AN ANALYTICAL STUDY OF THE EFFECTIVENESS OF FISCAL POLICY TOOLS IN ACHIEVING ECONOMIC STABILITY IN IRAQ

[1]NARMEN MAEROF GAFOR [2]DLOVAN ASAAD MOHAMMED

[1]PhD in economics, Economics Department /University of Sulaimani, Raparin Road/ Sulaimaniyah, Kurdistan Region of Iraq, Iraq

narmen.ghafor@univsul.edu.iq

[2]Master in Economics,Economics Department, University of Sulaimani/ Raparin Road/ Sulaimaniyah, Kurdistan Region of Iraq, Iraq

Dlovan_asad@yahoo.com

ABSTRACT

The majority of countries throughout the world struggle with the issue of economic stability. Financial policy measures may occasionally fall short of achieving the requisite level of economic stability. Therefore, the current research aims to know the impact of fiscal policy tools to attain financial stability and any of these tools that have the most significant impact in achieving the goal of economic stability, to reduce an effort made by officials to establish the fiscal situation in to achieve the best outcomes and so that they can develop specific aspirations that have the most considerable influence on the stability of the Iraqi financial system. For this study, data has been compiled from the World Bank (2022) database, which covers the variables of economic growth and fiscal policy, such as the gross domestic product of Iraq, financial policy instrument track, monetary policy tools, and impacts on Iraq (the effect of public expenditures on economic stability, impact of public revenues on economic stability, and the effect of the general budget on financial stability) were considered variables. The analysis of the study has presented the significance of economic stability and the favorable or unfavorable impacts it has on the economy. Given the oscillations and fluctuations that occur in the financial policy tools, it is determined from the research that fiscal policy has a limited impact on achieving the goal of economic stability for Iraq. However, compared to other fiscal policy tools, public spending has the most significant implications for monetary stability.

Keywords: Economy, Fiscal Policy, Fiscal Policy Tools, Economic Stability, Iraq

1- INTRODUCTION

Modern economic variables research is becoming more focused on fiscal policy and its capacity to stabilize economic growth. The ability of fiscal policy to boost economic growth during periods of severe economic slump is given particular consideration. Gaining significance is research investigating how the economy reacts to fiscal policy at various phases of the financial year(Baranowski et al., 2016). Fiscal policy might also significantly impact financial cycles, depending on whether it is pro-cyclical or counter-cyclical (Özer & Karagöl, 2018). Increased financing restrictions during economic downturns that force governments to implement fiscal modifications when they ought to have implemented fiscal growth may be the root cause of fiscal fluctuations in the value (Hussein & Abdullah, 2022). During the worldwide economic crisis, when authorities intervened to sustain financial institutions, stimulate growth, and lessen the effects of economic turmoil on vulnerable individuals, the function and goals of fiscal policy became increasingly important (Vernevskaya & BUDNIKOVA, 2021).

Some economists define fiscal policy as a program of fiscal action taken by the government based on rational decisions. Usually it is putted at the beginning of the fiscal year and use the public revenues and public expenditures, in addition to public loans, for that to achieve several goals, the most important of which is the advancement of the national economic situation, the establishment of financial stability and the advancement of the wheel development, achieving social justice, and working to achieve social welfare through several policies, such as the policy of wages and prices

and avoiding undesirable effects by society (Al–Fatlawi, 2019). To move the macroeconomic variables, represented in employment, national output, investment, and savings, to achieve the desired goals and avoid negative effects that affect both the national product and income, in addition to the level of employment and other economic variables(Alrawashdeh et al., 2022; Jarczok-Guzy, 2021).

