International Journal of Business & Law Research 7(1):25-33, Jan.-Mar., 2019

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Government Expenditure and Unemployment: Examination of the Nigerian Evidence

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ABSTRACT
This study empirically examined the causal relationship between government expenditure and unemployment from 1981 to 2017. Data used was secondary and obtained from Central Bank of Nigeria (CBN) Statistical Bulletin of various years and other reports. Unemployment rate was the dependent variable. Government expenditure was decomposed into recurrent and capital expenditure (independent variables). Unit root test indicates the variables were integrated in order (I). Cointegration test results indicate a long-run equilibrium relationship between unemployment rate (UEMR), recurrent expenditure (REXR) and capital expenditure (CEXR). There is negative and significant relationship between unemployment rate (UEMR) and recurrent expenditure (REXR). The negative relationship agrees with a priori expectations. On the other hand, relationship between unemployment rate (UNER) and capital expenditure (CEXR) is positive and significant. However, the positive relationship is contrary to our a priori expectation. This means that a change in government expenditure will impact unemployment rate. Increased government capital expenditure results in increased unemployment rate instead of a decrease. There is no causal relationship amongst all the variables of interest. As measures to reverse the above trend and reduce unemployment using government expenditure and borrowing as instruments, there should be re-allocation of capital expenditure so as to enhance employment opportunities for unemployed people. Increase in our capital expenditure should be channeled towards productive sectors, not to "luxuries" as depicted in the construction of houses and banquet halls.
Keywords: Cointegration, capital, recurrent expenditure, unemployment, Granger Causality.

INTRODUCTION
Over the years, the World Bank and the International Monetary Fund (IMF) have been embroiled in the development-policy controversy on the use of fiscal policy not only for economic stabilization but also the promotion of economic growth and increase in per capita income. At issue here is the effect of the components of government expenditure (such as capital and recurrent) on economic growth. Some authors have argued that spending on growth-stimulating activities would enhance future revenue and justify the provision of fiscal space in the budget. However, it appears that there are no simple ways to identify the growth-maximizing composition of government expenditure. The World Bank (2006, 2007) was of the opinion in two policy reports that governments in designing fiscal policy should seek to ensure macroeconomic stability as well as promote economic growth of a country. These are not new policy thrusts in economic and finance theory by any chance, but what is worthy of note is the re-emergence of interest and emphasis on the use of fiscal policy and no longer monetary policy of the IMF school. More specifically, the growth impact of the composition of public expenditure has been elevated as an important aspect of the design of fiscal policy. Many countries have in recent times pursued a policy of

inflation targeting, while others have full employment of resources as a cardinal economic objective that drives their policy constructs. Others yet have economic growth as their overriding objective. A complete study should examine the influence of the nominated fiscal policy variables because GDP is not the only indicator of performance of the economy. Thus, the real effect of the fiscal policy variable on the economy can further be investigated against unemployment as the relevant explained variable and not only GDP, which most studies have utilized in their analyses.

Unemployment is a situation in which an individual in an economy is looking for job and cannot find one. According to International Labour Organization (ILO) (2012), some scholars have argued that increase in government spending can be an effective tool to reduce unemployment rate. Also following the Keynesian view, government could reverse economic downturns by borrowing money from the private sector and then returning it through various spending programs. High levels of government consumption are likely to increase employment, profitability and investment via multiplier effects on aggregate demand. Thus, government expenditure, even of a recurrent nature, can contribute positively to the reduction of unemployment. John Maynard Keynes, probably the most influential economist of the 20th century, developed a theory that provided both an explanation for the prolonged unemployment of the 1930s and a recipe on how to generate recovery. His analysis indicated that fiscal policy could be used to maintain a high level of output and employment. According to the Keynesian theory, all fiscal measures that accelerate the pace of economic growth promote employment also. In line with this theory, most economists, especially macroeconomists, would agree that expansionary fiscal policy stimulates employment and lowers unemployment. The above theory is not true in Nigeria.

