

# Government Expenditure Composition- Impacts on Growth of the Economy<sup>1</sup>

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## Introduction

Fiscal policy could play pivotal role for stabilization and growth in developing countries which are thriving to eradicate poverty. If fiscal policy helps to facilitate private sector then it is better for the country rather than replacing private sector activities. Government should provide or spend on only those goods and services which private sector cannot produce due to the non-exclusion principle and free rider problem of public good. Government spending comprises government consumption, investment, transfers, subsidies and interest payments. Only eulogistic role of private sector cannot enhance the development of a country. Public sector has greater responsibility to ensure a sustainable and high growth rate. The impact of fiscal policy on growth depends on two indicators (1) the expenditure/GDP ratio and (2) Composition of government expenditure. The first one indicates the size of the government. The second one is also very important but was always neglected by economist during policy making. Composition of expenditure is not well thought out during the preparation of fiscal policy. Although in macroeconomics there are lot of research regarding the impacts of total government expenditure, a few research has been done on the composition of government expenditure. In this article our objective is to discuss the impacts of the change of government expenditure composition starting from an initial position and to sort out pertinent fiscal policy.

We want to describe here 1) Impacts of the change of government expenditure composition according to economic classification on income, growth and stabilization 2) Impacts of the change of government expenditure composition according to sector wise classification on growth and stabilization. The discussion is for a developing country perspective with certain assumptions.

Related theory and literature review is presented first. Then we assumed a model developing country with some assumptions. After that Government expenditure

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<sup>1</sup> The views expressed herein are those of the author and do not necessarily reflect the views of the Finance Division

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composition according to economic classification is discussed. Then sector wise government expenditure composition is explained especially the way of calculating the priority sector.

### **Theory and Literature Review**

Theoretically, output and price level is determined by the intersection of aggregate demand and aggregate supply. Aggregate demand and aggregate supply is determined by various variables. Government expenditure and government revenue are only two of many variables which determine aggregate demand. These two variables also can affect aggregate supply if structural reforms are done. Here we start from explaining the relationship between aggregate demand and growth and then explain the impact of government expenditure composition on growth. Aggregate demand management policy can ensure sustainability if there is internal or external imbalance in the economy. Three major types of internal imbalances are (1) when aggregate demand is greater than potential output (2) when fiscal deficit is monetized (3) when aggregate demand is less than potential output (Green, 2006). In all three cases government is capable of doing something to overcome the problem derived from imbalance, although in case (2) government may not be capable when monetary authority is completely independent to take its decision (Sergent and Wallace, 1981). Internal imbalance is also linked to external imbalance. Major external imbalance happens due to current account deficit. Heavy external debt service burden also creates external imbalances. These internal and external imbalances are also interrelated as we know that in short-run,

$$S-I=(S_g-I_g)+(S_p-I_p)=CAB=(X-M)+Y_f+TR_f$$

where S and I are national savings and investment,  $S_g$  and  $I_g$  are government savings and investment,  $S_p$  and  $I_p$  are private savings and investment. CAB is the current account balance.

The imbalances we have so far talked create problem for the economy such as high inflation and sluggish growth. Government can apply stabilization and structural policies as remedy for these imbalances. Two major stabilization policies are 1) Adjustment using AD which is called the expenditure reducing (augmenting) policies 2) Ensuring that relative prices in the economy gives appropriate signal through change in exchange rate which is called the expenditure switching policy. (Green, 2006). There are economic theories which prove the rationale for stabilization measures. Many economists believe that sustainable economic growth requires establishing reasonable price stability and a viable external position (Hemming et.al. 2002). We can also reduce imbalance

by adjusting AS. These are called structural policies and are long-term policies like price adjustment and liberalization, reforms in tax structure/rules, privatization etc. Again Aggregate Demand could influence aggregate supply in both short-term and long-term. Such as government investment on building roads, bridges or schools help to increase the aggregate supply. Aggregate demand increases the productive capacity and thus the ability of the economy to supply full employment level of production.

