



HISTORICAL: Journal of History and Social Sciences

Vol. 2, No. 1, (2023).

Journal website: <https://historical.pdfaii.org/>

Research Article

The Impact Of Fiscal Policy On Economic Growth

Omar Al-Kasasbeh

Universiti Sultan Zainal Abidin, Malaysia

Copyright © 2023 by Authors, Published by HISTORICAL: Journal of History and Social Sciences. This is an open access article under the CC BY License <https://creativecommons.org/licenses/by/4.0/>

Received : January 22, 2023

Revised : February 18, 2023

Accepted : March 06, 2023

Available online : March 13, 2023

How to Cite : Al-Kasasbeh, O. (2023). The Impact Of Fiscal Policy On Economic Growth. *HISTORICAL: Journal of History and Social Sciences*, 2(1), 16–24. <https://doi.org/10.58355/historical.v2i1.38>

Corresponding Author: Email: siz449@putra.unisza.edu.my

Abstract. The relationship between fiscal policy and economic growth has attracted a great deal of attention in recent years. The growth experience of several countries during the last decades has generated a growing strand of theoretical and empirical literature trying to explain these events. Although one could argue that economic growth and fiscal policy influence each other. The aim of this paper is to review the research work conducted on fiscal policies and economic growth, noting that there are three tools of fiscal policy; the first type is government expenditure, the second type is taxation, and the third type is debts. In addition, according to previous research, the relationship between fiscal policy and economic growth is not clear and consistent, where in some cases a positive relationship, while in others it may be a negative relationship. In this paper, we will discuss the concept of fiscal policies, economic growth, and the relationship between those two variables through some of the previous research

Keywords : Fiscal policy, Economic growth, Government Expenditure, Taxation

INTRODUCTION

The goal of achieving positive economic growth rates is one of the priorities sought by governments of different countries, especially in developing and underdeveloped countries (Xue, Weng & Yu, 2018). Such countries are always looking for economic growth to enhance and strengthen their economies. Economic growth has therefore become the main factor officially accepted for evaluating the success and development of the economy (Al-kasasbeh, 2022a). The importance of economic growth stems from the positive effects on the national economy that give a strong boost to new investment, resulting in job opportunities and increased purchasing power for the community (Murinde, 2012; Iamsiraroj, 2016).

The determinants of economic growth remain a crucial and motivating study issue in the field of economics and are almost unanswered. The critical question to be asked here is whether the fiscal policy has an impact on economic growth or otherwise? Theoretically, fiscal policy sector growth is debated from the three dimensions: feedback, demand, and supply hypotheses (Ziaei, 2015). When policy makers struggle to find possible economic growth and have a stable economy for their countries, fiscal policy and economic growth relationship becomes more critical. New research in this area is important refers to the significance of the economic growth for each country (Kasasbeh, 2021; Jayeola, 2022).

Furthermore, several studies have also been conducted on the relationship between government expenditure, taxes, public debt, and economic growth. The just mentioned topics have been diversely investigated by several studies with a concentration on fiscal policy variables. Such as Herndon and Pollin (2014); Lof and Malinen (2014); Kia and Mousavi (2015); Gale, Krupkin and Rueben (2015); Alawneh (2017); Abueid et al, (2018); Al-kasasbeh (2022); and Kasasbeh, (2021).

Indeed, the analysis of economic growth, fiscal policy is of significant interest to various, of researchers, including Tcherneva, (2011); Audu (2012); Karagöz and Keskin (2016); Nursini (2017); Ugwuanyi & Ugwunta (2017) and Al-kasasbeh et al, (2022). All these studies attempted to discover the link between them. It is frequently believed that economic growth performance is established by several factors such as energy consumption, international trade, financial development, CO₂ emission, population, monetary policy and many others.

Furthermore, current research indicates that advanced economies have concentrated on exploring the impact of fiscal policy determinants such as (Stoilova and Patonov, 2013; Atilgan, Kilic and Ertugrul, 2017; d'Agostino, Dunne, and Pieroni, 2018). The just-mentioned factors encouraged the researcher to try to identify fiscal policy as one of the most important tools of economic growth.

