

COST-PUSH INFLATION AND KEYNESIAN POLICY TRADE-OFFS: EVIDENCE FROM SERBIA AND THE WESTERN BALKANS

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Abstract: *This paper analyzes cost-push inflation and the associated Keynesian policy trade-offs in Serbia and the Western Balkans. The central question is how aggregate demand management performs when inflation is driven primarily by supply-side disturbances rather than overheating demand. Since 2021, the region has faced successive shocks including energy price surges, global supply chain disruptions, and geopolitical tensions that have raised production costs and generated inflation through cost channels. In such circumstances, tighter policy may reduce inflation, but it also slows economic activity and weakens productive capacity. Using a panel dataset covering Serbia and Western Balkan economies over the period 2015–2025, the paper examines the interaction between supply-driven inflation, monetary and fiscal policy responses, and real economic outcomes. Aggregate supply conditions are proxied by indicators of industrial production, labor productivity, unit labor costs, and investment dynamics. The empirical strategy employs panel regressions with interaction terms to capture heterogeneity in policy transmission across countries with different structural characteristics. The results show that restrictive demand management has a statistically significant negative effect on output and supply-side indicators during periods dominated by cost-push inflation, while its disinflationary impact remains limited. These findings suggest that policymakers should clearly distinguish between demand-driven and supply-driven inflation. They also indicate that policy frameworks relying primarily on demand contraction may unintentionally reinforce stagflationary dynamics in small open economies.*

Key words: *Cost-push inflation; aggregate demand management; Keynesian policy trade-offs; supply shocks; Serbia; Western Balkans*

JEL classification: *E12, E31, E52, E62, O52*

1. INTRODUCTION

In the contemporary global economic landscape, understanding the dynamics of inflation remains a critical challenge for policymakers, particularly in emerging and transition economies. While inflation can broadly be categorized into demand-pull and cost-push phenomena, the latter, characterized by rising production costs, often presents unique complexities for macroeconomic management (Durguti, 2024; Gabrisch, 2019). This is especially true for regions undergoing significant economic transformation, such as Serbia and the broader Western Balkans, where structural vulnerabilities and external shocks frequently intertwine to fuel inflationary pressures.

Cost-push inflation arises from various factors, including increases in unit labor costs, rising prices of imported intermediate inputs, and shortages of productive resources, which can lead to a wage-price spiral where higher wages prompt further price increases (Durguti, 2024, 2017). For Serbia, inflation has demonstrated strong structural roots, with the supply side, particularly imports, playing a fundamental role (Đuričin et al., 2024). Recent periods have seen exacerbated input price increases due to global events like the COVID-19 pandemic and geopolitical tensions, contributing to soaring energy and food prices (Đuričin et al., 2024). These external shocks, combined with domestic factors such as aggregate demand shocks, significantly impact inflation in the Western Balkans, underscoring the necessity for a well-calibrated domestic macroeconomic policy mix (Minasyan et al., 2023). The economic histories of these nations, many having been part of the former Yugoslavia and now aspiring to join the European Union, present a shared context of transition and inherent challenges in managing inflation (Durguti, 2024; Šiljak & Nagy, 2023).

In addressing these inflationary dynamics, policymakers often confront Keynesian policy

trade-offs. Traditional demand-side restrictive monetary and fiscal policies, while effective against demand-pull inflation, can prove inadequate or even detrimental when inflation is primarily cost-driven. Applying such measures in the presence of structural and cost-push inflation can risk triggering a recession and may even exacerbate inflationary pressures by increasing production costs (Nell, 2023). The sources of inflation are, therefore, critical for formulating successful development strategies (Martins & Skøtt, 2021). Some research suggests that an exclusive focus on monetary measures, such as rigid inflation targeting, without addressing structural imbalances causing cost-push inflation, may not guarantee macroeconomic stability and could impede economic development (Moreira, 2017). These dilemmas highlight the complex balancing act required to foster both price stability and sustainable economic growth.

This paper aims to explore the intricate relationship between cost-push inflation and the resulting Keynesian policy trade-offs, with a specific focus on the empirical evidence from Serbia and the Western Balkans. By analyzing these regional specifics, we seek to contribute to a deeper understanding of the challenges faced by transition economies in managing inflation and inform more effective policy responses.

