Macroeconomic effects of public investment spending: the case of Italy analysed with a post-Keynesian structural model

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Abstract

The debate on the National Recovery and Resilience Plan (NRRP) has revived the interest for the role of public investment in fostering economic growth, after decades of austerity policies. This paper presents an analysis on the macroeconomic effects of public investment spending in the Italian economy, and determining the value of the Keynesian multiplier, through a structural macroeconometric model. In particular, we follow the post-Keynesian theoretical approach, which takes into account the principle of effective demand in explaining the long-run level of production, where the supply side acts only as a closure of the model through the constraint of the labour force, which, if totally absorbed, determines the potential output of the economy. The empirical model presents 79 equations, of which 20 are stochastic, designed for medium and long-run analysis - on a sample of annual data from 1960 to 2019 - and is built using econometric techniques of cointegration and error correction, which consider not only the relationship between the variables, but also the presence of possible structural breaks in the estimation of long-run parameters. From the policy simulations carried out, we find the positive and permanent effects that public investment spending exerts directly and indirectly on labour productivity, employment, real wages and economic activity, because of the role played by increase in aggregate demand.

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Keywords: Model construction and estimation; Simulation methods; Quantitative policy modelling; post-Keynesian model; Fiscal policy; Public investment; Open economy macroeconomics; Forecasting and simulation.

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