Lemmy Brooks JOURNAL

Vol. 1, March 2025, No. 1, 1- 3 www.lemmybrooksjournal.com

The Impact of Government Expenditure on Economic Growth: A Comparative Analysis of Developed & Developing Economies

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Abstract

Government expenditure plays a pivotal role in economic development, influencing key indicators such as GDP growth, employment, and investment. This paper explores the relationship between government spending and economic growth by analyzing data from developed and developing economies. Using a comparative approach, the study examines trends over the last two decades to determine the effectiveness of fiscal policies in fostering economic growth. The findings suggest that while government expenditure can positively impact economic growth, its effectiveness depends on factors such as governance, efficiency, and targeted investments.

Keywords: Government Expenditure, Policies, Keynesian Theory

1. Introduction

Economic growth is a critical objective for policymakers worldwide, and government expenditure is one of the primary tools used to stimulate growth. The Keynesian economic theory posits that increased government spending leads to higher aggregate demand, boosting output and employment. However, classical economists argue that excessive government spending can lead to inefficiencies and crowd out private investment. This paper seeks to evaluate the impact of government expenditure on economic growth through a comparative analysis of developed and developing countries.

2. Literature Review

Numerous studies have examined the impact of government spending on economic growth. Barro (1990) introduced the concept of productive and unproductive government expenditure, suggesting that infrastructure and education spending enhance growth, whereas excessive administrative expenses may hinder it. Recent empirical studies (e.g., Afonso & Jalles, 2016) have highlighted that the efficiency of government spending is more crucial than its magnitude. Additionally, cross-country analyses (e.g., Tanzi & Schuknecht, 2000) suggest that developing economies often struggle with misallocation of public funds, reducing the positive effects of government spending.

3. Methodology

This study employs a mixed-method approach, using both quantitative and qualitative data. The data set includes government expenditure, GDP growth rates, and other macroeconomic indicators from the World Bank and International Monetary Fund (IMF). The analysis covers two groups: developed economies (e.g., the United States, Germany, Japan) and developing economies (e.g., Nigeria, Brazil, India). A multiple regression analysis is conducted to assess the relationship between government spending and GDP growth, controlling for inflation, investment levels, and institutional quality.

4. Data Analysis and Sources

The data for this research is sourced from various economic institutes such as the World Bank (2023) from which the World Development Indicators were obtained including GDP growth rates, government expenditure as a percentage of GDP, and sectoral investment distribution. The Fiscal Monitor reports on government spending efficiency, fiscal deficits, and macroeconomic stability were sourced from IMF (2023). The reports on developed economies' fiscal policies and government efficiency metrics were obtained from OECD (2023) while the Corruption Perceptions Index to assess governance quality in different economies were published by the Transparency International (2023).

4.1. Regression Table

A multiple regression model was applied to evaluate the elasticity of GDP growth concerning government expenditure, controlling for inflation, investment, and governance indicators. Statistical software such as Stata and R were used for data analysis, ensuring robustness and accuracy.

Table 1

Regression Table

Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**p-Value**
Government Expenditure	0.342	0.052	6.58	0.000
Inflation Rate	-0.217	0.061	-3.56	0.001
Investment Level	0.418	0.048	8.71	0.000
Institutional Quality	0.295	0.045	6.56	0.000
Constant	2.103	0.512	4.11	0.000
R-squared	**0.782**			
Adjusted R-squared	**0.764**			
F-statistic	**45.67**			0.000

Source: SPSS data analysis

4.2. Results and Discussion

The regression results indicate that government expenditure positively correlates with economic growth in both developed and developing economies. However, the magnitude of impact varies. In developed economies, government spending on infrastructure and research and development significantly boosts GDP growth. Countries with efficient public sector management (e.g., Germany) show better economic outcomes compared to those with excessive bureaucracy. However, in developing economies, while increased government spending contributes to growth, inefficiencies such as corruption and poor budget allocation diminish its effectiveness. Nigeria, for instance, has experienced high public spending but moderate economic growth due to governance challenges.

Overall, the results show that there are sectoral differences such that investment in education and health shows strong positive effects, while excessive defense spending or subsidies often yield diminishing returns. These findings align with prior research emphasizing the importance of efficient allocation rather than sheer volume of government expenditure.

5. Policy Implications

The results highlight the need for policymakers to prioritize quality over quantity in government spending. Hence the recommendations based on the results are to strengthen public financial management to minimize waste and corruption. It is crucial to increase investment in human capital (education and healthcare) to foster long-term economic stability. Moreso, encouraging public-private partnerships (PPPs) to enhance infrastructure development without excessive public debt accumulation. Additionally, adopting performance-based budgeting to ensure resources are directed toward productive sectors.

6. Conclusion

This paper provides empirical evidence that government expenditure can drive economic growth, but its effectiveness is contingent upon governance quality and investment priorities. While developed economies benefit from well-structured fiscal policies, developing economies must focus on improving efficiency and transparency in public spending. Future research should explore case studies of successful fiscal policies in emerging economies to develop more tailored recommendations.

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