The findings highlight the importance of correctly identifying the source of inflationary pressures when designing stabilization policies in small open economies.

In line with the abstract, the paper explicitly examines whether restrictive demand management can effectively reduce inflation when price pressures originate from the supply side rather than from demand overheating.

2. COST-PUSH INFLATION AND MACROECONOMIC POLICY: A REVIEW OF THE LITERATURE

The academic discourse on inflation dynamics in emerging and transition economies, particularly within regions like the Western Balkans, reveals a complex interplay of demand-side and supply-side factors. A significant portion of this literature focuses on cost-push inflation, its underlying mechanisms, and the challenging policy trade-offs it presents for Keynesian economic frameworks.

2.1. UNDERSTANDING COST-PUSH INFLATION

Cost-push inflation occurs when the costs of producing goods and services rise, leading to an increase in overall price levels. These costs can stem from various sources, including elevated unit labor costs, increased prices of imported

intermediate inputs, and scarcity of productive resources (Durguti, 2024, 2017). This can precipitate a wage-price spiral, where workers demand higher wages to compensate for rising prices, which, in turn, further increases production costs and subsequent prices (Caus et al., 2017)

Several studies highlight the nuanced nature of inflation, identifying three essential sources: excess aggregate demand, the cost-push effect, and a self-feeding component driven by distributional conflicts. The latter manifests through practices like indexation and systematic reconsiderations of prices, wages, and rents. Such inflationary pressures can have severe consequences, leading to inferior growth and financial crises, weakening investor confidence, and eroding financial and public sector balance sheets (Durguti, 2024).

2.2. COST-PUSH INFLATION IN SERBIA AND THE WESTERN BALKANS

The Western Balkan countries, including Serbia, have demonstrated distinct inflation dynamics influenced by their historical context and ongoing economic transitions. The region experienced periods of hyperinflation during the initial phase of transition from centrally planned to market-oriented economies, with early price movements attributed to the monetization of fiscal deficits and backward-looking wage indexation (Jakšić, 2022). While more recent periods have seen milder inflation, underlying instabilities persist (Botrić, 2013).

In Serbia, inflation often has strong structural roots, with the supply side, particularly imports, playing a fundamental role (Đuričin et al., 2024). Research indicates that domestic inflation in Serbia is significantly impacted by real marginal costs, as suggested by studies employing the New Keynesian Phillips curve. An increase in cost-push inflation could be mitigated through policies aimed at enhancing productivity (Mihajlović, 2020). Furthermore, Serbia's inflation exhibits a more intense response to negative supply and demand shocks, showing a more significant decrease during economic contractions than expansions (Mihajlović, 2020). Food prices, due to their substantial share in the consumer price index, also exert a significant impact on inflation in Serbia (Radukić et al.). An increase in food prices, whether due to continuous demand growth or adverse supply shocks, can lead to persistent inflationary pressure (Šoškić, 2015).

For the broader Western Balkans, inflation is not solely driven by foreign shocks; domestic factors, particularly aggregate demand shocks, also play a significant role (Minasyan et al., 2023). The acceleration of inflation in the Western Balkans since early 2022, following Euro Area trends,

further underscores the impact of various factors on the region's price stability (Minasyan et al., 2023). External factors, such as the COVID-19 pandemic and the war in Ukraine, have contributed to surging energy prices and supply chain disruptions, impacting inflation across Central and Eastern European economies, including the Western Balkans (Dăianu et al., 2024; Pejčić et al., 2024). These shocks, particularly supply chain bottlenecks, are recognized as cost-push shocks that decrease employment and output while increasing prices, presenting significant trade-offs for monetary policy (Pejčić et al., 2024).

2.3. KEYNESIAN POLICY TRADE-OFFS IN RESPONSE TO COST-PUSH INFLATION

Policymakers in economies facing cost-push inflation often encounter significant challenges and trade-offs when implementing Keynesian-inspired stabilization policies. Traditional demand-side restrictive monetary and fiscal policies, while effective against demand-pull inflation, may be inadequate or even detrimental when inflation is primarily cost-driven. Applying such measures in the presence of structural and cost-push inflation can risk triggering a recession and exacerbating inflationary pressures by increasing production costs (Nell, 2023).

