

Lessons from the Swedish fiscal framework

*Joint Workshop by IMF Fiscal Affairs Department
and Offices in Europe*

The Functions and Impact of Fiscal Councils

Paris, March 13, 2013

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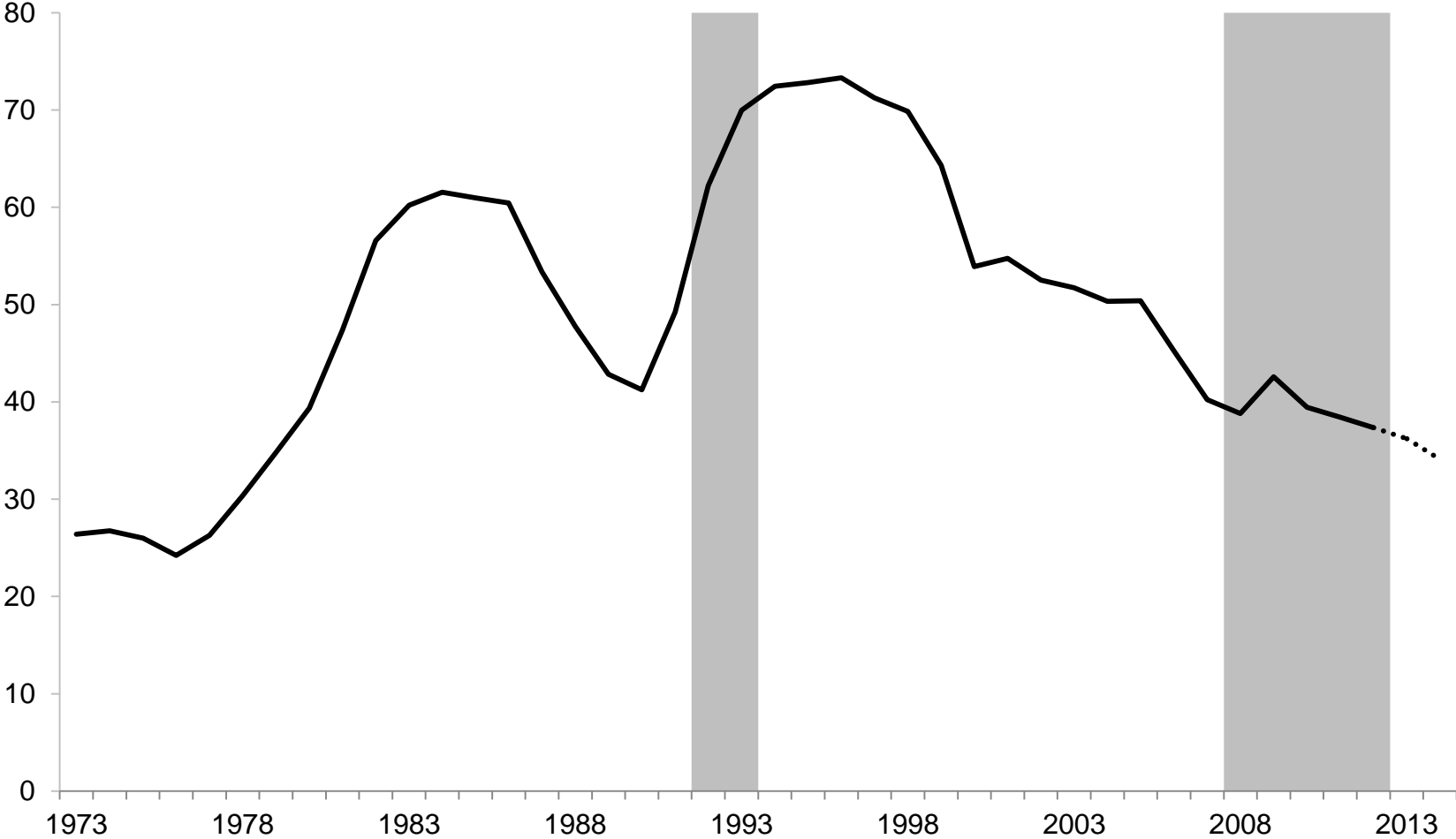
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Sweden's fiscal consolidation

Sweden has a successful record of fiscal consolidation after the crisis of the early 1990s.

