ISSN 2385-2755
DiSSE Working papers
[online]

SAPIENZA
UNIVERSITÀ DI ROMA

WORKING PAPERS SERIES
DIPARTIMENTO DI SCIENZE SOCIALI ED ECONOMICHE

Public spending and growth: some considerations in the light of the current economic situation

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N. 2/2025

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CF80209930587 – P.IVA 02133771002

Public spending and growth: some considerations in the light of the current economic situation

Claudio Sardoni*

February 2, 2025

Abstract

The economic phase through which many advanced market economies are currently going requires, this paper argues, economic policies which aim at raising the economy's overall productivity and, hence, its rate of growth. At the same time, the adopted policies should be such as not to undermine fiscal sustainability as expressed by at least stable public debt ratios.
Such policies can be successful if they are efficiently implemented by the state apparatus. It is not sufficient to design policies which, abstractly, are productivity-enhancing and growth-promoting; it is necessary that policy designs are accompanied by the analysis of the apparatuses responsible for their implementation along with the design of measures to ensure their efficient and effectual working.
The paper argues that dealing with these issue requires analyzing the quality and nature of the state organization as a whole. The state is a is complex organization which is functional and responding to interests that are not necessarily coincident with the general interest as expressed by higher rates of growth. Such issues, tackled by important economists, cannot, and should not, be ignored when dealing with economic policies to face the current critical phase.
JEL Classification: H10, H11, H50

*Honorary Professor of Economics, Sapienza University of Rome. This paper is an amply revised and extended version of a paper which I presented at Meiji University (Tokyo, July 31, 2024). I wish to thank Professor Takashi Yagi for inviting me and all the attendants at the seminar whose comments helped me improve my work. I wish also to thank B. Ingrao and P. Garzarelli for their suggestions and comments on a previous version of the paper.

1 Introduction

Currently most advanced market economies are experiencing a situation which is essentially characterized by low growth rates and a sluggish dynamics of productivity accompanied by high ratios of the public debt to GDP. This paper argues that such a situation requires effectual economic policies characterized by their emphasis being placed on the need to increase productivity and achieve higher growth rates without compromising the stability and sustainability of the public finances.

Further expansions of public spending to stimulate aggregate demand seem to be inadequate as well as dangerous. The already existing large public sectors and large public spending have not been capable to guarantee significant rises of productivity and growth; further increases in public spending are likely to compromise the stability and sustainability of public finance.

In a previous paper (Sardoni, 2024) I developed a basic growth model in which public spending plays an important role. Public outlays, if adequately devoted to expenditures that affect total productivity positively allow the economy to grow at rates that are sufficiently high to ensure the stability of the ratio of the public debt to GDP.

The present paper starts from these results to offer some general considerations concerning the problems of efficiency and effectiveness of policies aimed at promoting productivity and growth. It is not sufficient for economists to design and suggest such policies; it is also necessary to pay attention to the capacity and willingness of the state apparatus as a whole to actually implement them. From the analysis of the state apparatus should derive adequate policy proposals to raise its efficiency and effectiveness.

Dealing with such problems leads to considering a number of issues related to long-lasting debates on the nature and the functioning of the state in market economies. Without any pretense of exhaustiveness, these topics are dealt with by recalling the contributions of some authors who, though from different theoretical perspectives, emphasize the need for thorough analyses of the working of state apparatuses, and institutions in general, in different economic contexts and phases.

The paper is organized as follows. Section 2 briefly summarizes the main results of Sardoni (2024) and offers some further considerations concerning the possible negative effects of having high, though stable, public debt ratios. Section 3 argues that the current situation experienced by many market economies calls for policies aiming at promoting productivity and growth. Section 4 is concerned with the need for the efficient implementation of such policies. Section 5 deals the more general issue of the nature of the state in market economies and its willingness/capability to operate in the general interest as expressed by higher growth rates and sustainable public finances.

Section 6 concludes.

2 Public spending, productivity and growth

The model in Sardoni (2024) is derived from the well known Domar's growth model (Domar, 1946) and Domar's distinction between productive and unproductive public expenditures (Domar, 1944).

In Domar's model of a closed economy with no government the equilibrium growth rate (γ), which ensures the equality between aggregate demand and supply over time, is

$$\gamma = s\sigma$$

which is increasing in s (the marginal propensity to consume) and in σ which is the productivity of investment I,

$$\sigma = \frac{\dot{P}}{I}$$

($\dot{P}$ is the increase in the economy's productive capacity.)[1]

Domar's model is extended by introducing a government sector which spends on goods and services and levies taxes. Public expenditure (G) is divided into productive (I_g) and unproductive (C_g). The two types of expenditures are defined as follows:

1. productive public expenditures (also denoted *public investment* in physical and human capital) are all those expenditures that affect the economy's long-run growth rate *directly*;
2. unproductive public expenditures (also denoted *public consumption*) are all those outlays that do not have direct effects on the growth rate (Domar, 1944). In the model it is assumed that unproductice public expenditures are a share $u > 0$ of the total fiscal revenue.

The distinction between public investment and consumption does not coincide with the standard distinction between capital and current public expenditures. For example, in the present context current public expenditures on education are regarded as public investment, as they directly affect the rate of growth through their impact on productivity.

Public investment contributes directly to the growth of the economy's productive capacity, but it can affect the productive capacity also by determining a higher productivity of private investment (I_p) like, for example, in the case of investment in infrastructures or education.

[1] See Sardoni (2024) for the interpretation of the equilibrium growth rate being increasing in the propensity to save.

Thus, any increase in the total productive capacity $\dot{P}$ is determined by the productivity of private (I_p) and public investment I_g (σ_p and σ_g respectively). Global productivity σ is the weighted average of σ_g and σ_p.[2]

It is also assumed that the productivity of private investment is always larger than the productivity of public investment (I_g) and it is increasing in I_g at a decreasing rate. It is then easy to verify that, under some assumptions, total productivity σ is increasing in I_g and σ_g (see Sardoni, 2024).