The Nigerian economy presents some peculiar dynamics that are worrisome. First, since independence, Nigeria's fiscal policy objectives have included, among other things, availability of funds for financing economic development, the maximum flow of material resources consistent with minimum consumption requirements, minimizing inequalities in wealth, income and consumption standards, generation of employment and encouraging domestic production. Yet, it is unclear the exact relationship between rising government expenditure and social economic indicators like unemployment. Second, available data shows that unemployment has maintained a rising trend over the years from 4.1% in 1981 to 5.3% in 1983; 7.0% in 1987 to 13.1% in year 2000; 13.6% in 2001 to 14.9% in 2008; 19.7% in 2009 to 24.7% in 2013, but surprisingly, Nigeria's GDP has been increasing, with an average growth rate of 6.4 percent between 2000 and 2014. This paradoxical situation has led to a flurry of studies and postulations aimed at providing explanation and solution to the phenomenon. The growth of government expenditure over the years has been geometrical to say the least while employment cannot be said to be growing commensurately. Fiscal policy has been very effective in general economic growth of the GDP, but, very ineffective in some other areas like employment generation. If output had been growing as desired, the incidences of run-away inflationary pressures or unemployment noticeable in certain years would not have occurred going by the postulations of theory. That growth is generally below the desires and expectations of the people only testifies that the employment of resources - human, monetary and material - is far below capacity. In the face of these startling realities, the big question begging for an answer is: why is unemployment increasing despite increase in government expenditure and public borrowing (debt)? We cannot say in good conscience that the huge amounts of money which the government claims to have pumped into the economy have produced the desired results. Thus, it becomes imperative to make proper analysis of the actual impact of government expenditure on the nominated macroeconomic objectives of the country. Although, empirical literature on this issue have produced inconclusive results (Holden and Sparrman, 2013), the issue is even more worrisome as previous indigenous studies have paid little or no attention to this issue. Most of the indigenous studies on government spending has focused on government spending-economic growth nexus (Uma et al, 2013; Onakoya and Somoye, 2013; Bakare; Taiwo and Agbatogun, 2012). Not many of the relevant studies, to the best of the author's knowledge, covered the impact of government spending on employment/unemployment; none of these studies addressed the causality question as many devoted their attention to ordinary relational effects. More so, even the existing studies have largely been based on the experiences of developed countries. The experiences of developing countries like Nigeria are yet to be fully documented. Therefore, the

examination of this issue has become imperative because, increasing unemployment rate can have significant negative social and economic consequences, like making reforms difficult, constraining economic growth, undermining social cohesion and stability, derailing various ongoing policy reforms (Lin et al., 2008) or even undermining the country's long term desire of achieving improved national development. Thus, without utmost and urgent attention to this issue, it is doubtful how the Nigerian government hopes to attain the country's goal of becoming one of the top 20 economies by year 2020.

Recognizing this obvious research gap, the authors set out to make a contribution to the body of existing literature by empirically examining the causal relationship between government expenditure variables (measured by capital and recurrent expenditure) and the employment of human resources in Nigeria (measured by unemployment rate). For ease of analyses and presentation the rest of the study is organized as follows: Following this introduction is section two which reviews related literature and theoretical framework. Section three is the research methodology adopted for this study. In section four is data analyses and interpretation of empirical results. Conclusion and policy recommendations are in section five.

SECTION 2: LITERATURE REVIEW/THEORETICAL FRAMEWORK

2.1: The Keynesian model of employment determination

In the Keynesian model, aggregate employment depends on the level of aggregate demand in the country as a whole. When total spending is low, employers tend to produce a great deal because they do not want to end up with unsold goods. If production is low, they will not need many workers. If few workers are hired then aggregate income will be low which can become a vicious cycle. Keynes focus was on aggregate demand in the economy and on business expectations about future profitability. He believed that even if wages did not fall quickly in a number of labour markets, this might do more harm than good. If they do not buy as much, this reduces demands for the goods being produced by business all over the economy. If business cannot sell their goods, they will tend to cut back on their investments and on the number of workers they employ. Prices as well as wages may fall. Low aggregate demand for goods and services could lead to a vicious cycle of unemployment, low incomes, and low spending in the economy as a whole. He said that rather than blaming unemployment on "the wage being too high", aggregate demand in the economy has to be increased in other to stimulate living.

