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SINERGY MONETARY AND FISCAL POLICY IN THE FUNCTION ECONOMIC GROWTH REPUBLIC OF SERBIA

Apstract

The paper points to the interaction and mutual connection of monetary and fiscal policy and their synergetic effect on economic growth. Regardless of the fact that both policies are independent in the implementation of their goals and apply different measures and instruments, they are not at odds in shaping economic policy, on the contrary, they complement each other and jointly contribute to ensuring macroeconomic stability and economic growth. In the Republic of Serbia, the joint effect of monetary and fiscal policy measures is reflected in the provision of macroeconomic and price stability and the reduction of public debt and a stable budget, which are key prerequisites for long-term economic growth.

Key words: *monetary policy, fiscal policy, macroeconomic stability, economic growth*

JEL classification:*E60, E63, G28*

СИНЕРГИЈА МОНЕТАРНЕ И ФИСКАЛНЕ ПОЛИТИКЕ У ФУНКЦИЈИ ПРИВРЕДНОГ РАСТА РЕПУБЛИКЕ СРБИЈЕ

Сажетак

У раду се указује на интракцију и међусобну повезаност монетарне и фискалне политике и њихов синергетски ефекат на привредни раст. Без обзира што су обе политике независне у спровођењу својих циљева и примењују различите мере и инструменте, оне нису у супротности у обликовању економске политике, напротив оне допуњују једна другу и заједнички доприносе обезбеђењу макроеконмске стабилности и привредном расту. У Р. Србији заједнички ефекат мера монетарне и фискалне политике,

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се огледа у обезбеђењу макроеконмске и ценовне стабилности и смањење јавног дуга и стабилног буџета, што су клућни предуслови за дугорочни привредни раст.

Кључне речи: монетарна политика, фискална политика, макроекономска стабилност, привредни раст

Introduction

Every economic crisis indicates the necessity to review the basic postulates on which the management of monetary and fiscal policy is based. The development of monetary policy is mostly based on the modification of the strategic framework, i.e. flexible inflation targeting, through the active role of the central bank. Negative externalities, which are more and more pronounced after every economic crisis, represent one of the reasons for establishing the coordination of monetary and fiscal policy. „Coordination between monetary and fiscal authorities leads to better performance. One of the most important goals of macroeconomic policy is the achievement of sustainable economic growth, with the existence of price stability and foreign trade balance" (Laurens & Piedra 1998). In conducting economic, and therefore monetary and fiscal policy, a very important issue is the relationship to the public debt of the national economy. Public debt, in addition to being used to finance the budget deficit, is also an instrument that has its own monetary and fiscal function with a strong impact on the country's economic development. The objectives of monetary policy as an instrument of economic policy are short-term or current monetary objectives, and long-term or strategic monetary objectives, which are also basic objectives.

„Monetary policy measures had a primary role related to the correction of interest rates. Given that the coordination of fiscal and monetary measures is very important for macroeconomic stability, instead of economic policy makers using monetary policy to achieve price stability and fight inflation, Wrey starts from the position that the role of monetary policy is to determine short-term interest rates, while fiscal policy is expected to stabilize the value of the currency, which is important for maintaining a competitive advantage in the foreign market" (Wrey, 1998).

The development fiscal policy with numerous measures and instruments available to the holders of this policy represents a significant mechanism for encouraging economic development. The theoretical explanation of the impact of fiscal and monetary policy on the stimulation of economic activity depends on the model taken into consideration, which depends on the theoretical direction on the basis of which it was developed. „One of the most important goals of macroeconomic policy is the achievement of sustainable economic growth, with the existence of price stability and foreign trade balance" (Laurens & Piedra, 1998).

Economic growth and macroeconomic stability

Macroeconomic stability is a significant prerequisite for stable long-term economic growth. The key policies of macroeconomic stability are monetary and fiscal policies whose goals and activities are interconnected and conditioned by a synergistic effect on economic growth. In fact, it can be said that both policies, regardless of their different goals and the different instruments they use, are not in conflict, on the contrary, they complement each other, especially in the implementation of the adopted economic policy. In particular, their synergetic effect is reflected in the realization of fundamental economic and political goals, whose coordinated activity has a positive impact on economic growth.