Consider now the public budget constraint and its impact on the equilibrium growth rate. For brevity, only cases in which the government runs a primary deficit are examined.

At any point along the economy's equilibrium growth path, the public budget B is

$$\begin{aligned} 0 < B &= G - T = I_g + (u-1)tY \\ &= \beta Y = G - T = I_g + (u-1)tY \end{aligned} \tag{1}$$

where $0 < \beta = \frac{B}{Y} < 1$; T denotes the total tax revenue net of transfers and $0 \leq u \leq 1$ is the share of the total fiscal revenue devoted to unproductive expenditures.

From the aggregate equilibrium condition[3] and from (1) above, we obtain that along the equilibrium path, subject to some constraints, productive expenditures I_g are increasing in β.[4]

Finally, it is assumed that the share u of the fiscal revenue devoted to unproductive expenditures cannot be smaller than $\bar{u} > 0$ ($0 < \bar{u} \leq u < 1$), which amounts to assume that a certain share of the total fiscal revenue must be devoted to 'necessary' unproductive expenditures, like for example expenditures on defense, public order, etc.

By following the same procedure as in Domar (1946) and by setting $u = \bar{u}$ for simplicity, we obtain the equilibrium growth rate

$$\gamma(\beta) = [(1-t)s + t(1-\bar{u})]\sigma(\beta) \tag{2}$$

Given s, the equilibrium growth rate is increasing in σ which in turn is increasing in β under the conditions set in footnote 4.[5]

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[2] $\sigma = \frac{\sigma_g I_g + \sigma_p I_p}{I_g + I_p}$.

[3] $\dot{Y} = (1-s)(1-t)\dot{Y} + \dot{I}_p + \dot{I}_g + ut\dot{Y} = \dot{P}$.

[4] It is $I_g = \frac{I_p[\beta + t(1-u)]}{s(1-t)-\beta}$. If it is imposed that both public and private investment must be positive, it derives that it must be $0 < \beta < s(1-t)$. Within this interval I_g is increasing in β, but larger values of the public investment are associated with larger values of the productivity of total investment only if it is $I_g < I_p$. See Sardoni (2024) for the analytic determination of these constraints.

[5] Notice that $[(1-t)s + t(1-\bar{u})]$ is the equivalent of the private propensity to save s in Domar's model. It denotes the overall propensity to save.

However, the overall impact of β on the growth rate γ is ambiguous. Since β is positive, the public debt is positive and the government pays an interest on it. If the interests on the public debt are regarded as transfers to the private sector, they affect the tax rate t net of transfers.

As a consequence, if the government leaves the gross tax rate unvaried, the net rate t is decreasing in β and the interest rate on the debt (i). Therefore, the impact of a larger β on the rate of growth is ambiguous: the positive effect of a smaller t on private saving could be more than compensated for by the negative effect on $t(1-\bar{u})$ in (2) above.

Here it suffices to state that the equilibrium rate of growth in (2) is increasing in β only if its positive impact on productivity is sufficiently larger than its negative impact on the tax rate net of transfers.

Clearly, increases in β which determine a higher growth rate must derive from in increases in productive expenditures I_g. If a larger β were due to larger unproductive expenditures ($u > \bar{u}$ in equation 2) the equilibrium growth rate would be lower.

Let us now turn to consider the stability of the ratio of public debt to GDP. When the government runs a primary deficit this ratio can be stabilized if the economy grows at a rate $\gamma^* > i$ (i is the interest rate on the public debt). If we start from a situation in which $\gamma < i$ and $\beta > 0$, the public debt ratio ratio can be stabilized only if the economy grows at a rate higher than γ and the interest rate i.

In the model the growth rate can be raised thanks to:

1. a higher productivity of public investment, which also determines a higher productivity of total investment ;
2. the share of the total public expenditure devoted to necessary unproductive expenditures is smaller;[6]
3. a larger ratio β of the public deficit to GDP which, under the conditions recalled above, determines an increase in the rate of growth.

In all three cases, if the corresponding equilibrium rate of growth γ^* is larger than the interest rate i, the debt ratio converges to d^*, which is increasing in β and i and decreasing in γ^*.

$$d^* = \frac{\epsilon - t}{\gamma^* - i} = \frac{\beta}{\gamma^* - i} \tag{3}$$

(ϵ is the ratio of public spending to GDP.)

The stabilization of the public debt ratio to GDP is important. First– and most important, in a perspective which emphasizes growth–a debt ratio

[6]Notice that the value of $\bar{u}$ could be reduced by an increase of the efficiency of the government sector: a more efficient organization of the public administration could allow the provision of the same, or larger, amount of 'unproductive' services by spending less. We shall return to the efficiency of the state apparatus later on.

increasing over time denotes that the public sector is spending in the wrong way, that is to say it is wasting resources as they do not contribute to the overall growth of the economy.

Put in different terms, a growth rate lower than the interest rate on the public debt means that the social dividend (the economy's growth rate) of public spending is less than its cost (the interest rate on the public debt).

The model above shows that it is possible to achieve stable public debt ratios even at relatively high levels, but the level at which the public debt ratio is stabilized is a matter which should not be overlooked or underrated.

First, a large public debt, although associated to a stable ratio to GDP, increases the risk of speculative attacks. A conventional conviction that a the large debt puts the economy on the verge of default can be a fertile terrain for speculation, which causes a fall in bond prices and an increase in interest rates and risk premia.