2.2: Unemployment in the Theory of Innovations

This theory provided several ways by which the entrepreneur can make profits in order to reduce unemployment. According to Mohammed (2010), those ways are:

1. Finding particular markets,
2. Acquisition of productive agents,
3. Skillful combination of factors of production,
4. Successful sales policy, and
5. Innovations.

He supported the proposition that entrepreneurial profits will increase employment. He said that innovation which creates more jobs relative to job destruction is a basic force beyond the increase in employment and the decreases in unemployment. When entrepreneurs innovate something new such as new products, a new market, a new method of production, new technology or a new organization, they increase investments to materialize those innovations. Domestic investment expenditures will increase demand on the economic resources and will increase their prices. Other entrepreneurs will imitate the leaders by adopting the new innovations. Labour and materials will be employed to produce new items. Consequently, wages will be increasing and unemployment will be declining, assuming that employment creation will outweigh employment destruction due to the new innovations. He concluded that economically unemployment represents a loss in the Gross Domestic product (GDP).

2.3: Empirical review

Mayer, Moyen and Stahlar (2010) studied Government expenditure and unemployment in 2010. They investigated the unemployment rate after a government expenditure shock. They argued that it is an important objective of fiscal policy to cushion the labour market and in particular, the unemployment rate

from adverse business cycle effects. This objective prevailed especially in the aftermath of the current financial and economic depression when government Organization of Economic Co-operation and Development countries expanded structural deficits on average from – 2.3 percent in 2007 to a projected value of – 6.7 percent in 2010 in order to prevent economic activity and labour markets from imploding. Their analysis highlights the forces that shape the interaction between labour supply and labour demand following a fiscal policy shock. They revealed in particular that i) highly sticky prices, ii) high degrees of risk aversion, iii) low degree of 50 convexity in utility of labour, iv) high replacement rates, and v) debt – financed expenditures increase the fiscal unemployment multiplier.

In 2013, the effect of government purchases on unemployment was examined by Holden and Sparrman in 20 OECD countries from 1980 to 2007. The study observed that an increase in government purchases equals one percent of Gross Domestic Product and reduced unemployment by about 3 percentage points in the same year. The effect was observed to be greater in down turns than in booms, and also greater under a fixed exchange rate regime than a floating regime.

Adawo et al (2013) examined issues relating to high unemployment rate in Nigeria. The study observed that labour force in Nigeria grew at more or less a steady rate of 3% yearly while gross domestic product (GDP) growth rate grew at 3.5% over a period of 33 years, suggesting a jobless growth. The study also noted that the causes of unemployment in Nigeria include‟ poor infrastructure; non-diversification of the economy; insecurity; and poor educational system that does not readily produce employable graduates. The study recommended that government at all levels should partner with the private sector and diversify the economy in order to create jobs.

SECTION 3: DATA AND METHODOLOGY

Econometric modeling that gave rise to estimable equations is used to examine the relationship between the variables identified in this study. Estimation was done following the Ordinary Least Square Method (OLS) while the Eviews 9 software was used. Analyses include global that reveals the overall utility of the models, Unit root test, Johansen Multivariate Cointegration Technique and Granger Causality test were also employed.

3.1: Model Specification

The model is specified as follows:

The functional form on which the model is based is given as:

$Y = f(X_1, X_2)$ …….. (1)

This can be specifically expressed as:

UEMR $= f$ (CEXR, REXR)…. ……. (2)

Expressing equation (2) in its mathematical form, we have:

$UEMR = \beta_0 + \beta_1 (CEXR_t) + \beta_2 (REXR_t)$ …… (3)

Expressing equation (3) in its econometric form, we have:

$UMER = \beta_0 + \beta_1 (CEXR_t) + \beta_2 (REXR_t) + \mu_t$ ..... (4)

A priori expectation

$\beta_1, \beta_2 < 0$

Where:

UEMR = Unemployment Rate

CEXR = Capital Expenditure growth rate

REXR = Recurrent Expenditure growth rate

β_0 = constant variable in the model.

