic growth in OIC countries. Sensitivity analysis using a sample of developing and developed countries shows that tourism expansion also has a positive effect on economic growth in both groups. Consequently, the results make some policy recommendations of promoting tourism as a growth and development strategy for Islamic countries.

JEL Classification: O40: O50: C33
Key words: Tourism Expansion · Economic Growth · OIC Countries · GMM model

INTRODUCTION

According to the World Tourism Organization (WTO), tourism has become one of the fastest growing industries in the world in the last decade. In the analysis of tourism, economists emphasize the economic effects of tourism. The development of tourism industries increases household incomes and government revenues through multiplier effects and it also improves balance of payments. In addition, it increases foreign exchange income and creates employment opportunities [1, 2, 3]. Most of the Islamic countries are developing countries that suffer from many economic problems such as low economic growth rates and lack of physical capital, where the tourism industry is not a capital-intensive one and tourism development can be a low- cost solution to escape from low economic growth rates and unemployment. In addition, there are huge opportunities to develop Islamic tourism in these countries. Nowadays, Islamic tourism is a new tourist destination in the world. Tourism linked to religion acts as a powerful motivation for travel. Religious buildings, rituals, festivals and religious events, cultural and archeological heritages, historical civilizations and religious sites are important tourist attractions for those are the followers of the particular system of belief [4, 5]. Various organizations such as Organization of Islamic Conference (OIC) can play vital role in this regard and tourism development can ensure their economic sustainability [6]. Therefore, study of tourism business development and the investigation of its effects on macroeconomic performances, especially on economic growth, are highly important in Islamic countries.

With one and half billion followers across 57 countries, Islam's role in tourism is important to tourism and hospitality managers in both Muslim and non-Muslim countries. Islamic countries contain 30% of the world population by 2012. Tourism in Muslim countries is a major market with 10% of global tourism revenue going to these markets. Five countries of OIC members-Morocco, Egypt, Turkey, Saudi Arabia and Malaysia-dominate other Muslim countries in tourism arrivals with 85.5 million guests in 2011. Tourism is already a dominate industry in Muslim countries such as Morocco, Tunisia, Egypt, Turkey and Malaysia and a growing industry for the united Arab Emirates, Indonesia and Jordan. The WTO report shows a 706%, 53% and 329% increase in tourist arrivals, respectively in the UAE, Indonesia and Jordan from 2000 to 2010 [7].

The purpose of this study is to investigate the relationship between tourism expansion and economic

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growth in OIC countries through a panel data method. Therefore, the question that this study is going to answer is as follows: does tourism development have a positive effect on economic growth in OIC countries? This study consists of six sections. Following the introduction, in the second section, the literature review is presented. A brief picture of international tourism in OIC countries is discussed in section 3. Section 4 is about model specification and econometric method. Finally, the results and conclusions are presented in sections 5 and 6 respectively.

Literature Review: The economic impact of tourism expansion is well known and tourism is fastest growing industry in the world. Tourism can cause economic development through its impact on employment, enhancement of infrastructures, generation of income taxes, exports, profits and acceleration of global peace [8, 9]. Theoretical models that consider a causal relationship between non-traded goods, such as tourism and economic growth are recent phenomenon. There are two main hypotheses about the economic effects of tourism: Export Led Growth Hypothesis (ELGH) and Tourism-Led Growth Hypothesis (TLGH) [10]. In accordance to the export led growth hypothesis, tourism can be considered as an export that causes economic growth. But there is a variance between tourism and other goods and services which are being exported. Essentially, tourism is a kind of export that is used by consumers in host countries [11]. Directly derived from the export led growth hypothesis, the tourism led growth hypothesis has recently appeared in literature. It is a special type of export led growth hypothesis focusing on international tourism arrivals. It assumes tourism to be a major factor of long-run economic growth [12, 13]. Tourism-led growth may take place when tourism demonstrates a stimulating influence across the economy in the form of spillovers and other externalities [14].