This, in turn, contributes to make the debt problem even more serious as higher interest rates can rise over the growth rate and make the public debt ratio unstable and growing with the consequence that speculative attacks become even stronger.[7]

A stable but high ratio of the public debt ratio to GDP, especially if associated to a high level of the ratio of the public deficit to GDP, has another negative effect. If the interest rate on the public debt is increasing in the public deficit, given the tax rate gross of transfers the tax rate net of transfers is decreasing in the public deficit and debt, with distributional implications.

When the existence of different income and wealth groups is taken into consideration, it is rather obvious to surmise that the holding of government liabilities is unevenly distributed across the population and that the amount held by different groups of the population is increasing in each group's level of income and wealth. Thus, the flow of interests to the private sector has a regressive impact: the higher is the level of income and wealth the lower is the tax rate net of transfers.

Therefore, even though relatively high public debt ratios can be sustainable, the portion of the population which is most benefited is the same which is already better off. The regressive impact of high public debt and deficit raises issues concerning social equity and justice, but it is quite likely to be accompanied by a negative impact also on aggregate demand and private

[7]The possibility of a government default need not be grounded on objective factors but on opinions conventionally shared. Keynes (1936[1973], pp. 147-164) analyzed the crucial impact that conventions can have on the working of financial markets. On these issues see also Pasinetti (1997) and De Grauwe and Ji (2012). The latter find that, during the European crisis of the 2010s, rises in the spreads of a number of countries were essentially explained by 'market sentiment' rather than by increases in their debt ratios.

investment.[8]

Thus, the possibility to stabilize the public debt ratio should not justify a lack of concern about the absolute values of the debt at which stabilization is obtained.

This conclusion ratio raises the question whether it would be preferable to aim at reductions of the ratio rather than its mere stabilization. Like in the case of the above-mentioned regressive distributional effects of a high debt ratio, a proper and thorough answer of this question would require constructing a growth model containing demand functions. Here, it is only possible to outline a possible answer.

The reduction of the public debt ratio requires running primary surpluses ($\beta < 0$), which are likely to have a negative impact on aggregate demand in a general context of slow growth. Thus, in my opinion, the policy objective to reduce the 'public debt burden' should be postponed until the economy has experienced a relatively long phase of growth at higher rates which ensure the stability of the public debt ratio.

3 The current economic phase and the need for productivity-enhancing policies

In a short paper written in the 1930s, 'The snake and the worm' (Robertson, 1966).[9] Robertson deals with the problem of state economic interventions by considering its two sides, an easy one and a difficult one. The easy side concerns situations of economic depression; the difficult side has to do with the role of the state when a crisis is over (Robertson, 1966, p. 86).

In the case of a serious crisis, for Robertson the state must certainly intervene to prevent the crisis from precipitating: 'Whatever the cause of the original recession of trade (...) it seems evident that after a certain stage it is apt to degenerate into a purposeless orgy of destruction, like a snake eating its own tail. (...) It seems clear that in such circumstances it is right and reasonable to use the manifold powers of the State to reverse the evil process of cumulation' (Robertson, 1966, pp. 86-87).[10]

After having discussed the easy part of the problem, Robertson turns to deal with the difficult one, that is to say how to deal with the problem

[8]Dealing with the demand effects properly would require the construction of a growth model which contains demand functions whereas the one used in Sardoni (2024) there is no investment function like in Domar's model.

[9]Robertson's paper was presented at a conference on the state and economic fluctuations at Harvard in 1936 and published with the new title 30 years later. Robertson's paper was highly appreciated by Hicks (1967, p. x).

[10]See however Robertson (1966, pp. 87-91) for considerations about the nature and limits of the policies to adopt to fight a crisis.

once the snake has been prevented from 'eating its own tail'. In this regard Robertson distinguishes between those who see a crisis as a mere cyclical episode and those who, instead, see it a symptom of a more serious tendency to stagnation.

For the latter, the defeated 'snake' has become 'a sort of worm seated at the very heart of the institutional and psychological bases of our society, and battening on the very growth of wealth which he strives unavailingly to prevent.' (Robertson, 1966, p. 92).

Robertson himself was not sure whether, at his times, there was or not a worm at work but he made some policy recommendations for those who believed in the worm.

> The advocates of energetic State action against developed depression have had in all countries a hard fight to wage against the forces of apathy and despair. Let us salute them everywhere, in their victories or in their honourable defeats: but let us beg them, whether flushed with success or saddened with failure, to think again before concluding that cheap money and Government deficit, still less trade restriction and exchange manipulation, are the right diet for all phases of the trade cycle or the right remedy for all the economic ills of the world. (Robertson, 1966, p. 94)

Robertson's conceptual framework can be helpfully used also to look at the current economic situation which the major market economies are experiencing. In the last 15 years world economies have experienced two major crises, the 2007-2008 financial crisis and the 2019-2020 COVID pandemics.[11] In all cases states have effectively fought the danger of the 'snake eating its own tail'.

The post-crisis economic phase seems to be one in which Robertson's worm is at work and must be fought. A situation which is a matter of serious concern for international economic organizations like the IMF and the OECD.[12]

Here it suffices to look at some basic data regarding the G7 economies. In the general context of the growing aging of population (Figure 1), all countries are going through a phase which is essentially characterized by low growth rates and a sluggish dynamics of productivity accompanied by high ratios of the public debt to GDP as a consequence of the large increases in public expenditure to tackle the previous crises (see Figures 2 to 5).

[11] Additionally, European countries have experienced a third public finances crisis in 2011-2012.

[12] See, for example, the April 2024 IMF *World Economic Outlook* (IMF, 2024b) on slow growth and the September 2024 issue of the IMF journal *F&D*, largely devoted to the problem of productivity; see also the October 2024 IMF *Fiscal Monitor* which focuses on the dynamics of the public debt and the dangers of its high ratios to GDP (IMF, 2024a). On the European economies see the Report of the European Union on competitiveness and productivity, known as Draghi Report (European Commission, 2024).

