

The Asymmetric Effects of Government Spending Shocks: Empirical Evidence from Turkey

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Abstract. The purpose of this paper is to assess if expansionary and contractionary government spending shocks have an asymmetric effect for Turkish economy. Keynesian theory suggests that increase in government spending stimulate aggregate demand and increases output. However, there might be asymmetry for the effect of fiscal policy on economic outcome due to stickiness of prices, perception of changes (permanent versus transitory) and nearness to full employment. This paper assesses this asymmetry for Turkey by using quarterly data from 1987:I to 2001:I. The empirical evidence reported here reveals that private consumption and investment decrease in the face of expansionary government spending shocks; however, they either do not change or decrease very little under contractionary government spending shocks.

JEL Classification Codes: E20 ; E60; E62.

Key Words: Asymmetric effect; fiscal policy and economic performance.

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1. Introduction

Budget deficit and its sustainability have a prime importance in the establishment of economic policies in Turkey. Keynesian theory suggests that increased government spending stimulates aggregate demand and increases output. However, due to the increase in interest rates, government spending crowds out private consumption and private investment. Barro (1987) argues that, if the increase in the government spending is taken as permanent, then an increase in output will be realized without increasing interest rates. The purpose of this paper is to assess whether expansionary and contractionary government spending shocks have asymmetric effects on economic performance. The assessment of this asymmetric effect is important because it is often argued that decreasing government spending will be followed by decrease in prices, providing stability in the market. There might be various reasons for asymmetry effect. First, if wages and prices are sticky downward, a contractionary government spending shock decreases output more than expansionary government spending shock increases it. Price response will tend more to an increase than a decrease in government spending. Second, when prices and wages are perfectly flexible and output is equal to near full employment level, then an increase in government spending does not increase output but a decrease in government spending decreases output. Third, interest rates increase in the face of expansionary government spending shocks while there is no evidence of a reduction in the face of contractionary government spending shocks. The reason for this is that the response of private agents to an increase and a reduction in interest rates would be different; that is, the response of interest rates and private agents would be different to the expansionary and contractionary shocks (see, Kandil, 2001). Lastly, the economic outcome might be affected and changed by the perceptions and expectations of the public. If it is perceived to be permanent by the public, then the expansionary shock will increase aggregate demand, but if it is perceived to be temporary by the public, then the expansionary government spending shock will not affect aggregate demand very much. Thus, if the increase in government spending is perceived as permanent but the decrease in government spending is perceived as transitory, the effect of expansionary and contractionary fiscal policy on economic outcome will be asymmetric.

Cover (1992) illustrates the asymmetric effects in the face of expansionary and contractionary economic policy shocks using the quarterly data of real output in the United States. He finds that contractionary economic policy shocks affect output while expansionary economic policy

shocks do not affect output. Kandil (2001), using quarterly data for the United States, demonstrates the asymmetric effects of expansionary and contractionary shocks to government spending around an anticipated steady-state trend over time. She finds that while interest rates increase in the face of expansionary government spending shocks, there did not seem to be any evidence of a reduction in the face of contractionary shocks. Consequently, in the face of an expansionary government spending shock, an increase in government spending crowds out private investment. Moreover, there is evidence of a reduction in private consumption. As a result, output growth and price inflation decrease despite expansionary government spending shocks, on average, over time.

Studying the asymmetric effects of government spending shocks for the Turkish economy is interesting because Turkey has high persistent inflation without running into hyperinflation and this is a vital problem for the fiscal policies of the Turkish economy. Moreover, Turkish government spending is volatile, which can frequently create possible asymmetric effects. Thus, Turkey produces a laboratory environment to assess the effect of fiscal policy on economic performance. In the last two decades, the Turkish economy has performed unstable macroeconomic development. Growth during a period was followed by contraction in the next period. Every time that the government tried to compensate for the budget deficit, it affected the balance of the financial markets in the face of unstable interest rates. Therefore, explaining the asymmetric effects of Turkish government spending is an important macroeconomic topic to be worked on.

In order to investigate government spending shocks, we studied the effects of expansionary and contractionary government spending shocks on *aggregate demand*, *prices*, *total private consumption* and *total private investment*. Moreover, in order to carry out a more detailed investigation we also took into account the subcomponents of *total private consumption* and *total private investment*. We found that government spending shocks have asymmetric effects on the subcomponents of both *total private consumption* and *total private investment*. The empirical evidence reported here reveals that *total private consumption* and *total private investment* decrease in the face of expansionary government spending shocks; however, they do not change or decrease very little under contractionary government spending shocks. The analysis reveals that the private sector responds to the government spending shocks asymmetrically but there is no evidence as to the asymmetry in *prices* and *output* in the face of government spending shocks in Turkey.