Numerous studies (Jiang et al., 2022; Kumwenda, 2022; Postula & Radecka-Moroz, 2020; Raihan & Anjum, 2020) have examined the relationship between fiscal policy tools and economic growth. Few academics have studied the connections between fiscal policy tools and economic growth in developing economies(Al-Shammari & Al-Salem, 2022; Danylyshyn et al., 2021; Goryunov et al., 2021). Economic stability is one of the problems most countries face, regardless of their economic development. Financial policy tools may sometimes fail to reach the required economic stability state, or monetary policy tools may be inefficient in achieving the desired economic stability. Here, it is necessary to search for the flaws in this policy and to know the obstacles that limit the tools of this policy to reach a state of economic stability. The main aim of this study is to find out the impact of fiscal policy tools in achieving financial stability and whether any of these tools have the most significant impact in achieving the goal of economic stability to reduce the efforts made by officials About establishing the fiscal situation in to achieve the best outcomes and so that they can develop specific aspirations that have the most significant influence on the stability of the Iraqi financial system.

2-   RELATED LITERATURE WORK

The Keynesian economic theory, on which fiscal policy is founded, contends that governments can affect economic growth by raising or lowering tax rates and public spending. In turn, this impact keeps the value of money stable, restrains inflation, and boosts employment (Jahan et al., 2014). Numerous studies have looked at various facets of fiscal policy, particularly regarding economic expansion. Papaioannou (2018) used Markov Switching regression and quarterly data for Greece to examine the impact of government spending on economic growth. The findings demonstrated that government spending disproportionately impacts economic development throughout the economic cycle (Papaioannou, 2019).

When Madni and Chaudhary (2017) looked into the relationship between fiscal policy, democratic accountability, and economic growth in the context of Pakistan, they found that government spending and institutional factors had a positive impact on economic growth while private investment and educational achievement had a favorable effect (Madni & Chaudhary, 2017). Osebo (2017) looked at the long-term relationships between economic growth and fiscal policy variables. Furthermore, there was a significant correlation between economic growth and capital spending, direct tax, and budget balance(Osebo, 2017). Cyril (2016) conducted research AND showed the tremendous benefits to financial stability and growth that public spending on financial services (agricultural, building, transportation, and telecommunications) had (Ubesie, 2016).

To evaluate the effects of fiscal and economic policy shocks on economic activity for five significant rising economies—Brazil, Russia, India, China, and South Africa—Jawadi, Mallick, and Sousa (2016) used a panel Vector Autoregressive (VAR) model. The findings demonstrated that while government spending shocks had significant Keynesian impacts, economic contractions resulted in a lower actual economic output and tighter liquidity market conditions [20]. Ialomitianu, Danu, and Bucoi (2016) emphasized and investigated effective fiscal compression techniques. Significant fiscal contraction efforts are required in addition to substantial structural changes to re-establish the sustainability of public finances(Ialomitianu et al., 2016).

Economic stability is one of the problems most countries face, regardless of their economic development. Financial policy tools may sometimes fail to reach the required economic stability state or monetary policy tools may be inefficient in achieving the desired economic stability. Here, it is necessary to search for the flaws in this policy and to know the obstacles that limit the tools of this policy to reach a state of economic stability. The study's significance is derived from the importance of economic stability and the favorable or unfavorable impacts it has on the economy.

Given the oscillations and fluctuations that occur in the financial policy tools, it is determined from the research that studies from Iraq on fiscal policy were minimal and showed an impact on achieving the goal of economic stability for Iraq. However, public spending has the most significant effect on economic stability compared to other fiscal policy instruments. Although the importance of fiscal policy for maintaining financial stability cannot be disputed, there is currently a lack of scholarship in this field. This is in part because the efficiency of policy tools is still developing. However, this transformation has progressively altered how conventional fiscal policy goals are perceived.

3-   RESEARCH METHODOLOGY

In this research, we have discussed two of the most important indicators of economic stability, namely:

a)   Data

For this study, data has been compiled from the World Bank (2022) database, which covers the variables of economic growth and fiscal policy, such as the gross domestic product of Iraq, financial policy instrument track, monetary policy tools, and impacts on Iraq (the impact of public expenditures on economic stability, the impact of public revenues on economic stability, and the effect of the general budget on economic stability) were considered variables.

b)   Economic stability co-efficient

It is a quantitative measure of analyzing the quantity of money supplied to achieve economic objectives. The dimensions of the economic stability process are measured through this coefficient. Therefore, we can judge the level of economic stability. This measure depends on the money supply and its development to express the development. The incidence of means of payment in the economy in addition to the real GDP and its evolution to represent the number of transactions that occur in the community [Hussien, 2018], and it is possible to clarify this scale is simplified according to the following formula:

$$B = \frac{\Delta M/M}{\Delta Y/Y}$$

Whereas:

B represents the economic stability coefficient, ΔM/M represents the rate of change in the number of means of payment, and $\Delta Y/Y$ represents the rate of change in the gross domestic product. The value of the coefficient indicates the level of economic stability within the economy, and this value indicates three levels which are:

If the value of the coefficient is equal to the right one, this suggests the existence of economic stability

$$B = \frac{\Delta M/M}{\Delta Y/Y} = 1$$

If the coefficient value is more significant than one, then this indicates the lack of economic stability with hypertrophic pressures.

$$B = \frac{\Delta M/M}{\Delta Y/Y} > 1$$

If the value of the coefficient is less than one, this case also indicates the lack of economic stability with deflationary pressures.

$$B = \frac{\Delta M/M}{\Delta Y/Y} < 1$$

It is evident through the economic stability coefficient that if the rate of change in the number of means of payment is equal to the speed of the difference in the authentic gross national product, a state of economic stability is achieved. Prices are stable and nonexistent for inflation or stagnation. Still, in the case of an increase in the means of payment for the volume of transactions (output), this will cause inflationary pressures. A state of economic imbalance occurs within the economy, and vice versa; when there is a decrease in the amount of the means of payment for the volume of transactions, recessions will appear, prices will fall, and unemployment will gradually appear.

There will be no economic stability, which is the cornerstone for achieving financial stability (Agmour et al., 2018).

c)   General liquidity

Defining the concept of general liquidity in the economy varies depending on the degree of development and growth of the banking system for that economy, where the conceptual framework of public liquidity goes back to the Radcliffe approach (Oster, 2019). General liquidity has been defined as reflecting the overall liquidity position of the economy, and it is an essential factor. It influences spending decisions on goods and services, and public liquidity represents the mechanical center of economic policy. The economic meaning of general liquidity is the relative turn of investors of their securities into cash, that is, the degree of flexibility in which certain assets are converted into cash. European Commission for Economic and Financial Affairs has defined public liquidity as "a term used in the science of economics and finance to describe the ease of obtaining money; if companies and individuals in a particular economy can obtain the money they need for consumption and investment purposes, this leads to raising the level of economic activity" (Stojanović, 1986). The components and degrees of general liquidity can be summarized as legal money. It is the highest degree of liquidity because of its widespread acceptance in all economic transactions, the possibility of their transformation into goods and services, and the strength of their legal obligation to pay the debt. There is no right for creditors not to accept them because of their power. Legal releases, in addition to their characteristics of generality, binding, and comprehensiveness, are related to the multiple functions of money as a medium of exchange, a measure, a store of values, a unit of account, and an instrument of payment. In the deferred compensation, we find that money is on top of the liquid assets and then comes other assets, each according to their degree of liquidity and not to risk converting their capital value into cash without losses.