Keynes is the pioneer in explaining demand side effects of fiscal policy. He starts with basic assumptions 1) price rigidity 2) Excess capacity and 3) consumption as a function of current income. With these assumptions Keynes explains that, if a government spends more, then AD will increase and it will increase income. However how much aggregate demand will increase for a certain amount of government expenditure increase depends on various factors like change of interest rate, price level etc. Extension of simple Keynesian model allow for crowding out through induced change in interest rate and exchange rate i.e. explained by the IS-LM framework (Hemming et.al. 2002). The extent of crowding out affects the size of fiscal multiplier. So if there is less crowding out then output effect is high but high crowding out limit the performance of fiscal policy. The amount of crowding out depends on different types of relationship between investment, current income, interest rate, money demand and national income.

In an open economy, extent of crowding out depends on the system of exchange rate and capital mobility. In case of price flexibility crowding out happens with greater complexity. In an open economy with flexible exchange rate, there is scope that exchange rate is adjusted with domestic prices. If the domestic price responds rapidly with exchange rate then competitiveness of domestic goods are not hampered and exports are not reduced or imports are not increased. Now it is easily understandable that in case of fixed exchange rate and flexible price crowding out is higher.

Aggregate demand increase acts as the driving force for growth in short-term. Increased aggregate demand compels government to prepare deficit budget. So there are plenty of literatures on government budget deficit and its impact on growth. John Maynard Keynes first states theoretically the idea of budget deficit and included it in macro economic model as a variable. During that time the notion of cyclically balanced budget was developed as a norm for fiscal behaviour. Pre-Keynsian presumption was that in peacetime the budget should generally be balanced or even in surplus to pay off the government debt generated by wartime deficits. Keynes said that the aggregate demand depends on the budget deficit or fiscal policy (Fischer and Easterly,1990). But the concept of

balance budget multiplier shows that deficit is not the only measure of the effect of fiscal policy on aggregate demand. The theoretical development of life cycle and permanent income theories of consumption by Franco Modigliani and Milton Friedman is a deviation from standard Keynesian analysis on the effects of fiscal policy. Barro-Ricardo equivalence proposition is also an important contribution about consumption behaviour and thus has effect on aggregate demand. Although this theory was later rejected by Ricardo, Harvard professor Robert Barro have developed more sophisticated variations on the same idea particularly using the theory of rational expectations. Sargent and Wallace (1981) in their article "An unpleasant monetarist arithmetic" says about the coordination of monetary policy and fiscal policy and assumes that fiscal authority moves first. If fiscal authority has the dominance, monetary policy cannot restrain inflation. Because if the fiscal authority's deficits cannot be financed by new bond sales (i.e. less demand for bonds ) then the monetary authority is forced to finance the deficit with additional seigniorage which creates inflation.

All the above discussions are on total amount of government expenditure and how aggregate demand could be a driving force for economic growth in short-run. Now we want to dissect composition of government expenditure which is suitable for growth in short-term and long-term. Theoretically we cannot mention any approved shape of total government expenditure. Because, initial condition of the fiscal variables are very important, when we want to predict the impact of government expenditure. The economy could be highly indebted and thus external imbalance could be very high. In 1960s economists gave emphasis on finding out the relationship between fiscal policy and economic growth. In their model Arrow and Kurz (1970) assumed that consumers utility increase by private consumption as well as public capital stock. and all government investment are productive. Barro's work on endogenous growth has generated a model linking public spending and long-term growth rate of the economy. He takes government expenditure to be complementary with private consumption. Barro (1990) and many other economist were emphatic on segregating the role of public goods and services that enter into families utility function and those that complement private sector production. That is he differentiates public expenditure between the expenditure that facilitates private consumption and that which complement private sector production. Related literature regarding productive and unproductive government spending are Landau,1983; Aschauer, 1989; Barro 1990,1991 etc. One of the relevant literatures regarding our topic is by S.Devarajan et.al.(1996) presents a theoretical model and also have done empirical analysis. His model is on a strict assumption that budget is always balanced. He proves that a shift in composition to increase the growth rate depends both on the productivity of the components and also the initial share of