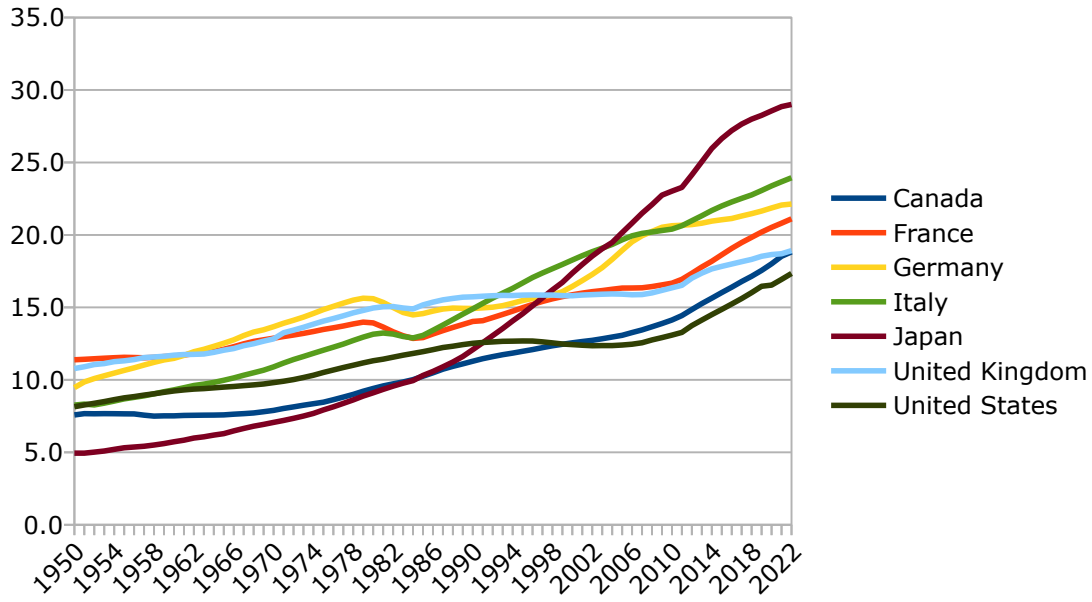

Figure 1: Population aged 65 or over (percentage of total population)

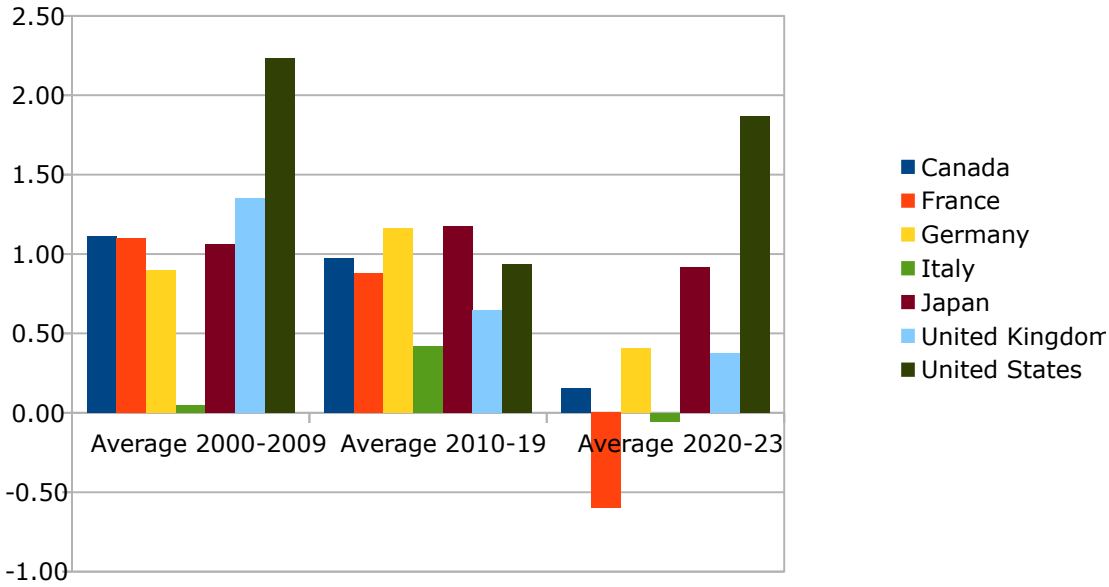

Figure 2: Average growth rates of productivity (real GDP for hour worked)

