Abstract

Using quarterly time series data of 13 years (2000-2012), this study investigates the impact of government expenditures and their components on economic growth in Palestine. It seeks to achieve several objectives, mainly identifying the categories of government expenditures (current and capital), calculating the percentage each category forms of the total government expenditures and comparing the effect of each category on economic growth. Moreover, this study discusses several policy implications that will be addressed to the opponent parties that might benefit from such a study.

This study discusses a very important economic fiscal tool, the government expenditures. Monetary policy isn't an option in the case of Palestine, as it doesn't have its own currency. Moreover, the fact that taxes, which are another fiscal tool, is affected by Israel, this leaves the Palestinian government with one economic tool to use in enhancing the economy, which is government expenditures. This study gains its value from using two methods, which few of the local studies use. It uses the Lisman and Sandee formula for transforming annual data into quarterly for some of the missing data. The study also uses the Incremental Capital Output Ratio (ICOR) method to estimate capital where direct data are missing for such a variable.

This study uses descriptive and statistical analysis of data. The descriptive analysis is used to describe and show the growth of some economic indicators such as capital, labor, current and capital expenditures as well as the total government expenditures. The data are based on secondary data obtained from Ministry of Finance concerning government expenditures while the other independent variables along with GDP are collected from Palestine Central

Bureau of Statistics. The data are also analyzed using the ARDL method to test if there is a long run relationship among the variables of interest. Moreover, VAR estimates are performed to capture the linear interdependencies among multiple time series. The Granger Causality Test in the VAR Environment using Toda and Yamamoto Procedure is performed to test causality among the variables. Two models are used in this study. In the first, real gross domestic product (RGDP) forms the dependent variable while capital (estimated using ICOR method), labor (employment), total government expenditures are adopted as the independent variables. In the second, RGDP also forms the dependent variable while labor, capital and the components of government expenditures (current and capital expenditures) form the independent variables. Two dummy variables are used in both models to represent the political and economic events that might effect the economy of Palestine during 2000-2012. R^2, F-test and t- test are calculated along with Durbin-Watson test of autocorrelation. The study is limited with the shortness of time coverage period as a result of recent establishment of Palestine Authority and its ministries in the past two decades as well as lacking some data for some of the variables at some of the quarters of the study.

Results show that labor and technology have an insignificant impact on economic growth for the period in Palestine. This is inconsistent with theory as well as the results of several literature reviews but similar to few other researches. However, capital shows a positive and significant impact on economic growth. This is consistent with theory and most of the studies of literature review. Moreover, results show that total government expenditures have a positive yet insignificant impact on economic growth, which is consistent with the neoclassical theory as well as several studies of literature review. As for current expenditures, they show negative but insignificant impact on economic growth, while capital expenditures show positive but insignificant impact on such growth. This means government expenditures, as a whole had no significant impact on economic growth. Dummy variables, however, turned out to be significant, which means that political and security events do affect economic growth in Palestine (2000-2012).

Based on these results, several policy implications are discussed. First, more attention might be paid to raise the productivity of labor through training and qualifications. Second, government might facilitate the import of new technologies and helps keeping the existing technology up to date. Third, policy makers might direct public investment to projects that have financial and economic returns in order to achieve self-sufficiency and stop being dependent on the donations and grants from other countries. Fourth, government might encourage investment in the private sector and give facilities to encourage the Palestinians outside the country to invest in their homeland. Finally, government efficiency can be improved by reallocating its expenditures. Extra share of the total government expenditures might be dedicated to the capital expenditures.