Although monetary and fiscal policy are conducted by independent bodies, they are interdependent, so it is crucial to achieve a consistent framework to avoid inconsistency. Lack of coordination between monetary and fiscal authorities leads to poor economic results. Inadequate direction of one policy is a limitation for another policy and is unsustainable in the long term.

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„Fiscal policy, through its transmission mechanism, transmits impulses in the economy that cause discretionary government measures aimed at increasing or contracting economic activity" (Gnjatović, Grbić, 2009). By means of its instruments, collecting public revenues (taxes) and executing public expenditures, fiscal policy acts through transmission channels on changes in the relations of basic macroeconomic aggregates and on the behavior of economic entities. The effect of the transmission mechanism of fiscal policy is manifested through the reduction of tax rates as a measure of restrictive economic policy, which the government wants to influence by curbing excessive demand and consumption.

Synergy of monetary and fiscal policies in the Republic of Serbia and their effect on economic growth

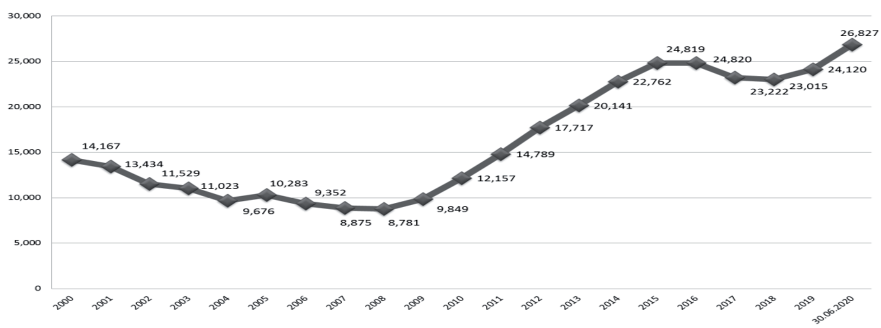
The success of the monetary policy, which is based on the independence of the central bank, is the coordination with the fiscal authorities. Sustainable economic growth, price stability and foreign trade balance are the most important goals of macroeconomic policy. In order to achieve economic growth, it is necessary to harmonize monetary and fiscal policies. The lack of coordination between the monetary and fixed authorities leads to an increase in interest rates, encourages inflation and ultimately threatens economic growth. The issue of public debt is of great importance for conducting economic policy. In addition to financing the budget deficit, public debt has a fiscal and monetary impact on the overall economic development of the national economy.

The presence and increase of public debt are not only the result of financial difficulties but also often occur as a consequence of the extraordinary needs of the state and due to changes like sources of public revenue. As an instrument of economic policy, public debt has both monetary and fiscal functions. "Depending on whether it is the borrowing of the state in domestic or foreign currency, financial or non-financial sector, public debt directly affects monetary aggregates, the amount of money in circulation and the value of the national currency." It should be emphasized that one of the most important instruments of monetary policy is based on the public debt, i.e. on the purchase and sale of government bonds, which are open market operations used by central banks to regulate the amount of money in circulation" (Kvrgić, Ćolić, Vujović, 2011).

Financing of the state on the domestic market has a disadvantage compared to the foreign market because it is crowding out private investments, the so-called crowding out effect. If there is a large increase in public debt, the demand for loans also increases, which ultimately increases interest rates. The rise in interest rates affects the fall in the prices of securities, which reduces private investment. Borrowing of the state by the private sector or companies leads only to the effect of crowding out investments, while if the state borrows abroad, it puts pressure on the exchange rate of the domestic currency. In such a situation, the Central Bank, through its monetary policy, takes measures to sterilize foreign currency inflows to prevent price increases and the appearance of illiquidity. State borrowing by commercial banks has no significant impact on monetary policy, because in this case there is a redistribution of funds in the bank's portfolio, as they will lend less to the population, and direct more of the money to loans to the state.

Fiscal policy affects monetary policy, directly and indirectly. Financing the budget deficit exclusively through market instruments leads to crowding out of the private sector. Expansive fiscal policy undermines price stability and neutralizes the effects of monetary policy. A more direct influence of fiscal policy on monetary policy is through the influence of indirect taxes on the price level and inflation. If indirect taxes (sales tax, value added tax) are increased, an inflationary spiral is triggered through the rise in prices, which encourages the growth of inflation and inflationary expectations. This further destabilizes movements in the bond market and the foreign exchange market, leading to the collapse of monetary policy. Monetary and fiscal policies have a positive effect on each other, if they reduce the risk premium found in the structure of long-term interest rates. Monetary authorities should inform fiscal authorities about the effects of government borrowing on the achievement of monetary goals.