Government gross debt (% of GDP)

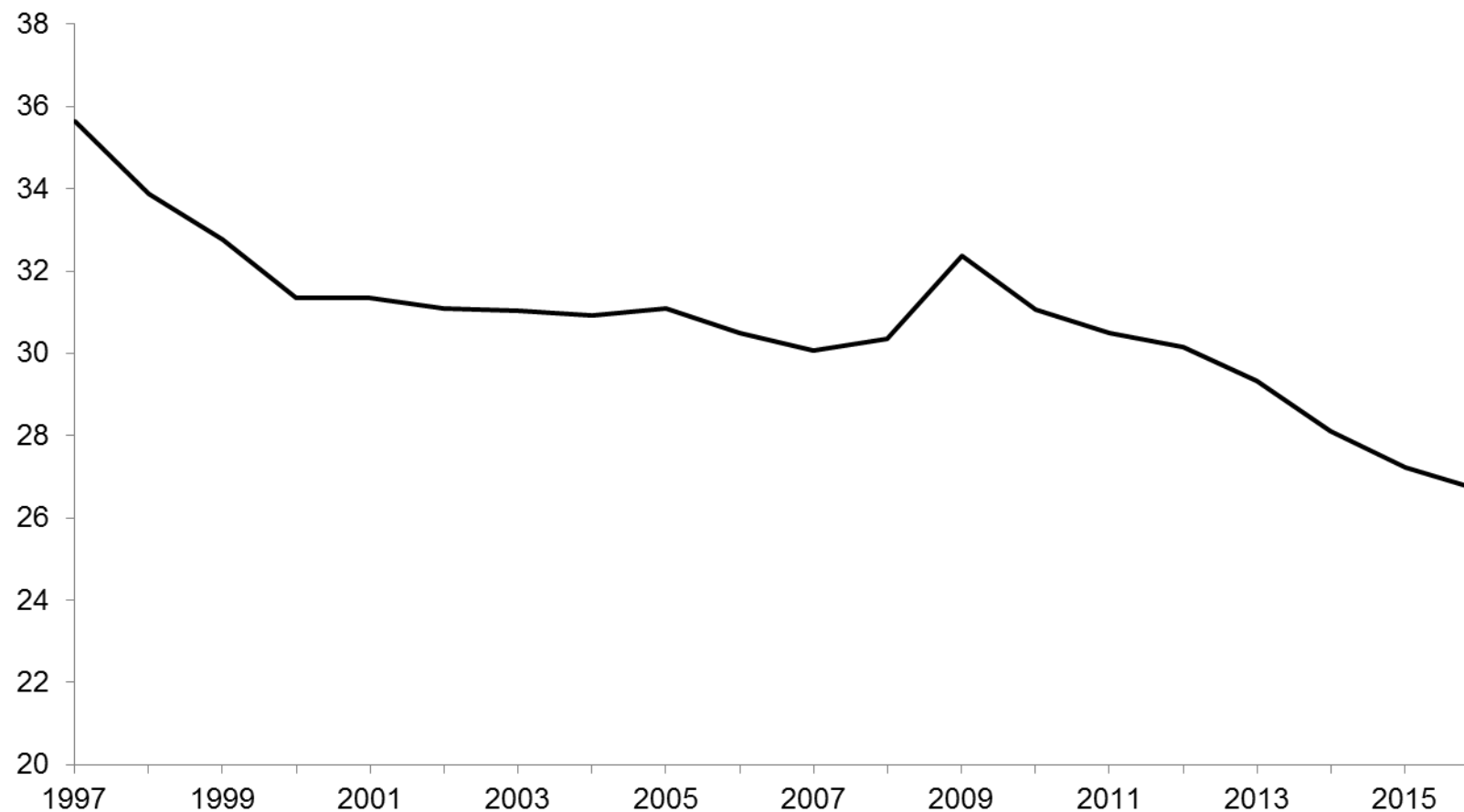


Source: AMECO