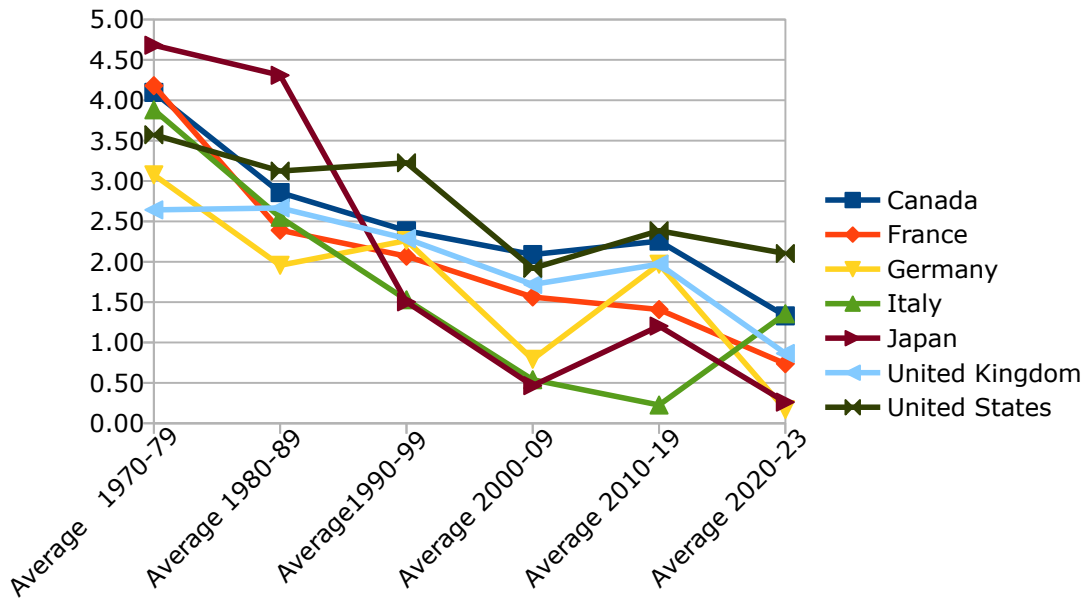

Figure 3: Average growth rates of real GDP

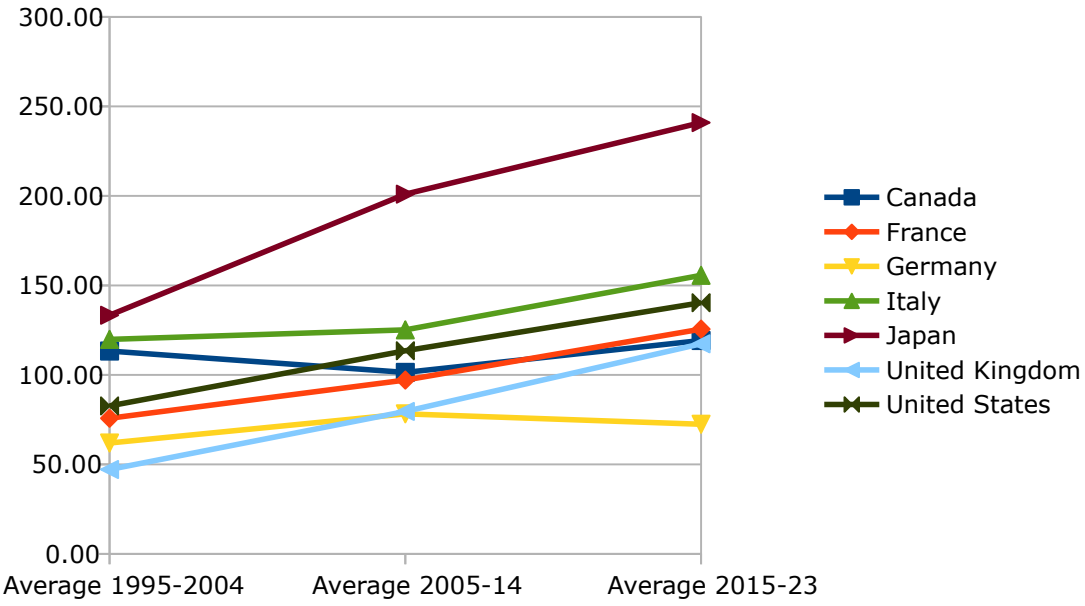

Figure 4: Government debt as percentage of GDP

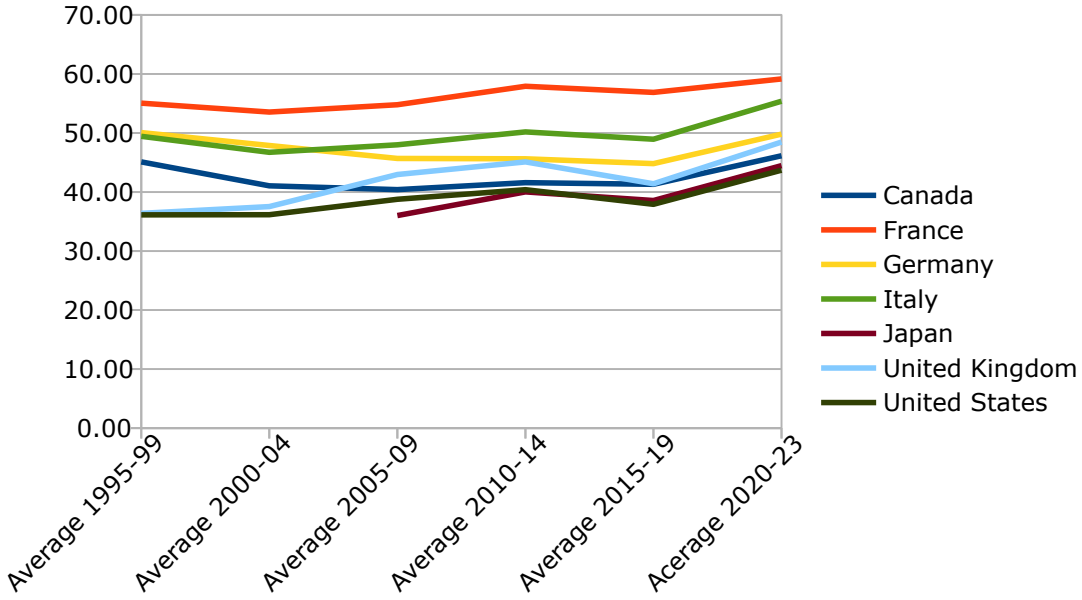

Figure 5: Average expenditure of general government (percentage of GDP)

In such a context, the US economy has been performing relatively better than the others but worse than in previous phases (see figures 2 and 3).[13]

It seems quite evident that such a situation requires economic policies characterized by their emphasis being placed on the need to increase productivity and achieve higher growth rates without compromising the stability and sustainability of the public finances.

Further expansions of public spending to stimulate aggregate demand seem to be inadequate as well as dangerous. The already existing large public sectors and large public spending have not been capable to guarantee significant rises of productivity and growth; additional increases in public spending are likely to compromise the stability and sustainability of public finance.

