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THESIS

**THE IMPACT OF FISCAL POLICIES ON  
ECONOMIC DEVELOPMENT IN POST-  
COMMUNIST STATES OF THE EUROPEAN  
UNION**

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## **1.Introduction**

Economic growth is one of the most important tools for achieving economic and social objectives, such as: poverty reduction, increasing the quality of life and supporting the competitiveness of the economy in a globalized economy. Economic growth has been associated with the emergence of so-called "virtuous circles", creating opportunities that lead to prosperity, which in turn leads to more economic opportunities for citizens. On the other hand, weak national economies and economic crises trigger vicious circles, where negative effects spread in the economy and society.

Considering the importance of economic growth for the development of the state and its medium and long-term economic position and its positive social effects, it is important to study economic development, especially how it can be encouraged or stimulated. In this work, we aim to study how a state can use fiscal policies to determine economic growth.

In the following we will present aspects such as the motivation of the studied subject, the main objective of the work, the literature, the placement of the work in the scientific context, the methodology and the results, as well as the structure of the work.

### **Motivation to the topic being studied**

The choice of the topic being studied is based on several reasons. On the one hand, it is about the importance of economic growth which should not be underestimated and the factors that could encourage. On the other hand is about at the national level about the choice of fiscal policy that generates positive economic effects.

The time of conducting this study is a favourable one. In the past 12 years, the trend of the economy was one breeder, followed by the recession, and in recent years economic growth has resumed. In the last period on the background of the growth of unhealthy economy in 2004-2008, it attaches great importance to the policies of the fiscal-budgetary applied. The degree of actuality of this problem in conjunction with the implications of financial policies have on the macroeconomic stability and economic development of a country there are aspects that justify the interest for the approach to this topic.

The emergence and evolution finance are closely related to the emergence and strengthening of the state. Public finances represent social relations of an economic nature that occur in the process of realization and distribution of the gross domestic product. Fiscal policies have an important role on the economic growth and well-being of society aim of reducing the fluctuations and economic instability, protecting consumers ' income and stimulating the

development. These represent a factor of particular importance in economic life and the influence and effects on the functioning of the economy must be analysed in detail.

The importance and necessity of research have in mind that many countries acted imprudently during the economic boom, registering deficits and accumulating debts. Robert Barro (1979) demonstrates that the public debt burden will sooner or later be transferred to the tax area, leading to increased taxation and reduced production potential. He says it is necessary to increase taxes to support public debt service. This decision will negatively affect the potential GDP.

### **The main objective of the paper**

This paper aims at highlighting and analyzing fiscal policies along with the strategies of the post-communist states in the European Union to ensure stable economic growth through the sustainability of public finances and avoiding budgetary slippages.

The accelerated rise in public debt in euro area countries has shown the possibility of a rapid deterioration of public finances in the context of economic recession, a significant increase in funding costs for countries considered to be unsafe and with large deficits, of lower budget revenues compared to budget expenditures.

Thus, the paper will answer questions about how fiscal policy has acted during the economic cycle in the post-communist states of the European Union and how the acyclical and procyclical policies affect economic growth. The classical and modern theories will be examined and interpreted, and then the tax policies implemented by post-communist states in the European Union (analyzes of revenues, expenditures, tax systems) will be analyzed. The paper will seek answers on the determinants of fiscal policies that have a positive or negative impact on economic growth in the European Union.

This research has gone from consulting the relevant literature in the field. Two major issues have been analyzed from this point of view: fiscal policy and economic growth.

The treatment of economic growth has included aspects such as the classification of types of economic growth (zero, positive or negative, extensive and intensive, exogenous and endogenous) and classical theories of economic growth, which include four main categories: linear growth model, theory and patterns of change the structural revolution, the revolution against international dependence and the neoclassic counter-revolution, the free market.

Among the main authors on economic growth, we mention Sundrum (1990), Foley and Michl (2010), Todaro and Smith (2015), Eltis (2000), to give some examples. At the same time, we present the central ideas of classical works of well-known personalities in this field:

François Quesnay, Adam Smith, Thomas R. Malthus, David Ricardo, Karl Marx, and Joseph Schumpeter. Among the neoclassical theories of economic growth are mentioned models such as those of Harrod (1939) and Domar (1949), Solow and Swan (1956), Cass (1965) and Koopmans (1965), Arrow (1962) and Sheshinski (1967), Romer (1986), Cass (1965) and Koopmans (1965). Of course, I also consulted on the work on economic growth by Romanian authors such as Goschin, Antonescu and Popa (2015), Mihuț (2013), Lupan (2009) or Dinu and Socol (2006).

