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Fiscal Policy and Its Relationship with Economic Growth: A Review Study

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Abstract: The fiscal policy reflects the state use of its economic programs, which includes revenues and expenditures in the best way. This is done by directing the state economic plans to determine the sources of income and how to spend them, and what are the most important spending trends such as wages of government employees and various service projects, to achieve the highest levels of economic balance. Economic growth represents the process of increasing real income in a cumulative and continuous manner over a period of time, where this increase must be greater than the rate of population growth. The aim of this paper is to review the research work conducted on fiscal policies and economic growth, noting that there are two types of fiscal policy; the first type is spending, while the second type is taxation. 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 previous research.

Keywords: Fiscal policies, economic growth.

INTRODUCTION

Fiscal policy considers one of the most important means of government intervention in economic activity, where it is the foundations and standards and frameworks developed by government for the conduct of financial and economic activity of the country.

Therefore, fiscal policy is the government's method of influencing the national economy in order to maintain overall economic stability and address its problems [1].

Economic policy includes a set of policies that each operate on a quantity or more of important amounts, such as fiscal policy, monetary and credit policy, exchange rate policy and trade policy. Fiscal policy occupies an important place among other policies because it can play the greater role in achieving the multiple objectives of the national economy [2].

Fiscal policy is one of the most important tools of economic management in achieving economic development and eliminating the problems that impede economic stability. In addition to the distributional and specialized effects of fiscal policy instruments, there are stable effects of the role of government spending and taxes on the overall demand and hence macroeconomic variables [3].

In addition, the fiscal policy is considered one of the most important economic policies affecting economic growth, where it can play an important role in achieving the various objectives of the national economy, especially in terms of raising the rate of economic growth through its various tools, which are easily controlled by the government [4].

Economic growth considers the main factor officially adopted in measuring the progress of countries. Most developed countries have high economic growth rates, unlike those of developing countries with very low growth rates, with the exception of some oil-producing countries that control their rate of growth. The importance of economic growth stems from its positive effects on the national economy and society, which giving a strong impetus to new investments, resulting in greater employment and purchasing power for the community [5].

Also, economic growth represents all processes that ensure high rates of income for individuals and enterprises by relying on the economic impact of supply and demand in the local market. This leads to an increase in the quantity of goods produced and the provision of services based on the availability of many economic elements associated with the production process, such as capital, labor, machinery, productive resources, and other means that contribute to economic growth [6].

In order to achieve the objective of the study, it was divided as follows: Section 1 Introduction about fiscal policy and economic growth, Section 2: Concept of fiscal policy, Section 3: Concept of economic growth, Section 4: Literature review, and finally Section 5: Conclusion.

CONCEPT OF FISCAL POLICY

Fiscal policy is one of the concepts that have undergone major transformations in economic, social and financial history, where it is the mirror that reflects the economic and social role of governments and is a reflection of it in every age.

Also, fiscal policy refers to determining the government of its sources of income and the means of disbursement of this income, in other words, explaining from where the income comes and which sources are most important and where the most important and best channels for distribute this income. This is done in order to realize the government for its economic and social objectives and to achieve success of its economic policy [7].

Fiscal policy is also part of the government's policy of achieving country revenues through taxation and other means to determine the level and pattern of expenditure of such revenues. In addition, the government can influence the level of aggregate demand of the country and thus the level of economic activity [8].

In addition, it is defined as a set of goals, directions, actions and activities adopted by the state to influence the national economy and society in order to preserve its general stability, its development, its problems and the changing circumstances [9].

Financial policy plays an important role because it can play a greater role in achieving the multiple objectives of the national economy because of its multiple instruments, which are among the most important tools of economic management in achieving economic development and eliminating the problems that impede economic stability [10].

The instruments of fiscal policy represented: taxation, distribution of spending, and the method of controlling public debt, and surplus income, where these tools can be explained as follow [11, 12].

Taxes: such as: income tax, corporate taxes, indirect taxes, government tariffs on domestic and foreign goods and services in terms of imports, in order to protect the national industry and encourage citizens to demand.

