

MONETARY-FISCAL POLICY COORDINATION AND MACROECONOMIC STABILIZATION: EVIDENCE FROM THE EUROPEAN UNION

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Abstract

Periods of economic turbulence pose significant challenges for macroeconomic stabilization and policy design. This paper examines the interaction between monetary and fiscal policies and assesses their joint effectiveness across three major crisis episodes affecting the European Union between 2008 and 2023: the Global Financial Crisis and the sovereign debt crisis that followed, the COVID-19 pandemic, and the inflationary surge of 2022 and 2023. While traditional frameworks emphasize the independence of monetary policy and the countercyclical role of fiscal policy, all three episodes demonstrated the increasing necessity of coordinated responses. The analysis adopts a qualitative and comparative approach, drawing on data from Eurostat, the European Central Bank, the International Monetary Fund, and the European Commission, focusing on real GDP growth, HICP inflation, general government consolidated gross debt, and fiscal balances. The findings suggest that effective stabilization depends not on the individual strength of monetary or fiscal instruments, but on their alignment within a coherent policy mix. Coordinated responses produced stronger stabilization outcomes, while misalignment generated real economic costs that proved difficult to reverse. The GFC demonstrated the damage of premature fiscal consolidation when monetary policy is constrained by the effective lower bound, while the pandemic response illustrated what becomes possible when both policy domains pull in the same direction. The inflationary episode that followed revealed that maintaining alignment is hardest when the short-term objectives of monetary and fiscal policy begin to diverge. The paper concludes that coordination mechanisms can considerably improve macroeconomic resilience. The EU's asymmetric institutional architecture, combining centralized monetary policy with decentralized fiscal authority, remains a structural challenge that instruments such as NextGenerationEU have only partially addressed.

Keywords

Monetary-fiscal policy coordination; Fiscal policy; Monetary policy; Policy mix; Macroeconomic stabilization; Economic turbulence; European Union.

JEL Classification: E52, E62, E63, F45, H12

1. Introduction

Macroeconomic stabilization has long been a central objective of economic policy, particularly during periods of sharp output contraction, financial instability, and high uncertainty. In standard frameworks, monetary and fiscal policy have independent roles: central banks manage price stability through interest rates and liquidity provision, while governments influence aggregate demand through spending and taxation. This institutional separation has traditionally been regarded as a prerequisite for credibility and sound macroeconomic management.

The Global Financial Crisis (GFC) of 2008-2009, the COVID-19 pandemic of 2020-2021, and the inflationary surge of 2022-2023 challenged this paradigm in successive ways. Each episode demonstrated that isolated policy interventions are often insufficient when economies face simultaneous shocks to financial markets, supply, and aggregate demand. As interest rates approached the effective lower bound during the GFC, unconventional monetary measures alone proved inadequate without fiscal support. Similarly, the unprecedented scale of the pandemic shock required a combination of large-scale fiscal expansion and highly accommodative monetary conditions to prevent deeper economic collapse (Bernanke, 2020). The inflationary surge that followed illustrated the opposite risk: that once inflation takes hold, sustained accommodation creates coordination tensions that are difficult to resolve without imposing real economic costs.

These experiences suggest that policy effectiveness depends not only on the strength of individual instruments, but critically on the degree to which monetary and fiscal policies are aligned, credibly communicated, and well-sequenced (Blanchard, 2019).

The European Union provides a particularly instructive setting for examining these dynamics. Its asymmetric institutional architecture, combining centralized monetary policy under the European Central Bank with decentralized national fiscal authorities constrained by the Stability and Growth Pact, creates structural tensions that amplify the consequences of coordination failures (Mundell, 1961). The EU's experience across three distinct episodes: the GFC, the pandemic, and the inflationary surge of 2022–2023, illustrates both the possibilities and the limits of policy coordination under an incomplete monetary union.

This paper examines how monetary-fiscal policy coordination influences macroeconomic stabilization during periods of economic turbulence, with particular focus on the European Union between 2008 and 2023. The analysis draws on macroeconomic theory and empirical evidence from institutional sources to assess how policy alignment, timing, and credibility shaped stabilization outcomes across the three episodes.

2. Literature review

The interaction between monetary and fiscal policy has occupied a central place in macroeconomic thinking for decades, and for good reason. Few questions bear more directly on a government's ability to stabilize its economy during periods of stress, and the literature has evolved considerably over time, moving from a theoretical distinction between the two policy domains toward admitting that their effectiveness is interdependent.

The analytical foundations of this interdependence were laid by Leeper (1991), who showed that macroeconomic stability hinges not on the strength of either policy instrument taken alone, but on the configuration of the two together. An active monetary authority paired with a passive fiscal authority produces one set of outcomes; reverse the configuration and the results can differ substantially. Woodford (2004) built on this insight by placing expectations at the center of the transmission mechanism, arguing that what matters is not only what policymakers do today, but what households and firms believe they will do in the future. So, credibility is not a luxury, but a precondition for policy effectiveness. Blanchard (2019) pushed the argument further, showing that in low interest rate environments the boundary between monetary and fiscal policy begins to dissolve. Fiscal expansions can become self-sustaining in ways that earlier frameworks had not anticipated, and the case for coordination becomes correspondingly stronger.

