

## Chapter 29

# The Effect of Defense Expenditures and Peace on Economic Growth: Evidence From European Union Transition Economies

**Mahmut Unsal Sasmaz**

*Usak University, Turkey*

**Abdullah Zeybekoglu**

*Usak University, Turkey*

### ABSTRACT

*Throughout history countries have tried to gain power in order to get advantages for the issues such as providing territorial integrity, social security and internal and external security. As a result of this power-gaining race, defense expenditures had a significant place in countries' economies. In its broad sense, defense expenditures are defined as the share reserved from the national income for the country's defense in order to provide internal and external security of the state and maintain the order and safety of the community. The size of defense expenditures varies from country to country for various reasons. In this study the effect of defense expenditures and peace as a global public good on economic growth was analyzed in 11 European Union countries (transition economies) between 2007 and 2017 with the help of panel data analysis. As a result of the study it was found out that there was a positive relationship between economic growth and defense expenditures. However, a negative relationship was identified between economic growth and peace level.*

## INTRODUCTION

It is a difficult process to identify the importance of human needs. Because to what extent human needs are based on individual benefits varies from one country to another. Although the importance of these needs varies from person to person, due to these differences, the needs such as eating, drinking, dressing and shelter in general are very important. Besides these needs, the basic needs of people are the ones for living in confidence. People, depending on their desire for living securely and freely, behave very careful about protecting territorial integrity of their state. This necessitates a series of expenditures by states for their border security, territorial integrity and sovereignty, whatever their economic condition is. These expenditures are defined as defense expenditures.

Along with the increases in defense expenditures following World War II defense service was accepted as the most important task of a state and it was considered as a public good. The state undertakes various expenses in order to fulfill the task of defense service. Considering that the share allocated to defense service in terms of covering the related costs has an effect on the country's budget and real economic variables, the economic aspect of defense service is considered as an important topic of discussion in the literature. The relationship between defense expenditures and economic growth is the focus of discussions and different views.

There are two different approaches expressing the relationship between defense expenditures and economic growth. These are Military Keynesian Approach and Neo-Classical Theoretical Approach (Giray, 2004: 189).

According to Military Keynesian Approach, the effect of defense expenditures on economic growth is based on positive externalities. As the defense expenditures increase, they may have a significant multiplier effect. The demand created following defense expenditures increases the capacity use and enlarges the output level. As a conclusion defense expenditures increase the capital gain rate, investment and growth (Looney, 1994: 46-47).

Since the Neo-Classical Theoretical Approach often considers defense expenditures as non-productive, there are wide range of discussions on defense expenditures due to the variety of expenditures that can be carried out instead of such expenditures and the benefits to be obtained as a result of these expenditures. It is suggested that transferring the resources that can be allocated to economic activities to defense expenditures would prevent the economic growth (Gökbunar, 2004: 161).

With reference to these discussions the relationship between defense expenditures and peace and economic growth was analyzed in this study. Since peace is a global good, the domestic defense expenditures of states will be limited. Because countries are easily affected by each other in a globalizing World, it is necessary to make material and nonmaterial efforts for world peace because defense expenditures of states for themselves are not sufficient.

In this study the effect of defense expenditures and peace on economic growth was analyzed in transition economies including 11 European Union countries (EU) between 2007 and 2017 by using panel data analysis. These 11 countries are Bulgaria, Czechia, Estonia, Croatia, Hungary, Poland, Slovakia, Slovenia, Romania, Latvia and Lithuania which are in the former Socialist block. In the analysis empirical results were obtained through cross sectional dependency test, panel root test (Pesaran, 2007; Pesaran & Yamagata; 2008) homogeneity test, panel cointegration test (Westerlund & Edgerton (2007) and panel FMOLS test, panel causality test (Emirmahmutoğlu & Köse, 2011). A general evaluation was made depending on the findings in conclusion section of the study.

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