



Discussion of Lucía Rodríguez Muñoz (Network of EU IFI)'s

How to strengthen fiscal surveillance towards a medium-term focus?

EFB Conference: “High Debt, Low Rates and Tail Events: Rules-Based Fiscal Frameworks under Stress”

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Gilles Mourre
European Commission ECFIN

Important disclaimer: The views expressed are my own only and do not, by any means, represent an official position by the European Commission. Valuable inputs from E. Bova, D. Radu and J. Mazur are acknowledged.

Outline

1. Summary and general appraisal of the paper
2. Taking a step back: **discussing the three key benchmarking concepts**
3. Taking a look back: **experience with fiscal surveillance**
4. Taking a look forward: **challenges ahead**

I. Summary (1)

Looking at public finances from **a multiannual perspective** to improve fiscal outcomes (design and execution)



- Potential of strengthening the medium-term budgetary frameworks (MTBFs) in addition to medium-term fiscal frameworks (MTFFs).
- Improving legal framework is not enough: implementation is key (in line with the Review of the Directive on Budgetary Frameworks)
- Medium-term frameworks have turned into a purely formal exercise in some MSs

I. Summary (2)

- The assessment is done across three dimensions, checking whether MTFF 1) deliver improvements in underlying fiscal positions; 2) are stable over time; 3) increase the predictability of fiscal policy.
- Overall, weak progress in the three dimensions and wide heterogeneity of performance across Member States. ‘Abstract’ fiscal plans end up being constantly changed or simply missed. Major reasons:
 - gaps between the legislation and implementation of MTFF;
 - the use of aspirational rather than binding targets;
 - challenges in the top-down reconciliation of fiscal requirement and budgetary concrete figures: MTFF are often either lacking or detached from more concrete medium-term fiscal frameworks (MTBF).
- Sound diagnosis and good practices

I. Summary (3)

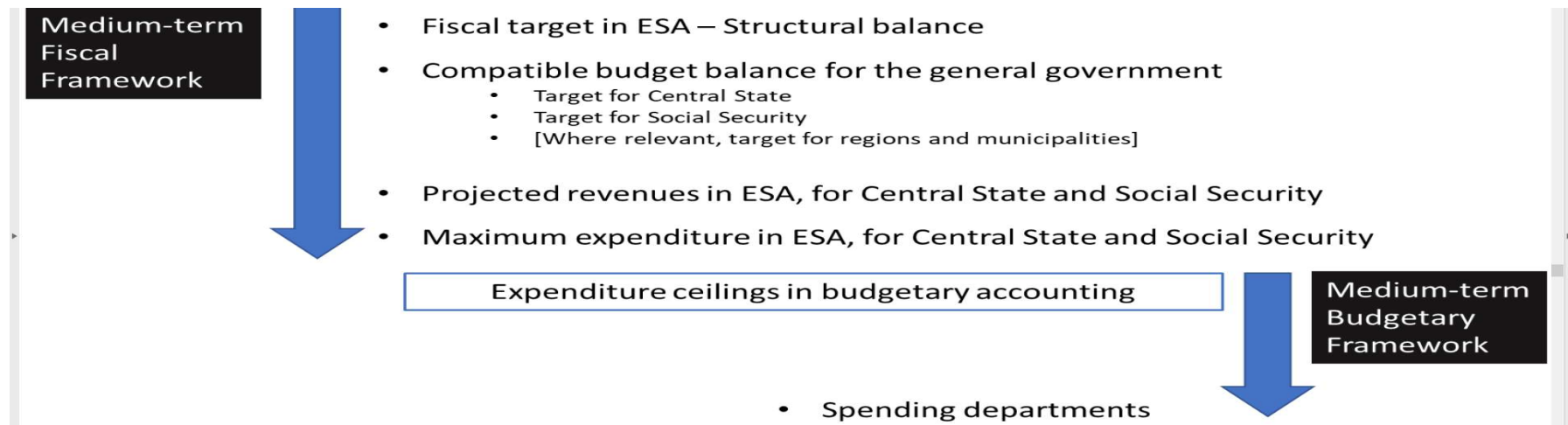
- A IFI survey stresses the relevance of four elements for medium-term frameworks to function effectively:

(i) strong political commitment - even with softer legal basis

(ii) articulated through constraining fiscal targets,

(iii) expressed with variables that are easily reconcilable with the fiscal and budgetary elements of the process,

(iv) are embedded in functional MTBFs that effectively translate aggregate fiscal requirements into clear and consistent budgetary expenditure ceilings.



