FISCAL MECHANISM OF MACROECONOMIC SUSTAINABILITY

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Abstract. Sustainable fiscal policy is an important element of macroeconomic balance as an important regulatory center of any economic system. The presented article is devoted to the issues of rational budgetary policy from the point of view of macroeconomic stability. Here are the ways to solve the problem.

Keywords: Procyclical policy, countercyclical policy, result budgeting, budget deficit.

The mechanism of the state budget including such economic categories as taxes and the public expenditures, not only smoothes economic inequalities, also at the same time stimulates the economic relations and defines the key development directions of national economy.

State budget with sustainable development trends as the main regulating motor of any economic system, became an important element of macroeconomic balance in the modern countries of the world.

Currently, leading research institutes of the world considering recent global trends intensively analyze problems of fiscal stability, including questions of sustainable budget deficit.

Such priority subjects of public finances as debt markets of the state, plans of fiscal consolidation, short-term and medium-term fiscal forecasts, an assessment of fiscal risks, selective questions of taxes and expenses are studied, fiscal consequences of the global financial crisis being the most hot topic of the last years, also the political framework which is even more strengthening public finances are estimated.
The analysis of the tendencies which are taking place on the global arena, shows that, now the fiscal policy of national economies is gradually redirected from maintenance of gross demand to huge reduction of the budget deficits.

Major factor in reduction of budget deficit in the developed countries is reduction of financial transfers to the financial sector.

In Developing Economies, there is a recovery tendency of economic activity, reduction of the budget deficit by the ways of tough fiscal policy and low interest payments.

Despite of considerable difference between the countries with low income, gradual reductions of the budget deficit mainly comes from tax revenues and grants.

But, in the oil countries the fiscal policy and macro-fiscal situation depends on the export price for oil. So, the rise in oil prices and policy toughening in some countries helps to fiscal balance.

The policy of fiscal consolidation should go deep in the developed countries generally for improvement of the macro-fiscal indicators and maintenance of economic activity in the long-term. At the same time, the consolidation volume between these economic systems widely differs depending on the budgetary balances and market pressure. But, the general approach is that, slow reduction of the budgetary deficiency is aimed by the purpose at slowly reduction of economic activity.

Recently at leading analytical and research institutes there are two opposite approaches. According to the first approach that, will toughen the budgetary policy irrationally, at unemployment preservation at stable level toughening of the budgetary policy is considered irrational. According to other approach, gives reason that, during the period when level of a public debt is great, fiscal consolidation is inevitable.

In fact, both approaches have a strong theoretical and empirical argument. So, in inadequate market conditions volume reduction of the budgetary deficiency is represented very risky. But at all this, for both reasons, the too long staying of fiscal regulation is also wrong. First, market subjects may lose trust to the state in respect of performance of debts by it. Secondly, big budget deficit increases a public debt that in turn negatively affects economic growth.

On materials of the International Monetary Fund, one of leading research institutes, in the developed countries the increase in a public debt at 10% reduces growth of gross domestic product by 0,15%. According to this source, refusal from or adjournment by the countries of fiscal consolidation policy during the global crisis, is considered the most rational decision. Along with it, for a start, the government should apply quite tough policy to create confidence at economic agents in accurate implementation of the future plans.

In the economy facing such political dilemmas as fiscal consolidation or fiscal incentive, tendencies though insignificant restoration of economic growth, namely the beginning of
revival of economy create possibilities for rendering, let even in limited scale, the direct help to the financial sector.

The strong political framework of economy with the low income creates possibility for internal financing of big fiscal deficits, without harming to financial stability. After the crisis beginning weakening of desire of investors to assume risk leads to reduction of debt terms of the government. Thus, stabilization of the market and increase of trust of investors leads to extension of debt terms of the government that reduces a share of short-term debts in total amount.

Reaction of the market to fiscal changes finds reflection in percentage rates and profitability of the government short-term obligations. This reaction mainly based on riskiness level of the countries. In economies with developed financial markets interest rate reduction of the government debt securities occurs a low inflationary expectation, increase of investors’ interests and positive expectations of economic growth.

In some economies increase of investors demand for the state debt securities is closely connected with full restoration of the banking sector’s stability. Thus, in a similar case investors perceive the state securities as assets with low risk level and interested in them for quality improvement of the investment portfolios.

Fiscal consolidation plans of majority countries on ensuring stability of fiscal sector and budget deficit generally cover the medium-term period, however in some countries this term relatively prolonged. Despite distinctions in market pressures, as a whole, the volume and speed of the declared consolidation provides balance between reduction of the budget deficit and maintenance of economic growth.

In recipes of fiscal stability the most part of plans provides expenditure consolidation and other part the revenue or mixed consolidation. Researches and experience of the past show that the expenditure consolidation, accompanied with monetary incentive, represents a small damage for economic growth. But, only one consolidation hasn’t enough for success. Therefore to reach goals is possible, in parallel from consolidations having realized fiscal and structural reforms, without rendering negative influence on economic growth.

Analyses Show That, in this practice the share of expenditure consolidation in total amount of consolidation makes at least 60%.