A related body of work has examined what these theoretical insights mean in the specific institutional context of the European Union, an environment that, as Mundell (1961) identified long before the euro existed, creates particular vulnerabilities by combining a single monetary policy with decentralized fiscal authorities. The sovereign debt crisis of 2010-2012 gave these theoretical concerns an uncomfortably concrete form. De Grauwe (2011, 2018) argued that euro area member states are structurally exposed to self-fulfilling liquidity crises in a way that monetarily sovereign countries are not, because they cannot issue debt in a currency they control. Obstfeld (2013) traced the feedback loops between sovereign stress and financial instability that amplified the crisis and proved so difficult to break. Blanchard and Zettelmeyer (2021) concluded that the asymmetry in fiscal capacity across member states is not an accident or a temporary condition, but a structural feature of the monetary union that episodic instruments cannot fully compensate for, however well-designed those instruments may be.

The empirical literature developed during successive crises has significantly expanded this understanding. Reinhart and Rogoff (2009, 2010) established how deep and prolonged the recessions associated with financial crises and sovereign debt episodes tend to be, providing a benchmark against which policy responses can be meaningfully evaluated. Blanchard and Leigh (2013) provided some of the most consequential empirical findings of the post-GFC period,

demonstrating that fiscal multipliers had been systematically underestimated during the consolidation phase, with the result that austerity proved more contractionary than policymakers had anticipated. This finding strongly influenced the way European institutions managed the withdrawal of fiscal support during the pandemic recovery. The IMF's World Economic Outlook series (IMF, 2013, 2021, 2022, 2023) offers a running empirical record of how policy effectiveness evolved across both crises, capturing the transition from coordinated stimulus to divergence and documenting its macroeconomic consequences. Altavilla, Giannone and Lenza (2014) emphasized that the ECB's OMT announcement in 2012 provided one of the clearest examples of the importance of institutional credibility, as sovereign bond spreads declined significantly even though no bonds were actually purchased. This outcome supports Woodford's argument that expectations play a central role in monetary policy effectiveness. More recently, Blanchard and Bernanke (2023) examined the debated causes of the post-pandemic inflation surge, a discussion with important implications for evaluating the monetary and fiscal policy mix implemented during 2022-2023.

What the existing literature has not done systematically is examine how coordination dynamics evolved across three distinct crisis episodes within the same institutional framework, and what the experience of each episode meant for the responses that followed. Most studies focus on a single shock, or treat the EU's policy architecture as a static backdrop rather than an evolving institutional reality. This paper attempts to fill that gap by tracing monetary-fiscal coordination across the Global Financial Crisis, the COVID-19 pandemic, and the inflationary surge of 2022-2023, with particular attention to the ways in which institutional learning and institutional constraint shaped outcomes at each turn.

3. Theoretical framework

3.1 monetary policy and transmission mechanisms

Monetary policy is a central instrument of macroeconomic stabilization, aimed at maintaining price stability and smoothing fluctuations in economic activity. Central banks influence aggregate demand mainly through short-term interest rates and liquidity conditions, with effectiveness strongly dependent on credibility, institutional design, and expectations (Woodford, 2004).

Transmission operates through multiple channels. The interest rate channel affects consumption and investment via borrowing costs and intertemporal decisions (Mishkin, 1995), while the credit channel highlights the role of bank lending and external finance constraints in amplifying policy effects (Bernanke et al., 1999). Expectations are central, as credible central banks shape inflation expectations and enhance policy effectiveness through forward-looking behavior. In open economies, the exchange rate channel transmits monetary shocks through trade flows and currency adjustments.

Monetary policy also affects financial stability through risk-taking and leverage dynamics. Low interest rates may encourage excessive risk-taking, while monetary conditions influence leverage cycles and credit supply in financial intermediaries (Adrian & Shin, 2010).

When policy rates approach the effective lower bound, conventional tools lose effectiveness, leading to liquidity trap conditions (Krugman et al., 1998). In response, central banks use unconventional instruments. Quantitative easing operates through portfolio rebalancing and term premium compression (Gagnon et al., 2011), while forward guidance shapes expectations about future policy paths (Del Negro et al., 2012). Targeted credit operations are also used to stabilize stressed financial segments.

3.2 Fiscal Policy and Demand Management

Fiscal policy affects the economy through government spending, taxation, and transfers, influencing consumption, investment, and overall demand. It plays an important stabilizing role, especially when private demand weakens.

During recessions, fiscal stimulus is often more effective because unused economic capacity allows increases in public spending or tax cuts to translate more directly into higher output (Blanchard, 2019). Public investment tends to have more persistent effects than temporary transfers, while automatic stabilizers help smooth fluctuations without new policy decisions (Blinder, 2004).

