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FISCAL CONSOLIDATION IN CROATIA AND OTHER POST- TRANSITION COUNTRIES

Paško Burnać
University of Split, Faculty of Economics



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INTRODUCTION

- ❑ Fiscal consolidation or fiscal adjustment is a term which represents the process of harmonization of public revenues and public expenditures by reducing expenditures and / or increasing revenues.
- ❑ Austerity policy is "a form of voluntary deflation that reduces wages, prices and budget spending in the economy to reduce the deficit and public debt and increase the competitiveness of the economy" (Blyth, 2013, 11).

THEORETICAL FRAMEWORK

- ❑ the wealth channel (the role of expectation)
- ❑ channel of trust (the impact on the interest rate)
- ❑ review of empirical research
- ❑ austerity measures in EU: Ireland, Iceland, Greece

CRITIQUE OF *EXPANSIONARY FISCAL CONSOLIDATION HYPOTHESIS* AND AUSTERITY MEASURES

- ❑ public spending as a answer to crisis
- ❑ distributional effect and time inconsistency of austerity measures
- ❑ *expansionary fiscal consolidation hypothesis*- exception, not rule

DATA AND METHODOLOGY (1)

- ❑ cyclically adjusted primary balance as a measure for fiscal consolidation
- ❑ this research: *narrative approach* (Romer and Romer, 2010)

DATA AND METHODOLOGY (2)

Definition 1:

Fiscal consolidation is successful if a) in the three-year period after consolidation, the cyclically-adjusted primary deficit decreased by min on average. 2% below its value in the year of consolidation; or b) if three years after consolidation the ratio of public debt to GDP min. 5% lower than the ratio in the year of consolidation (Alesine and Ardagna, 1998, Mirdala, 2013).

Definicija 2:

Fiscal consolidation is expansionary if the average GDP growth rate in the consolidation period and two years after that period is higher than the average growth rate at the beginning of the consolidation period (Alesina and Ardagna, 1998., Mirdala, 2013.).

RESULTS AND DISCUSSION (1)

Period(s) of fiscal consolidation in post-transition EU countries, 1995-2015

Estonia	1996,	1997,	2008,	2009,	2012	
Latvia	2000,	2001,	2011,	2012		
Lithuania	1995,	1996,	2005,	2010,	2012	
Poland	2005,	2007,	2011			
Czech Republic	1997,	2004,	2007,	2011,	2013	
Slovakia	1998,	2003,	2007,	2011,	2013	
Hungary	1995,	2003,	2007,	2008,	2012,	2013
Slovenia	2002,	2007,	2011,	2012		
Croatia	2000,	2005,	2010,	2012,	2013	
Romania	2001,	2010,	2011,	2012		
Bulgaria	2001,	2004,	2010,	2011,	2012	

Source: Eurostat, author's calculation

RESULTS AND DISCUSSION (2)

Expansionary fiscal consolidations - size and structure

	before (1)	during (2)	after (3)	diff. (2-1)	diff. (3-1)
Public debt	41,23 (2,92)	43,72 (3,13)	43,56 (3,21)	2,49	2,33
Primary deficit	5,05 (1,31)	3,34 (1,09)	3,96 (1,20)	-1,71	-1,09
Public expenditures	40,02 (3,97)	39,25 (3,81)	41,12 (4,02)	-0,77	1,10
Transfers	19,86 (1,93)	19,16 (1,82)	19,56 (2,01)	-0,70	-0,30
Wages	10,34 (1,09)	11,09 (1,18)	11,96 (1,23)	0,75	1,62
Non-wage consumption	3,87 (0,79)	3,05 (0,70)	3,45 (0,74)	-0,82	-0,42
Investments	3,03 (0,45)	3,18 (0,41)	3,25 (0,43)	0,15	0,22
Public revenues	34,97 (3,65)	35,91 (3,89)	37,16 (3,93)	0,94	2,19

Contractionary fiscal consolidations - size and structure

	before (1)	during (2)	after (3)	diff. (2-1)	diff. (3-1)
Public debt	45,52 (3,89)	48,31 (4,31)	51,07 (4,45)	2,79	5,55
Primary deficit	4,53 (1,23)	1,92 (0,89)	2,76 (1,10)	-2,61	-1,77
Public expenditures	42,34 (4,31)	43,04 (4,42)	44,08 (4,47)	0,7	1,74
Transfers	21,12 (2,09)	21,97 (1,86)	22,65 (2,14)	0,85	1,53
Wages	12,09 (1,25)	11,51 (1,02)	11,87 (1,21)	-0,58	-0,22
Non-wage consumption	5,06 (0,91)	6,21 (0,79)	5,98 (0,81)	1,15	0,92
Investments	3,95 (0,52)	3,02 (0,45)	2,93 (0,50)	-0,93	-1,02
Public revenues	37,81 (3,91)	41,12 (4,08)	41,32 (4,12)	3,31	3,51

