

The Impact of Uncertainty in Economic Policy on Sustainable Investment

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Abstract

Changes in policy are inevitable and may occur suddenly. Numerous alterations to individual and organisational decisions are driven by uncertainty. For the purpose of catching recent events or predicting dynamic advancement, political, social, economic, or both rules may be referred to. Uncertainty may occasionally result from dynamism, which can jolt the stock market. When the government announces several policy changes and creates a great deal of uncertainty, it will result in stock market volatility and correlations. The Economic Policy Uncertainty (EPU) index was created by Baker utilising a variety of variables as a proxy for the uncertainty in changes to economic policy. They discovered that the EPU has a considerable influence on both micro and macroeconomic parameters.

Keywords: Policy uncertainty • Environmental innovation • Environmental sustainability • Climate change • Sustainable development

Introduction

The impact of economic policy uncertainty on stock market returns has been investigated in a number of earlier forms of study. Interest in this impact has returned with the start of the global financial crisis in 2008 and the decline of the Chinese stock market in 2015. Pastor and Veronesi (2012) developed a general equilibrium model ten years ago that forecasts a decrease in stock prices following the announcement of a change in governmental policy. The likelihood of a decline in stock values will rise as policy uncertainty rises [1]. The authors then develop the fundamental model to show that political unrest comes with a higher risk premium under poorer economic conditions.

Description

Yu and Huang (2021) used the GARCH-MIDAS model in their most recent empirical studies in addition to the literature on the impact of EPU on the interaction between financial markets. They found that the unstable nature of Chinese economic policies may be a factor in the country's stock market's instability. Further investigating the impact of economic policy uncertainty on stock market returns and risk for G7 countries, Kundu and Paul (2022) discovered that EPU had a detrimental effect on stock market returns. In parallel periods, it was shown that increases in EPU increased market volatility and decreased returns [2].

There are various steps in the research methodology. Checking for outliers or missing data in the data for both the uncertainty of economic policy and stock prices comes before testing the variables. The Panel Autoregressive Distributed Lag (ARDL) models with Mean Group (MG) and Pooled Mean Group (PMG) estimates will then be used to examine the data [3]. The short-run and long-run connections between EPU and the returns of the prices of

gold, oil, bitcoin and sustainable stock markets were then examined using the panel ARDL model.

Additionally, the link between sustained stock market gains in the short term and Bitcoin as a cryptocurrency asset was evaluated. The outcome reveals that the price of Bitcoin had a favourable and significant impact on stock market returns in every nation, with the exception of Brazil, where the impact was not significant. This finding suggests that, in the short term, rising Bitcoin prices may improve stable stock market returns in these eleven nations. This outcome supported Ahmed's (2021) conclusion that, particularly under typical circumstances, Bitcoin volatility tends to have favourable and large effects on stock market performance [4].

Over the past ten years, India's economic policy uncertainty has dramatically decreased. Uncertainty in economic policy peaked in 2011–12, coinciding with the years of policy stalemate.

Since then, there has been a secular drop in economic policy uncertainty. Because it contrasts significantly with the rise in economic policy uncertainty in important nations at this time, notably the US, the ongoing decline in economic policy uncertainty in India after 2015 is remarkable. Episodes of heightened uncertainty, like the 2013 taper tantrum, are to be expected; they show elevated economic policy uncertainty. Uncertainty in economic policy is also highly correlated with the macroeconomic setting, the state of the economy and other economic factors that influence investment. Increasing systematic risk and, as a result, the cost of capital in the economy are two effects of rising economic policy uncertainty. As a result, increased economic policy uncertainty discourages investment, which is especially true given that investment is irreversible. This hypothesis is supported by the fact that India's investment growth slows down for roughly five quarters when economic policy uncertainty rises.

Policymakers may lessen economic policy uncertainty to promote a favourable investment climate in the nation, unlike general economic uncertainty, which is uncontrollable. It is advised that the following policy adjustments be made. To begin with, policymakers must make their activities predictable, offer clear direction on the direction of the policy and lessen ambiguity/arbitrariness in its execution. The second rule is that "what gets measured gets done." Therefore, the utmost degree of tracking the economic policy uncertainty index must be done on a quarterly basis. Finally, international quality certifications must be used in the government to implement quality assurance of the policy-making processes [5].

Therefore, a company included in the sustainable stock market index must be able to reduce risks, have high sustainability performance and generate strong returns for investors in order to draw in investors for sustainable

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investing. The findings of our study may be useful to policymakers as they take into account how policy uncertainty affects sustainable investment. As a result, in creating an economic policy, decision-makers should carefully watch for any spillover consequences. Volatility risks will be lessened and investment returns will be more dependable if policymakers can reduce the amount of uncertainty. As a result, it will entice more investors to enhance the flow of funds toward sustainable investment activities.

Conclusion

This study uses monthly data for the period from 2015 to 2020 to analyse the long- and short-term implications of economic policy uncertainty and commodity prices for commodities including gold, oil and Bitcoin as an alternative investment in the sustainable stock markets of 12 nations. First, we apply to this investigation the panel unit root tests created by Levin-Lin-Chiu and Im-Pesaran-Shin (IPS). Then, using both the Kao test and the Pedroni test to look at the integration of all the variables, we use the cointegration tests in our study.

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Conflict of Interest

The authors declare that there is no conflict of interest associated with this manuscript.

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