the components. His empirical results suggest that expenditures which are normally considered productive could become unproductive if there is an excessive amount of them. So the belief that capital expenditure always increases growth may not be true and it might be unproductive if the share of capital expenditure is high. The reduction of domestic financing during contraction has better effect than the reduction of foreign financing. The empirical evidence reinforces the active role of expenditure composition in promoting economic growth in low income countries. He also adds that additional research is needed to disentangle the channels through which fiscal policy affects growth. Another empirical research on expenditure composition is done by Gupta et.al.(2002). His study is on 39 ESAF and PRGF supported countries during the period 1990-2000. His data analysis proves that, in low income countries fiscal consolidations are not harmful for both short and long-term growth during that period. A reduction of one percentage point in the ratio of fiscal deficit to GDP leads to an average increase in per capita growth of 1/4 to 1/2 of a percentage point both in the long and in the short term. Perotti (1999) shows that consolidation tend to be expansionary when debt is high or growing rapidly, while Alesina and Perotti (1996) and Alesina and Ardanga, (1998) find that private sector responses to fiscal policy depends not only on the size or continuity of fiscal stance but also on the budget composition. Fiscal adjustments that rely primarily on cuts in transfers and wage bill tend to last longer and can be expansionary, while those that rely primarily on tax increases and cuts in public investment tend to be contractionary and unsustainable. Some empirical research has been done only on industrial countries to find out the conditions of small or negative fiscal multiplier. It happens that for some low income countries fiscal contraction might be expansionary by changing the ratio of expenditure composition. This means that there are unproductive or unnecessary expenditure which should be cut down. This expenditure reduction actually increases the growth. It is seen from different studies that in industrialized countries, growth is more sustainable in case of reducing transfers and wage bill than tax increase and capital spending cut. Ardagna ( 2001) shows that fiscal stabilization that rationalize public employment can stimulate the economy , provided that public employment does not have a positive effect on the productivity of capital and labour.( Gupta et.all 2002). Some economists also explain the impacts of fiscal policy assuming a production function approach. One of them is Phillip Gerson (1998) who assumes a production function with minor modification of the standard neo-classical form. Fiscal policy can affect the aggregate output through various ways/channels. Instead of total factor productivity he added two more variables in the production function. These are quality of the stock of labour and similar measure for physical capital. Increasing the amount of government expenditure for increasing the productivity of labour and capital could increase output growth. However, there

are two types of expenditure composition. One could be functional and the other could be sectoral. Functions are like pay and allowances, supplies and services, new purchase etc. Sector-wise components are like education, health, energy, local government etc.

### **Explanation with respect to a developing country perspective**

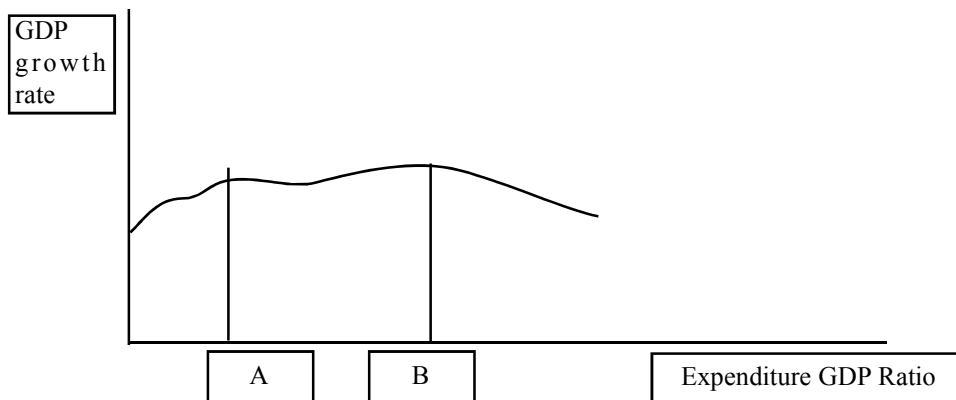
There are gulf of differences between developed and developing countries in various aspects like availability of labour, capital, resources, infrastructure, technology, law and order situation, anticorruption institution, laws related to development etc. However we are assuming a country with the following assumptions.