However, fiscal policy is constrained by public debt, which can limit fiscal space and increase borrowing costs. It is also influenced by political and institutional factors that may delay or weaken responses, as well as by implementation lags.

3.3 The Policy Mix and Strategic Interaction

The effectiveness of macroeconomic stabilization does not depend only on monetary and fiscal policy taken separately, but also on how they work together. When these two policies are aligned, they tend to reinforce each other and produce stronger and more stable economic outcomes. When they are not well coordinated, their effects can partially cancel out, making policy less effective overall (Leeper, 1991). At the same time, as Mugur Isărescu (2022), the governor of National Bank of Romania, emphasizes, effective coordination, presupposes a clear division of labour as a starting point: economic growth is promoted through structural and fiscal measures, price stability is the responsibility of monetary policy, and external competitiveness is supported by fiscal and income policy together. Only once these roles are clearly assigned can the two policy domains be meaningfully coordinated.

In practice, monetary and fiscal authorities constantly influence each other's decisions. Each side reacts not only to economic conditions, but also to what it expects the other side will do. For example, fiscal expansion tends to have a stronger impact when monetary policy supports it, while tighter monetary policy can reduce part of the effect of fiscal stimulus. Because of this, what ultimately matters is the overall combination of policies, not just each one individually. As Leonardo Badea (2021), the first-deputy governor of National Bank of Romania, emphasizes, the whole toolkit of monetary policy must act synchronously within the broad framework of the macroeconomic policy mix, alongside fiscal policy, macro-prudential policy, and structural policies, given that monetary policy acts mainly on short-term demand and has no influence on supply dynamics.

Expectations and credibility are also very important in this process. When people and firms believe that monetary and fiscal authorities are acting in a consistent and predictable way, uncertainty decreases and their behavior becomes more stable. This makes policy more effective in influencing real economic activity (Woodford, 2004). On the other hand, if policies seem inconsistent or poorly coordinated, confidence can weaken, and households and firms may react more cautiously, reducing the impact of policy measures.

3.4 Fiscal Dominance vs. Monetary Dominance

The relationship between fiscal and monetary policy is central to understanding macroeconomic stability. In practice, the balance of responsibility between these two authorities can vary depending on economic conditions and institutional arrangements.

Under fiscal dominance, monetary policy is effectively constrained by fiscal needs, particularly in contexts of high public debt. In such situations, the central bank may be inclined to maintain lower interest rates in order to support government financing conditions. While this can ease short-term fiscal pressures, it may also undermine price stability and increase the risk of inflation if monetary policy becomes less focused on its primary objective (Blanchard, 2019).

By contrast, monetary dominance refers to a regime in which the central bank maintains a clear priority on price stability, while fiscal policy adjusts to ensure debt sustainability. This arrangement is generally effective in anchoring inflation expectations and preserving monetary credibility. However, it may also reduce the flexibility of fiscal policy during periods of economic stress, when more active fiscal intervention may be required.

In practice, most economies operate between these two. The interaction between monetary and fiscal authorities is therefore characterized by a continuous need for balance: sufficient independence to ensure credibility, but also enough coordination to allow effective responses to large macroeconomic shocks. Excessive dominance in either direction can generate macroeconomic imbalances, while a more balanced configuration supports both stability and policy effectiveness.

As Isărescu (2015) observes, the countercyclical stance of both monetary and fiscal policies is essential for ensuring a smooth trajectory of the economy, and successful monetary policy is predicated on healthy fiscal policy and vice versa, since in the absence of a consistent macroeconomic policy mix, even well-designed central bank policies are likely to achieve at best sub-optimal outcomes.

4. Methodology

This paper adopts a qualitative and comparative analytical approach, combining theoretical insights from the macroeconomic literature with empirical evidence drawn from institutional sources. The analysis covers the period from 2008 to 2023, encompassing three distinct crisis episodes: the Global Financial Crisis and its sovereign debt aftermath, the COVID-19 pandemic, and the inflationary surge of 2022 and 2023. This timeframe was selected deliberately to allow for a structured comparison of coordination dynamics across episodes of fundamentally different character, within the same institutional framework.

The empirical evidence is drawn from data published by Eurostat, the European Central Bank, the International Monetary Fund, and the European Commission, focusing on four key macroeconomic indicators: real GDP growth, HICP inflation, general government consolidated gross debt as a percentage of GDP, and general government deficit and surplus as a percentage of GDP. These indicators were selected because they capture, respectively, the output consequences of policy decisions, the price stability dimension of monetary policy, the fiscal sustainability constraint on countercyclical policy, and the discretionary fiscal stance adopted during each episode.

The comparative approach examines the policy responses adopted during each crisis episode, assesses the degree of coordination between monetary and fiscal measures, and evaluates the outcomes in light of the main theoretical predictions from the literature. The analysis aims to identify the conditions under which coordination succeeded or failed and to draw lessons relevant for future policy design. The qualitative nature of the approach is a deliberate methodological choice, reflecting the complexity of the policy interactions examined and the difficulty of isolating the effects of coordination from the broader macroeconomic context in which it occurred.