I. General appraisal

This is a policy paper...

... but very rich, thoughtful and deep analytically...

... and institutionally grounded ...

... with country experience

II. Taking a step back: examining key concepts

Three benchmarks of performance: thread of the analysis

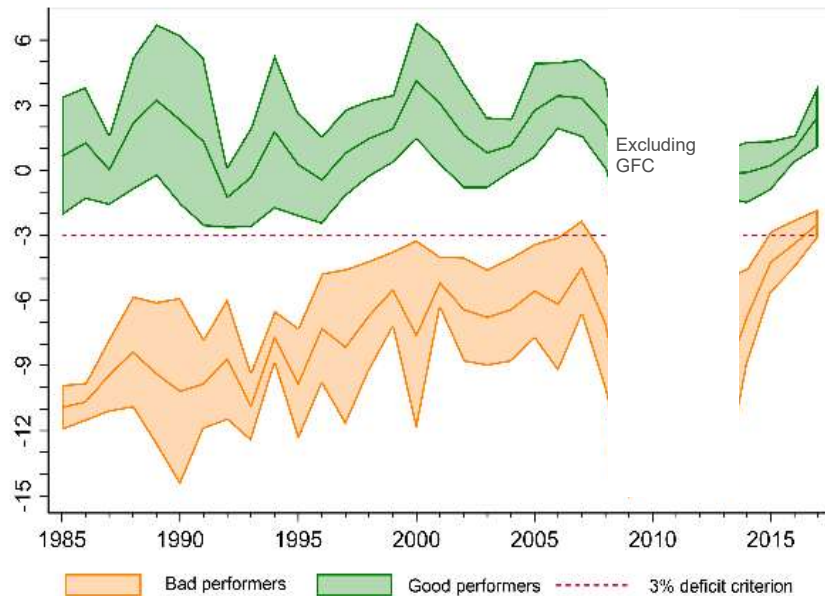
- Performance: Have MTFs delivered with respect to expected improvements in underlying fiscal positions?
 - **Anchoring/stabilising role of MTBF**, noticeably by anchoring (net) spending growth in medium term GDP growth (*with revenue fluctuation –Automatic Stabilisers*)
 - ...natural complement to a EU primary spending rule, such as expenditure benchmark, allowing cyclical revenue and windfall/shortfall and based on medium term potential trend
 - **MTBF to promote quality of public finance**: public investment, other productive spending and structural tax and spending reforms require a medium term planning
- Have they produced more stable fiscal plans?
 - **Key condition/means for anchoring.**
- Have they increased the predictability of fiscal policy?
 - **Key condition/means for planning high-quality measures** (toward green and digital, social cohesion spending but also fiscal structural reforms for ageing and taxation).

III. Taking a look back (2)

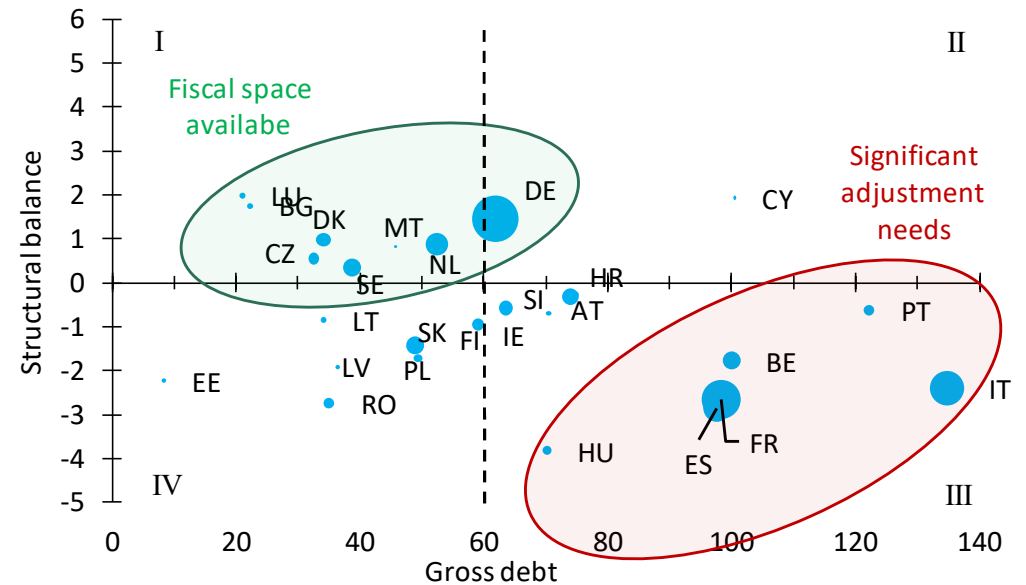
Let us focus on the success of the MTBFs with the lens of the SGP review