This paper is structured as follows. Section 2 describes the methodological framework. Section 3 gives the empirical evidence and interprets the estimates. Finally, section 4 concludes the paper.

2. Methodology

In order to investigate the possible asymmetric effects, we employ the following empirical model:

$$\begin{bmatrix} 1 & b_{12} \\ b_{21} & 1 \end{bmatrix} \begin{bmatrix} g_t \\ z_t \end{bmatrix} = \begin{bmatrix} b_{10} \\ b_{20} \end{bmatrix} + \begin{bmatrix} \gamma_{11} & \gamma_{12} \\ \gamma_{21} & \gamma_{22} \end{bmatrix} \begin{bmatrix} g_{t-1} \\ z_{t-1} \end{bmatrix} + \begin{bmatrix} \varepsilon_{gt} \\ \varepsilon_{zt} \end{bmatrix} \quad (1)$$

where g_t is for percentage change of real government spending, z_t is a vector of other economic variables of interest, and ε_{gt} and ε_{zt} are orthogonalized disturbances.

In this model, the set of relevant explanatory variables (z_t) includes logarithmic first differences of; the real GDP, the wholesale price index, the real total private consumption, the real total private investment, the government spending and the 3-month treasury bill rate. Furthermore, for a more specific investigation of the asymmetric effect of government spending shocks over consumption and investment; we have used some components of consumption and investment instead of *total private consumption* and *total private investment* themselves¹. During the estimation process, if one of the components of total consumption was used instead of *total private consumption* itself, *total private investment* itself was used rather than its components and vice versa. When the estimation is performed, various dummy variables are also included. In order to account for seasonality, three dummy variables, which are denoted as D_{it} , are used for the seasonality effects over the quarterly data. $D94_t$ stands for the self-inflicted 1994 crisis in the second quarter. Similarly, $D00_t$ stands for the crisis in the Turkish economy in the last quarter of 2000. The data for all the variables are

¹ Logarithmic first differences of durable goods, *semi-durable goods*, public sector consumption, public construction expenditures, *private sector consumption*, private sector machinery expenditures and private sector construction expenditures are taken as the components of total private consumption. Moreover, logarithmic first differences of mining and quarrying, manufacturing, total industrial and wholesale/retail productions are taken as the components of *total private investment*.

gathered from the Central Bank of the Republic of Turkey electronic data delivery system².

In order to assess the positive and negative government spending shocks to fiscal policy, we define two variables, pos_t and neg_t , which stand for the expansionary and contractionary government shocks, respectively. We measured the positive and negative government spending shocks in a similar way to Cover (1992) and Kandil (2001), as follows:

$$pos_t = 0.5 * (\varepsilon_{gov_t} + |\varepsilon_{gov_t}|) \quad (2)$$

$$neg_t = -1 * (\varepsilon_{gov_t} - pos_t) \quad (3)$$

Here, shock terms, which are denoted as ε_{gov_t} , are the residual terms created by regressing the logarithmic first difference of government spending over the same explanatory variables of our model. pos_t stands for the expansionary government spending shocks while neg_t stands for the contractionary government spending shocks. We include pos_t and neg_t in the models to observe the asymmetric effects of government spending shocks to assess their effect on *aggregate demand*, *price level*, *total private consumption* and *total private investment*. Therefore, we model the macroeconomic variable, which is claimed to be affected by government spending shocks asymmetrically. Then we include positive and negative shocks in the model as follows:

$$Y_t = \Gamma_0 + \Gamma_1 X_t + \Gamma_2 POS_t + \Gamma_3 NEG_t + \eta_t$$

Where Y_t is the variable under concern, Γ_0 stands for the constant terms and dummy variables, X_t is the set of explanatory variables, Γ_2 and Γ_3 are the coefficients of the lagged effects of the positive and negative government spending shocks on the concerned variables and η_t is the error term (see Appendix for details).

Aggregate demand, *prices*, *total private consumption* and *total private investment* are expected to react to the fluctuations in government spending shocks. The estimates Γ_2 and Γ_3 will allow us to examine the asymmetry on the dependent variables created by the government expansionary and contractionary spending shocks.

