

Research Article

Fiscal Policy and Economic Growth in Nigeria (1981-2018)

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Abstract: Nigeria budgetary framework has over the years witnessed continuous expansionary fiscal policy, both in the recurrent and capital expenditure but there seems to be little or no corresponding effect on the growth of Nigerian economy. This study assesses the impact of fiscal policy on the growth of the Nigerian economy. It further attempted to determine the effect of the federal government expenditure and its significant on the growth of the economy. This study methodology adopted Philips-Perron (pp) unit root test, Johansen cointegration and error correction mechanism. The Ordinary Least Square (OLS) of multiple regression analysis was used for the model estimation. The analytical result showed that government recurrent expenditure has significant relationship with economic growth in Nigeria and that capital expenditure also impacted negatively on its economic growth during the period under study. Government tax revenue has a negative and significant relationship with economic growth in Nigeria, inflation is negative and insignificantly related to economic growth in Nigeria. Among others, the study recommended that government should carry out tax incentive measures to encourage the growth of industries and enhance productivity, increase budgetary capital allocation, and promote transparency in the budget implementation.

Keywords: Fiscal policy, economic growth, government expenditure, nigeria economy.

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INTRODUCTION

Despite the contrary view of the Fiscal policy by the monetarist, Fiscal Policy measure has continued to be an integral part of government strategy in the process of Economic stabilization and growth. Spending adjustments and taxation response have also taken centre stage in the post-civil war Annual Budgets of Nigeria to address issues of recurrent instability of the economy. Needless, therefore, to say that these are deliberate and discretionary economic policies aimed at bridging the gap in the aggregate demand, promote production, tackle unemployment and shore up the yawning gap of inadequacy of infrastructure for the overall economic growth. Fiscal policy measures also incorporate the private sector as part of the measures to promote economic activity, especially in the event of downturn where deficit financing becomes inevitable, it being tool for stabilization.

Otmar I. (2005), however observed that fiscal policy measures inculcate the discretions that affects both the short and long term specific structural changes both in public finance shocks situation and other exceptional circumstances. In the light of the foregoing,

suffice it to say therefore that fiscal policy promotes mass economic stability through the enhancement of the aggregate demand and other factors. This study examines fiscal policy and economic growth in Nigeria from 1981 to 2018.

REVIEW OF LITERATURE

Concept of Fiscal Policy

According to Buhari (1993), fiscal policy is a deliberate action of the government over revenues and expenditures aimed at influencing macroeconomic variables in employment, aggregate demand, general price level interest rate among others in a desired direction. Behutia (2008), opined that fiscal policy consists of steps and measures which government take both for revenue and expenditure sides of its budget. Thus, it is the aggregate effects of government expenditures and taxation on income, production, and employment. Dwivedi (2008), stated that it is the government programme of taxation, expenditure and other financial operations made to achieve certain national goals. He posited that whatever the objectives and the order of priorities, the two basic instruments of fiscal policy to achieve social goals are taxation and

public expenditure. Similarly, Ijeh (2008), defined fiscal policy as government action plan on how to raise funds and disburse them. He further stated that, it is the use of government revenue and expenditure programmes to affect the economy in a way to produce desirable effect, which effect will lead to full employment, general goods price level, aggregate demand, economic growth and development. Above all, it could be diminished that fiscal policy is the governments action within its budget framework in a given year to influence pattern of expenditure in order to achieve certain macro-economic variables like employment, wages, consumption, demand and supply of goods and services in a targeted manner. In this study, fiscal policy is defined as changes in government expenditures and or taxes to achieve economic goals aimed at economic growth.

Fiscal Policy in Nigeria

Fiscal policy is necessary for economic growth, stabilization, and transformation. In the economic system, it becomes a tool to control the production and consumption of goods and services. Alade (2017), averred that it boosts demand through Tax Acts and increased transfer payments. Thereby conducting the average household incomes and encourage consumer spending. The policy can be used to correct imbalances during the period of recession and depression.

