

Conceptual Approaches to Development and Implementation of Budgetary Policy

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Abstract—The paper discusses methodological issues related to the development and implementation of good budgetary policy. The basic assumption is that modern challenges indicate that the budgetary policy is an appropriate tool to ensure countercyclical management efficiency and social equity. The analysis suggests a conclusion that the achievement of the appropriate quality of budgetary policy requires coordination between budgetary and monetary policies. The paper provides the classification of sources and types of fiscal risks, and formulates conditions that ensure the appropriate approach to the development and implementation of budgetary policy.

Keywords—good budgetary policy; fiscal risk; budgetary rules; macroeconomic sustainability; social equity

I. INTRODUCTION

Current trends in public financial management indicate, on the one hand, the expansion of scope of tasks solved in the process of formation and execution of budgets of governmental units, and on the other hand, the change of functions of the state and increase of the level of social demands to the efficiency and volume of budgetary allocations, the availability and quality of services provided by the state and the municipalities, the efficiency of budget entities, and the budgetary expenditures. In this regard, the challenge of forming a budgetary policy capable of ensuring, firstly, the effective use of limited budget funds, and secondly, the preservation of the potential impact of budgetary policy on socio-economic processes in the conditions of modern challenges still persists.

As a response to these requirements for public financial management, the IMF and OECD Codes of Best Practice have introduced the term “Good Budgetary Governance”, which allows to assess the degree to which the goals and objectives of fiscal policy pursued by countries comply with the principles of effective and responsible management within the framework of the concept of “good budgetary governance”, which implies an increase of transparency, openness and inclusiveness of public financial management [1].

Within the framework of the implementation of these requirements and taking into account the current challenges, the budgetary policy needs to focus on ensuring the long-term financial sustainability of public sector on the basis of risk assessment and the use of fiscal rules, and improvement of the efficiency of budget spending.

II. METHODOLOGY

This paper is based on the assumption that under current conditions the key for country's macroeconomic well-being is the budgetary policy which considers the emergence of new risks and becomes a stabilizing factor in the socio-economic development of the country avoiding being an additional source of risk. One of the main priorities of the budgetary policy is a “careful balance between the efficiency and equity goals” [2].

In fact, the high level of economic uncertainty, globalization challenges, and changes in the structure of the world economy have been the main reason to reconsider the role of budgetary policy, because the capabilities of monetary policy being an instrument of macroeconomic regulation revealed their limitations. “The crisis provided evidence that fiscal policy is an appropriate countercyclical policy tool when monetary policy is constrained by the zero-lower bound, the financial sector is weak, or the output gap is particularly large” [3].

This paper is based on the assumption that transformation of current requirements to the development and implementation of budgetary policy occurs under impact of various factors, such as:

- external factors, including economic (related to globalization, the change of world economy structure, high level of economic uncertainty), political (related to the creation of the new state-society social contract), social (deepening inequality, failure to implement existing social obligations of the state in full volume), demographic (changes in the gender and age structure of society, migration problems), technological (related to the development of information and communication technologies);
- internal factors related to (1) growth of the state apparatus amidst a decline in the efficiency of the hierarchically arranged system of democratic governance and the inability to ensure the competitiveness of national economies within the dynamically changing structure of the world economy, (2) discontent among citizens arising from the quality of public services and the growth of the cost of state apparatus maintenance expenses and the absence of an opportunity for citizens and civil society institutions to

influence the government's decision-making process affecting them.

III. CONCEPTUAL APPROACH TO DEFINITION OF GOOD BUDGETARY POLICY

The term “good budgetary policy” used in the IMF and OECD Codes of Best Practice, as well as in programming documents drafted by public authorities both in Russia and abroad presupposes a definition of this concept basing on the theory of managing complex socio-economic systems and public law principles in the context of effective and responsible management of public finances.

In scientific papers [e.g. see 4,5,6,7,8,9] on management and law, an appropriate approach to managing complex socio-economic systems implies the ability to influence the course of events, therefore, an appropriate fiscal policy should pursue both financial goals (related to the growth of income, increase in the efficiency of public entities' spending) and overall economic goals, defining activities and tools to influence the national economy and living standards of the population.

This requirement needs to be considered when defining goals, objectives and tools to implement the mid-term and long-term budgetary policy.

Under the conditions of current challenges, good budgetary policy implies a program of activities taken by public authorities and related to the use of government revenues and expenditures to influence the macroeconomic conditions in order to ensure sustainable economic growth and equitable income distribution.

Consequently, good budgetary policy ensures the following:

- conditions for sustainable economic growth;
- implementation of countercyclical and cyclically neutral policies;
- provision of access for all the economic subjects to public goods, implementation of the principles of equitable distribution of incomes and equal access to productive and financial assets, adaptation to the demands of changing economy;
- formation of sovereign debt of optimal volume and efficient structure, and creation of reserves to provide macroeconomic fiscal sustainability in adverse conditions.

