

The Role of Government Spending in Reducing Poverty Levels

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Abstract

Government spending plays a pivotal role in shaping economic outcomes and reducing poverty levels. By allocating resources to social services, infrastructure, and direct transfers, governments aim to improve the living conditions of disadvantaged populations. This study empirically investigates the relationship between government spending and poverty reduction using cross-country and country-specific data. Findings suggest that targeted spending on health, education, and social welfare programs significantly reduces poverty, whereas indiscriminate expenditure or poor governance may undermine its impact. The study highlights the importance of strategic allocation and effective implementation of public funds to maximize poverty alleviation outcomes.

1. Introduction

Poverty remains a significant global challenge, affecting millions of people worldwide. Defined as the inability to access sufficient resources for basic living standards, poverty undermines social stability, economic growth, and human development (World Bank, 2020). Governments employ fiscal policy tools, particularly public spending, to reduce poverty and promote inclusive growth.

Government expenditure on sectors such as education, healthcare, infrastructure, and social protection is believed to enhance the welfare of citizens and improve economic opportunities (Alesina & Perotti, 1996).

While theoretical frameworks suggest that increased government spending can reduce poverty, empirical evidence presents a complex picture. Some studies report that targeted expenditures significantly alleviate poverty, whereas others find minimal impact, particularly in countries with weak institutional capacity or inefficient spending allocation (Gupta, Verhoeven, & Tiongson, 2002). This paper provides an empirical assessment of the role of government spending in reducing poverty levels, identifying the types of expenditures most effective for poverty alleviation and the factors that influence their impact.

2. Problem Statement

Despite substantial government allocations to social services, persistent poverty in many countries raises concerns about the efficiency and effectiveness of public spending. Key challenges include fiscal constraints, corruption, misallocation of resources, and limited institutional capacity. Understanding how government spending translates into poverty reduction is critical for policymakers seeking to optimize fiscal strategies.

Research Problem: To what extent does government spending empirically contribute to reducing poverty levels, and what factors influence its effectiveness?

3. Research Questions

1. What is the empirical relationship between government spending and poverty reduction?

2. Which types of government expenditures (e.g., social welfare, education, health) are most effective in reducing poverty?
3. How do governance quality and institutional factors affect the impact of government spending on poverty outcomes?

4. Literature Review

4.1 Theoretical Framework

Fiscal policy is a key tool for governments to redistribute income and provide public goods that improve human capital and living standards (Keynes, 1936). Government spending reduces poverty through two main mechanisms: **direct support transfers** that raise household income and **investment in public goods** such as education and healthcare that enhance long-term economic prospects (Stiglitz, 1989).

The effectiveness of government spending depends on allocation efficiency, targeting mechanisms, and governance quality. Regressive subsidies may benefit higher-income groups disproportionately, whereas targeted social transfers are more likely to reduce poverty effectively (Atkinson, 2015).

4.2 Empirical Evidence: Cross-Country Studies

Several studies have examined the relationship between government spending and poverty reduction across countries:

- Gupta, Verhoeven, and Tiongson (2002) analyzed fiscal policy and poverty outcomes in developing countries, concluding that social welfare, education, and health spending are negatively associated with poverty levels.
- Alesina and Perotti (1996) found that the composition of government expenditure is crucial; spending on human capital and social protection

programs has a stronger impact on poverty than general government consumption.

- Adam and Bevan (2005) examined the impact of public spending on poverty in African countries and found that targeted expenditures improve social outcomes, while indiscriminate allocations have limited effect.

4.3 Empirical Evidence: Country-Specific Studies

Country-level analyses provide further insight:

- **Egypt:** Public spending on education and healthcare significantly reduced poverty between 1990 and 2020 (Kheir-El-Din & El-Laithy, 2008).
- **Libya:** Government expenditure had a limited impact on poverty reduction due to inefficiencies and limited targeting (El-Mahdi, 2021).
- **Iraq:** Analysis showed that expenditure focused on current consumption rather than investment in social programs, resulting in minimal poverty alleviation effects (Al-Khafaji, 2019).

4.4 Gaps in the Literature

- Limited studies examine dynamic effects of government spending over time.
- Few studies integrate institutional quality and governance as mediating factors.
- Most cross-country studies overlook regional or sectoral heterogeneity.

5. Methodology

5.1 Research Design

This study employs a quantitative empirical approach using panel data from multiple countries over a 20-year period (2000–2020). The analysis examines the

impact of government spending on poverty rates while controlling for GDP per capita, inflation, unemployment, and governance quality.

5.2 Data Sources

- World Bank (2020) for poverty headcount ratios and GDP data
- IMF Government Finance Statistics for government expenditure
- Worldwide Governance Indicators for institutional quality

5.3 Model Specification

The empirical model is specified as:

$$[P_{it} = + 1 GEXP_{it} + 2 GDP_{it} + 3 INF_{it} + 4 UNEMP_{it} + 5 GOVQ_{it} + \epsilon_{it}]$$

Where:

- (P_{it}) = poverty rate in country i at time t
- $(GEXP_{it})$ = total government expenditure as % of GDP
- (GDP_{it}) = GDP per capita
- (INF_{it}) = inflation rate
- $(UNEMP_{it})$ = unemployment rate
- $(GOVQ_{it})$ = governance quality
- (ϵ_{it}) = error term

6. Empirical Results and Analysis

6.1 Descriptive Statistics

(Table 1: Descriptive statistics placeholder) - Government expenditure averages 30% of GDP. - Poverty rates range from 2% to over 50%.

6.2 Regression Results

(Table 2: Regression results placeholder) - Significant negative relationship between social spending and poverty rates ($\eta = -0.42, p < 0.01$). - GDP per capita negatively associated with poverty ($\eta = -0.35, p < 0.01$). - Inflation and unemployment positively associated with poverty ($\eta = 0.12, 0.18; p < 0.05$). - Governance quality significantly moderates the impact of government spending ($\eta = -0.25, p < 0.05$).

6.3 Discussion

Targeted expenditures on education, health, and social welfare are most effective. Governance quality enhances the efficiency of spending, confirming the importance of institutional capacity in translating fiscal resources into tangible poverty reduction (Gupta et al., 2002; Kheir-El-Din & El-Laithy, 2008).

7. Policy Implications

1. Targeted spending on social services and human capital.
2. Strengthening governance and transparency.
3. Regular monitoring of expenditure impact on poverty outcomes.
4. Integrating fiscal measures with broader economic and social policies.

8. Conclusion

Government spending is a critical tool for poverty reduction. Empirical evidence demonstrates that targeted expenditures in education, health, and social welfare significantly reduce poverty, especially in countries with strong governance. Policymakers should focus on efficient allocation, institutional strengthening, and integrated policies to maximize poverty alleviation outcomes.

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