In addition of these hypotheses, there are some other channels in which tourism can cause economic growth. Some of them have been mentioned below:

- Foreign exchange generation created by tourism activities will have a positive contribution to the balance of payments, so it might create economic growth in the long- run. On the other hand, tourism increases local revenues and budget deficits can also benefit from increased tax revenues [11, 12].
- Tourism expansion also increases the demand of goods and services including lodging, restaurants, amusements, retail trade and transportation facilities [15]. Apart from this, tourism expenditure by foreign tourists can enhance domestic tourism construction as well as bring about an accumulation of physical and human capital [1].
- The foreign exchange that has been earned through the tourism industry can be used to import intermediate and capital goods to produce goods and services, which in turn leads to economic growth [16].
- International tourism has the potential of enhancing efficiency through increased competition among firms and local crafts for international tourism destinations and it facilitates the exploitation of economies of scale in local firms [17].
- It is often hoped that it will reduce hardships through the promotion of upward labor mobility [18]. In addition, tourism development stops emigration of the population from less developed regions of a country to mega-cities and therefore prevents some economic problems in mega-cities. Furthermore by developing the tourism sector, the other economic sectors such as international trade, transportation, communications, banking and agriculture would also be developed [13].

The related literature hosts some research into the issue, for example; Fayissa [19] indicated that revenues from the tourism industry positively contribute to economic growth of Latin American countries. Kreishan [2] examined the causality relations between tourism earnings and economic growth for Jordan. The findings showed that there is a positive relationship between tourism development and economic development in the long run. Khalil [20] resulted that there is a strong relationship among tourism, receipts and economic growth in Pakistan. They concluded that economic expansion in Pakistan requires tourism development. Schubert [21] found that development of tourism could cause economic growth and increase trade between Antigua and Barbuda. Seetanah [22] explored the potential contribution of tourism to economic growth and development in the economies of 19 islands. The results showed that tourism significantly contributes to the economic growth of these islands' economies. Akkemik [23] and Arsalanturk [24] showed that the GDP elastic of international tourism is relatively low and the impact of foreign tourist expenditures on domestic production, value added and employment in Turkey is modest.

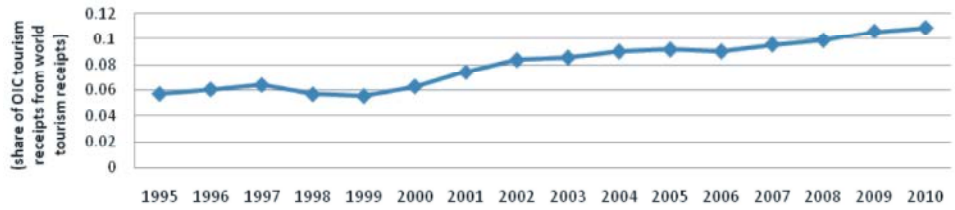

Fig. 1: Share of OIC tourism receipts from world tourism receipts
Source: World Development Indicator

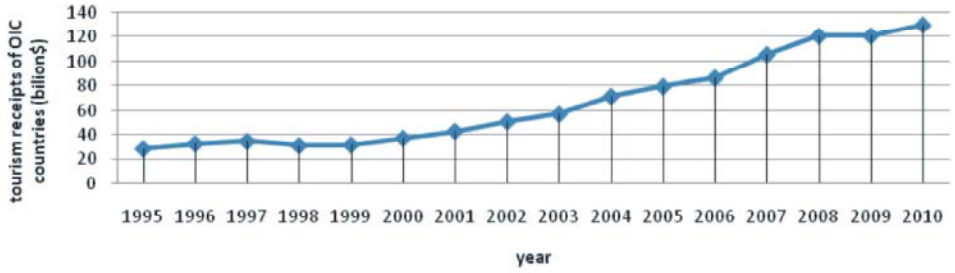

Fig. 2: Tourism receipts of OIC countries (billion$)
Source: World Development Indicator