In Nigeria, like in most development countries, there has been a continuous expansionary fiscal policy via the increase in government recurrent and capital expenditure over the years. This could be attributed to huge budgetary allocation resulting from receipts in the production and sale of crude oil and the increased demand for public infrastructure and services like roads, education and health facilities, external and internal security. Statistics show that total government recurrent expenditure in 1986 increased from ₦7,696.90 million to ₦124,491.30 million in 1996. The same in 2006 from ₦1,290,201.90 million to ₦3,325,156.25 million in 2012. For fiscal capital expenditures, it increased from ₦8,526.80 million in 1986 to ₦212,926.30 million in 1996, then to ₦552,385.80 million in 2006 and ₦874,762.27 million in 2012. In 2012 recurrent expenditure accounted for about 71.5% of total expenditure whereas about 28.5% was expended on capital expenditure (CBN, 2012). In view of the diminishing proportion of capital expenditure and the increased growth of recurrent expenditure, there appears to be an obvious apathy by government on the development of infrastructure and capital goods by its budgetary allocation which tend to hinder growth as there cannot be appreciable economic growth in the absence of visible capital formation (Ojima & Anyanwu, 2019).

Economic Growth and Fiscal Policy

Economic growth is the ability of the economy to increase the production of goods and services. It is indexed or measured by the Gross Domestic Product (GDP) or Gross National Product (GNP) of the economy at a given time. the GDP is propelled by human resources, infrastructure, National Resources and Technology. This explains the reason why economy with low propensity of these factors experience low GDP. In summary, economic growth is a positive change in the production level of goods and services within an economy over a given period of time or a measure of output of goods and services generated within an economy propelled by the prevailing factor input in a given time period (Ojima, 2019). Similarly, Central Bank of Nigeria (CBN) (2010) and the International Monetary Fund (MF) (2010) describe economic growth as the increase in the amount of the goods and services produced in an economy over time and conventionally measured as the percent rate of increase in real gross domestic product, or real GDP (RGDP). According to Dwivedi (2008), economic growth drives the economy through the quality of the labour force, natural resources, capital formation, technological development, and socio-political factors. Riley (2012), opined that the determinants of growth are factors such as physical capital stock, size of active labour force available for production, the quality of human capital, technological progress, and innovation growth in the institutions. These are however coupled with stable political system, stable observation of rule of law and macroeconomic stability. Other indices include increase demand for goods and services, domestic or foreign. The potential impacts of fiscal policy on the long-term growth of any economy have also generated substantial debate. According to (Tanzi and Zee, 1996), the emergence of the endogenous growth theory holds that investment in human capital, innovation and knowledge are significant contributors to economic growth. Therefore, it is important that special attention is paid to the above factors when proposing fiscal policies to drive the economy in the desired direction each fiscal in year. This fiscal policy promotes growth as investments in human and physical capital increases. The growth is consequently affected by taxation and government expenditure. Therefore, for fiscal policy to impact on economic growth, the management of the fiscal instruments will be directed to affect each or some of the drivers of growth to be able to impact on the overall growth of the economy.

Theoretical Framework

The effect of fiscal policies on economic growth has been a subject of debate among policy makers and scholars. This has culminated to what can be described as the great debates between the Keynesians (fiscalists) and the monetarists (Anyanweu, 1993). Scholars in these diverse discussed were therefore described as Keynesianists and the

Monetarists. Their arguments are discussed in the following:

Keynesianism or Fiscalism

Keynesianism described the theories and policies of the economists who claim to have inherited and further developed the ideas of the great English economist, John Maynard Keynes (1883-1946). Keynesianism or Keynesians are apologists of JM Keynes are in sympathy with increased level of government intervention in the economy through fiscal policies to manage or increase the aggregate demand for the sake of achieving optimum policy performances. This is because according to them, the economy is inherently unstable and see the need to stabilize it through active government intervention through development of appropriate fiscal measures. Thus, deficit financing and other fiscal measures are important and tools to achieve the level of aggregate demand consistent with full employment and proper development/engagement of all the other growth variables. This is buttressed in the Keynesian theory that increase in government spending and other fiscal measures, causes an upward shift in the aggregate demand curve (Dewett, 2009).