5. Analysis and discussion: european union policy mix (2008–2023)

5.1 institutional context

The European Union represents one of the most distinctive cases for studying macroeconomic policy coordination. Its institutional architecture combines a single monetary policy, administered by the European Central Bank for all euro area member states, with decentralized fiscal policies that remain under national jurisdiction, formally constrained by the Stability and Growth Pact. This asymmetric structure generates structural tensions that become particularly visible during periods of economic stress (Mundell, 1961). The absence of a common fiscal capacity at the federal level means that the adjustment burden falls disproportionately on

monetary policy and on national fiscal authorities whose room for maneuver is constrained by pre-existing debt levels (Obstfeld, 2013). Between 2008 and 2023, the EU experienced three major macroeconomic shocks of distinct character: the Global Financial Crisis and the following sovereign debt crisis (2008-2013), the COVID-19 pandemic shock (2020-2021), and the inflationary surge driven by supply disruptions and the Ukraine conflict (2022-2023). Each episode tested the capacity of European monetary and fiscal authorities to respond effectively, revealing both the strengths and the structural limitations of the EU's policy framework.

5.2 The Global Financial Crisis and the Euro Area Sovereign Debt Crisis (2008–2013)

The Global Financial Crisis triggered a sharp contraction in economic activity and a severe disruption of financial markets across advanced economies. Output declined rapidly, credit markets froze, and confidence collapsed, forcing simultaneous responses from both monetary and fiscal authorities. EU GDP contracted by approximately 4.3% in 2009, the steepest post-war decline recorded up to that point, with export-oriented and financially exposed economies experiencing the deepest contractions, while fiscally stronger economies proved more resilient (IMF, 2009).

Central banks reacted quickly by cutting policy interest rates aggressively, in many cases bringing them close to zero. As conventional tools became less effective, they introduced unconventional measures such as large-scale asset purchases and forward guidance to stabilize financial conditions and support credit flows. On the fiscal side, governments implemented expansionary stimulus packages in order to support aggregate demand, backed by the European Economic Recovery Plan, which called for coordinated fiscal stimulus of approximately 1.5% of EU GDP (European Commission, 2008). Fiscal multipliers during this period proved to be much larger than pre-crisis models had suggested, mainly in economies operating near the effective lower bound (Christiano et al., 2011).

The crisis quickly revealed the fragility of sovereign debt positions in several peripheral economies like Greece, Ireland, Portugal, and Spain, whose fiscal balances deteriorated sharply as automatic stabilizers operated and banking sector liabilities were absorbed onto public balance sheets (Blanchard & Leigh, 2013). By 2010, a cyclical downturn had transformed into a structural sovereign debt crisis, as financial markets differentiated between member states on the basis of perceived fiscal sustainability (De Grauwe, 2011). Sovereign spreads for Greece widened to over 900 basis points relative to German Bunds by mid-2012, while Irish and Portuguese spreads exceeded 700 basis points (ECB, 2012), reflecting not only fiscal concerns, but also an implicit redenomination risk.

As illustrated in Figure 1, public debt trajectories diverged sharply across member states during this period, with Greece exceeding 170% of GDP by 2011 and Italy surpassing 130%, while Germany maintained comparatively stable debt levels below 80% of GDP, underscoring the structural asymmetry in fiscal positions that constrained the capacity for coordinated stabilization across the euro area. The pandemic shock of 2020 produced a second wave of debt increases visible across all economies, with Spain approaching 120% of GDP and the EU27 average rising to approximately 92% of GDP, before a gradual consolidation began in 2022 and 2023.