RESULTS AND DISCUSSION

Fiscal Policy

There is no doubt that economic policies include several measures such as fiscal and monetary policy and policy on credit and exchange rates. Fiscal policy plays an important position in these policies, because the various objectives they are looking for can be reached. The national economy depends on its various tools, which can be adapted to affect all the economic and social aspects of society, the government's

approach to the economy was *laissez-faire*. After the Great Depression, ideas emerged calling for their intervention in economic life to regulate unemployment, inflation and business cycles.

Fiscal policy has become a major instrument of economic policy in guiding the economic course and addressing what is exposed to shocks and crises. Their different definitions of the concept of fiscal policy (Al-kasasbeh, 2022b). For example, it is defined as a set of public revenue policies for public expenditure in order to achieve specific objectives. On the other hand, some define it as a set of goals, directions, actions, and activities adopted by the state to influence the national economy and society to maintain its overall stability and development (Tcherneva, 2011).

The fiscal policy situation remained neutral until appeared on the horizon of the economic crisis that swept the world in 1929. It can be said that the significant development of fiscal policy has stemmed from the major contribution to the great economist John Maynard Keynes in his book "The General Theory of Jobs and Interest and Income", when emphasizing the weakness of market mechanisms alone in coping with economic problems, especially the Great Depression crisis, and the consequent need to follow Keynes views of state intervention in economic activity. Since then, fiscal policy has assumed a more critical role and has become a major instrument of economic policy tools to guide the economic entity's course and address what it is exposed to shocks and crises, as well as their impact on the development of the economy, in particular, in the growing countries (Hoover, 2015; Al-kasasbeh et al., 2022).

According to Ugwuanyi and Ugwunta (2017), fiscal policy includes many patterns affecting economic activities such as government spending, public debt, and taxation, as well as influencing employment and aggregate demand growth level. Fiscal policy strengthens policymakers ability to manage the economy by managing their income and spending power to achieve specific goals that lead to economic growth. Fiscal policy also represents government policies related to the state budget, which is represented in tax revenue, government borrowing, government spending, or even deficit financing (Sanni, 2012). Fiscal policy's main objective is to provide countries with economic stability by improving economic conditions and factors in a way that strengthens the state's business and ensures that government decisions are appropriate for economic stability (Ndubuisi, 2017).

Historically, there are numerous points of view on the success of fiscal policies that have been pursued by different economic schools from time to time. The classic approach, which prevailed until The Great Depression (1929), highlights the importance of a balanced budget for the efficiency of fiscal policies. It also pointed out that budget deficits are likely to create economic instability. Classical economists also claimed that budget should generally be identical, apart for some variations. They also argued that the effectiveness of government spending or tax regulations was related to strategies through which such policies were shaped and implemented (Erkam, 2010).

However, the classic approach with its assertion of financing the budget deficit through borrowing and its consequential obscurity has failed to resolve the crisis in the absence of its inability to predict The Great Depression. Confirming that the

government should intervene in the economy through revenue, public spending and the budget, Keynesian views opened the debate to the principle of a balanced budget and pointed to the relevance and macro-economic impact of the imbalanced budget (Karagöz and Keskin, 2016). Keynesian view argues that the effectiveness of monetary policy tools is limited due to liquidity trap and other factors and it argues that aggregate demand could be complemented by public spending and public revenue. Thus, in order to reduce inflation, fiscal policy should be applied by following budget surplus policy, while in the time of recession monetary expansion would be provided by budget deficit (Bozkurt & Göğül, 2010).

According to Keynesian argument, the fiscal contraction leads to a temporary contraction through aggregate demand channel. A frequently used and popular Keynesian-Monetarist contention in theory of economics further clarifies the effectiveness of fiscal policy. Monetarist view holds economy to be generally stable and believes interventionist monetary policy to be objectionable and thus, consequentially, fiscal policy to be harmful (Erkam, 2010). Meanwhile Friedman says, if intervention is inevitable, monetary policy should be preferred to fiscal policy because of the delayed impacts of fiscal policy (Dudley-Evans, 2017).