Government Expenditure

The government process of controlling the expenditure according to its size, and how it is distributed to the various activities within the country, where government expenditure has a strong impact on the activities of the country, and although the total expenditure is constant, however, redistribution of government expenditure on economic activities has a significant impact, such as increasing the proportion of expenditure on a particular economic activity and reducing it to another as a means of stimulation.

Public Debt

The size of the public debt, the size of its growth, and the way it is obtained are very important because of its strong influence on the general economic conditions of the country, such as a country of financial crisis in the period of economic inflation.

Fiscal policy derives its importance from its tools, where public expenditure affects national economic activity, and affects consumption, savings, investment, and revenues, which represent the resources that the state receives to cover its expenses, where increase the revenues and investment of the country will increase the economic growth in the country [5].

In addition, fiscal policy is an important part of economic policy, whose main objective is to achieve economic growth, achieve full employment, maintain price stability, achieve social justice and balance the balance of payments. The objectives of the fiscal policy are as follows [13].

Economic development represents the basis of growth, which is based on the volume of production and on the structure of this production.

Achieving Tax Justice: Achieving social justice involves in essence the achievement of tax justice, where the government plays the role of the collector; as it cuts some of the entries of individuals for provide services to them in various matters of their lives.

Settlement of the economic balance: Fiscal policy can effectively assist in settling economic conditions in times of recession and boom; the government does what the individual cannot do; encourages investment in times of recession, increasing production, while in times of prosperity, power limits public investment.

CONCEPT OF ECONOMIC GROWTH

Economic growth means "an increase in gross domestic product or gross national income, to achieve Increase in real per capita income. A steady increase in the actual production of goods and services, in addition to the increased ability of the economy to produce these goods and services" A continuous increase in average real per capita income over time, and we mean the per capita income ratio of the total income divided by the population [14].

Through the preceding definitions, several conditions can be observed in the definition of economic growth: The increase is in average per capita income, not in gross income only. Requires an increase in the average national income per capita is the rate of increase in national income is greater than the average Increase in population. The increase is real and not nominal, so it will achieve an increase in per capita income [15].

Real requires that the rate of increase in per capita national income is greater than the rate of increase in The general level of prices "inflation" (for the possibility of an increase in the value of output as a result of price increases only).Achieving a steady and stable increase in per capita real income per capita, real per capita income requires that this increase be a result of a real increase in the level of activity That is, they do not occur because of emergency circumstances, which may be due to the State receiving foreign aid for a period of time Or because of a sudden rise in the prices of goods exported abroad due to urgent circumstances [16].

Through the above conditions, a comprehensive definition of economic growth can be concluded as is what the economy produces more than in the previous period. To be accurate, inflation must be eliminated. If the economy produces more, companies are more profitable and stock prices rose. Companies have the capital to invest and recruit more employees. As employment increases, incomes rise. Consumers have more money to buy additional products and services, purchases are achieving higher economic growth. For this reason, all countries wish to achieve positive economic growth. Therefore economic growth is the most viewed economic indicator [17].

Economic growth contributes to the economy of countries and increases their self-sufficiency by providing all available means to support institutions and companies in providing their production and service in the markets and then measuring their success in achieving the required income during the financial period specified, this lead to increase in the market values of goods and services, which lead to continued economic growth [12].

Economic growth rate is the rate during the year in which the income of a particular industry or country increases. When this rate changes due to the impact of inflation it becomes known as real economic growth. If a decline in growth leads to a recession, economic growth is defined as a measure in the growth of the economy between different periods of time. In terms of the use of percentages, is also a measure the percentage of changes affecting the country's GDP from year to year [18].

The importance of economic growth is highlighted by its role in increasing the value of income, which leads to improving the level of income of individuals, providing all basic needs, especially food at reasonable prices, commensurate with the economic potential of all people, and to ensure that the health, education and social services of the community are improved [18].