■ Crisis years — Sweden

Expenditure ceiling

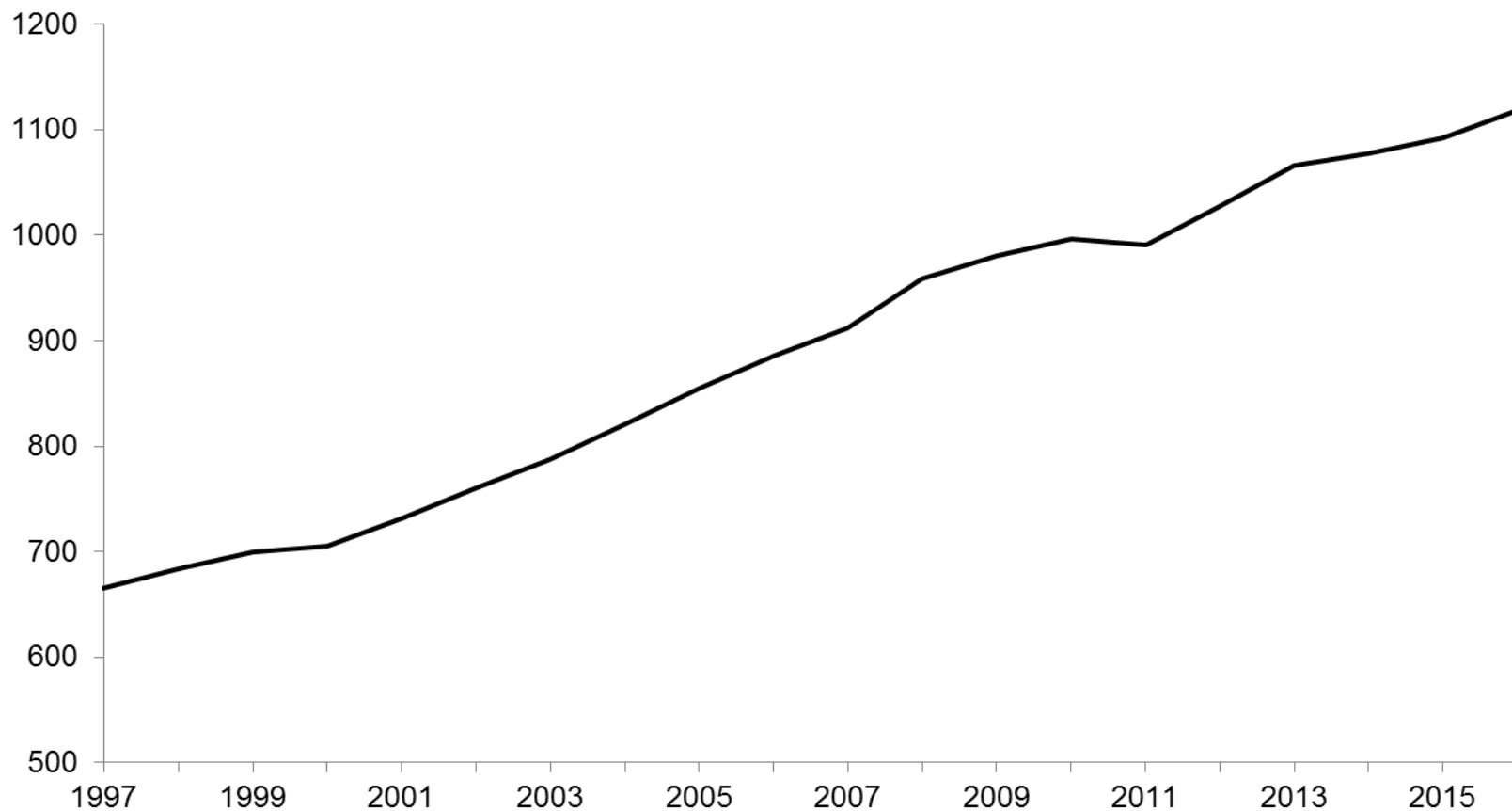
Per cent of GDP