Empirical Literature Review

In this section of the paper, a series of previous research and studies on the subject of fiscal policy and its relation to economic growth in a number of countries will be presented in order to gain a deep understanding of the nature of the relationship between fiscal policy and economic growth, as follows:

Table Error! No text of specified style in document.1: Summary of Previous Empirical Literature Review

	AUTHORS	COUNTRY AND DATA	METHOD	MAJOR FINDINGS
TAXES AND ECONOMIC GROWTH				
1	Ivanyna, Moumouras, and Rangazas, (2016)	developing countries	dynamic general equilibrium model	(-)
2	Aghion, Akcigit, Cage, and Kerr, (2016)	U.S states	Granger causality	→
3	Riba, (2017)	South Africa 2003 - 2016	ARDL cointegration and Granger causality	(+) ↔
4	Biswas, Chakraborty, and Hai, (2017)	U.S. state	GMM, and OLS model	(-)
5	Di Sanzo, Bella, and Graziano, (2017)	panel of twenty European countries 1970 to 2012	VAR model	(-)

6	Babatunde, Ibukun, and Oyeyemi, (2017)	Africa from 2004 to 2013	Hausman test	(+)
7	Grdinić, Drezgić, and Blažić, (2017)	Central and Eastern Europe from 1990 to 2010	(GMM) regressions	(-)
8	Juliana, (2018)	Nigeria 1994 to 2016	cointegration test	(+)

PUBLIC DEBT AND ECONOMIC GROWTH

9	Stylianou (2014)	Greece during the period 1980 to 2010	Granger causality test	~
10	Al-Refai (2015)	OECD nations 1981 to 1995	OLS	(-) (+)
11	Chiu and Lee (2017)	61 countries 1985–2009	panel data framework	(+) (-)
12	Cherif, and Hasanov (2018)	USA	VAR	(-)
13	Ferando and Serafim (2018)	Angola 2004-2015	panel data approach	(-)
14	Gómez-Puig, and Sosvilla (2018)	euro area (EA) the period 1961-2013	Autoregressive Distributed Lag (ARDL) bounds	(-)
15	Esteve, and Tamarit (2018)	Spanish economy 1851–2013	dynamic ordinary least squares (DOLS) method	(-)
16	Ncanywa, and Masoga (2018) Kasasbeh (2021)	South Africa Jordan	autoregressive distributive lag Granger causality	(-) ↔

GOVERNMENT EXPENDITURE AND ECONOMIC GROWTH

17	Alptekin, and Levine, (2012)	review 32 empirical studies	panel Granger causality test	~
18	Keho (2015)	Ten African countries. over the interval 1965 to 2013	Granger causality test	↔ →
19	Osei, Aglobitse, and Bentum-Ennin, (2017)	Thirty-three countries from 1990 to 2014.	Autoregressive Distributed Lag (ARDL)	(+)
20	Atilgan, Kilic, and Ertugrul, (2017)	Turkey 1975–2013	autoregressive-distributed lag approach (ARDL)	(+)

21	Paul, and Furahisha, (2017)	Tanzania over the period of 1978 to 2014.	Johansen test of cointegration and Granger causality panel data methods	(+) →
22	d'Agostino, and Dunne, and Pieroni, (2018)	109 countries 1998–2014		(-)
23	Abad, Haron, and. Abueid, (2018)	Jordan for the period 1970-2017	(ARDL)	→
24	Le Van, Nguyen-Van, Barbier-Gauchard, and Le (2019)	UAE 1975Q1-2012Q4	annual data analyses	(+)
	Alkasasbeha, Haron, Abueid, (2018)	Jordan 1970-2017	(ARDL)	(+)