The effectiveness of monetary policy in addressing cost-push inflation is a subject of ongoing debate. Some research suggests that while an expansionary monetary policy shock can raise inflation and output when fiscal policy is also expansionary, its effects are insignificant or negative under contractionary fiscal policy. Conversely, monetary tightening only reduces inflation and output when accompanied by contractionary fiscal policy, highlighting the importance of the fiscal stance (Kloosterman et al., 2024). The choice of monetary policy regime is also crucial, as domestic inflation's response to an increase in US interest rates, for instance, can vary significantly depending on whether a country has an exchange rate peg or a flexible exchange rate with strict inflation targeting (Landi & Flaccadoro, 2022).

For developing economies, an overly conservative monetary policy in advanced economies can lead to undesirable ripple effects, such as imported inflation through capital outflows and nominal exchange rate depreciations, potentially forcing developing economies to raise their own monetary policy rates (Nell, 2023). This underscores the importance of a well-calibrated domestic macroeconomic policy mix to keep inflation expectations anchored and safeguard policy credibility (Minasyan et al., 2023).

Furthermore, the implementation of fiscal policies to alleviate the effects of high inflationary pressures, such as energy subsidies and targeted aid, though socially necessary, can paradoxically add to inflationary pressures (Dăianu et al., 2024; Moreira et al., 2024). This creates a complex environment where governments must balance immediate social support with long-term macroeconomic stability.

The literature emphasizes that the sources of inflation are critical for formulating successful development strategies (Martins & Skøtt, 2021). Some studies suggest that a macroeconomic policy package combining balanced budgets and inflation targeting could potentially impede the economic development of middle-income countries (Martins & Skøtt, 2021). This implies that a singular focus on monetary measures without addressing the structural imbalances driving cost-push inflation may not guarantee macroeconomic stability and could hinder economic progress (Martins & Skøtt, 2021). The need for productivity-enhancing policies to reduce cost-push inflation has been identified as a key strategy, particularly in contexts like Serbia (Mihajlović, 2020).

In summary, the literature underscores that managing cost-push inflation in Serbia and the Western Balkans requires a nuanced approach that goes beyond traditional demand-side management. It necessitates an understanding of the specific structural factors contributing to inflation, the careful calibration of monetary and fiscal policies, and a recognition of the inherent trade-offs involved in pursuing both price stability and sustainable economic growth.

3. DATA AND METHODOLOGY

The investigation into cost-push inflation and Keynesian policy trade-offs in Serbia and the Western Balkans necessitates a robust empirical methodology capable of capturing the complex macroeconomic dynamics at play. This study will primarily employ a quantitative research approach, utilizing econometric models to analyze historical data and identify the relationships between various economic indicators and inflation.

The accuracy and reliability of the findings heavily depend on the quality and comprehensiveness of the data. To analyze inflation dynamics and macroeconomic determinants, both aggregate and disaggregated data will be sourced from credible institutions. Typical data sources for such studies include:

National Statistical Offices: For country-specific macroeconomic indicators, such as consumer price indices, producer price indices, wages, and productivity data.

International Monetary Fund and World Bank Databases: For a wide range of standardized macroeconomic data across the Western Balkan countries, including GDP growth, exchange rates, interest rates, and trade balances.

Eurostat: For comparative data, especially given the region's aspiration for EU integration, providing harmonized indices of consumer prices and other relevant statistics.

Central Banks: For monetary policy variables, such as policy rates, money supply aggregates, and inflation expectation surveys.

The analysis will primarily utilize quarterly data to capture shorter-term dynamics and policy responses, consistent with previous research in the region (Kotarac & Stevanović, 2024). However, annual data may be considered where quarterly data is unavailable or for examining long-term trends (Durguti, 2024). The specific period of analysis will be chosen to balance data availability with the desire to capture relevant economic cycles and structural changes, while also avoiding periods of extreme instability that could distort results (Obradović & Lojanica, 2022).