Source: Ministry of Finance

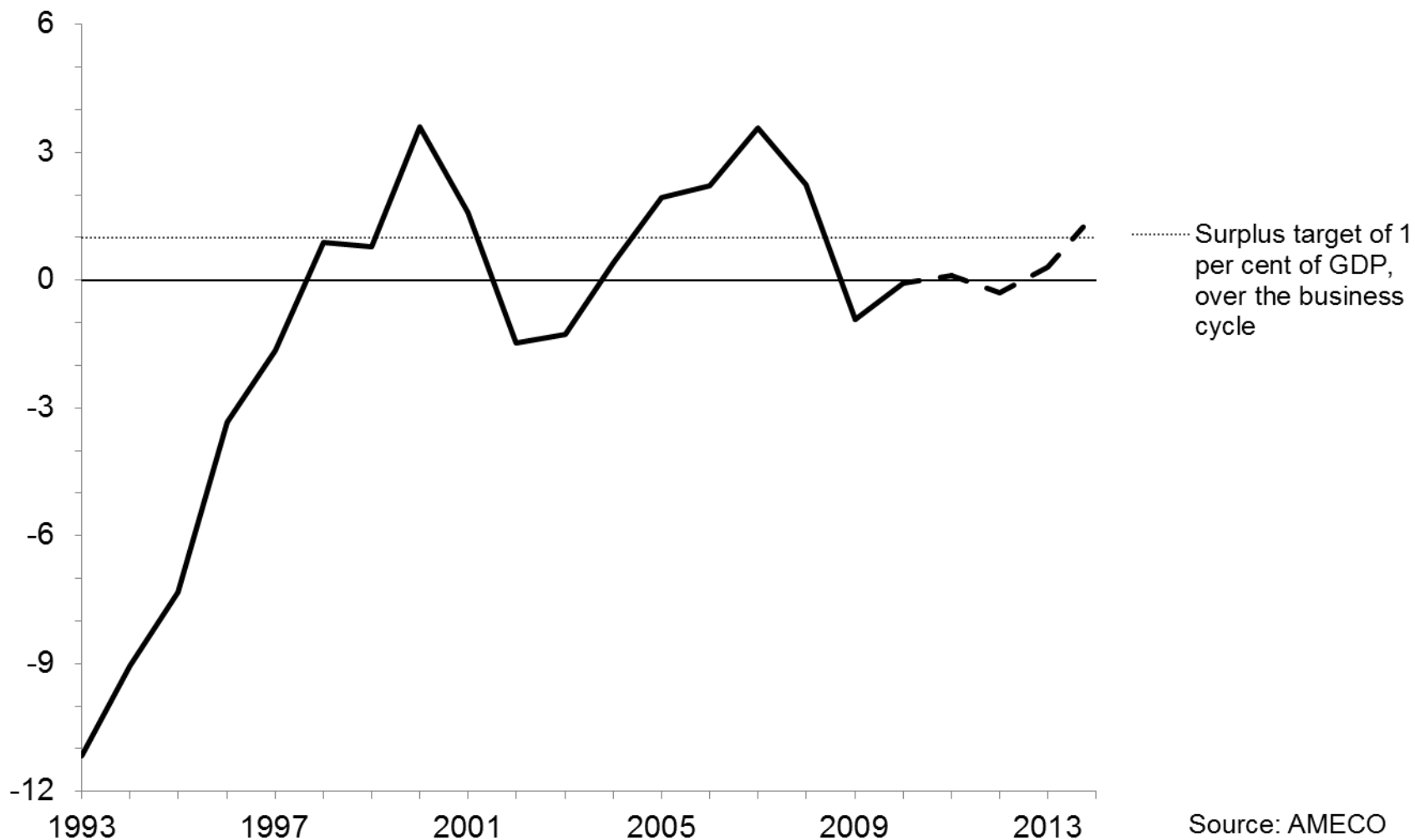
Government expenditures

SEK (billions)