→ Means that the causality runs from economic growth to its determinants

← Means that the causality runs from the determinant of the economic growth to economic growth

↔ Means that bi-directional causality exists between economic growth and its determinants

~ means that no causality exists between economic growth and its determinants

(+) Means positive relationships between economic growth and its determinants

(-) Means negative relationships between economic growth and its determinants

The various empirical studies analyzed here reported inconsistent and inconclusive outcomes. For example, there are substantial positive and bidirectional relationships between economic growth and government expenditure, taxes, and public debt, and negative relationships have been documented in some studies. Other studies record various results. This mixture of outcomes and conclusions comes from differences in methodology, specific times of study and variables used.

CONCLUSION

This paper seeks to determine whether a consensus exists about the impact of fiscal policy on economic growth. In reference to selected articles, were found to report a negative relationship between fiscal policy and economic growth. However, the results also suggested that the relationship may be positive. Similarly, there were studies that supported the neutrality of fiscal policy and economic growth. Therefore, there is no unanimity regarding the connection between fiscal policy and economic growth. The nature of the relationship may be positive, negative, or neutral. Overall, this review demonstrates that the effect of fiscal policy on economic growth is not constant and varies depending on a number of heterogeneous factors, such as the research methodology used, the level of development of the sampled countries, the relative size of the public sector, institutional quality, the composition, and the selected control variables, among others. The study finds, therefore, that the influence of fiscal policy on economic growth is ambiguous.

REFERENCES

- Abueid, A. I. S., Haron, N. F., & Abad, O. M. (2018). The Impact of Foreign Direct Investment, Aids and Economic Growth: Evidence from Structural Breaks for Jordan. *International Journal of Academic Research in Business and Social Sciences*, 8(11).
- Aghion, P., Akcigit, U., Cage, J., & Kerr, W. R. (2016). Taxation, corruption, and growth. *European Economic Review*, 86, 24-51.
- Alawneh, A. (2017). The impact of public expenditure and public debt on taxes: A case study of Jordan. *Accounting and Finance Research*, 6(3), 10-23.
- Al-kasasbeh, O. (2022). COVID-19 Pandemic: Macroeconomic Impacts and Understanding its Implications for Jordan. *Journal of Environmental Science and Economics*, 1(2), 51-57.
- Al-kasasbeh, O. (2022). The relationship between unemployment and economic growth: is Okun's Law valid for the Jordan case?. *International Journal of Economics Development Research (IJEDR)*, 3(3), 217-226.
- AL-KASASBEH, O. M. (2022). THE NEXUS BETWEEN FISCAL POLICY AND ECONOMIC GROWTH FOR JORDAN: FRESH INSIGHTS FROM MAKI COINTEGRATION. *Innovare Journal of Business Management*, 10(1), 1-4.
- Al-kasasbeh, O., Alzghoul, A., & Alghraibeh, K. (2022). Global FDI inflows and outflows in emerging economies Post-COVID-19 era. *Future Business Journal*, 8(1), 1-9.
- Al-Kasasbeh, O., Alzghoul, A., & Alhanatleh, H. (2022). Empirical Analysis of Air Pollution Impacts on Jordan Economy. *International Journal of Energy Economics and Policy*, 12(4), 512-516.
- Al-kasasbeh, O., Alzghoul, A., & Alhanatleh, H. (2022). The Impact of Fiscal Policy and Trade Liberalization on Economic Growth: Evidence from Structural Breaks for Jordan. *International Journal of Professional Business Review*, 7(6), e0850-e0850.
- Alkasasbeha, O. M. A., Haron, N. F., & Abueid, A. I. S. (2018). The Impact of Government Expenditures, Taxes on Economic Growth in Jordan. *American based research journal*, 7(12).
- Alptekin, A., & Levine, P. (2012). Military expenditure and economic growth: A meta-analysis. *European Journal of Political Economy*, 28(4), 636-650.
- Atilgan, E., Kilic, D., & Ertugrul, H. M. (2017). The dynamic relationship between health expenditure and economic growth: is the health-led growth hypothesis valid for Turkey?. *The European Journal of Health Economics*, 18(5), 567-574.
- Audu, N. P. (2012). The impact of fiscal policy on the Nigerian economy. *International Review of Social Sciences and Humanities*, 4(1), 142-150.
- Babatunde, O. A., Ibukun, A. O., & Oyeyemi, O. G. (2017). Taxation revenue and economic growth in Africa. *Journal of Accounting and Taxation*, 9(2), 11-22.
- Biswas, S., Chakraborty, I., & Hai, R. (2017). Income inequality, tax policy, and economic growth. *The Economic Journal*, 127(601), 688-727.
- Bozkurt, C. & Göğül, P. K. (2010), "Coordination of monetary and fiscal policies", *Akademik Araştırmalar ve Çalışmalar Dergisi*, 2 (2), 27 - 44.
- Cherif, R., & Hasanov, F. (2018). Public debt dynamics: the effects of austerity, inflation, and growth shocks. *Empirical Economics*, 54(3), 1087-1105.