² <http://tcmbf40.tcmb.gov.tr/cbt.html>

If the expansionary and contractionary government spending shocks are perceived as permanent by the public, then the expansionary shock will increase aggregate demand, but if it is perceived as temporary by the public, then the expansionary government spending shock will affect the aggregate demand at a smaller magnitude. It is also possible that the government's expansionary spending shock might be taken as permanent while the government contractionary spending shock is perceived as temporary. This suggests that the effect of unanticipated expansionary government spending would be greater than the effect of unanticipated contractionary government spending. Moreover, the way chosen by the government to finance the deficit would be important for the response of aggregate spending to expansionary and contractionary shocks. If the government borrows from the public to finance the gap which is induced by the expansionary spending shock, the public might see it as the increase of future wealth. This would trigger aggregate consumption and demand. But in order to capture the asymmetry, the level of the response of the aggregate demand to expansionary and contractionary shocks must not be balanced. In other words, an increase in the aggregate demand because of expansionary government shocks must be different from that of a decrease in the aggregate demand. It is expected that the expansionary effects of government spending shocks may exceed the contractionary effects on aggregate demand.

Consistent to the discussion about aggregate demand, private consumption would be determined with respect to the expectations of the public (expectations concerning the persistence of a shock), as well as the way of financing the spending shock by the government. It is expected that the expansionary effects of government spending will exceed the contractionary effects on private consumption.

Kandil (2001) also suggests that interest rates increase in the face of an increase in government spending. This fact causes a decrease in private investment. In addition, a decrease in government spending would decrease interest rates and increase investment demand. The rates of increase and decrease in private investment in response to government spending shocks will not be equal. That is why we are looking for asymmetry.

To sum up, the effect of unanticipated government shocks would be greater if they are accepted as permanent rather than temporary. The way chosen by the government to finance the deficit which is created by the government spending shock affects the amount of consumption and

investment by the private sector. Likewise, interest rates, which will increase or decrease separately in the face of expansionary or contractionary government spending shocks, would affect private sector consumption and investment to create asymmetry.

3. Empirical Evidence

The estimation process determines the asymmetric effect of government spending shocks on the dependent variables of our models. The models are estimated with four lags. We used two methods for the estimation: Least Squares (LS) and Three Stage Least Squares (3SLS). First, we used LS to assess the asymmetric effect of fiscal policy on the economy. For the LS estimates, we used a two step procedure. In the first step, using Equations (1), (2) and (3), we constructed the pos_t and neg_t terms to indicate the expansionary and contractionary government spending shocks. Then we regressed our four dependent variables (logarithmic first differences of aggregate demand -*real GDP*-, prices -*WPI*-, *total private consumption* and *total private investment*) over the explanatory variables. However, one may calculate pos_t and neg_t incorporating the reduced form setting. Hence, 3SLS will be in order. In 3SLS, we used 6 lagged logarithmic first differences of all the dependent variables, as well as the explanatory variables themselves as instrumental variables in addition to the ordinary models.

Table 1 reports the estimations of the lag values for pos_t and neg_t terms. Panel A shows the results of the LS estimation, while Panel B shows the results of the 3SLS process. In both of the panels, the first two columns present the sums of the coefficients of the pos_t and neg_t terms (in order to account for their long term effects), respectively. Column 3 for each panel presents the total effect generated by both expansionary and contractionary government spending shocks. Asymmetry in the effects of government spending shocks on unanticipated growth in the various explanatory variables of our model can be identified. Columns 4, 5 and 6 report the p -values of the Wald test statistics: column 4 reports the results of the hypothesis that the sum of the coefficients of pos_t terms is equal to zero; column 5 tests the hypothesis that the sum of the coefficients of neg_t terms is equal to zero; the last column of each panel tests the hypothesis that the sum of the coefficients of the pos_t terms is equal to the negative signed sum of the coefficients of neg_t terms.

Specifically, we concentrate on the sum of the coefficients for positive and negative government spending shocks on various explanatory variables. In Table 1 and Panel A, by using LS for the estimation, the cumulative effect of expansionary government spending shocks on *total private consumption* is negative but statistically insignificant³. This suggests that *total private consumption* decreases as the amount of government spending increases. This fact can be related to the public's opinion about the government's policy of financing the spending shock. The public may decide that the gap created by the spending shock will be financed by the future taxes; *total private consumption* decreases. The cumulative effect of contractionary government spending shocks on *total private consumption* is negative and statistically insignificant. The difference between the cumulative effects of positive and negative spending shocks is the key factor for the identification of the asymmetry. For *total private consumption*, this difference is positive and statistically insignificant. But this result does not help us to capture the asymmetric effect of a government spending shock. Furthermore, we find parallel results to the LS when we do the estimation by 3SLS to explain the effects of a government spending shock on *total private consumption*.

