International Economics 146 (2016) 59–84

Contents lists available at ScienceDirect

International Economics

journal homepage: www.elsevier.com/locate/inteco

Fiscal multipliers in Emerging Market Economies: Can we learn something from Advanced Economies? ☆

Marie-Pierre Hory

Université d'Orléans, Laboratoire d'Economie d'Orléans, UMR CNRS 7322, Rue de Blois, BP 26739, 45067 Orléans Cedex 2, France

ARTICLE INFO

Available online 22 November 2015

JEL classification:
E62
H5
O23

Keywords:
Fiscal multiplier
Spending Multiplier
PCH-VAR
Emerging Markets

ABSTRACT

It is a well-established fact that Emerging Market Economies (EMEs) have smaller fiscal multipliers than Advanced Economies (AEs). We confirm this difference for our sample using Panel VAR and Interactive Panel VAR (Saborowski and Weber, 2013) models. Then we analyze the impact of some macroeconomic factors on multiplier effects for EMEs and AEs separately. We argue that the development degree can modify the effect of the traditional determinants of fiscal multipliers. A Panel Conditionally Homogeneous VAR (Georgiadis, 2012) is used to test this statement. First of all, we find that the tested determinants (imports, public debt, savings, unemployment and financial development) act in the same way both in EMEs and in AEs. Secondly, public spending efficiency is relatively more sensitive to each tested determinant in EMEs than in AEs. Thirdly, the most important factor for improving fiscal policy efficiency in EMEs (public debt), differs from the one in AEs (openness to trade). Last but not least, we show that improving the tested determinants individually is not sufficient to achieve the same public spending efficiency in EMEs.

☆This paper has been presented at the 4th Ph.D. Student Conference in International Macroeconomics and Financial Econometrics organized by EconomiX-CNRS and held in Nanterre (France) on March 18, 2015.

E-mail address: marie-pierre.hory@univ-orleans.fr

http://dx.doi.org/10.1016/j.inteco.2015.11.002

1. Introduction

Following the global financial and economic crisis, large fiscal stimulus packages were set up in Advanced Economies (AEs) leading to a surge of interest for fiscal multipliers in these countries. Since 2009, many papers are interested in fiscal multipliers focusing on their size and determinants.

Regarding the value of fiscal multipliers, estimates range from zero to more than 2 (IMF, 2011) according to the methodology used and the country or period considered.

Since the particular context of the crisis, the determinants of multiplier effects are broadly studied, especially the state of the business cycle and the monetary policy interest rate, but also the state of public finances and the exchange rate regime for example.[1] These studies aim to explain the spread between fiscal multipliers over time and countries. Highlighting the main determinants of fiscal multipliers, these articles show when and why fiscal policy is the most efficient.

Although these empirical studies mainly focus on AEs, there are some articles about Emerging Market Economies (EMEs). The macroeconomic effects of public spending in EMEs are also an important issue since public spending can provide a boost to the development process. The few studies about multipliers in EMEs find smaller values than in AEs whatever the method used (Ilzetzki et al., 2013; Kraay, 2014). Why is this spread so large?

This difference is theoretically explained by structural characteristics that differentiate EMEs from AEs: EMEs face to a lesser supply-side flexibility, a faster growth over the last decades and a weaker management of public spending. However, there is no empirical explanation about this. Indeed, the determinants of multiplier effects in EMEs are poorly investigated. To the best of our knowledge, only Ilzetzki et al. (2013) deal with fiscal multipliers' determinants in EMEs but they are assumed to be the same as in AEs since the computed impact is homogeneous whatever the development degree. EMEs and AEs are studied together while the particularities of EMEs ask for a specific analysis of the multiplier mechanisms (Combes and Mustea, 2014). Since there is no empirical study about the determinants of multiplier effects considering EMEs specificities, can we really extend the conclusions about them from AEs to EMEs?

The contribution of this paper is twofold. Using a panel of 48 countries (EMEs and AEs) over the period 1990–2013, we first use PVAR and Interactive PVAR (Saborowski and Weber, 2013) models to (re)-estimate multiplier effects in AEs and EMEs to confirm previous results in the literature over our sample. Secondly, we select the main determinants of multiplier effects according to the literature and data availability (openness, public debt, savings, unemployment, and financial development). We use a Panel Conditionally Homogeneous VAR (Georgiadis, 2012) to allow multiplier effects to vary across the level of development and these chosen determinants. In this way, we can check that the development degree modifies the determinants and/or the extent in which the determinants act. To the best of our knowledge, this paper is the first to estimate the impact of fiscal multipliers' determinants conditionally to the development degree. More generally, it is the first to use the PCH-VAR model for studying the effects of fiscal policy both in EMEs and AEs.

As a result, we confirm that multiplier effects are smaller in EMEs than in AEs and we show that the tested determinants act in the same way in both groups. Nevertheless, since multiplier effects are weak in EMEs, they are relatively more sensitive to an improvement in the considered macroeconomic factors. However, none of these factors allow public spending efficiency in EMEs to become as efficient as in AEs.

This paper proceeds as follow. Section 2 surveys the main empirical methods used to estimate fiscal multipliers. Section 3 presents the estimation of multiplier effects in EMEs and AEs by using PVAR and Interactive PVAR models. Section 4 discusses the theoretical intuitions and justifications for differentiating the effects of some macroeconomic factors according to the development degree. Section 5 briefly introduces the PCH-VAR model and outlines the empirical results about the conditional effects of the considered determinants. Section 6 concludes.

[1] See Table 2 in appendix.