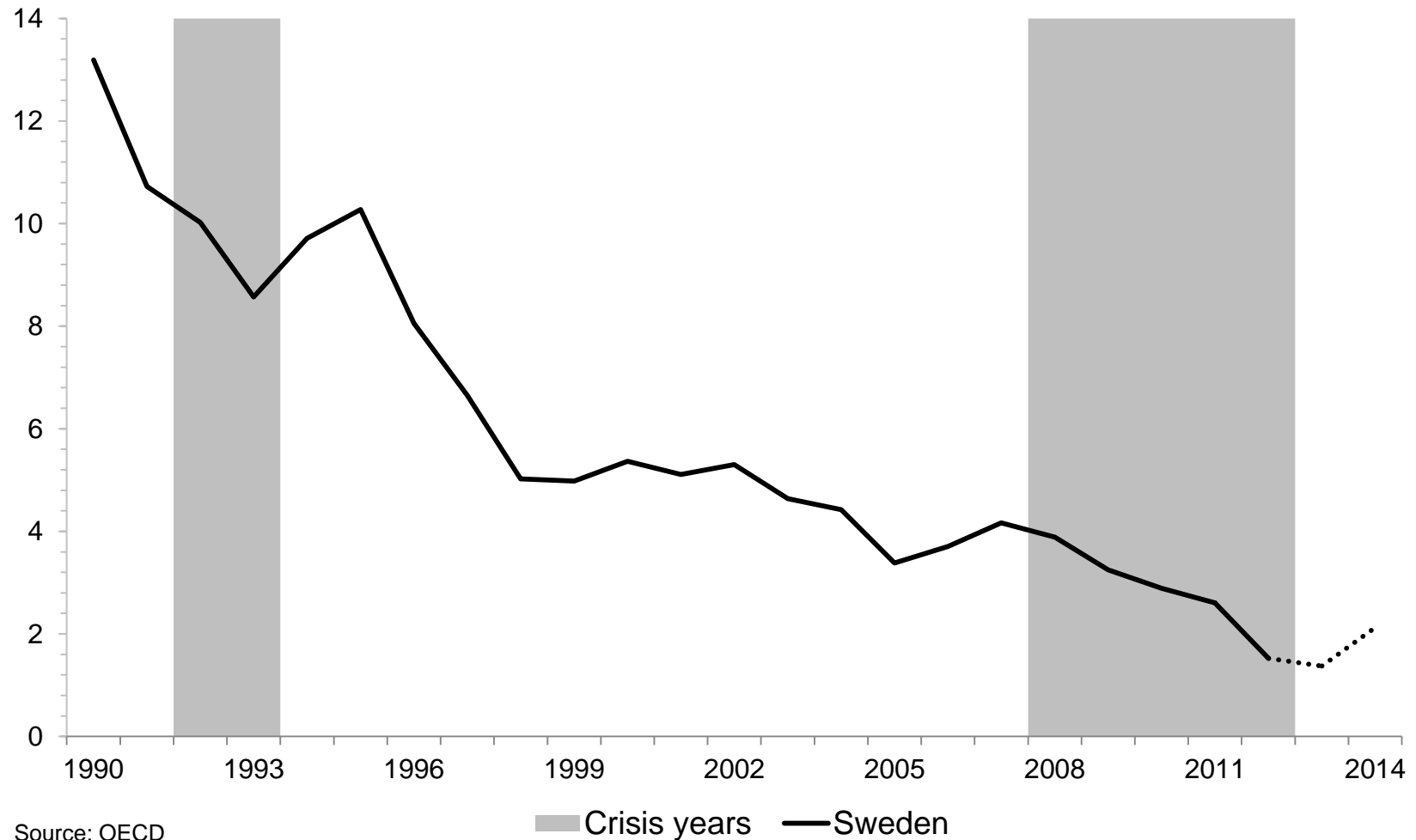


Source: Ministry of Finance