This is the rationale of the model presented in the previous section. It is based on the idea that state interventions, in the specific form of public spending, can promote growth through their positive impact on the productivity of both public and private investment rather than being based on the 'optimistic' idea that further generic increases of public spending are capable to stimulate significant processes of growth accompanied by stable and sustainable public finances.

[13]Italy was the only country to experience a growing average rate of growth in the period 2020-23, but it was also the country to have the worst performance in the previous period.

4 The efficient implementation of growth-promoting policies

The analysis of the effects of public spending on productivity and growth rests on two basic assumptions.

- The existence of classes of public 3xpenditures that are capable to raise the economy's growth rate thanks to their impact on global productivity.
- The state apparatus as a whole is able and willing to choose, adopt and implement such policies efficiently.

As for the first assumption above, it is quite safe to hold that there exist public expenditures with a potential positive overall impact on productivity and hence on growth. Expenditures on infrastructures, R&D, and education are obvious examples of ways in which the state can make private as well as public productivity rise through investment in human and physical capital.[14]

Things are more problematic when one turns to the second assumption, which involves, on the one hand, politicians and policy makers who choose and adopt particular policies and, on the other hand, the bureaucratic state apparatuses responsible for their implementation. This section concentrates on the implementation of productivity-enhancing and growth promoting policies. The next section deals with the more general problem of the political 'willingness' to adopt such policies.

State interventions which actually promote a more efficient and productive working of the economy require that the state bureaucratic apparatus functions efficiently. The importance of the productivity and efficiency of the state apparatus can be easily seen also by referring to the model of section 2. The increase in the efficiency of the government can impact on its unproductive expenditures. If the public unproductive activities are carried out in a more efficient way, the share u of the fiscal revenue to finance them can be reduced, so that more resources can be devoted to productive spending.

If the efficiency requirement is not satisfied, also expenditures that are conceived as growth-promoting might turn to be ineffectual with a negative impact on the public deficit and debt. It is then necessary that in designing these policies attention is paid also to the ways in which they should be implemented and include, when it is the case, measures to improve the efficiency of the apparatuses called to implemented them.

[14] For a recent attempt at measuring the impact of these classes of expenditures see, e.g., Ciaffi et al. (2024). For the effects of spending on education on growth in the European Union, see Coronel and Díaz-Roldán (2024). See also several contributions on productivity and growth published in *F&D* of September 2024 (in particular Bhatt, 2024; Li and Noureldin, 2024; Zymek, 2024).

The process of designing effectual policies should then be articulated into three distinct but connected phases.

1. The detection of the productivity and growth-enhancing measures on the grounds of thorough analyses of the state of the economy at a certain time.
2. The analysis of the bureaucratic apparatus to ascertain whether it is able to implement efficiently the detected policies.
3. The proposal of measures and interventions on the bureaucratic apparatus to raise its efficiency (productivity).[15]

In conclusion, to call for policies aiming at a more active economic role of the state is not sufficient. These policies are doomed to fail if not accompanied by a thorough analysis and reform of the bureaucratic agent. The failure of the policies has a major negative effect: the missed positive impact on the economy's growth and the consequent waste of resources. Schuck (2014, p. 10) points out other negative effects of failed policies: they damage especially those who mostly depend on state support and they threaten the state legitimacy.

The problem of the state apparatuses' ability to implement growth-promoting policies efficiently was dealt with by Hirschman in the 1950s. Hirschman (1958, pp. 50-61), although mainly interested in developing countries, offers a useful approach to the problem. He criticized the so-called 'doctrine of balanced growth', according to which a sustainable process of development in less advanced countries can start off only if a significantly large number of industries begin to grow in step. In such a way, supply as well as demand difficulties, which hinder the process, would be avoided.

A process of balanced growth requires significant state interventions.[16] Hirschman's main critique was that the theory of balanced growth hinges on the assumption that an undeveloped economy has all those 'creative abilities' required to start and sustain such an ambitious process of growth. This assumption, however, is denied by the fact itself that, until then, the social and economic system in question has been obviously incapable to give rise to its development.[17]

[15]For a collection of interesting contributions on the efficiency and productivity of the state apparatus in Italy see *Economia Italiana*, 2023 no. 2. and in particular the introductory editorial (Galli and Petrucci, 2023).

[16]For Hirschman, the doctrine of balanced growth is basically inspired by the Keynesian analysis of slumps. However, while Keynesian policies can succeed in developed economies, this is far from true in the case of underdeveloped economies, where unused productive resources do not exist.

[17]'... a people that is assumed to be ... entirely uninterested in change and satisfied with its lot is then expected to marshal sufficient entrepreneurial and managerial ability to set up at the same time a whole flock of industries that are going to take in each others' output! ... In other

More specifically, it is doubtful that the country's state apparatus is able and willing to implement growth-promoting policies.

> The fact that private entrepreneurs will be unable or unwilling to do certain jobs which we would like to see done does not in itself ensure that the government can handle them. We must examine whether these jobs are likely to be performed satisfactorily by public authorities, which function after all in the same society as the entrepreneurs. (Hirschman, 1958, p. 65)

Hirschman's critique of balanced growth can be expressed in the following terms. A process of growth and development cannot be started and driven by a state organization that is unable, and often unwilling, to sustain any significant process of growth. The theory of balanced growth, instead, predicates on the crucial role of the state without asking the question whether the state actually has the ability required to accomplish such an ambitious task.[18]

5 The quality and nature of the state apparatus

Hirschman's critique recalled in the previous section is twofold. On the one hand. he reminds us that the public sector cannot be regarded as an entity totally separated from the surrounding social and economic context in which it operates. In a society in which the private sector proves to be unable to promote growth there is no guarantee that the public sector can, or want to, do the job.