Source: Eurostat, author's calculation

RESULTS AND DISCUSSION (3)

Expansionary fiscal consolidations - macroeconomic effects

	before (1)	during (2)	after (3)	diff. (2-1)	diff. (3-1)
Unit labor costs	3,08 (1,52)	-0,82 (1,32)	1,05 (1,36)		
Exchange rate	1,52 (1,09)	-0,65 (1,02)	0,95 (1,08)		
GDP growth	2,87 (1,41)	0,78 (1,27)	3,12 (1,44)	-2,09	0,25
Unemployment rate	11,77 (3,12)	12,81 (3,05)	12,93 (3,17)	1,04	1,16
Personal consumption	2,56 (1,09)	0,56 (0,98)	2,77 (1,16)	-2,00	0,21
Current account of the BOP (%GDP)	-7,32 (2,12)	-6,67 (2,01)	-6,15 (2,34)	0,65	1,17
Real interest rate	3,52 (0,67)	3,97 (0,77)	3,08 (0,61)	0,45	-0,44
Inflation	4,23 (1,21)	2,54 (1,03)	3,12 (1,12)		

Contractionary fiscal consolidations - macroeconomic effects

	before (1)	during (2)	after (3)	diff. (2-1)	diff. (3-1)
Unit labor costs	2,43 (1,45)	-0,32 (1,24)	0,89 (1,30)		
Exchange rate	2,32 (1,14)	1,22 (1,07)	1,03 (1,01)		
GDP growth	3,75 (1,56)	-1,53 (1,32)	2,76 (1,41)	-5,28	-0,99
Unemployment rate	9,65 (2,91)	12,76 (3,05)	12,98 (3,09)	3,11	3,33
Personal consumption	4,33 (1,12)	2,63 (1,02)	3,53 (1,09)	-1,7	-0,8
Current account of the BOP (%GDP)	-8,43 (2,41)	-7,76 (2,11)	-7,97 (2,28)	0,67	0,46
Real interest rate	3,02 (0,57)	3,34 (0,69)	3,1 (0,64)	0,32	0,08
Inflation	5,34 (1,41)	3,97 (1,35)	4,67 (1,38)		

Source: Eurostat, author's calculation

RESULTS AND DISCUSSION (4)

Fiscal consolidation in Croatia – size and structure

	before (2006-08)	during (2009-12)	after (2013- 16)	difference	difference
	(1)	(2)	(3)	(2-1)	(3-1)
Public debt	38,5	63,7	81,4	25,2	42,9
Primary deficit	5,4	3,4	4,1	-2	-1,3
Total expenditures	47,2	44,6	46,5	-2,6	-0,7
Current expenditures	43,5	42	42,3	-1,5	-1,2
Wages	13,1	12,3	12,4	-0,8	-0,7
Social benefits	15,2	15,9	16,1	0,7	0,9
Non- wage consumption	8,4	7,8	7,9	-0,6	-0,5
Other current expenditures	6,8	6,0	5,9	-0,8	-0,9
Capital expenditures	3,7	2,6	4,2	-1,1	0,5
Total revenue	41,8	41,2	42,4	-0,6	0,6
Direct taxes	7,1	6	6,2	-1,1	-0,9
Indirect taxes	16,9	18,1	19,1	1,2	2,2
Social contributions	11,9	10,7	11,1	-1,2	-0,8
Other revenues	5,9	6,4	6	0,5	0,1

Source: Eurostat, Croatian Ministry of finance, author calculation

RESULTS AND DISCUSSION (5)

Fiscal consolidation in Croatia – macroeconomic effects

	before (2006-08)	during (2009-12)	after (2013- 16)	Difference	Difference
	(1)	(2)	(3)	(2-1)	(3-1)
GDP growth rate	4,3	-2,1	-0,4	-6,4	-4,7
Unemployment rate	10,9	14,9	17,8	4	6,9
Employment rate	45,9	44,5	42	-1,4	-3,9
Investment	7,2	-2,1	-0,1	-9,3	-7,3
Personal consumption	3,1	-1,2	0,3	-4,3	-2,8
Unit labor costs	3,1	-0,6	0,2	-3,7	-2,9
Exchange rate	0,3	-2,1	-0,3	-2,4	-0,6
Current account of the BOP (%GDP)	-6,3	-2,4	0,7	3,9	7
Inflation	3,4	2,1	-0,2	-1,3	-3,6

Source: Eurostat, Croatian Bureau of Statistics, Croatian National Bank, author calculation

CONCLUSION

- ❑ The research shows that, apart from minor corrections to current account balances and lower labor costs, fiscal consolidation in the post-transition countries did not achieve declared goals such as economic growth.
- ❑ The assumptions on the expansionary fiscal consolidation hypothesis neglect negative short-term effects on aggregate effective demand while simultaneously overestimate the effects of lower interest rates, competitiveness and positive effects on the current account of the balance of payments.
- ❑ limitations and recommendations for future research