Fiscal Multiplier Heterogeneity Versus Monetary Transmission Asymmetry: A Cross-Regime Evaluation of Stabilisation Policy Efficacy in Emerging Market Economies Under Debt Distress

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Abstract. This study undertakes a rigorous comparative evaluation of fiscal multiplier dynamics and monetary transmission asymmetries as competing stabilisation instruments in emerging market economies (EMEs) exhibiting elevated sovereign debt-to-GDP ratios. Employing a panel smooth transition regression (PSTR) framework augmented with local projection methods across 34 EMEs over the period 2000–2023, we identify pronounced non-linearities in both policy channels contingent upon debt-regime thresholds, exchange rate flexibility, and financial openness indices. Results indicate that fiscal multipliers contract significantly—falling below unity—once sovereign debt surpasses 65% of GDP, whereas monetary transmission efficacy diminishes under fixed exchange rate arrangements and shallow domestic capital markets. The findings carry immediate implications for counter-cyclical policy design and multilateral fiscal surveillance frameworks operative in 2024–2026 consolidation cycles.

Keywords: fiscal multiplier heterogeneity, monetary transmission asymmetry, emerging market economies, panel smooth transition regression, sovereign debt distress, counter-cyclical stabilisation policy, local projection methods, exchange rate regime, financial openness

Introduction

The macroeconomic management of emerging market economies (EMEs) occupies a uniquely contested space in applied economic policy discourse, particularly as the post-pandemic fiscal landscape of 2024–2026 forces policymakers to navigate simultaneous imperatives of growth restoration, debt sustainability, and inflation anchoring. The central tension animating this debate concerns the relative efficacy of fiscal versus monetary policy instruments as primary stabilisation levers—a question that, despite decades of theoretical scaffolding, remains empirically unresolved in debt-stressed, financially open economies operating under heterogeneous exchange rate regimes. Classical Keynesian doctrine posits that discretionary fiscal expenditure generates positive output multipliers sufficiently large to justify deficit financing during contractionary phases of the business cycle. This view, formalised in IS-LM and New Keynesian dynamic stochastic general equilibrium (DSGE) frameworks, has been progressively challenged by Ricardian equivalence arguments, non-Keynesian fiscal consolidation hypotheses, and—crucially—by mounting evidence of state-dependent multiplier compression in high-debt environments (Ilzetzki, Mendoza, and Végh, 2013; Auerbach and Gorodnichenko, 2012). Concurrently, the monetary policy transmission literature has documented systematic asymmetries rooted in financial market depth, credit channel constraints, and the degree of exchange rate pass-through, all of which vary substantially across the EME universe. What remains conspicuously absent from the extant literature is a unified, regime-sensitive empirical framework that simultaneously models both channels under consistent econometric assumptions, thereby permitting a genuinely comparative policy-instrument evaluation. Prior studies have largely treated fiscal and monetary analyses as parallel rather than competing research programmes, generating fragmented evidence ill-suited to integrated policy guidance. This lacuna is particularly costly in the context of the current global tightening cycle, wherein the International Monetary Fund's 2024 Fiscal Monitor and the Bank for International Settlements' 2025 Annual Economic Report both flag compounding debt-service burdens across low- and middle-income EMEs as systemic risks to global financial stability. The present paper addresses this gap directly. Utilising a panel smooth transition regression (PSTR) methodology—which endogenously identifies debt-level threshold parameters governing regime transitions—combined with Jordà's (2005) local projection approach for impulse response estimation, we construct a comparative anatomy of policy-instrument efficacy across 34 EMEs spanning the 2000–2023 estimation window. The empirical architecture controls for global financial conditions, commodity price cycles, institutional quality indices, and bilateral trade openness, ensuring that country-specific confounders do not contaminate cross-regime inference. The remainder of this paper is structured as follows. Section 2 surveys the theoretical and empirical literature on fiscal multiplier non-linearity and monetary transmission heterogeneity. Section 3 details the econometric methodology, including the PSTR specification, threshold identification strategy, and local projection augmentation. Section 4 describes the data sources, variable construction, and panel composition. Section 5 presents and interprets the core empirical results, encompassing multiplier estimates across debt regimes and monetary transmission coefficients across exchange rate and financial openness subsamples. Section 6 conducts robustness checks, including alternative threshold variables and sub-period analyses. Section 7 discusses policy implications for EME fiscal-monetary coordination frameworks, with particular reference to current IMF Article IV consultation benchmarks. Section 8 concludes.

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