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On the Coordination of China's Fiscal Policy and Monetary Policy

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Abstract

Monetary policy and fiscal policy are the center of modern macro policy. The report of the 19th National Congress of the Communist Party of China clearly stressed that "China's economy has developed from a period of high-speed growth to a period of high-quality development", and the coordination and cooperation between fiscal policy and monetary policy is very important. Compared with the rapid development of monetary policy and fiscal policy itself, the coordination and cooperation between monetary policy and fiscal policy has made slow progress. Therefore, based on relevant cases, this paper analyzes the coordination of China's fiscal policy and monetary policy in detail, hoping to provide effective reference for relevant people in the same industry.

Keywords

China's Fiscal Policy; Monetary Policy; Coordination and Cooperation.

1. Introduction

The basic objectives of monetary policy and fiscal policy are consistent, the transmission mechanism is interlinked, and the policy means are complementary. The efficient coordination of monetary policy and fiscal policy plays a key role in the sustainable development of the national economy. However, with the economic development entering the new normal, it is difficult to continue the rapid economic growth for nearly 40 consecutive years. In addition, the previous macro-control model can no longer meet the new requirements of the new period. In order to solve this problem, we must adjust and optimize the monetary policy, and more importantly, effectively cooperate with the efficient cooperation of fiscal policy and monetary policy.

2. Fiscal and Monetary Policy

2.1. Fiscal Policy

Improving employment level, reducing economic turbulence, preventing inflation and allowing it to grow continuously, as well as fiscal expenditure, taxation and government debt are relevant fiscal policies. The main tool is government financial payment and revenue. From the perspective of expenditure, government expenditure at all levels mainly includes government procurement and remittances, that is, government procurement of goods and services such as public project expenditure. Remittances refer to government expenditures on social security, poverty reduction and subsidies. Government expenditure, especially government procurement expenditure, will directly affect the increase or decrease of total social demand, and will have a significant impact on the management of macroeconomic aggregate. From the perspective of revenue, the revenue of governments at all levels includes, inter Alia, fiscal revenue and public debt. Tax is a means for the state to obtain obligatory and free financial revenue according to the standards stipulated by law. Public debt is a kind of public debt, which is a special form of financial financing raised by the government according to credit guarantee. In addition, other forms of management fees and state-owned capital projects are government revenue. Tax, like procurement expenditure and government remittance, has a multiplier effect

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on the change of national income. Government revenue and expenditure are the main sources of revenue and expenditure. Intervention in the economy is one of the main policies of fiscal policy, which is mainly biased towards the adjustment of government revenue and expenditure, and then used to change the overall demand and achieve the impact on national employment and income. The scale and intelligence of the national economy are also related to fiscal policy. It is mainly divided into three parts: ① Expansionary fiscal policy; ② Narrow fiscal policy; ③ Neutral fiscal policy. The economic cycle organization has divided it into automatic stable fiscal policy and discretionary fiscal policy.

2.2. Monetary Policy

Monetary policy, namely fiscal policy, is the policies and measures taken by the People's Bank of China to achieve its specific economic objectives. The purpose is to control the public supply of money and credit. Monetary policy mainly includes credit policy, interest rate policy and foreign exchange policy. In essence, this is the different stages of economic development and the different policy trends of "narrow", "loose" and "slow" in money supply. Monetary policy tools can be divided into general tools, selective tools and auxiliary tools. Public tools are three tools to adjust the amount of money: legal reserve rate, open market operation and tax rebate policy. Selective monetary policy tools include consumer credit control, securities market credit control, preferential interest rate, advance payment of import guarantee, etc. Auxiliary monetary policy includes the control of direct credit and indirect credit, and the main mechanism of monetary policy is to control the market interest rate through various money supply regulatory tools, so as to affect private capital investment, and then affect macro demand and even macroeconomic performance. Monetary policy can be divided into two categories: expansionary monetary policy (active monetary policy) and deflationary policy (sound monetary policy).

3. The Impact of Fiscal Policy and Monetary Policy on Inflation

Based on the empirical analysis of VAR model, this chapter will use China's historical data of 29 years from 1991 to 2019 to construct VAR model for analysis, and the conclusions will provide an important reference for the policy proposal in the next chapter.

