STAATSSCHULDENAUSSCHUSS

WORKSHOP: FISCAL POLICY COUNCILS – JANUARY 31, 2011

OPENING REMARKS

Bernhard Felderer

Introduction

In the past twenty years, a sizeable body of literature has been elaborated on the determinants of **successful fiscal consolidation**.

The **first wave** of these analyses – between the late 1980s and the mid-1990s – focused primarily on the **composition of the adjustment** and the role of the **political and institutional setting** (such as coalition versus single-party governments and the prevailing electoral system). According to this research, successful fiscal consolidations were predominantly **expenditure-based**, particularly through current expenditure cuts mainly of public wages and transfers.

The recent research has also highlighted the prominent role that some elements of **domestic fiscal frameworks** have played in the fiscal consolidation episodes since the early 1990s. The main **components** of domestic **fiscal frameworks** are (1) numerical fiscal rules, (2) **independent fiscal institutions** (specific public bodies acting in the field of budgetary policy), (3) medium-term budgetary frameworks for multi-annual budgetary planning, and (4) budgetary procedures governing the preparation, approval, and implementation of budget plans.

Today's workshop deals with one of these four components: namely, **Fiscal Policy Councils (FPCs).**

Session 1: The Rationale for Fiscal Policy Councils

Session 1 examines the **Rationale for Fiscal Policy Councils**. The focus of this session will be the **theoretical underpinning of independent fiscal institutions as a useful complementary policy option** to **reinforce fiscal governance**.

The persistence of deficits and the rise in public sector indebtedness over the past three decades in so many countries suggest that some **fundamental factors,** like **inadequate fiscal discipline**, **weak fiscal management** and **insufficient budgetary surveillance,** have played an eminent role in the past.

The underlying **reasons** for the **deficit bias** are well-known. They include the tendency of policymakers to focus primarily on the consequences of their discretionary actions in the short term. They also reflect political and distributive conflicts: i.e. the tendency for any given political constituency or group to use the available resources for their own distributive purposes without regard to the overall budgetary position.

In **the crisis**, fiscal policy initially served as an important stabilizing factor on a worldwide basis. The effect of automatic stabilizers, economic stimulus plans as well as bank bailout measures contributed to curbing the slump in the real economy and to stabilizing financial systems. By 2010, however, the budgetary situations in several EU countries had worsened so dramatically that financial markets lost trust in the sustainability of public finances in these countries. In further consequence, these countries found it increasingly difficult to meet their funding requirements. It was only possible to partly bring the situation under control after a rescue program had been established, in which the IMF, which grants financial support to Member States that are having exceptional economic or financial problems, played a major role.

For countries operating under **fixed exchange rates, or in a monetary union**, there may be a more general case for using discretionary countercyclical fiscal policy to deal with asymmetric shocks. But in this context, an FPC may have an important role in ensuring that fiscal policy does not play **a demand stabilization** role at the expense of **longer-term prudent debt policy**.

Session 2: National Fiscal Policy Councils: Mandate, Design and Effectiveness

In Session 2, The **Mandate and Design of Three Different National Fiscal Policy Councils (the Swedish FPC,** the **High Council** of **Finance** in **Belgium** and the **Government Debt Committee** in **Austria**) are presented and discussed. In a number of cases, these institutions have been successful in disseminating their policy advice and effectively influencing the conduct of fiscal policy.

By now, around **30 independent institutions** have been established in **about 20 EU countries.** But the role and mandate of these public bodies are quite different (i.e. macroeconomic forecasts, independent analysis on fiscal policy issues, recommendations addressing long-term sustainability issues or proposals containing fiscal targets for the different tiers of general government).

In my opinion, independent **FPCs can and should play a prominent role in fostering sound public finances:**

(1) Independent FPCs act as an **intermediary** between the government (especially the Minister of Finance) and the different political groups (and/or social partners). The ongoing **dialogue** helps to **raise the standards of the discussion** and promotes **medium- and long-term considerations** of fiscal policy issues. My impression is that the Government Debt Committee in Austria plays a “supervisory” role in the general economic policy debate.

(2) In addition, there is strong evidence that **high transparency** creates a policy environment that pushes governments to respect sound fiscal criteria and to discourage undesirable discretion and procyclicality. So it seems to me that the main **activities and outcomes of FPCs** (i.e. fiscal policy recommendations, monitoring reports, studies in economics) should be **published** and **broadly communicated** via the media and/or via public events.

(3) Furthermore, **financial markets** penalize **expected unsustainable policies** by raising interest rates, widening credit spreads and in extreme cases by refusing to lend at all. The financial crisis has clearly exhibited that fiscal policy can change very abruptly from being an anchor of stability to becoming a risk factor for the economic situation of a country. **But confidence** in a country’s ability to implement sound fiscal policies in future and **credibility** in general can be **strengthened by independent FPCs**.

Session 3: Gremien zur Stärkung der Fiskaldisziplin: Gibt es Schlüsselfaktoren für den Erfolg?

Let me now turn to the **third session,** which will be held in **German.** The workshop will conclude with **a panel discussion.** The discussion, which aims at fostering the dialogue between academics and politicians, will start at 5 p.m. after a break.

The panelists have been asked to present **their opinion on "the usefulness and key factors of National Fiscal Policy Councils"** with a view to strengthening sound public finances in Europe ("Gremien zur Stärkung der Fiskaldisziplin: Gibt es Schlüsselfaktoren für den Erfolg?").

It seems to me that many, but not all existing FPCs, play an important role in the national fiscal policy debate today. In my opinion, the **independence** of a **fiscal advisory agency** is one of the key success factors for its **reputation**.

Before I hand over the floor to Ernest Gnan, Head of the Economic Analysis Division of the Oesterreichische Nationalbank, who will chair the first session, let me conclude with the hope that you will enjoy the following presentations and discussions.

Literature:

European Commission, 2010 Report on Public Finances in EMU, p. 98 ff; 2011.

Staatsschuldenausschuss, Bericht über die öffentlichen Finanzen 2009, Anhang A1 Empfehlungen (Recommendation of the Government Debt Committee on Budget Policy and Financing).