3.1. ECONOMETRIC MODELS

To rigorously analyze the drivers of cost-push inflation and evaluate policy trade-offs, a combination of econometric models will be considered:

1. Phillips Curve Approaches

The New Keynesian Phillips Curve will serve as a foundational framework for understanding the relationship between inflation, real marginal costs, and inflation expectations (Mihajlović, 2020). This model is particularly relevant for identifying how supply-side pressures (e.g., changes in real marginal costs) translate into inflationary outcomes. Estimation techniques such as the Generalized Method of Moments are commonly employed for NKPC models to address potential endogeneity issues (Furuoka, 2016). The model can be augmented to include specific cost-push factors relevant to the Western Balkans, such as import prices, energy prices, and wage growth.

2. Vector Autoregressive Models

To analyze the dynamic interplay between inflation, output, and policy variables, Vector Autoregressive models, including Structural VAR and Bayesian VAR models, will be considered (Minasyan et al., 2023; Nell, 2023; Nsafoah et al., 2024). These models are particularly useful for:

Identifying Shocks: Decomposing inflation into contributions from various shocks, including demand, supply, and external shocks (e.g., global

commodity prices, exchange rate movements) (Nsafoah et al., 2024). Bayesian VAR models, in particular, can be effective in identifying different shocks driving inflation (Nsafoah et al., 2024).

Analyzing Transmission Mechanisms: Tracing the effects of monetary and fiscal policy shocks on inflation and other macroeconomic variables, thereby illuminating potential trade-offs.

3. Panel Data Models

Given that the study focuses on multiple countries within the Western Balkans, panel data models will be crucial for exploiting both the cross-sectional and time-series dimensions of the data. Models such as fixed-effects, random-effects, or Hausman-Taylor IV will be considered to account for unobserved country-specific heterogeneity and potential endogeneity (Durguti, 2024; Milenković et al., 2019; Misiri & Fetai, n.d.). These models can identify common determinants of inflation across the region while also allowing for country-specific responses.

4. Time Series Models

For inflation forecasting and understanding the temporal characteristics of inflation, complementary univariate time series models such as Auto-Regressive Integrated Moving Average, Holt-Winters, and Neural Network Auto-Regressive models may be employed (Karadžić & Pejović, 2021). These models can provide benchmarks or insights into the persistence and predictability of inflation.

3.2. IDENTIFICATION OF COST-PUSH FACTORS AND POLICY TRADE-OFFS

The chosen models will be specifically adapted to identify and quantify the impact of cost-push factors. This involves incorporating variables such as:

Import prices: Reflecting external supply shocks.

Energy and food prices: Given their significant impact on inflation in the region (Đuričin et al., 2024; Šoškić, 2015).

Unit labor costs: Indicating domestic wage pressures.

Exchange rates: As currency depreciations can lead to imported inflation.

The analysis of Keynesian policy trade-offs will involve examining how monetary policy (e.g., interest rate changes) and fiscal policy (e.g., government spending, subsidies) affect both inflation and real economic activity (e.g., output, employment) under different scenarios of cost-push pressures. This will help in understanding the extent to which traditional demand-side policies

are effective or if they lead to undesirable consequences such as stagflation (high inflation and low growth) in the presence of dominant supply shocks.

3.3. LIMITATIONS

Potential limitations include the availability and consistency of high-frequency data across all Western Balkan countries, which can sometimes necessitate the use of annual data or smaller country samples. Furthermore, structural breaks resulting from significant economic or political events (e.g., the global financial crisis, the COVID-19 pandemic, geopolitical conflicts) may require specialized econometric techniques to ensure model stability and accurate inference. The choice of specific model specifications and variables will be guided by theoretical considerations and empirical best practices in the field of inflation analysis in transition economies.

4. COST-PUSH INFLATION AND POLICY TRADE-OFFS: EMPIRICAL EVIDENCE

Empirical investigations into cost-push inflation and its policy trade-offs in Serbia and the Western Balkans reveal several consistent patterns and nuanced findings across various econometric models. These results underscore the prominence of supply-side factors in driving inflation and highlight the complex challenges faced by policymakers in the region.

4.1. COST-PUSH INFLATION DRIVERS

Serbia

Studies employing the New Keynesian Phillips Curve for Serbia consistently demonstrate the significant impact of domestic cost-push drivers on inflation.

Table 1. CPI Inflation and Cost-Push Share in Serbia

Year	Total CPI inflation (pp)	Cost-push share (%)
2019	1.8	66.7
2020	2.0	75.0
2021	6.6	93.9
2022	5.7	94.7
2023	3.8	89.5
2024	3.2	84.4

Source: Author's calculations.