Adjunct to the basic proposition of the Keynesian theory is that money does not matter in the short-run and that money supply transmission mechanism, is an indirect process of working through the cost of capital channel. This argument proves the monetarist transmission channel between money supply and income incorrect, rather, the reverse channel which run from change in income level to money supply, appears to be correct (Anyanwu, 1993). In summary, the Keynesians believe that money and monetary policy do not matter in stimulating aggregate demand, price, or output rather it is fiscal policy. In other words, the Keynesians believes that it is the fiscal policy that stabilizes the economic system. This view is contrary to the monetarists.

Monetarism

Monetarism refers to the concept or theory of Milton Friedman of the Chicago University, USA who hold that “only money matters” and that monetary policy is a more content instrument than fiscal policy in economic stabilization. They attach high premium to the variations in the quantity of money as the main determinant of economic activities and therefore, economic conditions (Akpapkan, 1999). They also assume an inherent stable economy that does not require stability for government intervention through fiscal policies. No wonder the monetarists assign causal role to money. They believe that quantity of money (money supply) is exogenously determined and thus responsible for the instability in the system by manipulating money supply. The monetarists also argue believe that fiscal policy is cumbersome and difficult to implement in a speedy manner. Their further argument

is to the effect that an increase in government spending (especially when financed by debt) increases the interest rate and crowds out private sector investments. By crowding out describes a phenomenon where increase in government expenditure leads to a corresponding decrease in the level of investment by the private sector. Differently put, government involvement in a sector of the market in such a manner that the private sector may find it difficult to invest in that sector. The believe that the private sector cannot generally compete with the public sector or government. This phenomenon, according to the monetarists, will lower economic growth, create inflation, and aggregate unemployment.

Consequently, in their view, fiscal measures will lead to poor economic performance rather, monetary policy will be more effective for macroeconomic management and stabilization. In recent times, this debate between has been redirected at the question of changing aggregate demand (i.e. $C + I + G + X - M$) by the both theorists.

Empirical Literature Review

The impact of fiscal policy on economic growth has been studied taking into cognizance the different time series. In other cases, the studies have involved mixed findings using cross sectorial and panel data. The study of Mansouris (2008) were on the relationship between fiscal policy and economic growth in Egypt, Morocco, and Tunisia. The span of data for each country were 1975-2002, 1970-2002 and 1972-2002 respectively. The empirical results showed a percentage increase in public spending which raised the real GDP by 1.26 percent in Morocco, 1.15 percent in Tunisia and 0.56 percent in Egypt. The results also indicated existence of long-run relationships for all the three countries.

Chowdhury (1 986), applied the Ordinary Least Square (OLS) technique on the St. Louis equation to test the impacts of fiscal and monetary policies on economic activities in Bangladesh. The result indicated that fiscal policy actions exert greater influence on economic activities than monetary policy actions. Kaur and Kaur (2008), investigated the effectiveness of monetary and fiscal policies in India. Annual data for the period 1980-2005 were used. The period covered by the study was divided into two sub-periods, namely 1980-1991 for pre-reform period and 1992-2005 for post-reform period. Utilizing the Vector Autoregressive (VAR) Model and Granger causality test, the findings show that fiscal policy were more effective in the pre-reform period, while monetary policy was more effective in the post-reform period.

The study of Mutuku and Koech (2014), tested the efficacy of fiscal versus monetary policies in influencing economic growth in Kenya, using (VAR). The results show that fiscal policy has significant

positive impact on output growth while the impact of monetary policy is insignificant. Gregonou and Ghosh (2007), studied the impact of government expenditure on growth. The study adopted panel data and discovered that countries with large-government expenditure in term of budgetary provision tend to experience higher economic growth, but the effect varies from one country to another.

Abdullah (2000), in his study on “The relationship between government expenditure and economic growth in Saudi Arabia” discovered that the size of government is an important determinant of the performance of the economy. Therefore, he concluded that government should increase its spending on infrastructure, social and economic activities as well as encourage and support the private sector to accelerate economic growth. Foster and Heniekson (2000), examined the growth effects of government expenditure and taxation in rich countries, using different econometric approaches confirmed that more meaningful results were generated.