- a) It is a developing country with plenty of labour, there is unemployment or disguised unemployment in the country. It happens if the country has market imperfection, sticky wage situation or for using capital intensive technology.
- b) There is lack of law enforcement or not a better law which affects revenue earning of the government. Only law enforcement and strengthening of administration can increase the revenue earning i.e. without increasing the tax base and tax rate. Expenditure/ GDP ratio is low.
- c) Government expenditure is not allocated among sectors/ministries according to priority. Rather budget is prepared on incremental basis. Ministries does not have long-term policy framework. So marginal social benefit among sectors are not considered. Ideal way is to calculate marginal social benefit of different sectors and additional amount is allocated chronologically from the highest one.
- d) Many people live below poverty line income, so if real income increases then demand for essential goods increases at a higher rate than demand for luxury goods.
- e) A vivid phenomena of most of the developing countries is that lot of people are working outside in different parts of the world. So although GDP is low, GNDI is very high. High GNDI keeps the external sector in a better position. Government buys food or import from outside by internal or external borrowing. The people who are earning from other countries, at first improve their daily consumption of food staffs, and then they invest on buying flats and plots. So investment is not happening on commerce and industry rather it is happening on long-term needs of the people. A few people are investing to set up new industries. It has hurdles and also various types of risks.
- f) It is assumed that fiscal dominance is prevailing. So monetary authority is in associative role to ensure sustainability and growth.

In such a country, a pertinent and prudent fiscal policy would be discussed. Our aim is to find out comfortable amount of total government expenditure as percentage of GDP and suggest a prudent composition of government expenditure for enhancing growth. Expenditure composition could be sector-wise or function-wise. Function wise classification of total expenditure are: 1) Purchase of Services like payments to employees, 2) Purchase of final goods and utilities like purchasing pens and papers and also paying electricity bills etc., 3) Purchase of capital goods like materials for public hospitals and materials for road construction and expenditure against depreciation i.e. repair and maintenance, 4) Interest payments, 5) Subsidy, 6) Net transfer etc. The impacts of the change of the above components on GDP growth, inflation and external sector of the economy are not similar and very much complex in reality.

It is difficult to suggest the best amount of total government expenditure of a country. Firstly a country can't raise tax as much as it wants. It is important but unpopular sometimes called necessary evil. However raising tax today with better law enforcement could have inter-temporal benefit. It depends on the attitude of the political leaders how much they want to sacrifice for the future generation. But even if politicians are afraid to be unpopular, they should think of the future as being lavish today could do tremendous harm in future blocking the outlets for sustainable growth.

There is link between 'Government expenditure to GDP' ratio and the GDP growth rate. It could be an upward sloping curve with diminishing slope. If expenditure/GDP ratio is low then GDP growth rate is low. If expenditure GDP ratio increases gradually then GDP growth rate also increases gradually. But there is a limit to increase government expenditure because government should only provide goods and services of public nature. Government should not produce private goods. So it is assumed that after certain level the upward sloping curve



would be flat and later on if expenditure ratio increases then expenditure goes to unproductive areas of the economy. Part of government expenditure is financed from tax and non-tax revenue. The rest amount is financed from domestic and foreign loans. These loans have also different types of adverse impacts in both short-term and long-term which are not covered by this article. Let us start from a zero situation or balanced budget  $E_g - R_g = 0$ , where  $E_g$  = Government expenditure and  $R_g$  = Government revenue. In the economy, there is no pressure or impact of deficit financing. Ratio of government expenditure to GDP is linked to GDP growth rate. This can be shown by the following figure,

The above figure is showing that as the expenditure/ GDP ratio increases from A to B, it increases the growth rate of the economy. But there is a limit to increase the amount of government expenditure. If government looks after everything, then there will be a downward pressure on growth as private sector activities would be constrained.