4-   ANALYSIS AND DISCUSSION

a)   Iraq's GDP and annual growth rate

Iraq's gross domestic product is shown in Figure 1. According to official World Bank figures, Iraq's GDP in 2021 was valued at 207.89 billion US dollars. Iraq's GDP accounts for just 0.01 percent of the global economy.
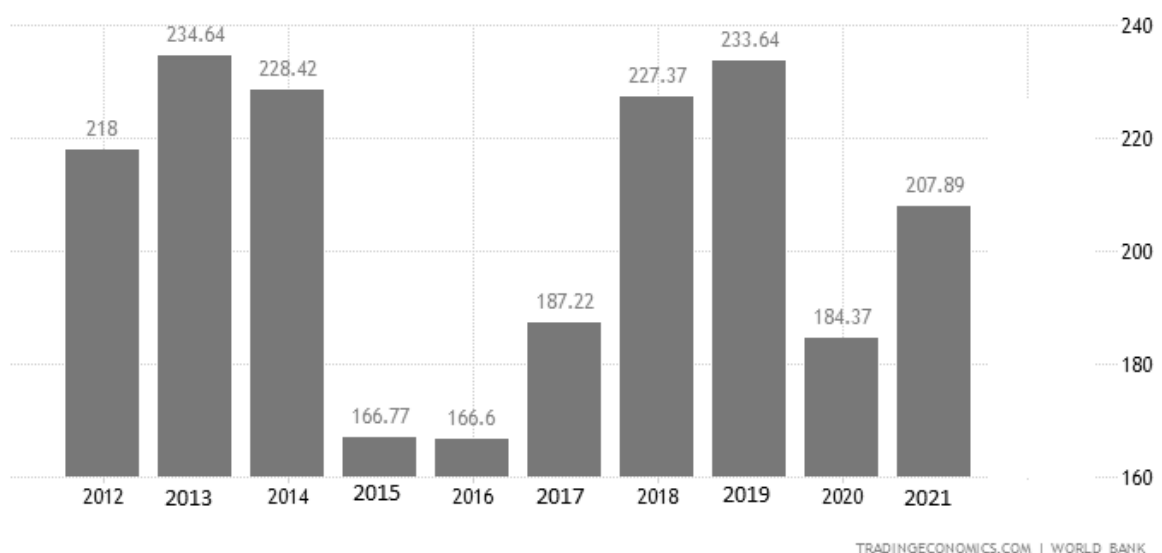

Figure 1: Iraq's gross domestic product is illustrated. From 2012 to 2021, Iraq's GDP averaged 63.44 billion dollars, with record highs of 234.64 billion dollars in 2013 and 166.77 billion dollars in 2015 [World Bank, 2023].

The Gross Domestic Product (GDP) in Iraq expanded 5.90 percent in 2021, as shown in Figure 2 below.
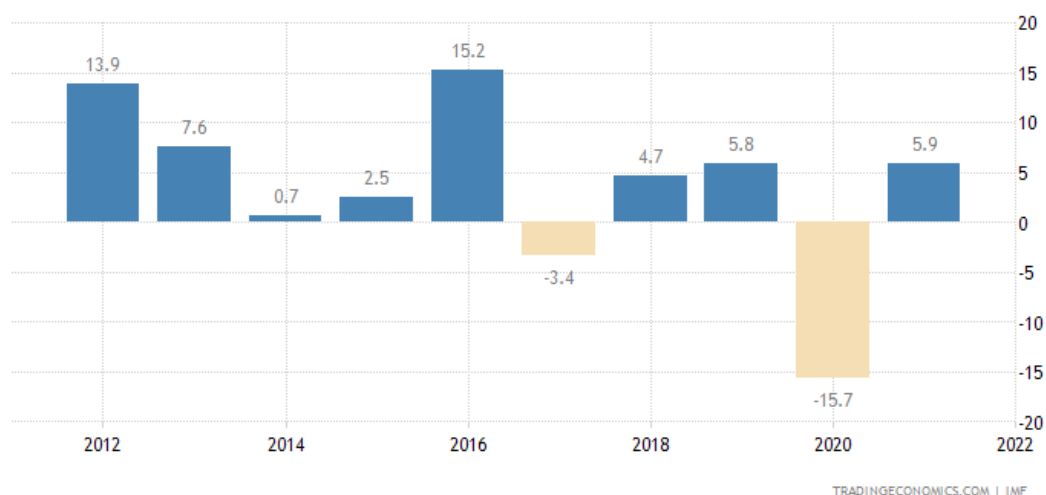
Figure 2: Graphical explanation of Iraq's GDP growth rate [World Bank, 2023]