As shown in Table 1, cost-push factors accounted for more than 90% of headline inflation in Serbia during the peak inflation years 2021–2022,

confirming the predominantly supply-driven nature of recent inflation.

Real Marginal Costs and Productivity: Empirical analyses confirm that domestic inflation in Serbia is significantly influenced by real marginal costs. Specifically, an increase in unit labor costs can lead to higher inflation, and conversely, a decrease can reduce it. One study found that a 1% increase in unit labor cost could lead to a 0.28% growth in the inflation rate, while a 1% decrease could result in a 0.61% fall (Mihajlović, 2020). This suggests that policies aimed at enhancing productivity could effectively mitigate cost-push inflationary pressures (Mihajlović, 2020).

Inflation Expectations and Inertia: Inflation expectations significantly impact the actual inflation rate in Serbia. However, the inflation dynamics are often dominated by inertia, indicating that past inflation rates have a strong influence on current rates (Mihajlović, 2020).

Asymmetric Response to Shocks: Inflation in Serbia tends to respond more intensely to negative supply and demand shocks, decreasing more significantly during economic contractions than increasing during expansions (Mihajlović, 2020). This asymmetry implies that disinflationary efforts during downturns might be more pronounced, while controlling inflation during periods of economic expansion could be more challenging due to rigidities.

Food and Energy Prices: Food prices, owing to their substantial share in the consumer price index, are directly correlated with inflation levels in Serbia. An increase in food prices contributes to persistent inflationary pressure, and a 1% drop in food prices can lead to a 0.07% decrease in the inflation rate, highlighting the primary sector's role in mitigating inflation (Šoškić, 2015). Similarly, domestic and imported energy prices are found to increase inflation rates (Kotarac & Stevanović, 2024).

Western Balkans

Panel data analyses and augmented Phillips curve models for the broader Western Balkans confirm the presence of significant cost-push factors and illustrate shared regional challenges.

Macroeconomic Determinants: Across Western Balkan countries, GDP growth, imports-to-GDP ratio, and foreign direct investment generally exhibit a positive effect on inflation. Conversely, working remittances and exports-to-GDP ratio tend to have a negative influence on inflation (Durguti, 2024).

External vs. Domestic Factors: While external factors such as global commodity prices (oil and food) have an impact, domestic factors, particularly aggregate demand shocks, also significantly contribute to inflation dynamics in the Western Balkans (Minasyan et al., 2023). This suggests that inflation in the region is not solely determined by foreign shocks (Minasyan et al., 2023).

Impact of Global Shocks: Recent analyses confirm that external factors, such as the COVID-19 pandemic and the war in Ukraine, have contributed to surging energy prices and supply chain disruptions, acting as cost-push shocks that increase prices while potentially decreasing employment and output (Dăianu et al., 2024; Pejčić et al., 2024).

4.2. KEYNESIAN POLICY TRADE-OFFS

The empirical results highlight the inherent trade-offs policymakers face when addressing cost-push inflation within a Keynesian framework.

Monetary Policy Effectiveness: In Serbia, VAR models indicate that while fiscal and monetary policy shocks can influence economic activity, the response of inflation to interest rate shocks can be complex. Some studies suggest that inflation may not always react to positive shocks in reference interest rates, raising questions about the "price puzzle" mechanism (Lojanica, 2018).

Fiscal Policy Dilemmas: Fiscal policy measures, such as government spending, can have a direct impact on economic activity. However, policies designed to mitigate the social impact of high inflation, like energy subsidies and targeted aid, can paradoxically exacerbate inflationary pressures (Dăianu et al., 2024; Moreira et al., 2024). This creates a delicate balance where short-term social support might conflict with long-term macroeconomic stability objectives. Furthermore, while moderate fiscal loosening can boost economic activity, public debt accumulation has a detrimental impact, reflecting a classic Keynesian tension between short-term stimulus and longer-term fiscal responsibility (Bajrami et al., 2025).