EMPIRICAL LITRATURE REVIEW

In this section of the paper, a series of previous research and studies on the subject of fiscal policy and their 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 the fiscal policy and economic growth, as follows:

Al-Shatti [19] investigated the impact of the fiscal policy on economic development in Jordan, in order to achieve this objectives the study designed mathematical model to analysis the data which covered the period (1989-2013), after analyzed the data the study found that there is positive impact of the fiscal policy (expenses and tax revenues) on economic development in Jordan, while the capital expenditures has negative impact on economic development in Jordan.

Macek and Janků [5] discussed the impact of fiscal policy on economic growth depending on the institutional conditions in the OECD countries, for the period 2000-2012, The method of least squares (OLS) is used. The study showed that In the case of government expenditure impact on economic growth in countries with lower financial transparency had a positive impact, while countries with high financial transparency had a negative impact on economic growth, It is clear that the negative impact of taxation is more detrimental to economic growth in countries with worse institutional conditions.

Oguanai and Ogunta [4] examined the impact of fiscal policy variables on the economic growth of sub-Saharan African countries. The results revealed distortionary taxes raising the rate of economic growth, while production expenditures hampered economic growth, and the results showed that the balance sheets of these countries, although having a positive but insignificant impact on economic growth in Africa.

Shihab [7], discussed the causal relationship between economic growth and fiscal policy in Jordan, in order to achieve this objectives the study designed mathematical model rely on Granger methodology, that used for determine the relationship between the study variables, the data of this study covered the period (2000-2012), after collected the data and analyzed the results showed that any change in budget deficit can explained through the changes in the economic growth,

also there is direction relationship between the study variables (fiscal policy and economic growth) in Jordan.

Nawaz and Khawaja [21] the study aims to demonstrate the impact of fiscal policy on economic growth. To achieve these goals, the study designed the Solo Growth Model. The analysis included a sample of 56 countries. After analyzing the findings of the study, the effect of fiscal policy on growth in developed economies is positively correlated, while fiscal policy has a negative correlation with developing economies.

Ngakosso [22] searched Fiscal Policy and Economic Cycles in Congo, the study analyzed the quarterly data from for the period 1989-2015, In order to achieve these study objectives used the mathematical model developed by Huart, the study showed that restrictive fiscal policy was rejected in favor of counter-cyclical restraint fiscal policy, As well as, the countercyclical expansionist fiscal policy has been confirmed.pro-cyclical expansionary fiscal policies have caused neither debt repayment nor accumulated arrears.

Audu [23] they study The Impact of Fiscal Policy on the Nigerian Economy. For the period 1970 to 2010.Co-integration error correction mechanism was used, to test the stability of the Nigerian economy, the study revealed a causal relationship between GDP and study variables. He also found a causal link between exports and GDP, and hence fiscal policies.

Karagöz and Keskin [24] The study aims to show Impact of Fiscal Policy on the Macroeconomic Aggregates in Turkey .in order to achieve this objectives the study used the by Bayesian vector auto regression (BVAR) technique. Covered the period (2003 – 2015), after analyzed the data the study found that government revenues and expenditures have limited impact on the macroeconomic variables set which includes gross domestic product (GDP), external debt, stock market index, inflation and interest rate.

Baballola and Amino [25] examined the impact of fiscal policy on economic growth in Nigeria. The data were analyzed from the period (1977 to 2009). The sample was examined using the enhanced Dicky Fuller model after which the Engel-Granger joint integration test was performed. The results showed that production expenditure positively affected economic growth during the study period, and the joint integration test confirmed that there is a long-term relationship between them

Alam *et al.*, [10] tested The Distributional Impact of Fiscal Policy in Jordan, the data of the Department of Statistics included interviews with approximately 11,000 families and the period during (2010 to 2011) over the 12 months was detailed data on household income and expenditure, as well as data on sources of income, domestic use of services, education and health, the results showed that the indirect tax system is inefficient and thus increases the gap between the poor and the rich, as the poor are paying a greater fraction of their income than the rich as sales tax.