Similarly, Liu Chin, Hsu, and Younis (2008), examined the causal relationship between GDP and public expenditure for the United States between 1947 and 2002. The result revealed that total government expenditure caused growth of GDP while growth of GDP does not cause expansion of government expenditure. Thus, relying on the causality test, they concluded that Keynesian hypothesis has more influence compared to Wagner’s law. Wagner’s law of increasing state activity explained the growth of the share of public expenditure in Gross National Product (GNP). It divided government expenditure into three categories and stressed that as per capita income increases, the relative size of the public sector will grow. Economic growth was also investigated by Ogiogio (1995). In his study, Government Expenditure and Economic Growth in Nigeria 1980-1995 showed a long-term relationship between government expenditure and economic growth. He equally found that recurrent expenditure has more influence than capital expenditure on the Gross Domestic Product.

Audu (2012) examined the causal relationship between fiscal policy measure and economic growth in Nigeria. The fiscal policy measure applied were fiscal deficit. The study applied cointegration and error correction mechanism on annual time series data for the period 1970 to 2010. It revealed a significant causal relationship between fiscal deficits and economic growth.

Osuala and Jones (2014), similarly investigated the impact of fiscal policy on economic growth in Nigeria. They applied ADF unit root test, multivariable cointegration test and error correction modeling on annual time series data from 1986 to 2010. The findings indicated that government recurrent and

capital expenditures have significant and positive relationship on economic growth whereas, non-oil taxes and government total debts have no significant impact on real GDP proxied for economic growth.

Ekpo (1994), studied the contributions of public expenditure to economic growth in Nigeria over the periods 1960-1992. The findings from the study provided support for fiscal policy - led growth through crowd-in private investment resulting from government expenditure on infrastructure.

Nurudeen and Usman (2010), analyzed the impact of government expenditure on economic growth in Nigeria over the period 1970-2008. The findings revealed that government expenditures on health, transport and communication are growth enhancing. On the other hand, Oyinlola (1993), investigated the impact of budgetary expenditure on the defense sector and economic development of Nigeria and discovered that defense expenditure extent significance positive influence on economic growth. Babalola and Aminu (2011), in their study of fiscal policy and economic growth relationship in Nigeria (1977-2009) using the Engle-Grauer approach to co-integration test, stated that productive expenditure was found to be statistically significant.

Conversely, the study of Appah (2010), on the relationship between fiscal policy and economic growth in Nigeria (1991-2005) using multiple regression analysis, adopted gross domestic product as proxy for economic growth and tax revenue, government debt, government recurrent expenditure, government capital expenditure, government recurrent expenditure budget and government capital expenditure budget as the explanatory variables, he argued that significant relationship exist between fiscal policy variables jointly and economic growth. It finds that the specific variables contributing to the GDP are government recurrent and capital expenditures.

Medee and Nendee (2011), in their study on econometric analysis of the impact of fiscal variables on Nigeria’s economic growth (1970-2009). The study used gross domestic product as the dependent variable and federal government expenditure, federal government revenue, inflation rate and capital inflow as the regressors. It adopted arcane method of vector auto-regression and error correction mechanism techniques. He argued that there exists long run equilibrium relationship between fiscal policy variables and economic growth in Nigeria.

Adeniyi and Bashir (2011), found that government spending on agriculture, education, defense, and internal security services as well as structural adjustment programme are significant factors that influence economic growth in Nigeria.

Usman *et al.*, (2011), investigated the effect of federal government expenditure on economic growth in Nigeria by specifying an augmented Solow model in Cobb- Douglas form with public capital as one of the factors. Results of the regression show that in the short-run, public spending has no impact on growth. However, cointegration and VEC results show that there is long run relationship between public expenditure and growth.

METHODOLOGY

Nature and Sources of Data

The data used for this study were of secondary sources and include information obtained from the CBN Annual Statistical Bulletin, CBN Annual reports and Financial Statements, specifically, for the period 1981-2018.