Alternatively, we can use subcomponents of *total private consumption*, instead of using *total private consumption* itself. Keep in mind that, if one of the components of *total private consumption* was used instead of *total private consumption* itself, *total private investment* itself was used rather than its components. When we examined the subcomponents of *total private consumption*, we found more supporting evidence. Explaining unanticipated growth in *durable goods* consumption, the cumulative effects of positive and negative government spending shocks are negative. The results are statistically significant for positive government spending shocks, although insignificant for the negative ones. Parallel to the discussion about *total private consumption*, the asymmetric effect can be identified in the 3rd column. The difference between the cumulative effects of positive and negative shocks is negative and statistically significant. When we do the same examination for *semi-durable goods* consumption to see the effects of government spending shocks, we find that the test results for asymmetry are statistically insignificant, although the cumulative effect of contractionary government spending shocks is negative and statistically significant.

³ The level of significance is 5% unless otherwise stated.

Explaining the effects of unanticipated government spending shocks on *private sector* consumption as being another subcomponent of *total private consumption*, the cumulative effect of expansionary government spending shocks is negative and statistically significant. In the same way, the cumulative effect of contractionary government shocks is also negative and statistically significant. As the core point, the difference between the cumulative effects of expansionary and contractionary shocks is negative and statistically significant, showing asymmetry. So we can say that, observing the asymmetric effects of government spending shocks, a contractionary spending shock decreases *private sector* consumption, and *private sector* consumption decreases even more under an expansionary spending shock. The results gathered from the 3SLS estimation are mostly parallel to the ones of LS, but empirical evidence is weaker.

In Table 1, the cumulative effect of expansionary government shocks on prices (*WPI*) is negative, although statistically insignificant. We can say that the reduction in private spending, along with the increase in the government spending, decreases prices over time. The cumulative effect of contractionary government spending is also negative and statistically insignificant. Finally, the difference between the cumulative effects of expansionary and contractionary government shocks is negative and statistically insignificant. Thus, once more, we could not capture the asymmetric effect at a meaningful significance level. With the 3SLS estimation method, the cumulative effect of expansionary government spending shock on prices is positive, although insignificant. This can be explained by the positive effect of government spending shock on aggregate demand in the 3SLS method. Increasing demand increases prices. The cumulative effect of contractionary government spending shocks is negative and insignificant. Finally, in the 3SLS method, to determine the asymmetry, we examine the 3rd column; the difference between the cumulative effects of expansionary and contractionary government spending shocks is positive, although statistically insignificant.

Although economic theory suggests an indirect relationship between government spending shocks and *total private investment*, our empirical study indicates the opposite situation with high *p*-values for both LS and 3SLS and also for some of the subcomponents of *total private investment*.

For aggregate demand, if we examine the effect of a government spending shock on the *real GDP*, in Panel A, by intersecting the last row and the first column, we see that the cumulative effect of expansionary

government spending shocks is negative, although statistically insignificant. The cumulative effect of contractionary government spending shocks on aggregate demand is negative and statistically significant. Asymmetry in aggregate demand shifts is captured by the difference between the expansionary and contractionary government shocks, which is positive and significant. When we do the estimation with 3SLS, we see that the cumulative effect of expansionary government spending shocks is positive, although statistically insignificant. The cumulative effect of contractionary government spending shocks on aggregate demand is positive and statistically significant. Finally, in the 3SLS method, to determine the asymmetry, we examine the 3rd column; the difference between the cumulative effects of expansionary and contractionary government spending shocks is negative and statistically significant. That is, demand contraction is evident in the face of expansionary and contractionary government spending shocks.

It can be seen in Table 1 that, using total government spending does not support what the economic theory suggests. When we used the total government spending variable to capture the government spending shocks on various explanatory variables, we could not reach statistically significant results except for *real GDP*, *durable goods* and *semi-durable goods* with LS and 3SLS. The same fact is true for *private sector consumption* when investigated with LS only. Since the results were insignificant when we used total government spending during the estimation process of government spending, we used the difference between the treasury auction interest rate and the previous quarter's interbank interest rate (so called *auction* in our work) alternatively to the total government spending variable. The reason for using treasury *auction* interest rates rather than the government spending variable should be explained. Total government spending includes figures from the consolidated budget; and in the very relaxed supervision of this consolidated budget system of Turkey, some public institutions (particularly local administrations) invoice their own spending to the government. Conversely, sometimes governments show their expenditures as if they were the expenditures of public institutions and avoid reporting these expenditures in the government budget⁴. Such budgetary movements are called hidden liabilities (Esfahani and Kim, 2002). This problem is not peculiar to Turkish economy. Most governments have financial commitments and contingent liabilities that do not receive explicit budgetary operations or even official recognition. Less transparent fiscal systems tend to produce more liabilities.

⁴ See Atiyas, Gunduz, Emil, Erdem and Ozgun (1999).