Graph no. 1: Growth dynamics of the public debt of the Republic of Serbia



Processing by the author based on data from the National Bank of the Republic of Serbia

Chart 1 shows three periods in the growth dynamics of the public debt of the Republic of Serbia. The first period from 2001-2008 consists of three short sub-periods, the first of which covers the period 2001-2002. which is characterized by the negative value of the public debt, which amounted to as much as -30% of GDP, primarily due to the write-off of debts by the London and Paris Club of Creditors. At the beginning of 2003, there is a slight stabilization, which is also reflected in the further period until 2005, so that during 2006 and 2007 there will be an increase in the structural fiscal deficit by about 1.7% of GDP due to the increase in wages in the public sector and the reduction of taxes on earnings. Period 2008-2014. characterized by accelerated growth of public debt. The 2014-2017 period includes fiscal consolidation, which was based on the reduction of nominal pensions (5%) and salaries in the public sector (10%). Graph 1 shows that changes in public debt are characterized by a slight negative linear trend, which implies that the Government of the Republic of Serbia managed to stop the further growth of public debt, stabilize its level below 70% of GDP, and ensure a gradual reduction of public debt. Noticeable decrease in performances during 2017. At the end of that calendar year, the public debt fell to 57.9%, in contrast to the previous year, when it amounted to 67.8%. of GDP. The downward trend continues in the next two years, at the end of 2018 it amounted to 53.7% and in the following year 2019 it was only 52.8% of the total GDP of the Republic of Serbia. In 2020, the positive trend is interrupted and the public debt begins to grow again, so that on 30.06. In 2020, it amounted to 57.3% of GDP or 26.827 billion euros in absolute terms.

The conclusion that emerges is that public debt cannot establish a positive or negative correlation with development, because public debt cannot be an instrument to stimulate economic growth. The aspiration of monetary and fiscal policy makers is to encourage economic activity. There is no universal model for the application of measures and instruments of monetary and fiscal policy, which will ensure macroeconomic stability. The creators of the economic policy of each national economy should define the individual directions of movement of the transmission channels of monetary and fiscal policy depending on the disturbances the economy is facing. An adequately formed fiscal-monetary model should be harmonized with other specific goals of economic policy in terms of balance sheet balance, stability of the national currency, and all with the aim of establishing a general balance. Due to the fact that monetary policy measures cannot independently act on the financial sector, just as fiscal policy measures cannot ensure a complete effect on the real sector, their coordination is necessary.

Conclusion

In the modern economy, which is burdened with many problems, in order to achieve and maintain macroeconomic stability and discipline, adequate synchronization of monetary and fiscal policy measures and their implementation in the entire economic policy management system is necessary. Due to the existence of unproductive economies, unemployment, and the increase in the public debt rate, great attention is paid to the interaction of monetary and fiscal policy measures. As in countries all over the world, there is no universal model of conducting economic policy in the Serbian economy.

A significant problem of underdeveloped economies is excessive consumption, which generates an increase in imports, inflation, balance of payments deficit, debt and low investment rate. In such conditions, insisting on short-term stability (inflation and exchange rate) would only increase the risks of collapse of the economic system. Coordination and cooperation of monetary and fiscal policy, in the direction of forming a more efficient and export-oriented economy, is a prerequisite for growth and establishing balance. Fiscal policy can help the recovery of the economy, but to overcome all problems, budgetary discipline is necessary, which will control public finances. Monetary policy, on the other hand, gives results through the monitoring of public debt, which manifests itself through inflationary pressure, by limiting available liquid assets.

In the area of economic policy, the transition to a new growth model would motivate economic actors. Investment and export orientation, as well as public debt regulation, should be supported by coordination measures of monetary and fiscal policy and other key sectoral policies. Within the framework of fiscal policy, tax policy reforms are necessary in the direction of encouraging GDP growth and production growth. Mitigating the negative tendencies of macroeconomic variables cannot be achieved with just one measure or just one policy, which is why coordination and cooperation of monetary and fiscal policy is inevitable, in order to act in sync.

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