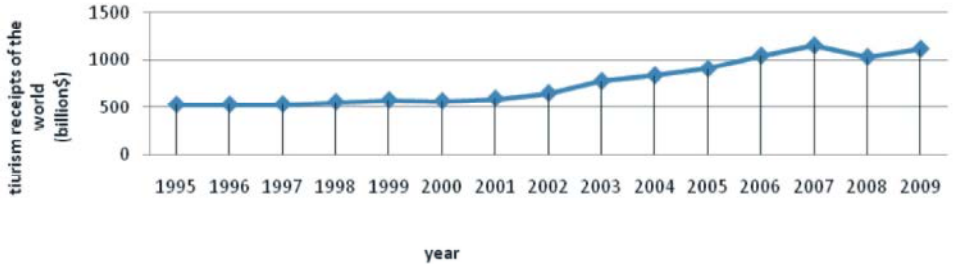

Fig. 3: Tourism receipts of the world (billion$)
Source: World Development Indicator

A Brief Picture of International Tourism in the Oic Countries: There are considerable potentials for a sustainable development of international tourism sector in OIC countries. Ancient civilizations, historical and religious monuments, spiritual atmospheres, common culture and language between some of OIC countries are factors that can increase tourism activity between these countries. In terms of geographical location, Muslim countries are very diverse and varied. This proper geographical location of OIC countries can ease economic, politic and communication relationships that can lead to the development of tourism in these countries.

This paper is going to assess the performance and economic role of the international tourism sector in OIC countries. The most traditionally used indicators to measure international tourism are international tourism arrivals and international tourism receipts. According to figure 1, the share of OIC countries from world tourism receipts was 11 percent in 2010. In the year of 1995, the share of tourism receipts of OIC countries from $498 billion of world tourism receipts were $28.6 billion (5.8 percent of world tourism receipts). But it reached to $130 billion in 2010 increasing by 354 percent over the period of 1995-2010. Therefore, the OIC countries' share in the world tourism receipts has been sustainably ascendant in the recent decade.

Figures 2 and 3 outline the trends in world and OIC countries international tourism receipts. The slope comparison of the two figures indicates that the tourism receipts growth rate in OIC countries is more than the world tourism receipts' growth rate.

The number of tourism arrivals in OIC countries in 1995 was 45378 thousand and it increased to 130479 thousand by 2010. So its growth rate in the period of 1995-2010 was 187 percent. Tables 1 show the top ten OIC countries with respect to their number of tourism arrivals and tourism receipts.

Table 1: Top ten OIC countries with respect to their number of tourism arrivals (thousands) and tourism receipts (million$)

Country (tourism arrivals)	2000	2010	Country (tourism receipts)	2000	2010
Turkey	9,586	27,000	Turkey	7,636	24,784
Malaysia	10,222	24,577	Malaysia	5,873	18,315
Egypt	5,116	14,051	Egypt	4,657	13,633
Saudi Arabia	6,585	10,850	Morocco	2,280	8,176
Morocco	4,278	9,288	Lebanon	742	8,174
Syria	2,100	8,546	Saudi Arabia		7,655
Indonesia	5,064	7,003	Indonesia	4,975	7,618
Tunisia	5,058	6,903	Syria	1,082	6,308
Bahrain	2,420	5000	Jordan	935	4,018
Jordan	1,580	4,557	Tunisia	1,977	3,477

Source: World Development Indicator

It shows that the tourism receipts and number of tourism arrivals in Turkey have been tripled in the recent decade and Turkey is the most tourism recipient country. The number of tourism arrivals and tourism receipts in Malaysia have been doubled and tripled within the last 10 years respectively. Also, the tourism receipts of Egypt, Morocco and Lebanon have been multiplied by 3, 3.5 and 11 over the period of 2000-2010, respectively. But the world tourism receipts have been just doubled in the recent decade. Therefore, the speed of tourism growth in some OIC members is more than world tourism growth speed.

