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Can Public Expenditure Stabilize Output?

Multipliers and policy interdependence in Queensland and Australia

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Abstract

The debate on the use of fiscal policy as a tool of macroeconomic stabilization is quite vehement in Australia and abroad. This paper contributes to the discussion by estimating government expenditure multipliers for Australia and one if its states, Queensland. Impulse response functions derived from a SVAR model indicate that the multipliers are positive and greater than one. This suggests that government consumption expenditure should be used counter-cyclically to stabilize output. However, a chronology of business cycles and government expenditure dynamics reveals that this is not frequently the case. At both national and state level, government consumption expenditure "aligns" with the business cycle only about one third of the times. This means that more often than not, fiscal policy is run pro-cyclically or (at best) a-cyclically. Moreover, from the point of view of Queensland, federal and state fiscal policies are jointly aligned with the Queensland business cycle only 20% of the times. Conversely, federal and state fiscal policies are jointly misaligned with the Queensland business cycle in 60 quarters out of 116, i.e. about 50% of the time. This misalignment is a factor of destabilization of the Queensland economy.

JEL Classification: C32, C54 E62, E63

Keywords: government consumption expenditure, multiplier, SVAR, Australia, Queensland.

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