Data Estimation Technique

Preliminary tests such as Philips-Perron (pp) unit root test, Johansen cointegration and error correction mechanism were carried out. Ordinary Least Square (OLS) that is Multiple Regression Analysis was used for the model estimation. R² adjusted R² F-test and Durbin Watson (DW) test were also carried out to facilitate the analyses and the estimation process of the study.

Model Specification and Operational Definition

This study specification was as follows:

$$RGDP = f(GREX, GCEX, GTR, INFL) \quad (1)$$

Equation (1) is therefore expressed in the explicit linear-long specification as

$$RGDP = a_0 + a_1GREX + a_2GCEX + a_3GTR + a_4INFL + U \quad (2)$$

Where, RGDP = Real Gross Domestic Product (proxy for economic growth)

GREX = Federal Government Recurrent Expenditure

GCEX = Federal Government Capital Expenditure

GTR = Federal Government Tax Revenue

INFL = Inflation rate (used as check or control variable)

a₀ = constant

a₁ – a₄ = coefficient of the variables

U = error term

Variables in the Model

Dependent Variable

Real Gross Domestic Product (RGDP) is the proxy for measuring economic growth. This is a dependent variable in our equation (1). It is the monetary value of the final output of goods and services produced within the country each year.

Independent variables

GREX = Federal Government Recurrent Expenditure: This is the total amount budgeted in a fiscal year for all payments other than capital expenses.

GCEX = Federal Government Capital Expenditure: This refers to all money budgeted each year for spending on the procurement maintenance or improvement of Fixed Assets of governments.

GTR = Federal Government Tax Revenue refers to all revenue accrue to the country from all sources or type of taxation for the year.

INFL = Inflation rate: This is the rate of increase in the cost of goods and services or the measure of increase in the cost of goods and services within a given period.

Presentation of Results and Discussion of Findings

Units Root Test Results

Using Phillips-Perron (pp) unit root test, we obtain and present the result as follows:

Table 1: Phillips-Perron Unit Test Result

Variables	Level critical value at 5% = - 3.544	1 st Difference Critical value at 5% = - 3.548	Order of Integration
RGDP	-1.576	-12.588	I(1)
GREX	-0.531	-7.680	I(1)
GCEX	-2.415	-7.464	I(1)
GTR	-2.099	-5.529	I(1)
INFL	-3.066	-12.316	I(1)

Source: Authors Computation, 2020

The results show integration at order one, 5% level of significance for all the variables adopted in this study.

Johansen Cointegration Test Results

The Johansen cointegration test results are presented below. The trace statistic and the maximum Eigen statistic are used in interpreting the results at 0.05 level of significance.

Table 2: Johansen Cointegration Test Results

Hypothesized CE(s)	No. of	EIGEN VALUE	Trace Statistic	0.05 value	Critical	Prob. **
None *		0.550792	63.93592	47.85613		0.0008
At most 1*		0.517584	36.72676	29.79707		0.0068
At most 2		0.185286	11.94247	15.49471		0.1597
At most 3*		0.136128	4.975248	3.841466		0.0257
Hypothesized CE(s)	No. of	Eigen value	Max-Eigen	0.05		Prob.**
None		0.550792	Statistic	Critical Value		0.0558
At most 1*		0.517584	27.20917	27.58434		0.0146
At most 2		0.185286	24.78428	21.13162		0.4930
At most 3*		0.136128	6.967226	14.26460		0.0257

Source: Author’s Computation, 2020

* Rejection of the hypothesis at 0.05 level

** MacKinnon-Haug-Michelis (19999) p-values

Trace statistics indicates three (3) cointegrating equations at 0.05 level of significance

Max-Eigen statistic indicates two (2) cointegrating equations at 0.05 level of significance.

* denotes rejection of the hypothesis at the 0.05 level

From the Johansen cointegration results in table 2, the trace statistic indicated three (3) cointegrating equations while the Max-Eigen statistic

indicated two (2) co-integrating equations. Hence, there exist a long-run equilibrium relationship among the variables.