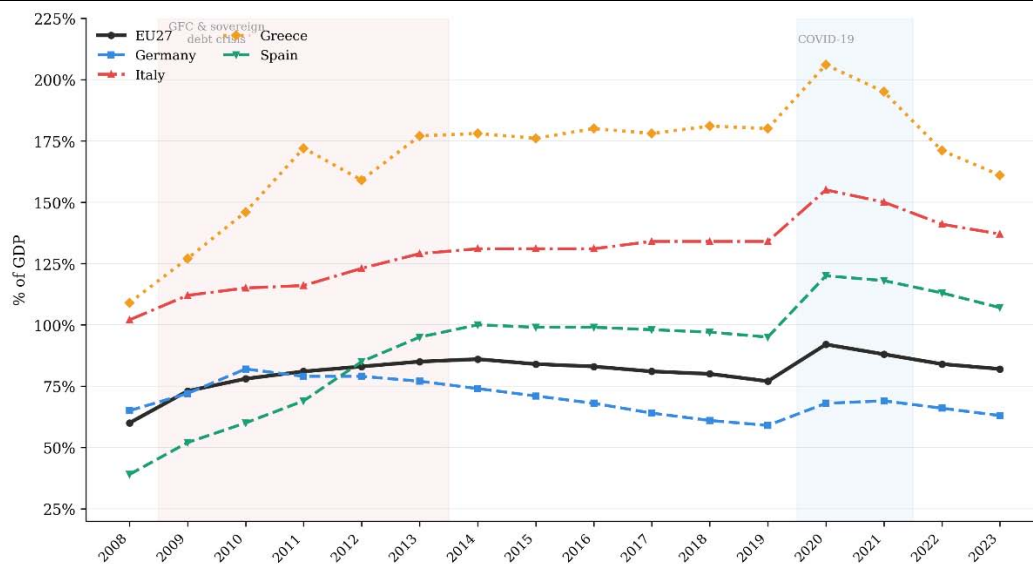


Figure 1. General government consolidated gross debt (% of GDP), EU27 and selected member states, 2008–2023

Source: own processing based on Eurostat data

As the initial recovery began, many countries quickly shifted toward fiscal consolidation while private demand remained weak. The Fiscal Compact of 2012 further institutionalized fiscal restraint, reinforcing the pro-cyclical bias of European fiscal governance exactly at the moment when countercyclical support was most needed (Fatás & Mihov, 2012). The simultaneous nature of fiscal tightening across multiple economies amplified its contractionary effect, a dynamic the IMF later acknowledged, admitting that fiscal multipliers had been significantly underestimated during this episode (IMF, 2013). As illustrated in Figure 2, EU27 GDP contracted sharply in 2009, partially recovered in 2010–2011, then contracted again in 2012, reflecting the double-dip dynamics produced by premature and synchronized fiscal adjustment across member states.

The ECB's response during this phase proved ultimately more decisive. In July 2012, ECB President Mario Draghi announced that the institution would do whatever it takes to preserve the euro, followed by the Outright Monetary Transactions program (ECB, 2012). Academic estimates suggest that the OMT announcement reduced sovereign spreads for Spain and Italy by approximately 200 basis points within weeks, demonstrating the extraordinary power of credible central bank communication even in the absence of actual instrument deployment. The policy mix during this period was therefore characterized by a fundamental asymmetry: monetary policy provided the decisive stabilizing impulse, while fiscal policy shifted too soon toward consolidation, producing a double-dip recession in the euro area between 2011 and 2013 (Blanchard & Leigh, 2013).

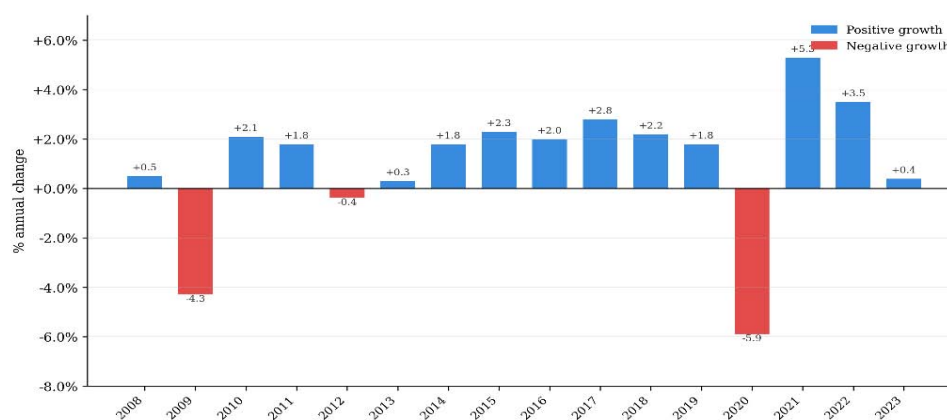


Figure 2. Real GDP growth rate (% annual change), EU27, 2008–2023

Source: own processing based on Eurostat data

5.3 the covid-19 pandemic (2020–2021)

The COVID-19 crisis represented a different type of shock: a simultaneous collapse in supply and demand originating in the real economy rather than the financial sector, triggered by mandatory lockdowns, mobility restrictions, and a rise in uncertainty. EU GDP declined by approximately 7.5% in 2020 (nearly double the contraction recorded during the GFC) with severe impacts in tourism-dependent economies such as Spain, Croatia, and Greece. Because the initial shock affected countries in a similar way, fiscal support became more politically acceptable, which increased the scope for coordinated policy responses. As Isărescu (2022b) recalls, governments and central banks stepped in simultaneously across the globe to counter the pandemic's negative impact through a combination of social, economic, fiscal and monetary measures, and this unprecedented mobilisation of authorities helped largely preserve the functioning of markets and economic mechanisms.

The European Commission activated the general escape clause of the SGP in March 2020, allowing member states to implement large-scale discretionary spending without triggering excessive deficit procedures (European Commission, 2020). Fiscal deficits widened to an average of approximately 7.2% of GDP across the EU, while aggregate public debt rose to approximately 92% of GDP (IMF, 2021). National support packages, including Germany's Kurzarbeit, France's chômage partiel, and Italy's Cassa Integrazione Guadagni, preserved employment and household incomes at a scale that would have been impossible under normal SGP constraints (IMF, 2021).