Model Specification and Econometric Method: The presented model in this section is the augmented Solow growth model and is based on the principles of the latest growth study of Seetanah [22] and Fayissa [19]. The model is:

$$\ln Gr_{it} = \beta_0 + \beta_1 \ln Gr_{it-1} + \beta_2 \ln in_{it} + \beta_3 \ln hu_{it} + \beta_4 \ln hce_{it} + \beta_5 \ln op_{it} + \beta_6 \ln tou_{it} + e_{it} \quad (1)$$

Where $lnGr_{it}$ is the log of GDP per capita, $lnGr_{it-1}$ is the log of GDP per capita in previous year which shows conditional convergence, $lnin_{it}$ is the log of gross fixed capital formation as percentage of real GDP that is used as investment in physical capital, $lnhu_{it}$ is log of human capital (sum of secondary and tertiary school enrolment), $lnhce_{it}$ is log of household consumption expenditure as percentage of real GDP per capita, $lnop_{it}$ is the log of openness (exports plus imports to GDP ratio) and finally $lntou_{it}$ is the log of tourism receipts per capita. Using the World Bank database, this study focuses on a sample of 53 OIC countries over the period of 1995-2010. Mauritania, Palestine, Tajikistan and Somalia have been dropped in the estimation through the lack of data. In order to do sensitivity analyses, the study is extended to two other samples of countries namely developing and developed countries and uses another tourism proxy "number of international tourism arrival".

In some econometric models especially in growth models, some explanatory variables are pre-determined (such as education years) or endogenous (such as foreign direct investment) and the growth in time t may depend on growth in previous year. So the use of panel data without considering the endogeneity would result in biased estimations [19, 15]. In order to overcome this problem, Arellano and Bond [25] developed a Generalized Method of Moment (GMM) dynamic panel data estimator, which can explain the dynamic factors of the growth model. This model includes lags of both the dependent and independent variables as instruments to explain the dynamic features of the model. The base model of GMM method is written as follows:

$$\Delta Y_{it} = \alpha \Delta X_{it-1} + \beta \Delta Y_{it-1} + YZ_{it} + v_i + \varepsilon_{it} \quad (2)$$

Where ΔY_{it} isthe first difference of natural logarithm of GDP growth in country i in time t. ΔY_{it-1} indicates the first difference of independent variable in previous year. ΔX_{it-1} is the vector of lagged variables and first differentiated endogenous variables. Z_{it} is the vector of endogens variables and v_i, ε_{it} are country specific effects and error terms respectively.

RESULTS

Using fixed and random effect models, this paper starts to do necessary estimations. The results of the Housman test suggested using the fixed effect model. To test for heteroskedasticity of error terms problem, the Likelihood Ratio test has been used.

Table 2: The results of FGLS estimations for OIC countries

variables	Coefficient
C	-0.01
	(-2.03)*
LGD(-1)	-0.007
	(-4.45)*
LIN	0.02
	(5.64)*
LHU	0.002
	(1.99)*
LOPEN	0.001
	(0.043)
LHC	0.002
	(2.52)*
LTOUR RECEIPTS	0.002
	(2.32)*
Number of observation	614
Wald statistic	96.69

The numbers in parentheses shows t statistics

**,*,shows significant level at 99 and 95 percent respectively.

Table 3: The results of GMM estimation for OIC members

Variables	Coefficient
Gr (L1)	0.14
	(15.32)*
LIN	0.019
	(5.89)*
LHU	0.009
	(11.22)*
LOPEN	0.029
	(7.48)*
LHC	-0.03
	(-9.41)*
LTOUR RECEIPTS	0.008
	(9.00)*

Sargan test of over identifying restrictions probe>chi2 = 1.0000

Arellano- Bond test for zero autocorrelation in first differenced errors probe>chi2 = 0.25

Wald test of joint significance probe> chi2 = 0.00

The numbers in parentheses shows t statistics

**,*shows significant level at 99 and 95 percent respectively.

The results showed that there is heteroskedasticity problem between the error terms. To avoid this problem, at the last stage the Fixed- Generalized Least Square (FGLS) method has been used. The results of FGLS estimation for the members of OIC countries has been presented in table 2.