1) Fiscal sustainability

Headline balances in the EU Member States (% of GDP)



Structural balance and debt ratios (% of GDP, 2018)

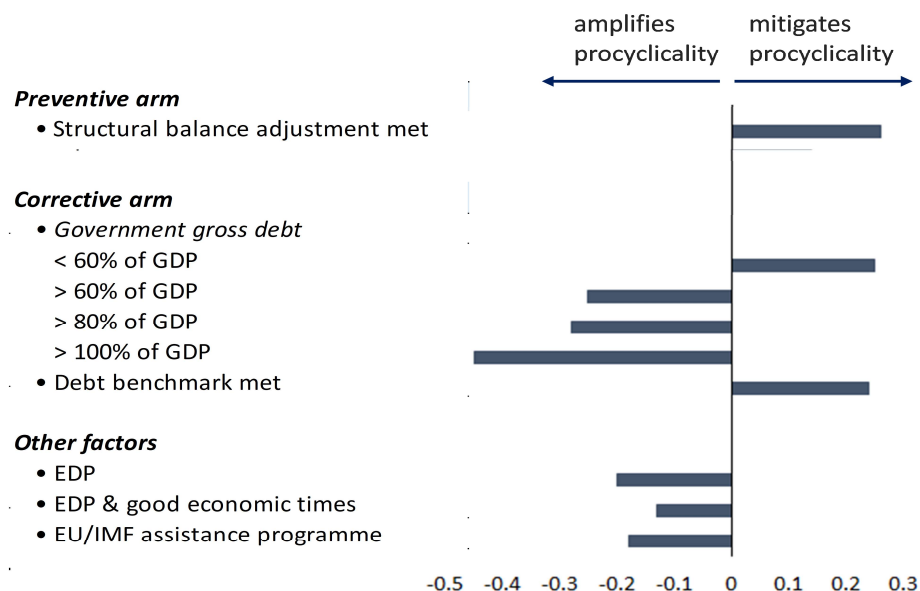


- Sustainability: 3% Nominal anchor for the laggards
- Heterogeneous behaviour: very mixed fiscal effort and debt developments due to paradoxical apparent budgetary behaviour: ‘the higher the debt, the lower the adjustment?’
- *MTBF may have help achieve fiscal sustainability but not enough in the most vulnerable countries*

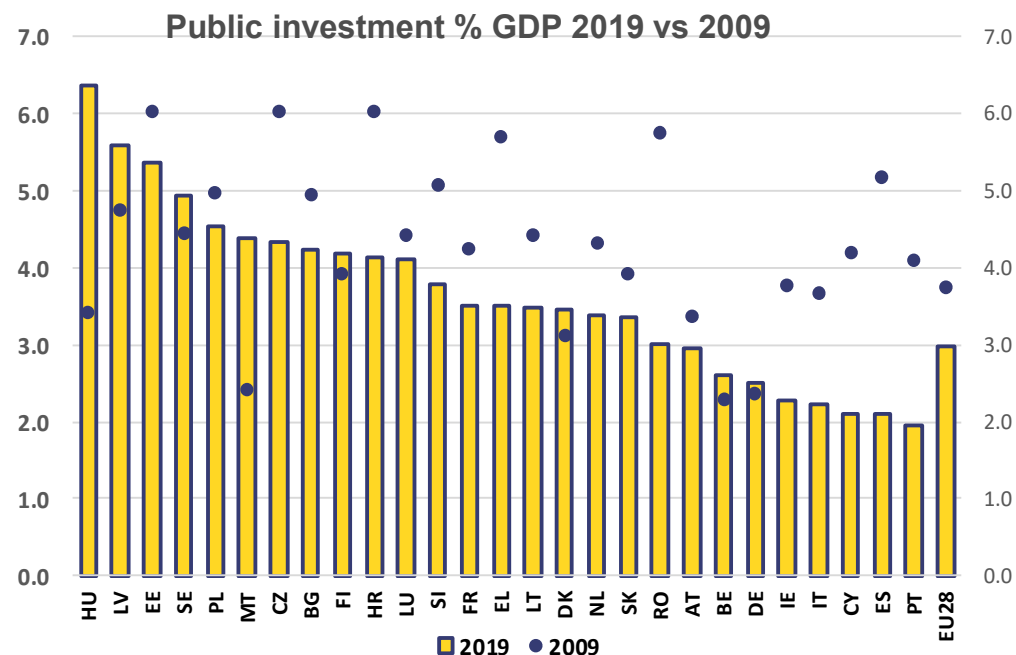
III. Taking a look back (3)