In a social system prone to stagnation rather than growth it is likely that a considerable part of the state apparatus as a whole is equally unable and/or unwilling to favor growth-promoting policies in alternative to 'easier' policies better received by a non-dynamic social and economic environment.

On the other hand, Hirschman criticizes those economists and/or policy makers who call for public economic interventions aimed at promoting growth and development without asking the question whether the state apparatus which should implement such policies is actually able and willing to accomplish the task,

Several, from different theoretical stands and perspectives, have contributed to the debate on such issues. Here it is not possible to enter into a

words, if a country were ready to apply the doctrine of balanced growth, then it would not be underdeveloped in the first place.' (Hirschman, 1958, pp. 53-4).

[18] On the grounds of the critique of balanced growth, Hirschman developed his own approach by developing the notion of *unbalanced growth*. See Hirschman (1958, pp. 62-75) and Hirschman (1992).

thorough analysis of such debates. It will suffice to recall some crucial issues raised and dealt with by some representative contributors.

A first issue to take into consideration is the so-called shortsightedness of politicians and policy makers. Productivity-enhancing and growth promoting policies generally have a long-period perspective. Thus, their adoption requires that policy makers should decide and operate in the same long rather than short-sighted perspective.

Politicians and policy makers are generally in favour of a large public expenditure.[19]. However, politicians might not be in favour of expenditures with positive effects that manifest themselves too late for their electoral horizons and with negative effects that manifest themselves in the short period (like the reduction of unproductive expenditures which possibly affect groups of potential voters).

Although there is not a general consensus on the notion of the politicians' 'short-sightedness',[20] it seems reasonable to argue that, in situations of economic sluggishness with the public sector's inability to effectively promote growth and public finances stability, the shortsightedness of policy makers tends to prevail over more long-term perspectives. Or, more generally, the political and economic particular interests of the political parties and groups in power prevail over the general interest as expressed by the growth of the economy as a whole.

Acemoglu and Robinson (2012) delve into the nature and quality of the state and institutions in general to see how they affect the prosperity and growth of nations.[21] The two authors distinguish between inclusive and extractive economic and political institutions.

Inclusive economic institutions 'create inclusive markets, which not only give people freedom to pursue the vocations in life that best suit their talents but also provide a level playing field that gives them the opportunity to do so. (...) [They] also pave the way for two other engines of prosperity, technology and education.' (Acemoglu and Robinson, 2012, pp. 76-77)

Inclusive political institutions, strictly connected to inclusive economic institutions, are those which are sufficiently centralized and pluralistic (Acemoglu and Robinson, 2012, p. 81).[22]

[19]For an analysis of the politicians' attitude towards the expansion of the public expenditure, see Cao et al. (2024).

[20]On the topic see, e.g., Zannoni (1976); MacKenzie (2021) and Aidt and Dutta (2007) who deal with the topic specifically in relation to growth.

[21]Acemoglu and Robinson, jointlyt with Johnson, were awarded the Nobel Prize in Economics in 2024. For an extensive survey of their 2012 book, see MacLeod (2013); For an heterodox criticism of their theoretical approach, see Reddy (2024).

[22]Pluralism allows different economic and social groups to participate in the processes by which crucial decisions are made and speak for their own interests and finalities. A certain degree of centralization allows the state to play its role as law enforcer and regulator of economic activities as well as to provide efficient public services (Acemoglu and Robinson, 2012, pp. 80-81).

Extractive economic and political institutions are the opposite of the inclusive ones. They are 'designed to extract incomes and wealth from one subset of society to benefit a different subset' (Acemoglu and Robinson, 2012, p. 76). Also extractive economic institutions are connected to political extractive institutions, which aim to guarantee the power of the particular dominant subset (Acemoglu and Robinson, 2012, p. 81). Extractive institutions generally are an impediment to nations' prosperity and growth.[23]

Prosperity and growth might seem to be in the interests of the whole social system,[24] but for Acemoglu and Robinson, this is not the case. Growth is a 'Schumpeterian' process which creates winners and losers in the economic as well as political arena, so that the dominant groups in an extractive system at a certain time can block the process for the fear of losing their power: 'Fear of creative destruction is often at the root of the opposition to inclusive economic and political institutions' (Acemoglu and Robinson, 2012, p. 84).

From the considerations above it derives that the state should not be regarded as an agent which necessarily works in favor of the general interest, as expressed by the promotion of prosperity and growth for the whole social and economic system, The state can 'fail' to accomplish such a task for its inefficiency and, more importantly, because its interventions are in favor of the interest of particular social and economic groups which do not favor growth and development.

It is then necessary that economists concerned with policies to suggest to policy makers and governments take into serious account such crucial aspects. Not to take account of them can, in fact, cause their ineffectiveness, or even the production of perverse effects

In this perspective, it is useful to briefly take into consideration some of Buchanan's ideas. Inspired by Wicksell (1967[1896]) Buchanan invites economists to 'cease proffering policy advice as if they were employed by a benevolent despot, and they should look to the structure within which political decisions are made' (Buchanan, 1987, p. 243).

More in particular, he criticizes the influence of socialist ideas on those concerned with welfare economics. 'The socialist ideology was pervasive, and this ideology was supported by the allegedly neutral research program called–'theoretical welfare economics,' which concentrated on the identification of the failures of observed markets to meet idealized standards. (...) The implicit presumption was always that politicized corrections for market failures would work perfectly. In other words, market failures were set

[23]Acemoglu and Robinson (2012, pp. 91-95) do not exclude that in some cases extractive institutions can be associated with periods of growth of more or less limited length.

[24]'Wouldn't every citizen, every politician, and even a predatory dictator want to make his country as wealthy as possible?' (Acemoglu and Robinson, 2012, p. 83).

against an idealized politics.' (Buchanan, 2003, pp. 8-9).