Conditioning the fiscal transparency to attain fiscal discipline is also emphasized in various international pacts and multilateral arrangements as in the European Union's Maastricht Treaty and the IMF conditionality. In fact, since Turkey is a candidate country for entry to the European Union and has close relations with IMF, one of the main planning reforms of the ongoing economic program of the Turkish economy concerns the restructuring of public fiscal management and fiscal transparency.⁵ Thus, some non-government spending is included in the total government spending in the budget and independent of the government spending shocks. However, the borrowing cost of the government, treasury auction interest rates, reflects the true value of government spending, which is done purely by the treasury. Berument (2002) suggests using the spread between the treasury auction interest rate and the lagged value of the interbank interest rate to account for fiscal policy.

In Table 2, we can see the effects of expansionary government shocks when we take treasury auction interest rates as government spending. This time the shock term, ε_{gov} , is generated by regressing treasury auction interest rates on the various explanatory variables. Table 2 is constructed the same as Table 1.

In Panel A of Table 2, by using LS for the estimation, the cumulative effect of expansionary government spending shocks on *total private consumption* is positive and statistically significant. This means that an increase in government spending increases *total private consumption*. The increase in *total private consumption* in the face of an expansionary government shock can be explained in such a way that the income effect dominates the substitution effect. On the other hand, the cumulative effect of contractionary government spending shocks on *total private consumption* is positive but statistically insignificant. The difference between the cumulative effects of positive and negative shocks is positive and statistically significant. Therefore, we can capture the asymmetry in the effects of expansionary and contractionary government shocks on *total private consumption*. Moreover, when we do the estimation with 3SLS, we find results similar to those reported in Panel B of Table 2 with higher levels of significance.

⁵ See the report drawn up by *Special Ad Hoc Committee on Restructuring of Public Fiscal Management and Fiscal Transparency*, March 2000, <http://ekutup.dpt.gov.tr/kamumali/oik8/pubfinan.doc>.

When we examined the subcomponents of *total private consumption* to see if they are affected by expansionary and contractionary government shocks, measured with treasury auction interest rates, we found more evidence to support asymmetric effects. Explaining unanticipated growth in *durable goods* consumption, after the 3SLS estimation (presented in Panel B of Table 2), the cumulative effect of expansionary government shocks is positive and statistically significant. This means that the consumption of *durable goods* increases in the face of an increase in government spending. On the other hand, the cumulative effect of contractionary government shocks on *durable goods* consumption is positive but statistically significant at the 10% level. The difference between the cumulative effects of positive and negative shocks is positive and statistically significant, which indicates asymmetry.

Explaining the unanticipated expansionary and contractionary government shocks measured with treasury auction interest rates on *private sector* consumption as being another subcomponent of *total private consumption* like we did before, in Panel A, the cumulative effect of expansionary government shocks is positive and statistically significant at the 10% level. The cumulative effect of contractionary government shocks is also positive and statistically significant. The difference between the cumulative effects of expansionary and contractionary shocks is positive and statistically significant, thus indicates asymmetry. As a result, by observing the asymmetric effects of government shocks, we can argue that *private sector* consumption increases with both expansionary and contractionary shocks. The 3SLS estimation method also indicates an asymmetric effect of government spending on *private sector* consumption. The results that are reported in Panel B of Table 2 are statistically significant and this time results are statistically significant also for the contractionary government spending shocks.

When we investigated the asymmetric effects of expansionary and contractionary government shocks on *machinery* consumption, we found supporting evidence with 3SLS. As reported in Panel B of Table 2, *machinery* consumption is decreased by the effect of expansionary government shock. This result is statistically significant. It can be seen in the same panel that contractionary government shocks decrease the *machinery* spending more than expansionary shocks do, and this is statistically significant. The difference between the cumulative effects of expansionary and contractionary shocks is positive and statistically significant, indicating asymmetry.

Identifying the effects of government shocks on *private construction* consumption with LS estimation, we find results similar to those for *private sector* consumption. The cumulative effect of expansionary government shocks is positive and statistically significant at the 5.7% level. The cumulative effect of contractionary government shocks is also positive and statistically significant. The difference between the cumulative effects of expansionary and contractionary shocks is positive and statistically significant, showing asymmetry. Thus, observing the asymmetric effects of unanticipated government shocks, we can say that private construction consumption increases for both expansionary and contractionary shocks. When we do the estimation with 3SLS, the expansionary and contractionary government shocks and the difference between the cumulative effects of expansionary and contractionary shocks is positive and statistically significant, indicating asymmetry.