2) Procyclicality

Cyclicality of the fiscal effort and compliance with EU rules



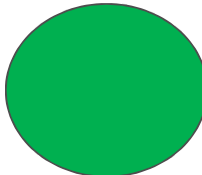
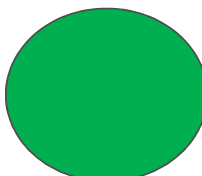
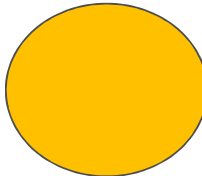
3) Quality of public finance



- Macro stabilisation: Problem of pro-cyclicality, but reduced by compliance with fiscal rules
- Mixed records and heterogeneity: *can MTBF do better with better compliance in some MSs?*
- Quality of public finances: public investment declined during the last decade (pre-Covid)
- *Capital spending needs to be framed in MTBFs to be sustainable and provide clarity to the decision-makers on the available envelope over the planning horizon.*

III. Taking a look back (4)

4) Policy tool : spending rules (EB more akin to MTBF) superior to structural balance rules (defining most MTFF) (Mohl & Mourre, 2020)

Objective	Key findings	Objective achieved	Better indicator
Guarantee predictability	<ul style="list-style-type: none">• Commission forecasts of fiscal efforts are not systematically biased• Broadly similar size of forecast errors of EB- and SB-based fiscal efforts		EB/ SB
Ensure sustainability	<ul style="list-style-type: none">• Public debt-to-GDP ratios would have been significantly lower than today if the current SGP had been applied since 1999, in particular in high-debt Member States• EB and SB deliver similar results, but EB seems slightly more growth-friendly.		EB/ (SB)
Foster stabilisation	<ul style="list-style-type: none">• The fiscal effort has, on average, been procyclical in the EU since 2000, the main reason for this being fiscal loosening in good times.• The expenditure benchmark appears to be a more effective indicator in reducing procyclicality than the structural balance.• Strict compliance with fiscal rules would have resulted in an acyclical fiscal effort.		EB

IV. Taking a look forward

1. Recovery and Resilience Facility (missing in the analysis)

- A game changer for the coming three years with challenges
- Increase in investment projects prompted by the RRF makes the focus on MTFF extremely relevant.
- Capital spending needs to be framed in MTBFs to be sustainable and provide clarity to the decision-makers on the available envelope over the planning horizon.

2. The role of Independent Fiscal Institutions

- Helped to increase the reputational costs;
- Increased importance of IFIs in national medium-term planning (Van Hagen, 2010; Sherwood, 2015);
- Exchange of good practice via EFB analysis and the Network of EU Independent Fiscal Institutions;
- But different influence and administrative capacity across MSs (Debrun & Jonung, 2019; Beetsma et al. 2019).

IV. Taking a look forward (2)

3. Budgetary short-termism

- Public attention in the EU Member States focused on short-term budgets only;
- Medium-term budgetary plans, as presented in the SCPs, have limited impact on national budgetary decisions. **Efforts very often back-loaded and based on vague objectives** (also reflecting fairly weak SCPs role as a driver of national budgetary process in many countries).

4. Further reflections on how to fix the issues?

- Moving to a rule anchored in debt will help, instilling a medium-term perspective;
- Moving from structural balance rules to a expenditure rule would help (COM-PFR 2020; EFB 2020);
- Continuing the exchange of good practices.

Thank you