Buchanan is a major representative of the Public Choice approach, which pays much attention to the so-called government failures as opposed to market failures. It criticizes the widely accepted opinion that the state plays a crucial role to tackle market failures and, in so doing, it raises the general economic welfare. The state cannot be simply regarded as a 'benevolent' agent guided by the objective of raising general welfare.

The public-choice approach, based on three constitutive elements: methodological individualism, the concept of *homo oecomicus* and the idea of politics as exchange (see, e.g., Buchanan, 1987), has been criticized from several different theoretical perspectives.[25]

However, independently of Buchanan's theoretical explanation of why the state apparatus' concern is not necessarily for the general interest, one can agree with the view that the state may respond to and function in favour of, the social and economic interests, of particular groups as well as specific political and/or bureaucratic interests which are not necessarily coincident with the general interest. Policies that might appear as obviously in favour of the general social welfare in reality are designed and implemented in ways that favor particular groups.

For example, policies which ask for large public expenditures for education would appear to be in favour of the general interest as they positively affect the economy's overall productivity, but this could not be the case if they are not carefully scrutinized to avoid that they are 'captured' by particular interest groups, within or without the public administration, and used mainly to their benefit.

Thus, in conclusion, efforts to design and propose adequate policies should necessarily be accompanied by the analysis of the state apparatus in terms of efficiency and productivity as well as in political and organizational terms. Such analyses should also be concerned with the actual possibility to check and control the implementation of the suggested policies to ensure that they actually produce the desired effects.

Relying on large public interventions that affect significantly the working of the economy as a whole gives the state a significant power. To try to

[25]For example, Hirschman's viewpoint as expressed in *Exit, Voice, and Loyalty* (1970) is an alternative to the Public Choice's view of the state (Hirschman's critique of Public Choice is well documented by Galvão de Almeida (2021)). Furton and Martin (2019) suggest to abandon the dichotomy market/government failure and concentrate on 'institutional mismatch', that is to say cases in which the interaction between the market and the state is dealt with badly. Stiglitz (1989) looks at the problem from the perspective of the pervasiveness of incomplete markets and imperfect information which affect both the market and the public sector. Stiglitz emphasizes that both markets and governments are imperfect: 'problems of incomplete markets and imperfect information are at least as pervasive in the public sector as they are in the private, raising questions about whether the government could or would remedy the problems.' (Stiglitz, 1989, p. 39).

avoid that such a power is used in favour of particular interests requires the existence of institutions and institutional arrangements, which function as 'guardians'.[26]

6 The need for opening the 'state black box': concluding remarks

The main point made in this paper is that state economic interventions, more specifically in the form of public spending, can play a positive role in the process of growth by promoting productivity rather than by simply augmenting aggregate demand.

Such a positive role for public spending is however contingent on the conditions that the state as a whole operates efficiently and in ways that favor the general interest rather than the particular interests of social, political and economic groups outside or inside the public sector.

These requirements make it necessary to carry out thorough and careful analyses of the state apparatus. In other words, the state should not be regarded as a sort of 'black box' which does not require to be opened and be subjected to thorough analyses and adequate measures to make it work better and with the objective to promote, to the maximum possible extent, the interests of the social and economic system as a whole.

However, it seems that those theoretical strands which are mostly characterized by their claims for large and possibly growing state economic interventions do not regard the opening of the state black box as an impellent necessity.

Those who currently characterize themselves for positions in favor of large state economic interventions in market economies are economists more or less directly influenced by Marxist and socialist ideas and Keynesian or Post Keynesians.[27] Both of them tend to see the state as a sort of 'obedient agent' which responds to the policy input coming from the 'principal' (politicians, intellectuals) in a neutral way, that is to say by implementing the policies in the general interest, or at least in the interests supported by the principal.

Such an 'optimistic' view of the state and its working is, as argued by Buchanan (2003, pp. 10-11), somewhat paradoxical for those who draw inspiration from Marxism. On the one hand the existent state organizations

[26]Even though the existence of guardians raises the problem of who, in turn, control them (Hurwicz, 2008). On the issue of control of the working of the state apparatuses see also Stiglitz (1989).

[27]Kalecki's ideas and analyses of capitalism often play the role of a bridge between these two strands.

are seen by Marxism as the instrument to further the interests of the bourgeoisie (Marx and Engels, 1848[1976], p. 486); on the other hand, the state is expected to transform into a benevolent and omniscient agent after the revolution, or at least the coming to power of a government inspired by socialist principles.

As to Keynesian positions, their confidence in state interventions to solve the problems and contradictions affecting market economies is quite often accompanied by a lack of interest in its efficiency and productivity. For these economists, what counts most is that the state enlarges its presence in the economy by making substantial expenditures which will promote growth and employment thanks to the response of household and firms which react positively to them by raising their demand for consumption and investment. Hicks (1974) held that this is one of the worst aspect of the Keynesian doctrine.[28]

In this context, at least among those with more extreme positions, it is not surprising that there is little, if any, concern about large and growing public deficits and debt.[29] The unconcern for public deficits and debt however did not characterize Keynes's own position. He was in favor of normally keeping the current public budget in balance while public borrowing was justified only to finance investment (Keynes, 1980, pp. 319-320).

Differently, this paper argues that, especially for those most favorable to significant state interventions to open the state black box and proceed to a more thorough comprehension of the nature and functioning of the state organization. This should be seen as a *sine qua non* to design effective and efficient measures.

[28]'...one form of investment appears as good as another. Only investment expenditure is taken into account; the productivity of investment appears as good as another. Only investment expenditure is taken into account; the productivity of investment is neglected. (One remembers those pyramids!) Once one accepts that one form of investment is not as good as another, it follows that itis socially productive that the form of investment should be wisely chosen.' (Hicks, 1974, p. 57).

[29]See, e.g., Kelton (2020).

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