The estimates from *total private investment* do not reflect asymmetric effects in the face of government spending shocks. However, if we use the lower components of *total private investment* instead of itself, we find supporting evidence with 3SLS estimation. The effect of expansionary government shocks on *manufacturing* is negative and statistically significant. In other words, manufacturing investment decreases in the face of expansionary government shocks. Contractionary government shocks also affect manufacturing negatively and the results are statistically significant. As the core point, the difference between the cumulative effects of expansionary and contractionary shocks is negative and statistically significant, showing asymmetry. We reach the same results with total industrial and wholesale/retail investments.

Compared with the results of the asymmetric effects of government spending shocks in Table 1, we find more supporting results in Table 2. In fact, this supports our hypothesis that treasury auction interest rates are more suitable for representing government spending. As reported in Table 2, using *treasury auction interest rates*, there is evidence that unanticipated government spending has asymmetric effects on total private consumption and on the subcomponents of *total private consumption* and *total private investment*. Although supported weakly with LS estimation, with 3SLS there is greater supporting evidence for our hypothesis. In Panel B of Table 2, the results for *total private consumption*, *durable goods* consumption, *private sector* consumption, *machinery* consumption, and *private construction* consumption are statistically significant. In addition, the results for the subcomponents of *total private investment*, specifically for *manufacturing*,

total industrial production and *wholesale/retail* production are statistically significant, capturing the asymmetric effects of expansionary and contractionary government spending shocks.

4. Summary and Conclusions:

Government spending and its effects is an imported topic to be worked on, especially for the countries, like Turkey, which have chronic budget deficits. There has been considerable discussion regarding government spending in Turkey. Government spending has some direct and indirect impacts on the various macroeconomic variables. An increase in government spending would cause aggregate demand to increase. Correspondingly, increasing demand stimulates output growth and price inflation, so this situation affects private consumption and investment although we do not observe that the decrease in government spending affects the economy.

However, the relationship between government spending and the variables affected by the government spending is asymmetric, such that the effect of an increase in government spending may be different from that of a decrease in government spending. One reason for the asymmetry is the capacity constraints in the credit market. A positive shock to government spending above an anticipated steady-state trend increases the demand for loanable funds and raises the interest rate. The increasing interest rate crowds out the expansionary government spending shocks. However, the interest rate does not decrease in the face of contractionary government spending shocks. Of course, private investment does not increase in the face of contractionary government spending shocks.

Another source of asymmetry may be the response of *private consumption* to government spending shocks. The perception of the government spending shock by private agents is important in clarifying the effect of government spending shocks. Specifically, agents decrease consumption in anticipation of future tax liability in the face of expansionary government spending shocks.

In this paper, it is shown that asymmetry in the effects of government spending shocks can be best captured when treasury auction interest rates were used to indicate the government's fiscal stance. Moreover, when we used subcomponents of *private consumption* and *private investment*, the results of estimation results became more supportive.

The effects of expansionary government spending are closely related to the economy's ongoing state. Asymmetry in the face of government spending shocks indicates that the stabilizing effects of fiscal policies are dependent on the state of the business cycle. During recessions, the expansionary effects of an increase in government spending are likely to be pronounced, speeding up recovery towards full-equilibrium. In contrast, a decline in government spending during boom periods is likely to stimulate a fast increase in private spending, hindering the success of contractionary fiscal policy in moderating excess demand.

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TABLE 1: The Asymmetric Effects of Government Spending Innovations