The results of FGLS estimations indicate that the effect of tourism expansion on economic growth in OIC members is positive and significant. These results are consistent with economic theories and results obtained by Seetanah [22], Po [26] and Fayissa [19, 27]. The effect of initial GDP per capita on economic growth is negative and significant. This result is consistent with the results of Seetanah [22] and Fayissa [19, 27] and it shows the existence of conditional convergence theory in economic growth at aforesaid countries. Our results confirm that investment in physical capital has a positive and significant effect on economic growth in OIC countries. Theoretically, gross capital formation directly increases the physical capital stock and it results in economic growth. It also leads to technological improvements indirectly and therefore it gives rise to economic growth [28, 29]. The effect of human capital on economic growth is positive and significant. Some of economic theories consider human capital as an endogenous factor for economic growth, because education and manpower training is an investment which can improve labor productivity and cause economic growth. Openness also has a positive and significant effect on the economic growth of these countries. Household consumption expenditures have a positive effect on economic growth in OIC. This result indicates that household expenditures have been mostly expended on training, housing, nutrition and other factors which increased labor productivity.

In addition to FGLS method, we used Generalized Methods of Moments (GMM) to estimate the model. The result of GMM estimation for equation 1 in OIC countries has been reported in table 3.

Having expected signs of all coefficients, the results show that tourism expansion has a positive and significant effect on economic growth in OIC members. Physical investment, human capital and openness have also positive and significant effects on economic growth. In addition, the positive sign of initial GDP shows that economic growth has dynamic patterns in OIC countries. This result is consistent with the results of Seetanah [22] and Fayissa [19]. In according to the results of the Sargan test, it is concluded that there is no correlation between error terms and instrumental variables, so the validity of results has been confirmed to be interpreted. The null hypothesis that all coefficients are equal to zero has been rejected at the 1% significant level through the results of the Wald test. So the validity of the estimated coefficients has been approved. Also the Arellano- Bond test shows that there is no autocorrelation in first differenced error terms.

Table 4: results of FGLS and GMM estimation for OIC countries

The results of FGLS estimation for OIC countries		The result of GMM estimation for OIC countries	
Variable	Coefficient	variable	coefficient
C	-0.0005		0.14
	(-0.06)*	Gr (L1)	(14.16)*
LGD(-1)	-0.01		0.02
	(-7.03)*	LIN	(8.32)*
LIN	0.01		0.003
	(4.27)*	LHU	(2.50)*
LHU	0.002		0.3
	(2.23)*	LOPEN	(8.43)*
LOPEN	0.003		-0.03
	(1.56)**	LHC	(-9.45)*
LHC	0.002	LTOUR	0.024
	(2.05)*	NUMBER	(7.82)*
LTOUR NUMBER	0.004	Sargan test probe>chi2=1.00	
	(4.01)*		
Number of		Arellano- Bond test	
observation	620	probe>chi2 =0.25	
Wald statistic	116.11	Wald test probe> chi2 = 0.00	

The numbers in parentheses shows t statistics,**,*shows significant level at 99 and 95 percent respectively.

Table 5: the results of FGLS estimation for developing and developed countries

	Developing countries		Developed countries	
Coefficient	model 1	model2	model 1	model2
C	-0.027	-0.03	0.11	0.11
	(-3.53)*	(-3.64)*	(5.31)*	(5.11)*
LGD(-1)	-0.003	0.003-	-0.07	-0.07
	(-3.14)*	(-3.16)*	(-9.44)*	(-9.19)*
LIN	0.027	0.03	0.05	0.05
	(0.004)*	(6.61)*	(6.53)*	(6.27)*
LHU	0.005	0.002	0.01	0.01
	(1.87)**	(0.82)	(1.63)**	(1.73)**
LOPEN	0.012	0.01	0.01	0.017
	(4.33)*	(4.21)*	(6.08)*	(5.64)*
LHC	-0.01	-0.01	0.02	0.024
	(-6.43)*	(-5.13)*	(5.25)*	(5.42)*
LTOUR RECEIPTS	0.002		0.003	
	(2.85)*	-	(3.29)*	-
LTOUR NUMBER	-	0.0014		0.002
		(1.10)	-	(2.55)*
Number of observation	581	556	575	575
Wald statistic	244.38	233.14	175.23	165.23

In order to do a sensitivity analysis, the equation (1) has been estimated again by using number of international tourism arrival proxy. The results have been presented in table 4.