β_1 = parameter of Capital Expenditure (CEXR)

β_2 = parameter of Recurrent Expenditure (REXR)

μ_t = error term

$_t$ = time series data

Looking at the above equations, it is easy to see that not all the variables are on the same base. Some are in naira (capital and recurrent expenditure) while others are in rates (Unemployment). In this study, the entire variables shall be casted into rates of growth over the period of the study to achieve a uniform data

base. Thus, we use the growth rate of capital expenditure or CEXR, and growth rate of recurrent expenditure or REXR. The use of uniform rates of change or growth rates will help reduce or eliminate obvious econometric problems.

3.2: Unit Root Test

Examining the stationary properties of the variables is important because if two or more variables in a regression model are not stationary, then the standard errors produced by the regression estimate would be biased, making the conventional principle used in evaluating the existence of relationship among the variables in the model unreliable (Mahadeva and Robinson, 2004). The properties of the variables in equation are examined employing the Augmented Dickey-Fuller (ADF) (1981) and Philips-Perrron (PP) unit root tests to determine the stationary status of the time series data.

3.3: Johansen Multivariate Cointegration Technique

The first step we employed was to check the stationarity status of the variables using unit root tests namely Augmented Dickey–Fuller (ADF) and Phillips-Peron (PP) test statistics. These are then followed by the Johansen multivariate cointegration Test (Trace and Maximum Eigenvalue) after the order of linear deterministic trend in order to determine the long run effects

3.4: Granger Causality Test

Next, the study used the Pairwise Granger Causality test of the Granger procedure to determine the causal effects. The causality tests follow Granger (1969) and Granger and Newbold (1979) formulation and was examined based on the expression

$$H_t = \sum_{j=1}^{m} a_j H_{t-j} + \sum_{j=1}^{m} \beta_j P_{t-j} + U_1 \quad \text{..... (Eq. 3.1)}$$

The causality model above regresses a variable, H, on lagged values of itself and another variable P. If P is significant, it means that it explains some of the variance in H that is not explained by lagged values of H itself. This indicates that P is causally prior to H and is said to dynamically cause or Granger cause P. With Equation 3.2 above, the paper determines if money causes output or vice versa; and if government expenditure causes unemployment or the other way round. Also, the possibility of dual causation was also examined.

3.5: Summary

This section has laid out the procedures and tools by which the study is undertaken and analyses made. The emphasis was basically finametric methods applied to macroeconomic phenomena.

SECTION 4: ANALYSES OF ESTIMATION RESULTS

4.1: Relationship between Unemployment rate (UEMR) and Government Expenditure

Stationarity Analysis between UEMR, CEXR and REXR

The relationships between unemployment rate (UEMR) and the public expenditure variables (CEXR and REXR) are estimated starting with the series unit root tests namely Augmented Dickey-Fuller (ADF) test statistics. These are followed by the Unrestricted Cointegration Rank Tests (Trace and Maximum Eigenvalue) after the order of linear deterministic trend in order to determine the long run effects. The next were the study used the Generalized Method of Moments method to estimate the short-run effects. Finally the Pairwise Granger Causality Tests of the Granger procedure to determine the causal effects. The results of these procedures are summarized on Tables 4.1 through 4.3 respectively.

Table 4.1: ADF Unit root test Results

VARIABLES	1st difference 5% critical val.	T-statistics	Order of Integration
CEXR	-2.951125	-9.349392	I (I)
REXR	-2.954021	-6.246251	I (I)
UEMR	-2.948404	-5.880565	I (I)

Source: Authors compilation from EVIEWS 9. Results

The result from the table 4.1 above indicates that all the three variables in the model capital expenditure (CEXR), Recurrent expenditure (REXR), the independent variables and unemployment rate (UEMR) the dependent variable were all stationary at 1st differences using the Augmented Dickey-Fuller (ADF) test at 5% level of significance.