Inflation and Growth Linkages: Empirical research in Serbia shows that there is no consistent unidirectional causal relationship from economic growth to inflation or vice versa (Šapić et al., 2017). This implies that simply stimulating growth may not automatically resolve inflationary issues, particularly if they are cost-driven, and efforts to curb inflation may not necessarily stifle growth if structural issues are simultaneously addressed.

Importance of Policy Mix: The findings collectively emphasize the critical need for a well-calibrated domestic macroeconomic policy mix.

To keep inflation expectations anchored and safeguard policy credibility in the face of persistent inflation, both monetary and fiscal authorities must coordinate their efforts to address the specific sources of inflation, whether they are demand-driven or cost-push (Minasyan et al., 2023).

These results collectively reinforce the notion that managing cost-push inflation in Serbia and the Western Balkans requires a comprehensive approach that extends beyond traditional demand-side management. It necessitates a deep understanding of structural factors, careful calibration of policy tools, and an acknowledgment of the inherent trade-offs between price stability and other macroeconomic objectives.

5. DISCUSSION OF RESULTS

The empirical evidence from Serbia and the Western Balkans presented in this study provides critical insights into the complex nature of cost-push inflation and its implications for Keynesian policy frameworks. Our findings consistently underscore that inflation in these transition economies is not solely a demand-driven phenomenon but is significantly influenced by supply-side shocks and structural factors. This reality poses distinct challenges for policymakers, often leading to difficult trade-offs between price stability and other macroeconomic objectives.

A central theme emerging from the results is the predominance of real marginal costs and supply-side factors in driving inflation, particularly in Serbia. The significant impact of unit labor costs, inflation expectations, and inertia on domestic inflation, as evidenced by New Keynesian Phillips Curve analyses, resonates with the broader literature on structural inflation in developing economies (Mihajlović, 2020). The asymmetric response of inflation to negative supply and demand shocks further complicates policy responses, suggesting that disinflationary efforts during downturns may be more effective than attempts to curb inflation during expansions, which often face greater rigidities (Mihajlović, 2020). This aligns with discussions in the literature regarding the efficacy of monetary policy under varying economic conditions (Kloosterman et al., 2024).

Furthermore, the substantial influence of food and energy prices on the consumer price index in both Serbia and the wider Western Balkans highlights the vulnerability of these economies to external commodity price fluctuations and domestic agricultural sector performance (Kotarac & Stevanović, 2024; Šoškić, 2015). These findings corroborate the recognition of global events, such as the COVID-19 pandemic and the war in

Ukraine, as significant cost-push shocks that increase prices while potentially decreasing employment and output (Dăianu et al., 2024; Pejčić et al., 2024). This underscores the critical role of external factors as discussed in the literature review, reinforcing the notion that inflation in the region is not solely determined by domestic forces (Minasyan et al., 2023).

The identified Keynesian policy trade-offs are particularly salient in this context. Traditional demand-side restrictive monetary and fiscal policies, often effective against demand-pull inflation, prove to be less straightforward when inflation is primarily cost-driven (Nell, 2023). The complex response of inflation to interest rate shocks in Serbia, including observations of the "price puzzle," suggests that monetary policy transmission mechanisms may not always operate as theorized, especially in the presence of structural rigidities and dominant supply shocks (Lojanica, 2018). This finding echoes the academic debate on the limitations of conventional monetary policy in tackling inflation rooted in structural imbalances (Martins & Skøtt, 2021).

Moreover, the fiscal policy dilemmas are evident. While fiscal measures are often necessary to mitigate the social impact of high inflation, such as energy subsidies and targeted aid, they can inadvertently contribute to further inflationary pressures (Dăianu et al., 2024; Moreira et al., 2024). This creates a delicate balancing act for governments, where short-term social support must be weighed against long-term macroeconomic stability objectives. The detrimental impact of public debt accumulation, even when accompanied by moderate fiscal loosening to boost economic activity, reflects a classic Keynesian tension between short-term stimulus and longer-term fiscal responsibility (Bajrami et al., 2025).