### **Economic category wise explanation**

Let us start our discussion regarding purchase of services by the government. Expenditure on wages and salaries could change either for new employments and retirements or salary and wage increase (New pay commission). Public sector employment opportunity increases in every country. If population growth rate is positive, then more people enter into the labour force. A country with increasing population needs higher number of people from all professions i.e. more doctors and more civil servants. In the same way government also needs to employ more people than the number of people going for retirement. However, government expenditure increases over time for net new employments and for adjusting the salaries with the inflation rate. Government pays wages and salaries for buying 'service' from the people. On the other hand a government employee sells his service to the government. This expenditure is a part of the aggregate demand of the economy. There are empirical investigations on this area (Gupta et.al. 2002). Gupta and others find that spending increase in wages and salaries decreases the growth rate of the economy in long-run. Although this study says that pay and allowances has adverse impact on growth but in reality it may not be true in our model country. It depends on total population of the country and number of people in government services. Expenditure on wages and salaries could create inflation as it increases demand for consumer goods in short-term. In the long-run demand and price increase actually encourages the suppliers to produce more which will reduce the price and bring the economy in equilibrium only if other things remain same. Short-term impact also depends on the acts of the monetary authority. So we cannot make a conclusion about inflation as it is an outcome of aggregate impact- both fiscal and monetary. The impact on external sector depends on the



behaviour of the people which depends on the marginal propensity of imports. Also it depends on the degree of trade liberalization and other status with neighbouring countries. It increases demand for consumer goods, so it will also increase demand for imported goods which could create current account imbalance. Now if exchange rate is flexible and capital is not mobile then crowding out would increase the interest rate but there is no exchange rate appreciation. The exchange rate will only depend on the flow of goods and services i.e. on the current account components. So there could be exchange rate depreciation due to increased demand for imported goods. In short-term expenditure on purchasing services could create stabilization problem but in long-run it might be expansionary as more police, teachers, doctors or judges will make the society better off, if they have integrity and honesty in work and there will be trivial risk for investment. People will be encouraged to invest.

Expenditure on purchasing final goods and utilities includes payments for pens and papers, petrol and lubricant, office materials and miscellaneous expenditures and utilities like telephone, electricity etc. These are operational expenditures of the government. So it creates demand for consumer goods and services. But a portion of this expenditure goes to the autonomous bodies of the government although some are non-tax income of the government. If these bodies are financially solvent then government has to pay lesser amount of money to them as grants or loans-indicates lower degree of quasi-fiscal expenditure. These service providing agencies has to fix prices consulting with the government and in most of the cases these are administered prices not the competitive market prices. It ensures better service to the people by the government employees. Estimating the amount of expenditure is very important as there is immense scope of misuse. It is mentionable that utility price increase has both positive and negative effects. On the one hand due to administered prices fixed by the government, they get grants or loans from the government. So government has to allocate grants or loans to these autonomous bodies. On the other hand if they are independent and run the business like a private firm then government will not need to give resources to them from the revenue income of the government. It is not good to allow market prices for these semi-public goods. If utility prices are increased by the government then like other private businesses, it increases the cost for the government as well as for all the people of the country. This could create price level increase and thus inflation. Expenditure on utilities could be higher, if public sector gradually becomes bigger.

