

Do institutional aspects shape the effectiveness of IFIs?

THE CASE OF COUNTRIES' COMPLIANCE WITH EU FISCAL RULES

COMMENTARY

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The views expressed are of the author and not necessarily representing the views of the World Bank.

Objectives of the study

- The study by Capraru et a. (2024) examines which institutional aspects of IFIs determine their effectiveness in terms of supporting compliance with fiscal rules.
- It also considers how this relationship changes based on the number of rules in place.
- It confirms some earlier findings (by Debrun, Nerlich, Reuter, Capraru, Beetsma et al), broadens the research to specific institutional aspects of IFIs, and tests the interaction of IFIs and fiscal rules on compliance with the rules.
- Finally, it provides insights on reforms that would help strengthen the role of IFIs.

Data and methodology

- Dataset of 30 IFIs across 26 EU MS, applying the fixed effects estimation method and robustness check of standard errors to control for heteroscedasticity and autocorrelation in the residuals.
- Several new rich data sources:
 - An *overall compliance index* using compliance with four fiscal rules from EFB (Larch et al 2023)
 - An *overall index of institutional aspects* as a sum of seven indices (public disclosure, resources, access to information, existence of the comply or explain principle, independence, the breadth of IFI tasks and media visibility) that are also assessed separately.
 - Seven institutional indices are derived from the survey of the Network of EUIFIs conducted in 2022 through a self-assessment questionnaire.

Results

- There is a positive and statistically significant relationship between the presence of IFIs and compliance with fiscal rules.
- The results are robust when there is an interaction between IFIs and the fiscal rules framework. However, the interaction is efficient when the number of rules is moderate (not high).
- Better compliance with fiscal rules is in countries with IFIs that carry out mandates like public disclosure, have a sufficient level of resources, good and timely access to information, a high degree of independence, a broader mandate of IFI tasks, and a prominent media visibility. Comply or explain principle was not statistically significant and the study offers rationale.
- Some earlier results are also confirmed, including the negative correlation of election years and compliance with fiscal rules.

New contributions

- The study investigates whether IFIs have the capability to monitor simultaneously all four rules, due to some specific institutional features, and if they impact positively the compliance with those rules.
- The study also finds that past compliance positively correlates with current compliance that could be more researched – what drives the compliance discipline/culture?
- The study finds that the impact of IFI features diminishes with a more complex fiscal framework that reduces the discretion policy space. When the number of rules is low, institutional features of IFIs become significant and important for compliance gap (including for expenditure-rule compliance gap).
- A very useful literature/research overview on relationship between effective IFIs (or their specific features) and compliance with some fiscal rules, fiscal policy procyclicality, macro projections or borrowing costs. A summary table of literature on institutional aspects would also be useful.
- A data rich survey of EU IFIs, extremely useful for comparisons and could serve as a guide to newly established IFIs.

Some considerations...

- Potential self-reporting bias: Data on institutional aspects are collected through self-assessment of IFIs: some information is binary (like public disclosure, access to information, existence of the comply or explain principle, the breadth of IFI tasks), but some involve self-assessment and therefore bias (independence, resources, and media visibility).
 - Comparison with the EU Scorecard results developed by ECFIN as a more objective observer?
- The compliance indicator is correlated with the fiscal rules indicator. The latter refers to national fiscal rules while the compliance index refers to EU rules which are not necessarily consistent (EFB's annual report of 2023).
- The study controls for the electoral cycle but not for the activation of the escape clauses.
 - Are they treated as compliance with rules? Escape clauses would affect compliance gap.
- Also, apart from institutional factors, compliance with fiscal rules will typically depend on the economic cycle. How the authors control for such factors?

Some considerations

- Toning down the claim that the new Fiscal Governance Framework is a simplification of the previous one:
 - It allows for the extension of adjustment path based on promised reforms.
 - It defines the fiscal requirement effort based on the DSA which depends on the projected growth and fiscal path (optimistic bias?).
 - It introduces quantitative safeguards that define a lower bound for the adjustment.
 - For IFIs it might be difficult to assess the compliance ex-ante given the lack of predictability and complexity.
- Publishing the questionnaire and all survey data (including on the annual budget, remuneration ratio, government involvement in IFI elections, application of the comply-or-explain principle) would be helpful and useful for further research.

Congratulations and thank you!