3.1. Selection and Description of Empirical Data

When measuring inflation, this paper uses the inflation rate (recorded as INF) calculated by CPI to express it. When measuring fiscal policy, the fiscal expenditure with the greatest impact on inflation is selected as the measurement basis. At present, the fixed base budget method is often used in the formulation of budget plans, and the growth rate of fiscal expenditure (recorded as FEG) is selected in the data analysis, which is also convenient to make the conclusion more suitable for the needs of policy formulation. When measuring monetary policy, we take the index of the change directly brought about by the regulation of monetary policy, the growth rate of generalized money supply (recorded as MSG), as the measurement basis. At the same time, we also select the growth rate of generalized money for quantitative analysis. The inflation rate is converted from China's CPI data, and the changes in growth rates are also converted from absolute quantities. The data are derived from China Statistical Yearbook. In the selection of research model, this paper makes a quantitative analysis of the long-term dynamic relationship between variables through vector autoregressive model. VAR model takes all variables as endogenous variables and brings them into each regression equation, which can comprehensively analyze the two-way dynamic characteristics between variables. At the same time, the model is less constrained by traditional theories, so it is a worthy method in time series analysis. Generally, for p-order vector autoregressive process, VAR (P) system is constructed:

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$$Z_t = X_0 + X_1 Z_{t-1} + \cdots + X_p Z_{t-p} + \varepsilon_t\ ,\ \ \varepsilon_t \sim N(0, \sigma_t^2),\ \ t = 1, \cdots, n$$

Including ZT, x0, εT is an n-dimensional column vector, and XP is n when the lag order is p × N-order coefficient matrix, t is the number of selected sample dependent variables, P is the number of lag periods, and it is assumed that there is no autocorrelation in the residual vector.

3.2. Empirical Analysis Results

The empirical results are obtained:

3.2.1. Monetary Policy has a Rapid and Dramatic Impact on Inflation, and May have a Lagging Inhibitory Effect on Inflation under Certain Conditions

A reasonable explanation is that the high inflation rate caused by the increase of short-term money supply will form the expectation of the future government's tightening monetary policy, so prices can't continue to grow in the long term. However, in the short term, the timely positive effect of monetary policy is the most significant.

3.2.2. Fiscal Policy is More Effective than Monetary Policy in Controlling Inflation in the Long Run

The impact of monetary policy plays an intense regulatory role in the short term, but it subsides rapidly. When formulating long-term policies and plans, we need to give more consideration to the means and methods of financial regulation and control, so as to ensure the long-term stable and effective operation of the economy.

In short, fiscal expenditure and money supply not only have a certain impact on China's inflation, but also restrict each other in different ways and degrees.

3.3. Policy Suggestions

3.3.1. Accelerate the Transformation and Optimization of the Economic Structure and Optimize the Supply and Demand Structure

In recent years, China's economic development has gradually slowed down, and a new round of industrial revolution in the world is growing. The new round of economic take-off urgently needs the transformation and development of industrial structure and supply structure, improve supply capacity and quality, and curb inflation risk. Therefore, we should strengthen the guidance of fiscal policy, strengthen the support of innovative enterprises and industries, reduce the burden for small and medium-sized enterprises, and provide exit mechanism and policy channel for transformation and upgrading for traditional industries and backward production capacity. At the same time, monetary policy takes the word "stability" as the head, provides auxiliary support for fiscal policy, and ensures the smooth operation of money market in the transformation of market structure. Accelerate the transformation, optimization and upgrading of economic structure, create new economic growth points, and improve the two major cycles at home and abroad.

3.3.2. Improve the Fiscal and Monetary System and Flexibly Use the Combination of Policy Tools

Both fiscal policy and monetary policy are the means of government intervention in the economy. To meet new opportunities and challenges and achieve stable and healthy high-quality development, we need to improve the fiscal and monetary system and the coordination mechanism between policy tools, combine the short-term and long-term regulatory effects of policy tools, especially pay attention to adjusting the structure of fiscal expenditure and flexibly use diversified monetary policy tools to reduce the negative impact of inflation on economic development.

3.3.3. Build a Monitoring System for Policy Effects and Track and Monitor Policy Effects

Generally, there is a deviation between the theoretical effect and actual effect of policy role. To effectively carry out macroeconomic regulation, it is necessary to build a reasonable monitoring system, determine a series of evaluation standards, clarify the key economic indicators on the policy transmission chain, track and observe their changes at any time, and adjust the policy plan in time. Therefore, we should not only consider the influencing factors from multiple angles before policy formulation, but also carry out effective monitoring after specific implementation, so as to achieve the final macro-control goal.

4. Conclusion

In a word, the effective coordination between fiscal policy and monetary policy has always been centered on ensuring national economic development. In the process of China's long-term economic practice, the effective coordination between fiscal policy and monetary policy is becoming more and more skilled, and its effect is becoming more and more remarkable.

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