	Panel A: Least Square Estimates						Panel B: 3 Stage Least Square Estimates					
	The sum of the coefficients of the pos_t terms, with lag values 1 to 4	The sum of the coefficients of the neg_t terms, with lag values 1 to 4	The difference of sums	Wald test of pos_t terms	Wald test of neg_t terms	Wald test of the model	The sum of the coefficients of the pos_t terms, with lag values 1 to 4	The sum of the coefficients of the neg_t terms, with lag values 1 to 4	The difference of sums	Wald test of post terms	Wald test of negt terms	Wald test of the model
TOTAL PRIVATE CONSUMPTION	-14.621	-50.400	35.779	0.607	0.128	0.187	-26.312	-38.043	11.732	0.511	0.219	0.323
Durable goods	-307.427(**)	-188.340	119.087(**)	0.019	0.169	0.043	-380.705	-513.131(*)	132.426(*)	0.152	0.088	0.088
Semi-durable goods	-16.703	-265.791(*)	249.088	0.911	0.085	0.224	369.039(**)	-214.803	583.842	0.041	0.208	0.570
Public sector	-73.082	-170.846	97.764	0.704	0.379	0.428	-229.628	-19.623	-210.005	0.217	0.934	0.490
Public construction	-174.862	-106.831	-68.031	0.229	0.677	0.386	-381.975	35.392	-417.368	0.279	0.946	0.468
Private sector	-385.454(**)	-203.043(*)	182.410(**)	0.020	0.071	0.011	-168.345	79.596	-247.941	0.631	0.853	0.895
Machinery	-414.978	-25.325	-389.653	0.112	0.895	0.122	-2102.093	734.167	-2836.260	0.440	0.559	0.475
Private construction	23.845	27.349	-3.504	0.567	0.650	0.553	23.622	46.755	-23.133	0.586	0.696	0.655
TOTAL PRIVATE INVESTMENT	266.238	-81.194	347.432	0.117	0.682	0.530	444.726(*)	-150.606	595.333	0.063	0.416	0.450
Mining and quarrying	16.408	55.239	-38.831	0.827	0.533	0.604	-27.861	-139.665	111.804	0.864	0.748	0.764
Manufacturing	-30.969	-34.204	3.235	0.379	0.435	0.367	1.107	34.947	-33.840	0.967	0.327	0.531
Industrial total	-40.718	-18.616	-22.101	0.420	0.754	0.545	-61.596	221.498	-283.094	0.914	0.615	0.845
Construction industry	30.734	-19.387	50.120	0.434	0.695	0.880	69.505	38.520	30.985	0.359	0.655	0.473
Wholesale, retail	2.915	72.605	-69.690	0.939	0.491	0.561	10.647	136.183	-125.536	0.847	0.354	0.454
WPI	-53.165	-47.191	-5.974	0.148	0.270	0.115	4.006	-13.270	17.276	0.943	0.759	0.919
Real GDP	-33.202	-57.849(*)	24.646(**)	0.193	0.052	0.039	3.295	38.834(**)	-35.539(*)	0.140	0.030	0.052

* Indicates significance at the 10% level.

** Indicates significance at the 5% level.

Note: The first column of both of the panels is multiplied by 100 for simplicity.

TABLE 2: The Asymmetric Effects of Treasury Interest Rate Innovations

	Panel A: Least Square Estimates						Panel B: 3 Stage Least Square Estimates					
	The sum of the coefficients of the pos_t terms, with lag values 1 to 4	The sum of the coefficients of the neg_t terms, with lag values 1 to 4	The difference of sums	Wald test of pos_t terms	Wald test of neg_t terms	Wald test of the model	The sum of the coefficients of the pos_t terms, with lag values 1 to 4	The sum of the coefficients of the neg_t terms, with lag values 1 to 4	The difference of sums	Wald test of pos_t terms	Wald test of neg_t terms	Wald test of the model
TOTAL PRIVATE CONSUMPTION	5.446(**)	3.180	2.266(**)	0.028	0.101	0.047	4.281(**)	1.708(*)	2.574(**)	0.000	0.088	0.003
Durable goods	3.957	2.666	1.292	0.307	0.239	0.162	7.367(**)	2.010(*)	5.357(**)	0.001	0.084	0.000
Semi-durable goods	2.038	1.022	1.016	0.934	0.913	0.927	6.950	2.509	4.441	0.167	0.223	0.176
Public sector	-2.483	-1.170	-1.313	0.732	0.853	0.706	-10.598(*)	12.797(*)	-23.396	0.074	0.090	0.744
Public construction	-2.177	-0.046	-2.131	0.876	0.996	0.901	-1.246	8.516(*)	-9.762	0.786	0.052	0.287
Private sector	8.853(*)	6.821(**)	2.032(**)	0.069	0.032	0.043	8.685(**)	7.163(**)	1.523(**)	0.000	0.000	0.000
Machinery	-8.262	-9.995	1.733	0.629	0.610	0.615	-14.226(**)	-16.348(**)	2.122(**)	0.021	0.018	0.019
Private construction	4.193(*)	3.122(**)	1.071(**)	0.057	0.009	0.021	6.186(**)	3.727(**)	2.460(**)	0.000	0.000	0.000
TOTAL PRIVATE INVESTMENT	-40.053	-37.204	-2.849	0.199	0.127	0.158	-17.654	-8.875	-8.779	0.316	0.586	0.426
Mining and quarrying	-4.174	-2.442	-1.732	0.410	0.604	0.413	-5.620(*)	-1.748	-3.871(**)	0.078	0.372	0.009
Manufacturing	-2.387	-0.036	-2.351	0.185	0.984	0.442	-3.585(**)	-2.371(**)	-1.214(**)	0.000	0.026	0.001
Industrial total	0.235	-0.090	0.325	0.325	0.386	0.597	-1.035(**)	-0.018(**)	-1.018(**)	0.000	0.015	0.023
Construction industry	-0.085	0.720	-0.805	0.976	0.645	0.871	0.770	0.798(*)	-0.028	0.389	0.092	0.196
Wholesale, retail	-1.889	0.701	-2.590	0.325	0.386	0.597	-2.139(**)	0.592(**)	-2.730(**)	0.000	0.015	0.023
WPI	-0.939	-0.538	-0.401	0.823	0.869	0.841	0.416	1.175	-0.760	0.790	0.416	0.590
Real GDP	1.262	0.659	0.604	0.606	0.731	0.654	0.627	-0.144	0.772	0.464	0.856	0.766

* Indicates significance at the 10% level.