At the supranational level, the creation of NextGenerationEU, a €750 billion recovery programme funded through joint EU borrowing, represented a major change in how fiscal policy is managed in Europe. For the first time, the EU borrowed at scale on behalf of member states, introducing a degree of fiscal solidarity that economists had argued for years was a prerequisite for a resilient monetary union (Blanchard & Zettelmeyer, 2021). The ECB complemented fiscal expansion through the Pandemic Emergency Purchase Programme, a €1.85 trillion asset purchase program, enabling targeted spread compression in more vulnerable economies (Schnabel, 2020). ECB analysis estimated that PEPP purchases reduced 10-year sovereign yields in Italy and Spain by approximately 45-70 basis points relative to a counterfactual without the program (Altavilla et al., 2021).

The interaction between monetary and fiscal policy was broadly complementary: expansionary fiscal measures were supported by accommodative monetary conditions, which kept financing costs low, reduced borrowing constraints, and limited crowding-out effects. The coordinated policy mix contributed to a strong and rapid recovery: EU GDP rebounded by 5.3% in 2021, broadly recovering the output lost during the pandemic contraction (European Commission, 2022). The contrast with the post-GFC decade suggests that institutional learning had occurred, and that the lessons of the 2010-2013 episode had been at least partially internalized by European policymakers.

5.4 The Inflationary Surge and Policy Normalization (2022–2023)

As the recovery continued in 2021 and 2022, a strong rebound in demand, together with supply chain disruptions and higher energy prices, led to a rapid rise in inflation. On an annual average basis, HICP inflation in the EU reached 9.2% in 2022, the highest level recorded since the inception of the monetary union. At the monthly level, inflation in the euro area peaked at 8.4% in 2022 before gradually declining, driven primarily by energy price shocks following the Ukraine conflict, persistent global supply chain disruptions, and residual demand pressures from the pandemic recovery. Core inflation peaked above 5.7% in March 2023, indicating that price pressures had broadened beyond the initial supply-side impulse, while the inflationary shock was asymmetric across member states, with Baltic states and several Central and Eastern European economies recording monthly rates above 15% (Eurostat, 2022).

The ECB responded with the most rapid tightening cycle in its institutional history, raising the deposit facility rate from -0.5% in June 2022 to 4.0% by September 2023, an increase of 450 basis points in fourteen months (ECB, 2023). As illustrated in Figure 3, which tracks both the monthly HICP inflation and the monthly ECB deposit facility rate for the euro area between 2008 and 2023, the sharp monetary tightening cycle of 2022 and 2023 coincided with a gradual deceleration of inflation from its monthly peak. This illustrates the transmission lag between policy decisions and price dynamics. Nonetheless, several member states maintained expansionary fiscal stances through energy-related interventions and recovery investments, implementing energy support measures estimated at 1 to 3% of GDP on an annual basis (European Commission, 2022c). While each measure was justified on distributional grounds, the expansion in fiscal policy partly offset the effects of monetary tightening, which may have contributed to a longer period of high inflation by keeping demand elevated. This mismatch between fast monetary tightening and slower fiscal adjustment created coordination tensions that were different in structure from those after the GFC, but similar in analytical terms.

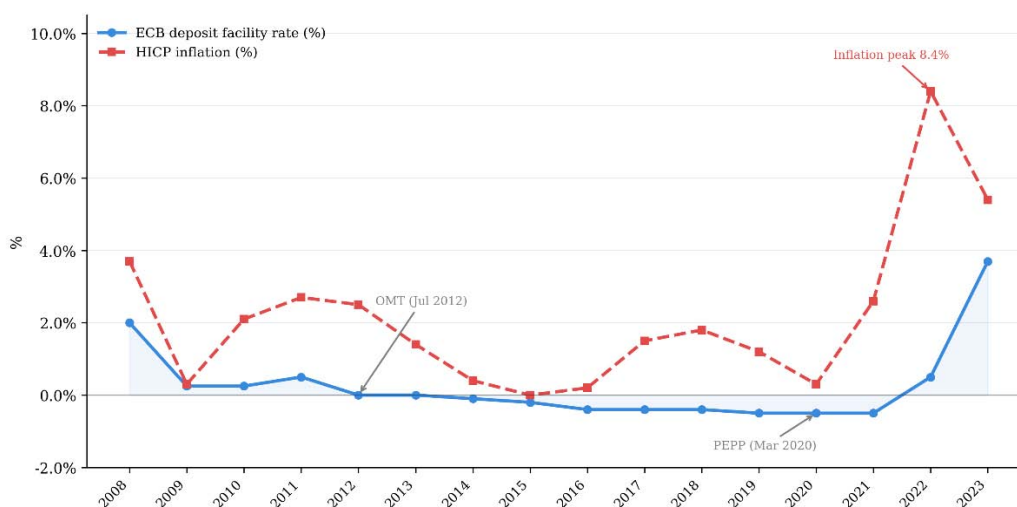


Figure 3. HICP inflation and ECB deposit facility rate euro area, monthly data, 2008–2023
Source: own processing based on Eurostat data

As Isărescu (2026) highlights from the perspective of a governor of a central bank in CEE navigating the same period, the interplay between fiscal and monetary policy requires the delicate balancing act of maintaining fiscal discipline, supporting sustainable wage and productivity growth, and encouraging investment, while preserving price and financial stability.