With a share of GDP of 55%, the oil industry is Iraq's most significant economic sector. Thirty-three percent of the output is made up of the services industry. The three largest service sectors by GDP are community, social, and personal services (13%); finance, insurance, and real estate services (9%); retail and wholesale commerce; and restaurants and hotels (7 percent). Agriculture, forestry, hunting, and fishing make up the remaining 4% of the wealth, while manufacturing, building, and the distribution and production of water and energy comprise 8% of total wealth (Figure 2). GDP is calculated as the total gross value added by all producers who are residents of the economy, plus any applicable product taxes and unaccounted-for subsidies. It is estimated without considering the deterioration and depletion of natural resources or the depreciation of manufactured assets [World Bank,2023]. The World Bank's collection of development indicators, assembled from officially recognized sources, shows Iraq's annual percentage growth rate of GDP at market prices based on constant 2010 US Dollars. Actual figures and predictions for Iraq's GDP at market rates based on constant 2010 US dollars were obtained from the World Bank in October 2022 (Figure 3).
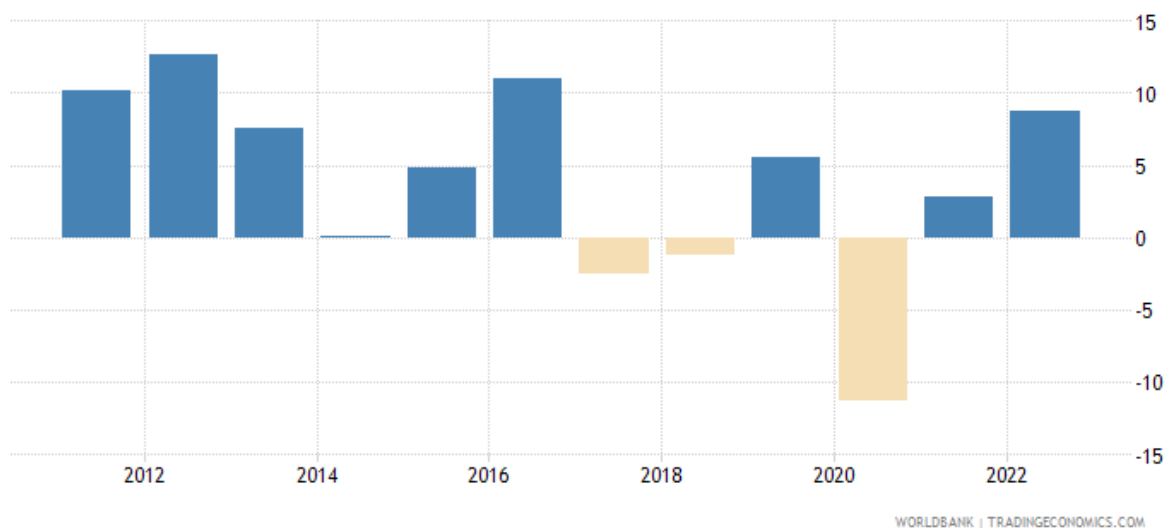

Figure 3: Graphical explanation of Annual Percentage Growth Rate of GDP at market prices [World Bank, 2023]

b)   *Fiscal Policy Instruments Track*

Fiscal policy is one of the main factors in achieving and sustaining economic stability through its ability to control inflation rates on the one hand and unemployment on the other hand. This is thanks to the tools available to them. As mentioned earlier, a topic taught us that the most

important fiscal policy tools are: public expenditures, public revenues, and the budget. The following is a review of the changes to these tools in Iraq during the study years (Table 1).

Table 1: Financial policy tools in Iraq for a period

Years	Public Expenditure (Billion Dinar)	Growth Rate Overhead %	Public Revenue (Billion Dinar)	Growth Rate Revenue %	Budget Public Balance (Billion Dinar)	Growth Rate Budget %
2012	105,140	51	119, 817	20	14, 678	-52
2013	119,128	13	113, 840	-5	-5,287	-136
2014	113,474	-5	105, 387	-7	-8,087	53
2015	70,398	-38	66, 391	-37	-4,007	-50
2016	67,067	-5	54, 409	-18	-12,658	216
2017	75,490	13	79, 011	45	3,521	-128
2018	80, 873	7	91, 644	16	10,770	206
2019	111, 724	38	107, 567	17	-4,157	-139
2020	76, 082	-32	63, 200	-41	-12, 883	210

*Source:
- Ministry of Finance, Budget Department, Iraq's general budget, different years.
- Central Bank of Iraq, Directorate General of Statistics and Research, Annual Statistical Bulletins, years