** Indicates significance at the 5% level.

Note: The first column of both of the panels is multiplied by 100 for simplicity.

Appendix:

The particular model we estimated in this paper is:

$$\Delta \ln Y = \alpha_0 + \sum_{i=1}^3 \alpha_i D_{it} + \alpha_2 D94_t + \alpha_3 D00_t + \sum_{i=1}^4 \alpha_{4i} R_{t-i} + \sum_{i=1}^4 \alpha_{5i} Y_{t-i} + \sum_{i=1}^4 \alpha_{6i} P_{t-i} + (A1)$$

$$+ \sum_{i=1}^4 \alpha_{7i} C_{t-i} + \sum_{i=1}^4 \alpha_{8i} I_{t-i} + \sum_{i=1}^4 \alpha_{9i} G_{t-i} + \sum_{i=1}^4 \alpha_{10i} pos_{t-i} + \sum_{i=1}^4 \alpha_{11i} neg_{t-i} + \varepsilon_{yt}$$

$$\Delta \ln P = \beta_0 + \sum_{i=1}^3 \beta_i D_{it} + \beta_2 D94_t + \beta_3 D00_t + \sum_{i=1}^4 \beta_{4i} R_{t-i} + \sum_{i=1}^4 \beta_{5i} Y_{t-i} + \sum_{i=1}^4 \beta_{6i} P_{t-i} + (A2)$$

$$+ \sum_{i=1}^4 \beta_{7i} C_{t-i} + \sum_{i=1}^4 \beta_{8i} I_{t-i} + \sum_{i=1}^4 \beta_{9i} G_{t-i} + \sum_{i=1}^4 \beta_{10i} pos_{t-i} + \sum_{i=1}^4 \beta_{11i} neg_{t-i} + \varepsilon_{pt}$$

$$\Delta \ln C = \gamma_0 + \sum_{i=1}^3 \gamma_i D_{it} + \gamma_2 D94_t + \gamma_3 D00_t + \sum_{i=1}^4 \gamma_{4i} R_{t-i} + \sum_{i=1}^4 \gamma_{5i} Y_{t-i} + \sum_{i=1}^4 \gamma_{6i} P_{t-i} + (A3)$$

$$+ \sum_{i=1}^4 \gamma_{7i} C_{t-i} + \sum_{i=1}^4 \gamma_{8i} I_{t-i} + \sum_{i=1}^4 \gamma_{9i} G_{t-i} + \sum_{i=1}^4 \gamma_{10i} pos_{t-i} + \sum_{i=1}^4 \gamma_{11i} neg_{t-i} + \varepsilon_{ct}$$

$$\Delta \ln I = \theta_0 + \sum_{i=1}^3 \theta_i D_{it} + \theta_2 D94_t + \theta_3 D00_t + \sum_{i=1}^4 \theta_{4i} R_{t-i} + \sum_{i=1}^4 \theta_{5i} Y_{t-i} + \sum_{i=1}^4 \theta_{6i} P_{t-i} + (A4)$$

$$+ \sum_{i=1}^4 \theta_{7i} C_{t-i} + \sum_{i=1}^4 \theta_{8i} I_{t-i} + \sum_{i=1}^4 \theta_{9i} G_{t-i} + \sum_{i=1}^4 \theta_{10i} pos_{t-i} + \sum_{i=1}^4 \theta_{11i} neg_{t-i} + \varepsilon_{it}$$

$\Delta \ln Y_t$: Logarithmic first difference of real GDP.

$\Delta \ln P_t$: Logarithmic first difference of wholesale price index.

$\Delta \ln C_t$: Logarithmic first difference of real total private consumption.

$\Delta \ln I_t$: Logarithmic first difference of real total private investment.

$\Delta \ln G_t$: Logarithmic first difference of government spending.

R_t : 3-month treasury bill rate

D_{it} : Dummy variable for seasonal effects.

$D94_t$: Dummy variable for 1994 crisis occurred in the second quarter.

$D00_t$: Dummy variable for 2000 crisis occurred in the fourth quarter.

pos_t : Positive government shocks.

neg_t : Negative government shocks.