In response to higher debt servicing costs in highly indebted member states, the ECB introduced the Transmission Protection Instrument in July 2022, which allowed unlimited purchases of government bonds in countries facing unjustified increases in borrowing costs caused by financial fragmentation rather than economic fundamentals. At the same time, the reactivation of the Stability and Growth Pact fiscal rules for 2024 was accompanied by a reform of the EU fiscal framework, replacing common fiscal rules with country-specific medium-term fiscal plans focused on debt sustainability (European Commission, 2023). In 2023, economic growth in the euro area slowed to around 0.4%, as the effects of tighter monetary policy spread through the economy and recession risks appeared in several member states (IMF, 2023).

5.5 Channels of Interaction

The interaction between monetary and fiscal policy is especially clear during major crises, when normal transmission channels are strengthened or disrupted. Across both the GFC and the COVID-19 pandemic, policy effectiveness depended critically on how four key channels operated under different macroeconomic conditions.

Essential in both episodes were the interest rate and financing cost channel. During the GFC, monetary policy reached the effective lower bound, making fiscal expansion more powerful by eliminating crowding-out effects and reducing the cost of public borrowing (Blanchard, 2019). During COVID-19, central banks actively supported sovereign financing conditions through large-scale asset purchases. In this manner, they enabled the extensive fiscal response without triggering adverse market reactions, a form of implicit monetary-fiscal coordination that amplified the overall stabilization impact.

The expectations channel operated through credibility and communication. During both crises, coordinated and clearly communicated policy responses helped stabilize expectations regarding income, inflation, and financial stability, strengthening the behavioral transmission of policy measures to household and firm decisions (Woodford, 2004). Conversely, during normalization phases, when policy signals became less aligned, expectations became more volatile, reducing the effectiveness of both monetary and fiscal interventions.

The debt sustainability channel shaped the duration and intensity of fiscal support. During the GFC, concerns about rising public debt led to early consolidation, limiting the duration of fiscal stimulus and slowing recovery dynamics in several economies (Reinhart & Rogoff, 2010). During COVID-19, low interest rates and active central bank support temporarily relaxed these constraints, allowing a more sustained fiscal response, but this relief proved temporary, because the inflationary surge of 2022 restored debt sustainability concerns.

The financial stability channel was particularly important during the Global Financial Crisis, as the shock began in the financial sector, making liquidity support and banking system stabilization necessary conditions for a broader economic recovery (Bernanke, 2020). During COVID-19, financial systems entered the crisis in better condition, but central bank interventions remained necessary to prevent liquidity stress and preserve market functioning. In both cases, coordination between monetary and fiscal authorities helped contain adverse feedback loops between sovereign risk and financial instability, a dynamic that, if unaddressed, could have transformed cyclical downturns into structural crises.

5.6 comparative analysis

A comparison of the three crises shows several important differences. Over time, policy coordination became more effective: while the response during the Global Financial Crisis was fragmented and uneven, the response during the pandemic was more unified and included new institutional measures, reflecting lessons learned from previous crises and changing political conditions. The role of the ECB evolved progressively from conventional interest rate management toward a broader stabilization function encompassing financial fragmentation prevention, sovereign market backstop, and targeted credit provision, a transformation that effectively compensated for the limitations of decentralized fiscal policy (Draghi, 2014).

The three episodes also illustrate different dimensions of the coordination problem: during the GFC, the primary failure was premature fiscal austerity while monetary policy was constrained by the zero lower bound; during the pandemic, coordination was broadly successful because the symmetric shock facilitated collective action; during the inflationary episode, the challenge shifted to ensuring that fiscal and monetary policies work in the same direction when their objectives temporarily diverge. Throughout all three episodes, the asymmetry was determined by cross-

country heterogeneity in fiscal capacity and debt levels, which confirmed that the scope for countercyclical fiscal policy is unequal across member states.

As shown in Figure 4, fiscal balances deteriorated sharply and uniformly across all economies during the pandemic year of 2020, reflecting the large-scale discretionary fiscal expansion deployed in response to the crisis. Romania recorded among the most persistent deficits throughout the entire period, consistently exceeding the EU27 average, while the subsequent years reveal an uneven consolidation path across member states. Hungary and Romania maintained the deepest deficits in 2023 and 2024, while Bulgaria and the Czech Republic showed greater fiscal adjustment capacity. These divergences confirm that the scope for countercyclical fiscal policy remains asymmetric across member states, both within the EU27 and specifically within Central and Eastern Europe.