Public expenditures fluctuated between high and low until the year (2013) when general prices reached their highest level. During the research period, it amounted to (128,119) billion dinars, with a growth rate of (13%). Public expenditures are on the way to decreasing further, as the decline of public spending was due to the lack of budget approval. In (2014) it prompted the Ministry of Finance to restrict spending from the actual monthly expenditures. Public spending increased as compared to the previous year, and this increase is attributed to (13%) in 2017, reaching (490.75) billion dinars to the rise of most components of spending, especially capital expenditures, service requirements, commodity requirements, and the rest exchange doors in varying proportions. Public expenses continued to rise for the following years until the year 2019 (where they reached (724,111) billion dinars, recording a growth rate of (38%). In the year (2020) public expenditures decreased by 32%. General revenues constitute the basis on which to finance public expenditures that the state performs through its financial activities, and following the goals it seeks to achieve through its economic policy, the state's general budget, which is one of the most important financial planning tools, because it is the essential tool that defines the government's objectives, programs, policies, and how resources are used and distributed. In 2017, the general budget recorded a state of improvement, as the available funding recorded this year a financial surplus of the amount of (521,3) billion dinars, and in 2019 (the general budget recorded a deficit of (157.4) billion dinars. This is due to the increase in public expenditures, which is matched by an insufficient increase in public revenues.

c)   The impact of fiscal policy tools on economic stability

In Table 2, it is possible to observe the growth in the money supply (the quantity of money) with its two parts (M1 - M2) and compare it. The rate of growth of the gross domestic product, and this indicates that the Iraqi economy is recording a significant increase in size and the means of payment, where it is noted that the growth rate of the money supply records a state of growth throughout the research period, and this indicates that there is a cash surplus. An increase in the volume of means of payment by an amount that exceeds the local potential in the provision of services and goods makes the price trends a dangerous escalation case and, thus, the occurrence of cash instability.

i. The impact of public expenditures on economic stability

The data mentioned in Table (2) that the economic stability coefficient of both types were affected. In 2016 (65.0 percent), public expenditures declined, but the economic stability coefficient was deflationary. The economic stability coefficient continued. It fell significantly away from the stable state and registered pressure. The fluctuation in the following period between high and low is affected by the decrease in public expenditures; the more they increase public expenditures, the closer the economic stability coefficient is to the state of inflation, and vice versa, the lower the expenses. In general, the economic stability coefficient was recorded in the case of instability (inflationary or deflationary pressures). The relationship between public expenditures and the liquidity rate is discussed in Table 2. Next, for example, the public spending in the first years of the research was relatively low, and therefore the liquidity rate was recorded. In a rising state, it was far from a stable condition, and in the following years, when public expenditures began to rise, began liquidity rate declined, approaching 2012 (which is the period of stability in the year). The downward trend was recorded due to the rise in public expenditures, and the liquidity rate continued. The liquidity rate recorded a significant increase, with a boost and a decrease in the following years (2012-2020). The following figure shows the changes for each public expenditure and the liquidity ratio (2012-2020).

ii. The impact of public revenues on economic stability

The following Table 2 reviewed both public revenues and economic stability qualitatively. Through the data for each of them, we note in the year (2012) that the general revenues were at their highest value during the research period and that the stability coefficient is the financial record scored (11.0) and (24.0), which indicates deflationary pressures during this year. Still, in the year (2020), revenues decreased, and the stability coefficient deviated significantly from economic stability, recording a state of -0.56 and -0.67 with a shrinkage rate. In 2012, public revenues recorded the highest value, while the liquidity ratio decreased. The liquidity rate fluctuates with the fluctuation of general revenues.