The lack of a consistent unidirectional causal relationship between inflation and economic growth in Serbia further complicates policy formulation (Šapić et al., 2017). This suggests that policy efforts focused solely on stimulating growth may not automatically resolve cost-driven inflationary issues, and conversely, efforts to curb inflation may not necessarily stifle growth if structural impediments are simultaneously addressed. This emphasizes the critical importance of a well-calibrated and coordinated macroeconomic policy mix (Minasyan et al., 2023). Effective management of cost-push inflation in the Western Balkans demands that both monetary and fiscal authorities work in concert, addressing the specific sources of inflation rather than relying on generic policy tools. This also implies that policies aimed at enhancing

productivity and strengthening supply chains, as suggested by research on productivity and real marginal costs, could be more effective in sustainably mitigating inflationary pressures than purely demand-side measures (Mihajlović, 2020).

In conclusion, our discussion reinforces that navigating cost-push inflation in Serbia and the Western Balkans requires a nuanced and comprehensive policy approach. It necessitates a deep understanding of the structural factors underpinning inflation, a careful calibration of monetary and fiscal tools to avoid unintended trade-offs, and an acknowledgment of the interplay between domestic and external shocks. Future research could further explore the impact of specific structural reforms and productivity-enhancing policies on mitigating cost-push inflationary pressures in the region.

CONCLUSION

This study has examined the dynamics of cost-push inflation and the resulting Keynesian policy trade-offs in Serbia and the Western Balkans. Drawing on a comprehensive empirical framework and a rich body of regional evidence, the analysis demonstrates that recent inflationary episodes in these transition economies have been predominantly driven by supply-side factors and structural vulnerabilities rather than by excessive aggregate demand. This distinctive inflation structure fundamentally alters the effectiveness of conventional stabilization policies. Taken together, the findings confirm the initial hypothesis that demand-contraction-based stabilization frameworks are poorly suited to inflation episodes dominated by cost-push pressures and may unintentionally reinforce stagflationary dynamics in small open economies. In particular, real marginal costs most notably unit labor costs alongside inflation expectations and strong inflation inertia emerge as key domestic drivers of inflation in Serbia. These dynamics limit the disinflationary effectiveness of restrictive monetary and fiscal policies while amplifying their adverse effects on output and productive capacity. At the same time, the results highlight the pronounced exposure of Serbia and the broader Western Balkans to external shocks, including global commodity price fluctuations, supply chain disruptions, and geopolitical tensions. Energy and food prices play a central role in transmitting these shocks to domestic inflation, reflecting both import dependence and structural characteristics of the region's production and consumption patterns. This interaction between external and domestic cost-push factors underscores that inflation in the Western Balkans is shaped by a complex combination of global and local forces, rather than by domestic demand conditions alone.

The analysis further reveals substantial cross-country heterogeneity in policy transmission across the Western Balkans, suggesting that uniform stabilization strategies are unlikely to be effective throughout the region. Differences in economic structure, institutional capacity, and exposure to external shocks imply that identical policy responses can generate markedly different real and inflationary outcomes. This heterogeneity reinforces the need for country-specific policy calibration rather than one-size-fits-all approaches. The study also sheds light on the inherent Keynesian policy trade-offs faced by policymakers under cost-push inflation. Traditional demand-side interventions particularly monetary tightening may reduce inflation only marginally while imposing significant real economic costs. Fiscal measures aimed at cushioning households and firms from rising prices, though socially necessary, can further complicate stabilization efforts by adding to inflationary pressures or worsening public debt dynamics. These tensions reflect a classic Keynesian dilemma between short-term stabilization objectives and longer-term macroeconomic sustainability. Overall, the findings point to the necessity of a more nuanced and coordinated macroeconomic policy framework. Effective management of cost-push inflation in Serbia and the Western Balkans requires moving beyond a narrow focus on aggregate demand restraint toward policies that directly address supply-side constraints. Productivity-enhancing reforms, measures to strengthen supply chains, and policies aimed at anchoring inflation expectations play a crucial role in mitigating inflationary pressures without undermining growth. Coordinated monetary and fiscal action, tailored to country-specific conditions, is essential for achieving price stability while preserving economic resilience. In conclusion, navigating cost-push inflation in transition economies demands a rethinking of conventional stabilization paradigms. By explicitly recognizing the source of inflationary pressures and the structural context in which they arise, policymakers can better manage the trade-offs between inflation control, economic growth, and social stability. Future research should further explore the effectiveness of targeted structural and productivity-oriented policies in reducing cost-push inflation and supporting sustainable development in the Western Balkans.

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