- Chiu, Y. B., & Lee, C. C. (2017). On the Impact of Public Debt on Economic Growth: Does Country Risk Matter? *Contemporary Economic Policy*, 35(4), 751-766.
- d'Agostino, G., Dunne, J. P., & Pieroni, L. (2016). Government spending, corruption and economic growth. *World Development*, 84, 190-205.
- d'Agostino, G., Dunne, J. P., & Pieroni, L. (2018). Military expenditure, endogeneity and economic growth. *Defence and Peace Economics*, 1-16.
- Di Sanzo, S., Bella, M., & Graziano, G. (2017). Tax Structure and Economic Growth: A Panel Cointegrated VAR Analysis. *Italian Economic Journal*, 3(2), 239-253.
- Dudley-Evans, T. (2017). The debate over Milton Friedman's theoretical framework: an applied linguist's view. In *Economics and language* (pp. 132-152). Routledge.
- Erkam, S. (2010), *Effectiveness of Fiscal Policies: Theory and an Application*, Maliye Bakanlığı SGB Publishing No: 2010/407, Ankara.
- Ferando Reis, C., & Serafim, J. (2018). Growth and Debt in Angola at Provincial Level (No. 172). CEAs-Center for African, Asian and Latin American Studies.
- Gale, W. G., Krupkin, A., & Rueben, K. (2015). The relationship between taxes and growth at the state level: new evidence. *National Tax Journal*, 68(4), 919.
- Gómez-Puig, M., & Sosvilla-Rivero, S. (2018). Nonfinancial debt and economic growth in euro-area countries. *Journal of International Financial Markets, Institutions and Money*, 56, 17-37.
- Grdinić, M., Drezgić, S., & Blažić, H. (2017). An Empirical Analysis of the Relationship between Tax Structures and Economic Growth in CEE Countries 1. *Ekonomicky Casopis*, 65(5), 426.
- Herndon, T., Ash, M., & Pollin, R. (2014). Does high public debt consistently stifle economic growth? A critique of Reinhart and Rogoff. *Cambridge journal of economics*, 38(2), 257-279.
- Hoover, H. (2015). *The Memoirs of Herbert Hoover-The Great Depression, 1929-1941*. Read Books Ltd.
- Iamsiraroj, S. (2016). The foreign direct investment-economic growth nexus. *International Review of Economics & Finance*, 42, 116-133.
- Ivanyna, M., Moumouras, A., & Rangazas, P. (2016). The culture of corruption, tax evasion, and economic growth. *Economic inquiry*, 54(1), 520-542.
- Jayeola, O., Sidek, S., Abdul-Samad, Z., Hasbullah, N. N., Anwar, S., An, N. B., ... & Ray, S. (2022). The Mediating and Moderating Effects of Top Management Support on the Cloud ERP Implementation-Financial Performance Relationship. *Sustainability*, 14(9), 5688.
- Juliana, M. I. (2018). Effect of Tax Structure on Economic Growth in Nigeria *Journal of Innovative Finance and Economics Research* 6(1):1-11, Jan-Mar.
- Karagöz, and Keskin, (2016). Impact of Fiscal Policy on the Macroeconomic Aggregates in Turkey: Evidence from BVAR Model. *Procedia economics and finance*, 38, 408-420.
- Kasasbeh, O. (2021). Fiscal Policy and its Relationship with Economic Growth a Review Study. Available at SSRN 3789109.
- Kasasbeh, O. (2021). Public Debt and Economic Growth: Is There Any Causal Effect? An Empirical Analysis with Structural Breaks and Granger Causality for Jordan. *INTERNATIONAL JOURNAL OF TRENDS IN ACCOUNTING*