In our view, this is possible provided that there are clear, controllable fiscal rules and strategic objectives of public policy, which will enable the citizens and economic agents to understand government's current, medium-term and long-term policy throughout the whole economic cycle.

The appropriate approach to the development and implementation of budgetary policy in current situation requires an understanding that parameters of the budget should not grow faster than the economic parameters. In particular, if the country's sustainability depends on the external economic conditions, the cyclical problems occur when the income from the sale of natural resources gives rise to public spending which leads to fiscal impetus. Sustainability challenges occur when the expenditures of such countries outperform their

expected long-term income from the sale of natural resources. This may happen when they extrapolate temporary price increase and, therefore, they proceed from the wrong estimated value of their natural resources and (or) do not form the appropriate budgetary reserves to maintain the prevailing level of current expenditures. All of these issues may lead to cycles of sharp ups and downs, which are quite frequent in countries rich in natural resources. In this regard, the development and implementation of good budgetary policy requires the evaluation of the capability of the state to maintain current expenditures, to preserve optimum level of taxation in a long-term perspective without endangering their solvency and execution of their spending commitments.

A study conducted by the IMF in 2006–2012 [10] shows that lower inequality is associated with greater macroeconomic sustainability and more stable economic growth. This means that the development of budgetary policy in current conditions requires the focus not only on the effective use of budget funds, but also on the implementation of the principles of social equity.

IV. METHODOLOGICAL REQUIREMENTS FOR THE DEVELOPMENT AND IMPLEMENTATION OF GOOD BUDGETARY POLICY

The rates and level of economic growth are conditioned by the development of real production, functioning of the financial sector, and currency circulation. The impact of the budgetary policy implementation tools on each of these elements is great.

On the one hand, the flow of financial resources outlines the reproduction structure of the real sector of economy and remains at the core of the financial market activities, and on the other hand the money attribute of formation and redistribution of financial resources affects the main elements of currency circulation.

Accordingly, when choosing the tools to implement good budgetary policy aimed at ensuring macroeconomic sustainability, it is important to consider their impact on:

- the level of prices (volume and structure of monetary base);
- the national currency rate;
- the interest rate (cost of resources) at the financial market;
- the distribution of added value within the budget system.

Thereby, good budgetary policy can prevent overheating of economy and emergence of associated problems. Limitation of budget spending may reduce internal demand and the need for tightening monetary policy, and encourage the reduction of pressure imposed by the short-term capital inflows on economy, national currency, and the financial market. Accordingly, there is a need for the indicators to evaluate: (a) the short-term orientation of budgetary policy (e.g., whether the budgetary policy that stimulates economic growth leads to inflation and the increase in the current account deficit of country's balance of payments), and (b) solvency (i.e. the ability of the state to observe the budgetary constraints during different periods).

The global financial crisis of 2008-2011 has shown that “while monetary policies caused a temporary decrease in volatility and increase in liquidity in North American stock markets, the shocks were mainly domestic and ineffective at generating liquidity in the banking sector. In contrast, government spending shocks had a positive impact on credit and consumption, especially in Europe and Canada. Moreover, budgetary policies also had a positive international spillover effect on consumption and credit, especially for smaller economies such as Canada” [11].

The considered directions and tools of influence of the good budgetary policy on macroeconomic sustainability indicate their close interrelation and, consequently, their multiple impacts on economic processes. This raises a question on coherence and priorities of budgetary policy, the need to use various tools for its implementation, and its coordination with monetary and tariff policy of the state.

Accordingly, in our view, the conditions listed below provide an appropriate approach to the development and implementation of budgetary policy:

1) Compliance of the goals and objectives of the budgetary policy with the strategic goals of the development of governmental units

2) Coordination with monetary and tariff policy

Monetary and public financial policies have different yet overlapping objectives. Monetary policy is expected to ensure sustainability of the monetary unit, adequacy of credit resources in the economy, sufficient volume of forex reserves, and price stability. In this regard, the monetary policy, as well as the budgetary policy, aims to regulate economic growth, to control inflation and to ensure employment.

For example, strengthening the income base of country’s budgets and ensuring their balance are key elements of anti-inflationary policy. In this regard, the following points appear to be relevant: (a) the choice of methods used to overcome deficits and to avoid inflationary effects; (b) the development and implementation of effective budgetary policy, improvement of tax collection; (c) increase of efficiency of the budget expenditures at various levels; (d) development of state and municipal stock market. The level of development of state and municipal stock market has a direct impact on banks liquidity and their financial stability.

3) Consistency in development and implementation of budgetary policy, assessment of mid-term and long-term implications of such a policy.

4) Identification and management of fiscal risks.

5) Development and implementation of budgetary rules coordinating incomes, expenditures and attraction of funds from the deficit financing sources.

Analysis of the budget legislation of the Russian Federation shows that the fiscal rules are currently established only with regard to the oil and gas revenues, the formation of the sovereign wealth fund, the size of the budget deficit, the volume of borrowings made by municipalities and federal subjects, the volume of sovereign debt of municipalities and subjects of the Russian Federation, and their debt maintenance expenses.