Expenditure on 'resource acquisition, purchase, public works and repair & maintenance' is investment expenditure. New things are bought here like furniture, computers, raw materials, machinery and parts and other capital equipments. This type of expenditure also includes new school buildings, repair

and maintenance of roads etc. In 1946, Domar argues that investment has a dual nature. That is, an increase in investment increases aggregate demand in the short run; and also increases productive capacity in the long run. Keynes did not mention that investment increases productive capacity. These investments have short-term and long-term impacts on the economy. In short-term it increases aggregate demand and income and foster growth. But if the demand is more than the capacity of the economy then inflation happens. Here we can mention that growth depends on the amount of crowding out and inflation. However in the long run it could create a downward pressure on price or at least not increase the price as this type of spending increases the productivity of capital and labour. Public sector capital expenditure acts as a catalyst to increase the productivity of both labour and capital. Suppose government is going to build a new road. The communication facility will reduce the transport cost and also the risk of damage that would have been due to time consuming old transportation system. This type of expenditure will have positive impact on the economy. Empirical evidence also shows that if the share of capital expenditure increases in total expenditure then it has positive impact on growth. A portion of this expenditure consists of imports. If capital goods are available in the domestic market, then there will be less pressure on external sector of the economy. If there are imported goods then it will have impact on balance of payments as well as on exchange rate. Impact on price level could be better as this type of expenditure reduces the cost of production. Although this may not be in the short run due to supply constraint but must be in the long run

Expenditure on transfer is very important as it increases the aggregate demand. In case of transfer income is shifted from rich individual to the poor. It helps to maintain social fabric (Gerson 1998). There are many literatures on the relationship between unemployment and crime. Gary S. Becker's (1968) seminal paper on "Crime and Punishment: An Economic Approach" was a breakthrough in Economics. He says that a person commits a crime when the expected utility by doing the crime is greater than the utility he could have gained by using his time and resource in other activities. His paper increases concern over the public cost of crime along with the relationship between economic variables and crime. So if the government gives unemployment benefits, then crime rate is reduced. Sala-i-Martin (1992) considers data of 75 countries and finds that public transfers have positive effect on per capita income growth. On the other hand some other economists (Von Hagen et.al. 2001) empirically proves that if government cuts transfer payments for ensuring fiscal adjustment, then it is expansionary. Presumably it does not increase saving as it is given to the poor people of the society. Reduced saving rate would reduce capital formation in the country. But in long-term, as this money is increasing the demand it will also increase the

supply if price increases. Transfers normally increase aggregate demand for essential goods. As here we assume a country with plenty of labour and there is massive unemployment, here government needs a lot of money to pay for unemployment benefit if it wants to. It has a bulk fiscal burden which most of the developing country's government cannot bear with poor government expenditure/GDP ratio. However it increases the welfare of the people of the country which could reduce social unrest and congenial atmosphere in the society. In the long run this type of social benefit could also create economic benefit. In these circumstances transfers should be given only to the most vulnerable groups of the society like old people, distressed woman, acid burnt woman etc. The area of transfer should only be increased for higher level of government expenditure/GDP ratio. Transfers may have impact on inflation. If transfers are an important share of total government expenditure or GDP then this could create inflationary pressure on essentials. But if transfers are given in kind, government has to buy items of transfers from local or international market. If it is imported then it will also affect the external sector of the economy. There is possibility of exchange rate change.

Subsidy normally hampers the free market pricing system. But it helps the producer to produce higher amount of output which otherwise would have been imported. Subsidy on inputs helps to reduce price of the commodities or not increase the price. Subsidy is acceptable if it ensures a certain degree of fairness in income distribution. Suppose fertilizer subsidy helps to prevent price hike of food items and helps people from all walks of life. It is also true that subsidy should be given when government has minor deficits.