Ndubuisi [17] studied the dynamic relationship between fiscal policy and economic growth in Nigeria covered the period 1985-2015, the data were analyzed used OLS, unit root test, Error Correction mechanism and co-integration. The results revealed showed that fiscal policy significantly influenced the growth in Nigeria economy.

Sarangi *et al.*, [26] investigated the effectiveness of fiscal policy in Jordan: For the period during 1990-2015, by used a Structural vector autoregressive (SVAR) model. The result showed current expenditure, subsidies, social benefits and compensation to employees have positive impact, as well as it also shows that remittances are an effective factor in reducing poverty and inequality in Jordan

Zabiullah *et al.*, [13] tested the role of fiscal policy in developing of Indian economy: a conceptual observation. This study was based on the source of secondary data such as the role of Fiscal policy in influencing the Indian economy and its evolution in addition to articles, magazines and books and so on the study found that Fiscal policy has an influential role in the Indian economy. Because it is useful to use resources in the best way, Making use of national income in proper distribution, providing financial incentives and reducing inequality. The success of fiscal policy depends on taking the right time, reducing public spending, increasing revenues, and reducing taxes that will help to strengthen the economy and manage it effectively during implementation. The importance of establishing industries in the public sector and the government has a prominent role in achieving balanced development in the country.

Najaf [27] examined the Impact of Fiscal Policy Shocks on the Indian Economy, the study covered the period (1981 to 2010), the data were analyzed applied the error correction model, variance decomposition and Johansen co integration test model, the standard analysis showed that there is long run association between Gross Domestic Product and other variables.

CONCLUSION

This paper is a review of the fiscal policy and economic growth through previous research. This paper focused on the importance of fiscal policy and its role in the economic growth and economic development through various financial policy instruments, This paper also shows that the sources of income and expenditure in fiscal policy vary and their relative importance varies from one country to another, where income for some

countries rely heavily on their income from taxes. Therefore, taxes are important for them, such as Jordan, while country such as Saudi Arabia consider oil is more important because it is its biggest source of income.

While the expenditure includes salaries of employees and wages of employees in the government sectors and the disbursement or spending on infrastructure such as roads, bridges, water, electricity and utilities in general, even the assistance it pays to other countries.

The paper also notes that economic conditions differ from country to country according to the economic and political systems prevailing in each country, and therefore cannot provide a single study that is valid for all these systems. It also indicates the need to find out which variables are most influential to economic growth. The issue of economic growth reflects the strength of the State economy, and the State is more attractive to foreign investment, the better the rate of economic growth, which indicates a state of equilibrium and recovery in the economy.

In addition, the paper found that the impact of economic policies on economic activity is an important subject in macroeconomic analysis that is still controversial, because fiscal and monetary policies are closely linked and often mutually reinforcing, fiscal policy affects monetary policy. In order for the country to achieve economic objectives such as increasing economic growth rate or full employment, it pursues an economic policy based on the structure and development of the state economy. The relationship between fiscal policy and economic growth is a very important issue, which has been a key issue for many economists, policymakers, and growth models have differed over the impact of fiscal policy on economic growth.

The fiscal policy also represents the use of government spending and taxes to influence economic activity and quality, as well as improving overall output and job creation, with the aim of achieving macroeconomic growth through sustained economic growth.

In reviewing the theoretical literature on financial policy, the paper found that the state's adoption of a fiscal policy leads to the stability of government spending policies and guarantees that they will not be changed, and the use of financial policy instruments in a thoughtful and organized manner will contribute to improving economic growth opportunities.

In addition, the relationship of fiscal policy to economic growth is not fixed and constant in all countries and situations. In some cases, fiscal policy alone cannot provide economic growth, and in some cases the degree of fiscal policy impact on long-term economic growth is better than the extent Short, and the opposite may happen.

The relationship between fiscal policy and economic growth is a subject of great interest in financial and economic studies, which has an impact on economic growth both in the short and long term. Attention to the relationship of fiscal policy to economic growth has focused on the policy of public spending in particular and its impact on long-term economic growth.

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