However, the growing deficit of regional and local budgets, as well as the numerous cases when the subjects violated the rules established by the Budget Code of the Russian Federation, indicate a decrease in the sustainability of the budget system and the insufficiency of the existing legal norms aimed to implement the good budgetary policy in the process of execution of budgets of the national budgetary system.

V. IDENTIFICATION OF FISCAL RISKS

The term “fiscal risk” in the economic literature has a number of interpretations that characterize its content. Thus, in the scientific publication and IMF analytical reviews, the term “fiscal risk” (originally – “budgetary risk”) is considered as “the risk of non-fulfillment of the planned budget” [11, 13]. In the documents of international financial organizations, the fiscal risks are understood as factors that, under certain circumstances, can lead to significant deviations of the actual budget parameters from planned and forecasted figures. [1, 14, 15] Most of these factors cannot be controlled or regulated by the public authorities (for example, global prices of basic export goods). At the same time, part of the fiscal risks is related to the activities of public authorities when, for example, they are forced to provide state financial assistance to systematically important commercial banks to prevent risks of the collapse of financial system. It should be noted, that this approach fully discloses the content of the notion of “fiscal risks”.

It is necessary to distinguish the concepts of “fiscal risks”, implying the uncertainty of “one time” events, and, when some long-drawn-out budgetary indicators are quite predictable. In the first case, on the one hand, the objectives of financial authorities consist of preventing the realization of risk. On the other hand, it includes the preparation of scenarios to neutralize the risk negative consequences if the risk is nevertheless realized. In the second case, the objective is formulated in a fundamentally different way: the effect of preventive actions compensates the challenge in the long-term perspective, i.e. keeps the key budget parameters unchanged. An example of a short-term fiscal risk is a sharp drop in oil prices, and an example of a long-term “challenge” is aging population and significant increase in pension costs.

At the same time, there is a close connection between risks and challenges. If a country does not take measures proportionate to the scale of the challenges that it faces, then eventually they turn into large-scale risks and lead to negative consequences. Sometimes it takes a long time, but during the crisis shocks the potential risks materialize unexpectedly quickly. Thus, the global financial crisis brought to light all the hidden risks and problems that have been accumulated in advanced economies.

TABLE I. THE CLASSIFICATION OF THE SOURCES AND TYPES OF FISCAL RISKS

Source of fiscal risk	Type of fiscal risk
The slowdown in the economy	The risk of a shortfall in budgetary revenues from oil and gas industry The risk of a steady decline in budgetary revenues from of concrete taxes (indirect taxes, personal income tax, corporate income tax)
Change in GDP structure	The risk of the excess of the rates of budget expenditures over the rates of budgetary revenues
Instability of the national currency exchange rate	

	The risk of growth of "unfunded mandates"
Deterioration of the trade balance and balance of payments	The risk of the decline in budgetary revenues from the foreign trade The risk of growing costs of central and local governments' investment projects and long-term purchase contracts
Instability of the national currency exchange rate	The risk of the excess of the rates of budget expenditures over the rates of budgetary revenues
Aging population	The risk of increase in mandatory social indexed expenditures The risk of the structure of budget expenditures and increase in budgetary spending on education, healthcare and social policy
Slowdown in the economic growth	Intergovernmental relation risks: - The risk of instability of state and local budgets of the budgetary system (risk of the vertical imbalance); - The risk of increased differentiation of the tax potential of various regions and municipalities; - The risk of imbalance in off-budgetary funds of central and local governments
Change in GDP structure	
Instability of the national currency exchange rate	
Aging population	
Changes in sovereign debt market and growing cost of the debt	Risk of growth of the debt burden: - The risk of exceeding the costs of servicing and paying off regional and municipal debt in comparison with the planned ones and norms established by the Budget Law - The risk of the debt structure worsening, such as shortening the debt maturity and borrowing from socially vulnerable financial institutions - The risk of governments' technical default and the debt restructuring - The risk of an increase in contingent liabilities
The deterioration of the geopolitical situation	The risk of an increase in defense expenditures The risk of increased expenses on servicing and repayment of public debt The risk of governments' technical default and the debt restructuring

^a Source: Compiled by the author

VI. CONCLUSION

The study concludes that the main methodological principles of developing and implementing the good budgetary policy include:

1) Clarity of objectives and goals of budgetary policy, their compliance with strategic priorities of social and economic development of governmental units and their conformity to modern requirements and development conditions.

2) Ensuring public confidence in the developed and implemented budget policy within the framework of ensuring fiscal transparency by communicating it to public in various ways.

3) Identification and assessment of fiscal risks, which implies coordination of budget policy development, medium-term fiscal planning and long-term forecasting.

4) Development and implementation of budgetary policy in compliance with budgetary rules (use of market revenues, funding for budget capital expenses, etc.) and budgetary constraints.

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