Interest payment also has impacts on the economy. Interest payments are determined by the agreement of the government with internal or external lenders. Sometimes borrowing becomes essential for running day to day activities of the government. In many cases this happens due to poor revenue performance. If government has to pay very bulk amount of interest due to high debt then it has negative effect on the economy. In short-term government cannot reduce the amount of interest payments. So this part of expenditure composition is beyond the authority of fiscal policy. Fiscal authority can only reduce the long-term burden.

### **Sector wise Priority Calculation**

Now let us look into the sector wise allocation of government expenditure. Initiative should be taken to improve the sector wise optimum allocation. There are many sectors like human resource development (health, education etc.), energy, public administration, local government, agriculture & fisheries, industry

& commerce etc. We start from existing allocation and suppose total expenditure has increased due to higher level of revenue income. Now our concern is to find out the best way of additional resource utilization. Here marginal cost/benefit or marginal social cost/benefit of different sectors should be calculated. At first, resources should be allocated in the sector with the highest marginal social benefit. According to the ranking – resources could be allocated to different sectors of the economy. Here it should be mentioned that marginal amount is different for different sectors. We can build a school with smaller amount of money than building a power plant. So if a country has enough money to build a power plant and its marginal social cost/benefit is higher than building five or six schools (which is possible with same amount of money) then definitely allocation should go to the power plant.

The concept of marginal social cost/benefit is different from the concept of marginal cost/benefit. But calculating marginal social cost/benefit could be a hectic task and should be done with caution. In many countries budgeting is done as incremental basis. Marginal social cost/benefit concept is not considered in public sector which is a bottleneck for sustainable development of many developing countries. Sometimes it is also envisaged that marginal benefit is negative but allocation is increasing at a very high rate. This happens due to the pressure groups in the government. Many developing countries are unable to concise their unproductive expenditure although it's marginal benefit could hardly be positive.

Now let us look at the impacts on growth. If we could follow the marginal productivity principle then expansionary fiscal policy could ensure sustainability and growth. Sector wise expenditure also has short-term and long-term impacts. In short-term it increases aggregate demand thereby impacts on growth if there is little amount of crowding out. This demand increase also has impact on increasing productive capacity of the economy. But it takes time. In medium or long term, benefits come out from present day expenditure. A power plant takes time to be installed, in schools or training institutions people learn for many years then the society gets the benefit. So government expenditure continuously increases the productive capacity of the economy and this shifts the aggregate supply schedule rightward and we are always assuming a higher level of full-employment level of output. In the assumed country expenditure should be increased in both consumption and investment as the expenditure to GDP ratio is very low. The investment on education, health, nutrition, infrastructures have short-term and long-term effects. These investments are associative and help to facilitate the economy in a better way to ensure equal price almost all over the country. So although in such a country both government consumption and investment is necessary, growth rate of government investment should be higher.

**Conclusion**

In the assumed country firstly, internal resource mobilization is needed as the government expenditure to GDP ratio is low. The country can do it only by reducing tax evasion. No change in income tax rate or tax base is required. Secondly, special thrust should be given to governance, act or rule formulation and property ownership laws. Governance can be ensured only by framing self-explanatory and transparent acts, rules and regulations with a view to strengthen civil services. Governance also includes good property rights situation. These actions need higher level of government expenditure on public administration. Thirdly, Government should look at the prioritization issue. If energy sector has the highest marginal social benefit then resource should go in that sector. Thus government expenditure composition should change in line with marginal social benefit/cost. Also fiscal authority should be in the leading role. Lastly a question could arise that during resource allocation- whether we should consider the economic classification first or sector wise classification. In this respect we should start from sector wise classification. Then in each sector we should think of the amount of government expenditure in each economic category. It is true that education and health are priority sectors, but if there is lack of rules and regulations then economy cannot run in a better way. Civil service should be strengthened, unproductive expenditure should be curtailed. If the size of government expenditure is not high, then for ensuring governance and better internal resource mobilization more employment might be expansionary in the long-run. Transfer payment should be linked to internal resource mobilization. Capital expenditure should be given the highest priority.

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