Cointegration between UEMR, CEXR and REXR

The analysis was pushed further to ascertain whether the variables are co-integrated or not. Thus, the study employed the Unrestricted Cointegration Rank Tests (Trace and Maximum Eigenvalue) after the order of linear deterministic trend. The results of which are on Table 4.2a and 4.2b respectively

Co-integration test

Given that the variables are integrated of order one, this study proceeds to examine the presence of co-integration among the variables. Thus, the unrestricted Cointegration Rank tests (Trace and Maximum Eigenvalue) after the order of linear deterministic trend. This technique is utilized because the specified model is multi-variate and also there exists the possibility of having more than one co-integrating vector.

Table 4.2a Unrestricted Cointegration Rank Test (Trace):

Series: UEMR, CEXR and REXR Trend assumption: Linear deterministic trend

Date: 01/10/19 Time: 12:44
Sample (adjusted): 3 37
Included observations: 35 after adjustments
Trend assumption: Linear deterministic trend
Series: UEMR CEXR REXR
Lags interval (in first differences): 1 to 1

Unrestricted Cointegration Rank Test (Trace)

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.466686	38.09953	29.79707	0.0044
At most 1 *	0.349129	16.09697	15.49471	0.0406
At most 2	0.030009	1.066407	3.841466	0.3018

Trace test indicates 2 cointegrating eqn(s) at the 0.05 level
* denotes rejection of the hypothesis at the 0.05 level
**MacKinnon-Haug-Michelis (1999) p-values

Source: EVIEWS 9 Printout.

Table 4.2b: Unrestricted cointegration rank test (Maximum Eigenvalue)
Series: UEMR, CEXR and REXR. Trend Assumption: Linear Deterministic trend

Unrestricted Cointegration Rank Test (Maximum Eigenvalue)

Hypothesized No. of CE(s)	Eigenvalue	Max-Eigen Statistic	0.05 Critical Value	Prob.**
None *	0.466686	22.00256	21.13162	0.0376
At most 1 *	0.349129	15.03056	14.26460	0.0378
At most 2	0.030009	1.066407	3.841466	0.3018

Max-eigenvalue test indicates 2 cointegrating eqn(s) at the 0.05 level
* denotes rejection of the hypothesis at the 0.05 level
**MacKinnon-Haug-Michelis (1999) p-values

Source: EVIEWS 9 Printout

From Table 4.2a, it can be seen that the Trace Statistic is computed to be 38.09953 and 16.09697 while the critical value at alpha 0.05 is 29.79707 and 15.49471 respectively , which indicates a rejection of the null of no co-integrating equation. Thus the alternate hypothesis of two cointegrating equations is accepted. Equally, the Max-eigenvalue test indicates 2 cointegrating eqn(s) at the 0.05 level (statistic = 22.00256 and 15.03056; critical value = 21.13162 and 14.26460). These results indicate that there exist a sustainable long run equilibrium relationship between the UEMR and the duo of CEXR and REXR.

Relative Long run relationships between UEMR, CEXR and REXR
Table 4.3 Normalized cointegrating coefficients (standard error in parentheses)

Normalized cointegrating coefficients (standard error in parentheses)

UEMR	CEXR	REXR
1.000000	13859.64	-20915.18
	(4143.20)	(4463.12)

Source: EVIEWS 9 Printout

Table 4.3 depicts the long run cointegration equation showing the nature and magnitude of the observed long run relationships. The equation is normalized for UEMR – the dependent variable.
The normalized beta coefficient representing the long run relative statistical relationship between the UEMR and CEXR is shown to be 13859.64 and Standard error of 4143.20, suggestion a t-statistic of 3.345. This is significant at 5% level. By implication, there exist a statistically significant relationship between the UEMR and the CEXR variable. The sign implication suggests a positive relationship which disagrees with a priori expectation. On the other hand the normalized beta coefficient representing the long run relative statistical relationship between the UEMR and REXR is calculated to be -20915.18 with a standard error of 4463.12 (t-statistic = -4.686). The computed t-statistic is significant at 5% significant level. Thus the relationship between UEMR and REXR is negative as a priori expected and statistically significant at the conventional 5% level.