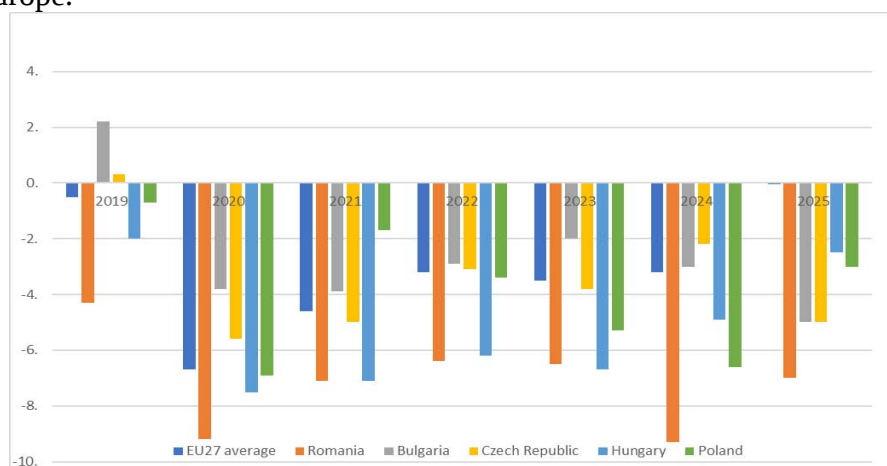


Figure 4. General government deficit/surplus (% of GDP), EU27 average and selected member states

Source: own processing based on Eurostat data

6. Conclusions

The three episodes examined in this paper: the Global Financial Crisis, the COVID-19 pandemic, and the inflationary surge of 2022 and 2023 posed the same underlying question to European policymakers: does it matter whether monetary and fiscal authorities pull in the same direction, and if so, what determines whether they actually do? The evidence presented here clearly supports the first part of the question. The second part, however, is less straightforward. The most consistent finding across all three episodes is that neither monetary nor fiscal policy operates effectively in isolation. Coordinated responses produced stronger stabilization outcomes than either instrument could have achieved independently, while misalignment generated real economic costs that proved difficult to reverse. The GFC demonstrated the damage that premature fiscal consolidation can produce when monetary policy is already constrained by the effective lower bound (Blanchard & Leigh, 2013). The pandemic response demonstrated, by contrast, what becomes possible when the two policy domains pull in the same direction and are supported by credible institutional commitments. The inflationary episode that followed illustrated yet another dimension of the coordination problem: that maintaining alignment is hardest precisely when the short-term objectives of monetary and fiscal policy begin to diverge. Across fifteen years and three crises of fundamentally different character, the same pattern emerges: coordination works, and its absence has costs that are difficult to undo.

What the evidence also shows is that credibility is not an optional quality of good policy, it is what makes policy work in the first place. The ECB demonstrated this repeatedly: in 2012 with the OMT, in 2020 with the PEPP, and in 2022 with the Transmission Protection Instrument, markets stabilized not because the instruments were deployed, but because their deployment was credible. It suggests that the institutional setup in which policy is made is just as important as the

size of any single intervention, and that credibility, once built, becomes a kind of policy space that is, in some ways, more valuable than fiscal or monetary room alone.

The EU's asymmetric institutional architecture remains, however, an unresolved structural challenge. Highly indebted member states were repeatedly constrained when countercyclical support was most needed, and the difference in stabilization capacity between stronger and weaker fiscal economies widened rather than narrowed across the three episodes. NextGenerationEU represented an institutional innovation, and its importance should not be understated, but it remains a temporary instrument rather than a permanent stabilization mechanism. The broader implication is that deepening fiscal integration, including through the development of common stabilization tools capable of providing countercyclical support independently of national fiscal positions, would strengthen the EU's collective resilience to future shocks. The reformed SGP framework adopted in 2024 represents a step in the right direction, but the asymmetry between centralized monetary policy and decentralized fiscal authority remains intact.

The post-pandemic inflationary episode also serves as a reminder that sustained policy accommodation carries medium-term risks that are easily underestimated during crisis. The tension between short-term stabilization and long-term fiscal and monetary sustainability is not a problem that coordination alone can resolve. It requires institutional frameworks capable of enforcing credible exit strategies even under political pressure, and policymakers who are willing to accept the short-term costs of normalization in order to preserve the policy space needed to respond to future crises.

Regarding limitations, the qualitative and comparative approach adopted here allows for a broad assessment of coordination dynamics across episodes, but does not permit precise quantification of the individual contribution of specific policy instruments to observed macroeconomic outcomes. Future research could usefully extend this analysis by examining the distributional consequences of monetary-fiscal coordination across income groups and member states, by modeling the long-term fiscal sustainability implications of expanded supranational stabilization mechanisms, and by investigating the conditions under which institutional coordination can be maintained during the politically difficult transition from crisis support to policy normalization. As the frequency and complexity of macroeconomic shocks show no signs of diminishing, these questions are likely to remain at the center of both academic and policy debate for years to come.

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