To achieve sustainable budget deficit, reduction of the budgetary expenses should provide reduction of salaries, volume of public services and social transfers. Increase of the budgetary income in these purposes should be based on increase in direct taxes. Individual and corporate income tax, also social insurance fees make 50% of the total share of revenue consolidation. Increase of the VAT and excises makes 1/3 introduced methods of revenue increasing.

Structural reforms in economy have a big importance for financing of the budget deficit which was far beyond the sustainable level in the midterm. Gradual transfer of weight of some
expenditure directions from the state budget creates possibilities for mobilization of fiscal resources on more important needs (for example, expenses for education and health).

With emergence of economic cataclysms on a global scale, also, strengthening of their pressure force, political institutes recommend state regulation of economy, in particular strengthening of fiscal and budgetary institutes. In support of this thought we may show application of a rule of the constitutional structural budgetary balance in Germany and formation of Management of the Budgetary Responsibility of Great Britain.

Strengthening of a fiscal arsenal of the country with a view of ensuring stability not only serves the purpose of increase of tax collecting and expansion of government expenses. In parallel these reforms also promote maintenance by consolidation process. For example, here it is possible to refer strengthening and improvement of the fiscal reporting, forecasting and risk management in the countries “G20” recently.

Achievement of budget deficit reduction to sustainable level for the short and medium-term period doesn't speak unequivocally about perfection of fiscal policy of the government. Here some factors can play important role. Firstly, the consolidation methods can be reflected inexact and not detailed. Secondly, wide reforms for reduction of expenses can be not defined in the medium and long-term period, despite of planned reforms in social sectors for the short-term period. Thirdly, refusing the obligations for volume of public debts by the government for the long-term period will break sustainability of public debts that can result unsustainable budget deficit at the next stage.

Assessment of fiscal risks is one of important elements of fiscal sector’s sustainability, of which the sustainability of budget deficit. It depends on three factors:
- A long-term fiscal orientation, that is solvency for the long-term period;
- Possible negative shocks which can arise round a fiscal orientation;
- Sensitivity of the market.

Despite an initiative of fiscal consolidation with a view of the fiscal sustainability of the countries, in many cases level of public debt continues grows in the medium-term period. As, reduction of government debts and their sustainability level depends on two factors:

First, the fiscal consolidation reforms should be for the long-term;
Secondly, the government should have strong political will.

Lessons of modern global practice show that when the governments don't take the obligation for reduction of public debts before fiscal consolidation, at a stage after achievement of relative stability, show smaller interest in reduction of state expenses not to lose the political trust.

Reforms of tax and budgetary expenses are the following important element of ensuring of fiscal deficit sustainability. Carrying out the fiscal reforms directed on strengthening of public finances, without rendering of negative influence on economic growth is the most important thesis here. Thus, without watching close similarity of fiscal results of the reforms
which have been carried out on several different scenarios, from the economic growth point of view these scenarios can considerably differ.

The assessment of tax policy adequacy of rather financial sector is one of conditions of fiscal stability problem. Global crises of the last times show that, some developed countries for compensation of the damage put with crisis, started to raise temporary taxes on financial sector. For example, Great Britain has an opportunity to raise funds for the sum of 1.3 billion pound sterling after 50% taxation to bonuses of financial sector. In some countries were created the financial stability funds for the prevention of potential crises, including for ensuring requirement of economy for the financial help or were created financial stability funds for financing of potential damages.

Global research institutes suggest taxation on obligations of financial institutions (except for the insured deposits, insurance reserves) for decrease in system risks of financial sector in economy and financings of future financial requirements. Also, are offered tax reforms on payment of taxes in funds financial institutions at differential rates, depending on system risks of each institute. Estimates of IMF show that on the average taxation on 0.1% allows to collect resources about 2.4% to GDP for financing of financial stability fund in 10 years. It is considered that this mechanism also will help to considerably increase financial stability level of the country.

Promotion of need of distinction of pro-cyclical and countercyclical policy and advantages of countercyclical policy became one of useful lessons of the last financial crisis from macroeconomic and fiscal policy points of view. Thus, in the majority of the countries, including in Azerbaijan, there was a need for new model of macroeconomic regulation.

Approaches to concepts of pro-cyclical and countercyclical policy are ambiguous. As a whole, the pro-cyclical macroeconomic policy is an increase of the budgetary expenses on the highest phases of economic growth, which is spending of financial resources during “good times”.

And the countercyclical macroeconomic policy is economize of fiscal resources on the highest phases of economic growth, increase of the budgetary expenses on the lowest phases of economic growth, that is demand stimulation. Thus, in the approach of countercyclical macroeconomic policy is supposed the concept of spending of financial resources for "bad times" of economy.

The business cycle is the main determinant for definition of the specified forms of policy. That is feature of policy is estimated concerning a business cycle. In that case the choice of criterion of a business cycle also is very important.

That is need of formation of new model about macroeconomic regulation arose even prior to the beginning of last global crisis processes.