- RESEARCH, 2(1), 106-110.
- Keho, Y. (2015). Revisiting Wagner's law for selected African countries: A frequency domain causality analysis. *Journal of Statistical and Econometrics Method*, 4(4), 55-69.
- Kia, A. S., & Mousavi, Z. (2015). The evaluation of the impact of income tax on economic growth and development in the Islamic republic of Iran during 1971-2006.
- Le Van, C., Nguyen-Van, P., Barbier-Gauchard, A., & Le, D. A. (2019). Government expenditure, external and domestic public debt, and economic growth. *Journal of Public Economic Theory*.
- Lof, M., & Malinen, T. (2014). Does sovereign debt weaken economic growth? A panel VAR analysis. *Economics Letters*, 122(3), 403-407.
- Murinde, V.: Financial development and economic growth: global and African evidence. *J. Afr. Econ.* 21 (suppl), 110-i56 (2012).
- Ndubuisi, P. (2017). Dynamic Relationship between Fiscal Policy and Economic Growth in Nigeria (Long and Short Run Analysis). *Journal of Business and Economic Development*, 2(4).
- Nursini, N. (2017). Effect of fiscal policy and trade openness on economic growth in Indonesia: 1990-2015. *International Journal of Economics and Financial Issues*, 7(1), 358-364.
- Osei, D. B., Aglobitse, P. B., & Bentum-Ennin, I. (2017). Relationship between construction expenditure and economic growth in sub-Saharan Africa. *Ghanaian Journal of Economics*, 5(1), 28-55.
- Paul, F., & Furahisha, G. (2017). Government expenditure and economic growth nexus: Wagner's law or Keynesian hypothesis for Tanzania? *African Journal of Economic Review*, 5(1), 32-47.
- Sanni, A. (2012). Public expenditure and economic growth. *African journal of economic policy*, 1 (1) .Nigeria, university of Ibadan press.
- Stoilova, D., & Patonov, N. (2013). An empirical evidence for the impact of taxation on economy growth in the European Union. *Tourism & Management Studies*, 1031-1039.
- Stylianou, T. (2014). Debt and economic growth: Is there any causal effect? An empirical analysis with structural breaks and Granger causality for Greece. *Theoretical and Applied Economics*, 21(1), 51-62.
- Tcherneva, P. (2011). Fiscal policy effectiveness: Lessons from the Great Recession. Working paper, Levy Economics Institute of Bard College.
- Ugwuanyi, U. B., & Ugwunta, O. D. (2017). Fiscal Policy and Economic Growth: An Examination of Selected Countries in Sub-Saharan Africa. *International Journal of Academic Research in Accounting, Finance and Management Sciences*, 7(1), 117-130.
- Xue, L., Weng, L., & Yu, H. (2018). Addressing policy challenges in implementing Sustainable Development Goals through an adaptive governance approach: A view from transitional China. *Sustainable Development*, 26(2), 150-158.
- Ziaei, S. M. (2015). Effects of financial development indicators on energy consumption and CO₂ emission of European, East Asian and Oceania countries. *Renewable*

Omar Al-Kasasbeh

The Impact Of Fiscal Policy On Economic Growth

and Sustainable Energy Reviews, 42, 752-759.