Table 2: Financial policy tools and economic stability indicators in Iraq for the period (2004-2020) (Billion Dinar)

Years	Cash Offer M1 (1)	Modified growth M1 % (2)	Cash Offer M2 (3)	Modified growth M2 % (4)	For domestic product total GDP (5)	Modified growth GDP (6)	Economic stability indicators		
							Stability Cash M1 2/6	Stability Cash M2 4/6	Liquidity 1/5
2012	63,736	2	75,466	5	251,907	19	0.11	0.24	25
2013	73,830	16	87,679	16	271,100	8	2	2.12	27
2014	72,692	-2	90,728	3	258,900	-5	0.4	-0.77	28
2015	65,435	-10	82,595	-9	207,900	-20	0.5	0.46	31
2016	70,733	8	88,081	7	203,900	-2	-4	-3.45	35
2017	71,161	1	89,441	2	225,700	11	0.09	0.14	32
2018	68,766	-3	87,175	-3	254,800	13	-0.23	-0.20	27
2019	86,800	26	103,400	19	277,885	9	2.89	2.05	31
2020	103,400	19	119,900	16	198,774	-28	-0.67	-0.56	52

* Source:
- Ministry of Finance, Budget Department, Iraq's general budget, different years.
- Central Bank of Iraq, Directorate General of Statistics and Research, Annual Statistical Bulletins, years
Scattered

iii. The effect of the general budget on economic stability

The general budget was significantly fluctuating between a deficit and a surplus during the research period. The available budget is in the form of debt. As for the economic stability coefficient in quality, it was far from the state of stability. Inflationary pressures during this year, the general budget recorded a surplus of 439.4 (the amount of) deflationary and in the following years rose billion dinars, while the economic stability coefficient decreased, recording pressures, the economic stability coefficient, then returned to decline. In 2020, economic stability coefficients were low, and their value was away from the state of stability. The general budget suffered from a deficit of (883.12)-billion dinars. As for the liquidity ratio, the liquidity rate is more and away from the state of stability, and during this period, the general budget recorded a surplus. The liquidity ratio was stable at the standard ratio, while the available funding recorded a surplus of (359.30) billion dinars. In the year (2020) the liquidity ratio was high, reaching (52%); the general budget was recording a deficit during that period. This deterioration in the economic stability coefficient indicates that the fiscal policy has not adopted a real stability goal. It also suggests that most of the measures taken by the financial policy involve managing and directing economic variables. The direction of economic stability is improper measures that led to the deteriorating growth rates of the domestic product. This is evidence of the absence of real trends to achieve stability and the lack of seriousness of the fiscal policy that followed in these years because it was unable to overcome the emergency conditions that the Iraqi economy faced during this period which had a vital role in the weak economic performance and fluctuations in economic stability.

5- CONCLUSION

The absence of economic visions and the lack of clarity on the direction of the economic system in Iraq led to the administration's weakness and the lack of transparency in the order of the economic system in Iraq. The country's economic policies, and the confusion of economic policies in their performance over the years of research, led to the scaling of the work of fiscal policy tools and reducing its role in achieving the goal of economic stability. The lack of economic awareness of individuals harmed the career of the financial policy's tools and indicators, distorted the economic market's functioning, and had a role in the lack of response indicators of economic stability to change. The significant dependence on oil revenues and the fluctuation of their prices in the world markets occurred in the Iraqi economy's growth rate, which almost entirely depends on oil imports to finance expenditures. This, in turn, robbed the fiscal policy of much of the effectiveness of their tools, causing a state of the inadequacy of economic stability during the years of research. The economic stability coefficient did not record any state of stability during the research period, despite the fluctuation. In the coefficient of stability, the dominant feature is deflationary pressures. The liquidity rate was far from stable for most of the research period and recorded a state of contraction in most of the years. The economic stability coefficient that was extracted from the money supply in the narrow sense (M1) is not very different from the economic stability coefficient that was removed from the money supply in the broad sense (M2). In most cases, it was more influential on the economic stability coefficient than the rest of the fiscal policy tools. Work to rationalize Iraq's public expenditures, which continue to rise significantly, by following the principles of more effective to ensure accurate and actual economic stability, reconsidering the methods and tools pursued by fiscal policy in dealing with economic instability, in the way to create a mechanism or means that is more effective to reach stability cash, building a monetary policy aimed at revitalizing the agricultural, productive, industrial and tourism sectors, to fill increasing demand, and reducing dependence on imports (which causes inflationary pressures), causes a state of non-existence economic stability.

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