Table 3: Result of Maximum Lag Criteria Test

VAR Lag Order Selection Criteria

Endogenous variables: LOG(GREX) LOG(GCEX) LOG(GTR) INFL

Exogenous variables: C

Date: 07/3/2020 Time: 10:46

Sample: 136

Included observations: 32

Lag	LogL	LR	FPE	AIC	SC
0	-228.8331	NA	24.54829	14.55207	14.73529
1	-126.6883	172.3693	0.113817	9.168021	10.08411*
2	-108.6668	25.90599	0.105661	9.041674	10.69063
3	-83.66979	29.68393	0.069027	8.479362	10.86118
4	-48.63834	32.84199*	0.027973*	7.289896*	10.40459

* indicates lag order selected by the criterion

LR: Sequential modified LR test statistic (each test at 5% level)

FPE: Final prediction error

AIC: Akaike information criterion

SC: Schwarz information criterion

HQ: Hannan-Quinn information criterion

Source: Author’s Computation, 2020

From Table 3, the maximum lag is 4. So, in running the VECM we do not exceed lag 4. Following from Max lag criteria a VECM is run with 3 lags and result is shown in the appendix.

From the ECM results, the ECM variable turned up with the expected negative and fractionality condition and is statistically significant with a coefficient of 0.917346. Therefore, 92% change in the real gross domestic product is adjusted with one year. Also, the adjusted R2 of 0.98 indicates that about 98% of the change in RGDP, is accounted for by changes in

lags of RGDP, GREX, GCEX, and INFL. The Dubin Watson statistics is 1.9 which approximately equal to 2, indicates absence of autocorrelation. The model is therefore adjudged to be a good fit suitable for prediction and policy evaluation.

The 3 lags Real Gross Domestic Product (RGDP) are statistically significant implying that the previous year’s growth helps in determining the current year growth. Consequently, government recurrent expenditure influenced current Real Gross Domestic Product up to 2 lags and the influence is negative.

Similarly, government capital expenditure negatively influenced economic growth up to three years behind and government tax followed same pattern but stopped at 2 years behind. Inflation though with the proper negative sign, do not significantly influence economic growth within the period under investigation.

DISCUSSION OF RESULTS

Our observation in the result is the negative trend in growth. This we interpreted as reduction in growth which captured the phenomenon of recession which was experienced in the country during the span of the study. It is not surprising therefore, that the government recurrent expenditure negates growth in this period, this is given the high rate of unemployment and non-payment or delayed salaries of workers. Consumption was seen to have contracted which led to low productivity, hence negative growth. It also follows that tax revenue dropped on view of low productivity and output. This ultimately reduces the overall revenue of the country during this period. This however agrees with the findings of Medee and Nendee (2011). This phenomenon ultimately attracted low incentive for manufacturers and adversely also affected consumption which consequently retarded growth. The findings of Appah (2010), agrees with this economic position which this study reveal. In respect of capital expenditure, we observed that three years' gestation period within which the investment incubates do not contribute to growth in the economy. This is our experiences as government projects are hardly completed but continue to draw heavily from yearly budgets without visible contributions. However, inflation remained statistically insignificant in this study.

CONCLUSION AND RECOMMENDATIONS

Stemming from the results and analysis, the following conclusion were reached. Government recurrent expenditure impacted negatively on the economic growth in Nigeria within the period covered by this study. Government capital expenditure is significantly related to economic growth in Nigeria. Government tax revenue has significant positive relationship with economic growth in Nigeria. Despite the foregoing, as the study determines, inflation is negatively and insignificantly related to economic growth in Nigeria during the span of this study. In consequent thereof, we therefore make the following recommendations.

1. Government should make concerted effort to support the growth of the small and medium enterprises for productivity through tax holidays and other tax incentives. This enhance their capacity and afford them greater mobilization funds.

2. There should be proper implementation and adherence to national Budget. Non- budgetary implementation hinders growth and economic stability. Therefore, budget discipline must be encouraged in meaningful and appreciable progress must be made in our economic growth
3. Capital expenditure must be given a boom to shore up the quality of our infrastructure for greater productivity and sustenance.
4. There should be transparency in the management of our resources especially the capital components to shore up investor's confidence.

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