Ricardian vs non-Ricardian Regimes in the Long-Run Posture of Turkish Public Finances

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Abstract

There are two competing theories in the literature regarding the interactions between monetary and fiscal policies for achieving fiscal stability, namely, the monetary dominant (Ricardian) regime and the fiscal dominant (non-Ricardian) regime. The former refers to the case where the government adjusts the primary balance for restoring fiscal stability no matter what the price level is which liberates the central bank in the price determination procedure. In the latter setting, however, the primary balance set by the fiscal authorities follows an arbitrary process and they do not make a binding commitment to reach fiscal sustainability. In such a case, the fiscal policy in a way impels the central bank to adjust the price level endogenously to the primary surplus generated by the budgetary authorities for preserving fiscal stability. In this context, the central bank can only detect the timing of inflation. In this study, we attempt to explore the posture of Turkey from the viewpoint of these theories and empirically determine which policy is active in Turkish public finances. For this purpose, we use the primary balance and public debt series retrieved from the IMF database which covers the 1970-2019 period. We carry out the empirical analyses via ARDL and Toda-Yamamoto causality test techniques. The empirical findings suggest that the monetary dominant (Ricardian) regime is actively employed in Turkey, which implies that the primary surplus is endogenously determined based on the public debt realizations.

Keywords: Fiscal stability, Ricardian Regime, Non-Ricardian Regime, Public Debt

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