Causality between UEMR, CEXR and CEXR

Although regression analysis deals with the dependence of one variable on other variables, it does not necessarily imply causation or the direction of influence (Gujarati and Porter, 2009). To test the existence of causality, the study employs the Granger Causality procedure to test the direction of causality among the nominated variables of UEMR, REXR, and CEXR. The results of the pairwise Granger Causality test are summarized on Table 4.4

Table 4.4: Pairwise Granger Causality Tests

Pairwise Granger Causality Tests
Date: 01/10/19 Time: 13:30
Sample: 1 38
Lags: 2

Null Hypothesis:	Obs	F-Statistic	Prob.
REXR does not Granger Cause CEXR	35	1.15111	0.3299
CEXR does not Granger Cause REXR		1.23398	0.3055
UEMR does not Granger Cause CEXR	35	0.88458	0.4234
CEXR does not Granger Cause UEMR		0.60133	0.5546
UEMR does not Granger Cause REXR	35	0.55361	0.5806
REXR does not Granger Cause UEMR		0.01848	0.9817

Source: EVIEWS 9 PRINTOUT

It can be seen from the Table that the coefficient of the variables are not statistically significant in either of the regressions up to 11 lags. There is no causal relationship between the three variables in our model and therefore independence is suggested. Thus we do not reject the null hypothesis of no causal relationship between UEMR, CEXR and REXR.

SECTION 5: CONCLUSION AND RECOMMENDATIONS

This study empirically examined the relationship between government spending and unemployment rate from 1981 to 2017. Data used was secondary and obtained from Central Bank of Nigeria (CBN) Statistical Bulletin of various years and other reports. The study adopted econometric tools in its data analyses. Government expenditure was decomposed into recurrent and capital expenditure. Test results indicate a long-run equilibrium relationship between unemployment rate (UEMR), recurrent expenditure (REXR) and capital expenditure (CEXR). There is negative and significant relationship between unemployment rate (UEMR) and recurrent expenditure (REXR). The negative relationship agrees with a priori expectations. On the other hand, relationship between unemployment rate (UNER) and capital expenditure (CEXR) is positive and significant. There is no causal relationship between unemployment rate (UNER), recurrent and capital expenditure (CEXR).. There is a significant and positive relationship between UNER and CEXR. However, the positive relationship is contrary to our a priori expectation. This means that a change in government expenditure will impact unemployment rate. Increased government capital expenditure results in increased unemployment rate instead of a decrease. The relationship between UEMR and REXR was significant implying that government recurrent expenditure affects unemployment significantly.

Based on reviewed literature, amongst the reasons our expenditures, instead of creating employment, widen unemployment rate is that most of our expenditures are not productive- based. In addition, our expenses are not targeted; they are provided, approved and spent based on interests, mostly political than economic. As measures to reverse the above trend and reduce unemployment using government expenditure and borrowing as instruments, there should be re-allocation of capital expenditure so as to enhance employment opportunities for unemployed people. Increase in our capital expenditure should be channeled towards productive sectors, not to "luxuries" as depicted in the construction of houses and banquet halls.

A well-planned, articulated and structured policy should be put in place and financial grant provided to the unemployed. As a means of tracking progress and achievements, empirically measurable indicators and benchmarks must be developed and made an integral part of the policy. In addition, further efforts should be made by the government to encourage foreign and domestic investors to invest in the key

sectors of agriculture and manufacturing (outside petroleum) so as to help diversify the economy and increase investment and employment opportunities. There should be conscientious and deliberate move towards setting our priorities right and reducing misappropriation of fund. In other words, fiscal indiscipline on the part of the government should be curbed while a good, transparent and accountable expenditure system should be put in place

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