According to table 4, the results are not sensitive to tourism proxy. In both cases tourism expansion has a positive and significant effect on economic growth. The study is also extended to two other samples of countries namely developing and developed countries for useful sensitivity analysis. Therefore the equation (1) has been re-estimated considering both developing and developed countries. The results of FGLS estimation has been reported in table 5.

The results show that tourism receipts and number of tourism arrivals have positive and significant effects on economic growth in developing and developed countries. Physical capital formation, human capital and openness have positive and significant effects on economic growth in the mentioned countries. Household consumption expenditure has negative and significant effect on economic growth in developing countries. According to the neoclassical theory, household consumption expenditure reduces saving rates and causes lower investment and lower economic growth in developing countries. Nonetheless, it has positive effect on economic growth in developed countries because household consumption expenditures expends on health, nutrition and education so it causes greater economic growth because of the higher productivity of healthy and educated households.

Finally in order to examine the long-run relationship between tourism expansion and economic growth in OIC countries, we should first examine the stationarity of variables. If the variables were non-stationary in the long-run, the results of OLS estimations would be biased and misleading [30]. Therefore, the unit root test has been conducted and Philips-Peron index has been used. The results in table 6 show that there is no unit root in both variables of economic growth rate and the number of international tourism arrivals and they are stationary in levels.

After investigation for unit roots, we adapt Johansen's multivariate test based on a VAR representation of the variables in order to investigate the long-run relationship between economic growth and tourism expansion. There are two indexes of the trace test and maximum Eigenvalue test to determine the number of co integration vectors between the mentioned variables. The results of trace test and Eigenvalue tests have been presented in tables 7 and 8.

Table 6: Panel unit root tests on levels of variables

Variables	PP statistics	Probe
Lgr	394.756	0.0000
Ltour number	87.47	0.05

Table 7: co integration test between economic growth and tourism expansion (trace test)

Null hypotheses (r: number of integrated vectors)	Eigenvalue	Trace Statistic	critical value (0.05)	probe
R=0	0.20	113.60	15.49	0.0001
R<= 1	0.002	1.04	3.84	0.30

Table 8: co integration test between economic growth and tourism expansion (Eigenvalue test)

Null hypotheses (r: number of integrated vectors)	Eigenvalue	Trace Statistic	critical value (0.05)	Probe
R=0	0.200	112.55	14.26	0.0001
R<= 1	0.002	1.04	3.84	0.306

The results of both trace and Eigenvalue tests show that there is one co integration equation between economic growth and tourism expansion. Therefore there exists a long-run relationship between economic growth and tourism expansion in OIC countries.

CONCLUSION

The purpose of this study is to investigate the relationship between tourism expansion and economic growth in OIC countries by using a panel data method and GMM model over the period of 1995-2010. The results show that tourism expansion has a positive and significant effect on economic growth in OIC countries. Many of Islamic countries are developing countries that suffer from lack of physical capital, where the tourism industry is not a capital-intensive one and tourism development can be a low-cost solution to escape from low economic growth rates and unemployment. Moreover, some of these countries have a single-product economy (such as oil or agriculture), but tourism development can cause a variety of growth factors that can lead to economic growth. Tourism expansion has positive and significant effect on economic growth in both developed and developing countries. Investment, human capital and openness have positive and significant effects on economic growth in both of the two groups of countries. The result of the co integration test shows that there is a long-run relationship between tourism expansion and economic growth in OIC countries. So policy makers should have continuous programs to support the tourism industry agents.

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