Expert literature on tax policies has included both general studies on this issue and papers dealing in particular with public spending or public debt. For example, on budget expenditures, we include explanations about Wagner's Law, but also about the travel effect, a concept proposed by Peacock and Wiseman.

Among the authors consulted for the section on literature on tax policies, we include Saez (2012), Zai (2014), Shaw (1972), Zagler (2003) to give some examples and among the Romanian authors quote on this theme, we mention Mara (2011), Inceu and Lazar (2003), Holt and Craciun (2009).

### **Structure of the paper**

In the first chapter of the paper, called Classical and Modern Theories of Economic Growth, the main theories and models of economic growth will be presented, mainly from a chronological perspective. Thus, starting from classical theories, then presenting the neoclassical, linear and some aspects of alternative theories of growth, concluding with a brief comparison of the main theories. We mention the theories addressed in this chapter. Among the classics, there are growth theories proposed by Adam Smith, David Ricardo and Thomas Robert Malthus; Modern theories include: the new theory of economic growth, Schumpeter's theory, neoclassical and linear theories.

At the same time, this first chapter focuses on analyzing and presenting the factors that influence economic growth. Thus, concepts used during the work, both in the theoretical and the research, are theoretically grounded in this section. Subchapter Elements and principles of economic theory of the public sector include key aspects of the public economy, indicators on the use of budgetary resources, the evolution of economic thinking in the public economy, aspects of the role of the state in the economy. At the same time, this chapter also deals with introductory issues regarding certain aspects of fiscal policy, that will be discussed in depth in the second chapter. We refer to: public expenditures and revenues, tools and techniques to finance the budget deficit, but also to the objectives and impact of fiscal policies.



The second chapter, Fiscal Policy - a tool for ensuring macroeconomic stability and stimulating economic growth, analyzes fiscal policy from two perspectives, combining the theory of tax policy and studies in the field, especially those made on European countries. There is a link between tax policies and macroeconomic stability, but also theoretical and practical notions of the fiscal balance and its objectives. The second chapter is structured in four subchapters entitled: Tax Policy Instruments, Automated Stabilizers, Procyclical Tax Policy versus Procyclical Tax Policy and Tax Policy Impact on Economic Growth. In particular, this chapter deals with concepts and presents the main studies on fiscal policy, as well as the link between fiscal policy and economic growth. In particular, we mention that we have discussed the unique tax rate and progressive tax rates, the fiscal policy cycle, and the comparative analysis of the anti-cyclical and procyclical tax policy, and the main factors, as they appear from the literature on tax policies, on growth economic.

Chapter Three, the first research on the economic and fiscal situation of post-communist states in the European Union, is called the Analysis of Tax Policies in the European Union before, during and after the economic crisis of 2007-2011. The analysis was applied to: Bulgaria, the Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia and Hungary. For these countries, three main analyzes were carried out: the analysis of tax systems, the choice and implication of choosing the single rate or the progressive tax rates, but also the fiscal measures according to the economic cycle phases. By addressing these issues, this chapter also examines the measures taken by the post-communist countries of the European Union to break out of the economic crisis, framing them in acyclical or procyclical politics.

One of the main conclusions of this chapter, which is also indicated by other studies in the literature, is that developing countries and emerging countries typically use a pro-cyclical policy, and the developed countries usually base their acyclical policy. Moreover, we have studied the way in which fiscal policy acted during the economic cycle in the above mentioned states, in relation to the phases of economic development. The role of automated stabilizers as fiscal stabilization tools has been highlighted and the extent to which they contribute to smoothing the economic cycle and lowering the volatility of GDP,

The next chapter, Analysis of the Impact of Tax Policies, focuses on developing econometric models that attempt to capture the impact of fiscal policy on economic growth. The chapter includes the methodology, the results of the research and the discussion about them. Single and multiple regressions have been used as research tools to highlight those determinants of fiscal policies that have a positive or negative impact on economic growth in

the post-communist states of the European Union. The data panel was used (data series in time and