Thus, before crisis in the majority of the countries, especially in resource economies are possible to group the conceptual emptiness existing in macroeconomic management as follows:
Default of rules of idle time, (outrun of permanent expenses limit, outrun of non-oil budget deficit limits and so forth) a disagreement of expenditure policy with strategic targets, low transparency level of the public finance relations.

On monetary policy: existence partially or completely fixed currency regime, restriction on inflation control and weak coordination between political components (fiscal, monetary, price and so forth) at macroeconomic level.

Prior to the beginning of global crisis such emptiness are capable to lead to local crises in resource economies. In addition, the last global crises made actual a number of new calls:

On fiscal policy: high pro-cyclicality in the boom period, observance of fiscal sustainability.

On macro-prudential policy: pro-cyclicality, the accounting of system risks, limitation of counter-cyclical tools, as a result uncontrolled bubbles, lack of the mechanism of their tracing and management;

On resource income’s expenditure: prevention of the Dutch Decease in economies by means of application of accurate rules and strengthening of financial legibility.

Observance of financial stability rules covers the following:

- Principle application “permanent real expenses”;
- Maintenance of fiscal deficit (non-oil deficit) within a certain limit;
- "Golden rule" application: An attachment of resource incomes only to capital expenditure and human capital;
- Building of sustainable social financing, acceleration of pension reforms.

In this direction a number of the countries have progressive experience: for example, in the European Union the budget deficit shouldn't exceed 3% of gross domestic product. In addition, for ensuring stability in Norway non-oil budget deficit is limited at level of the percentage incomes of the Fund and so forth.

Counter-cyclical fiscal policy should be carried out directly within sustainability principles. As depending on the arisen situation in many cases these two principles connected with fiscal policy, may be uncoordinated.

So, if during the recession counter-cyclical fiscal policy needs to increase in expenses, realization of it at resource income expenses means violation of a sustainability principle.

In that case, it is necessary to achieve counter-cyclical fiscal policy only in the ways fitting to stability conditions. For example, in the last crises in a number of the resource countries there was a need for maintenance of economic growth through the demand channel by counter-cyclical fiscal policy.

Currently, most leading theoretical concepts concerning questions of fiscal stability, recommend increase in counter-cyclicality of fiscal policy.

Pro-cyclic character of fiscal policy at the moment can be considered as one of the main gaps of economic management in the majority of the resource countries.
So, in years when global prices, especially energy prices were high, also alternative financial sources of economic growth existed, there was a fiscal expansion in that countries.

In the conditions of source restrictions for economic growth under the influence of global crises by primary reaction of fiscal institutions on falling of the prices mainly was toughening of fiscal administration and freezing of new investment projects. And it is anything other, as the new recipe of recession deepening.

One of important problems in the direction of fiscal policy counter-cyclicality increasing is studying of automatic stabilizing mechanisms. In the resource countries use of the automatic stabilizing mechanism depends on the following:

- Coordination of the operating budgetary expenditures with non-resource incomes;
- Increase of sensitivity of the public investment expenditures to a cycle;
- Cyclic regulation of stabilization funds using.

As an example in the field from foreign experience we can show that in Chile budget surplus relieved of cyclic changes, shouldn't exceed 1% of gross domestic product. In Turkey such counter-cyclical mechanism was developed at which the standard of annual growth rate of a budget deficit should be reduced to 1/3 above 5% of real growth rate of gross domestic product.

The modern theoretical schools developing on the basic empirical researches put forward on the first place the importance of various institutional and economic reforms in the field of fiscal management. From them it is possible to note: transition to the system of “result budgeting” planning; ensuring competitive tax burden, improvement of tax administration; formation of effective management system for public debt; development of sustainable model of a public debt and coordination with counter-cyclical fiscal policy; support of rhythmic realization of the budgetary expenses, strict observance of fiscal transparency rules and reporting, creation of comprehensive fiscal statistic system.

**Conclusion.** Finally, the article gives following conclusion items:

- State budget mechanism including such economic categories as taxes and the public expenditures, not only smoothes economic inequalities, also at the same time stimulates the economic relations and defines the key development directions of national economy.
- While fiscal policy has not been countercyclical in all countries, monetary policy has been relatively more flexible in responding to the growth slowdown.
- Fiscal consolidation policy should go deep in the developed countries generally for improvement of the macro-fiscal indicators and maintenance of economic activity in the long-term.
- Counter-cyclical fiscal policy should be carried out directly within sustainability principles. As depending on the arisen situation in many cases these two principles connected with fiscal policy, may be uncoordinated.
- Reforms of tax and budgetary expenses are the following important element of ensuring of fiscal deficit sustainability.
- Planning of “Result budgeting”; ensuring competitive tax burden, improvement of tax administration; formation of effective management system for public debt; development of sustainable model of a public debt and coordination with counter-cyclical fiscal policy; support of rhythmic realization of the budgetary expenses, strict observance of fiscal transparency rules and reporting, creation of comprehensive fiscal statistic system are key institutional and economic reforms in the field of fiscal management for long term macroeconomic sustainability needs.

References