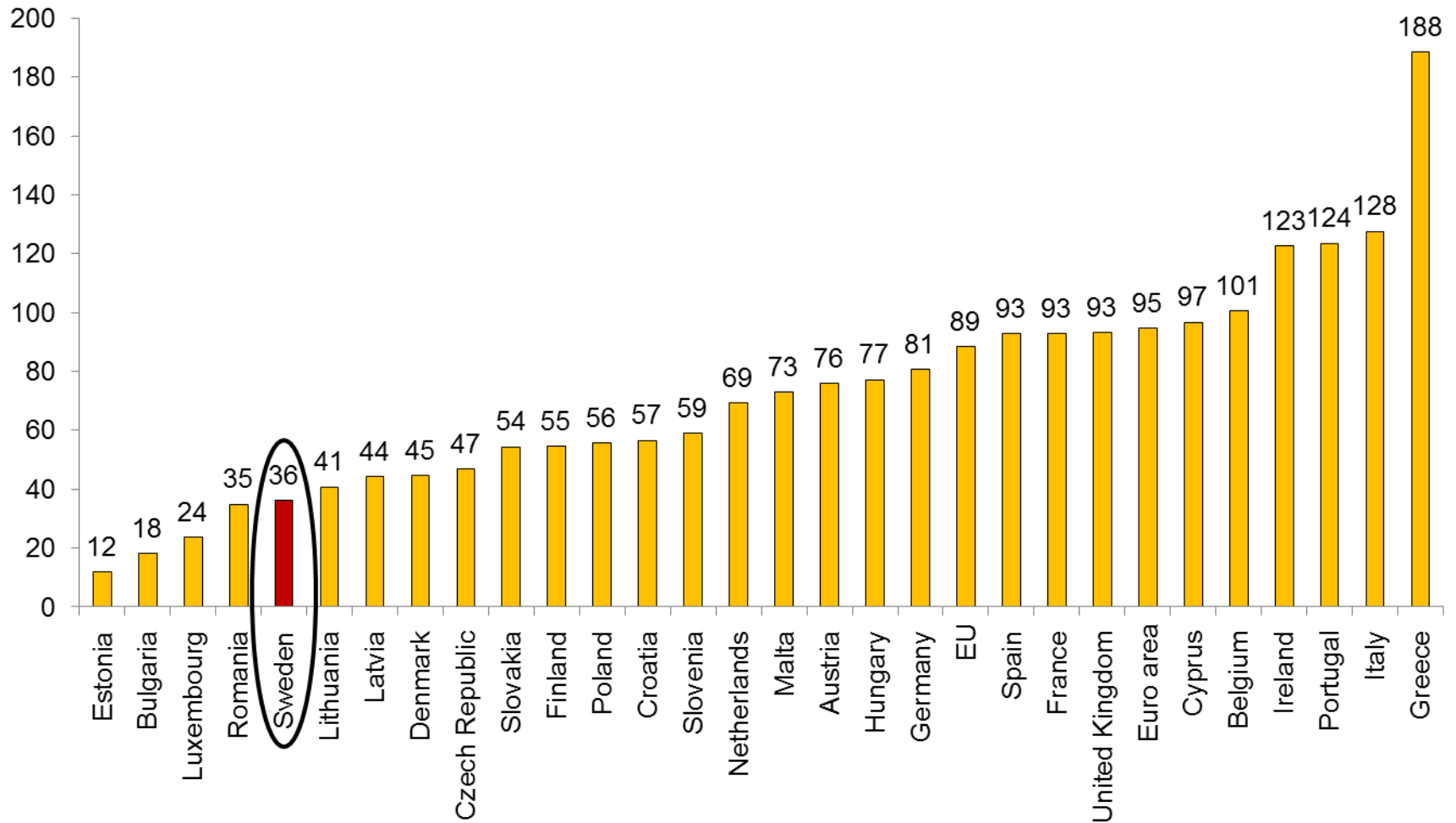
Surplus target



Long-term interest rate on government bonds (%)

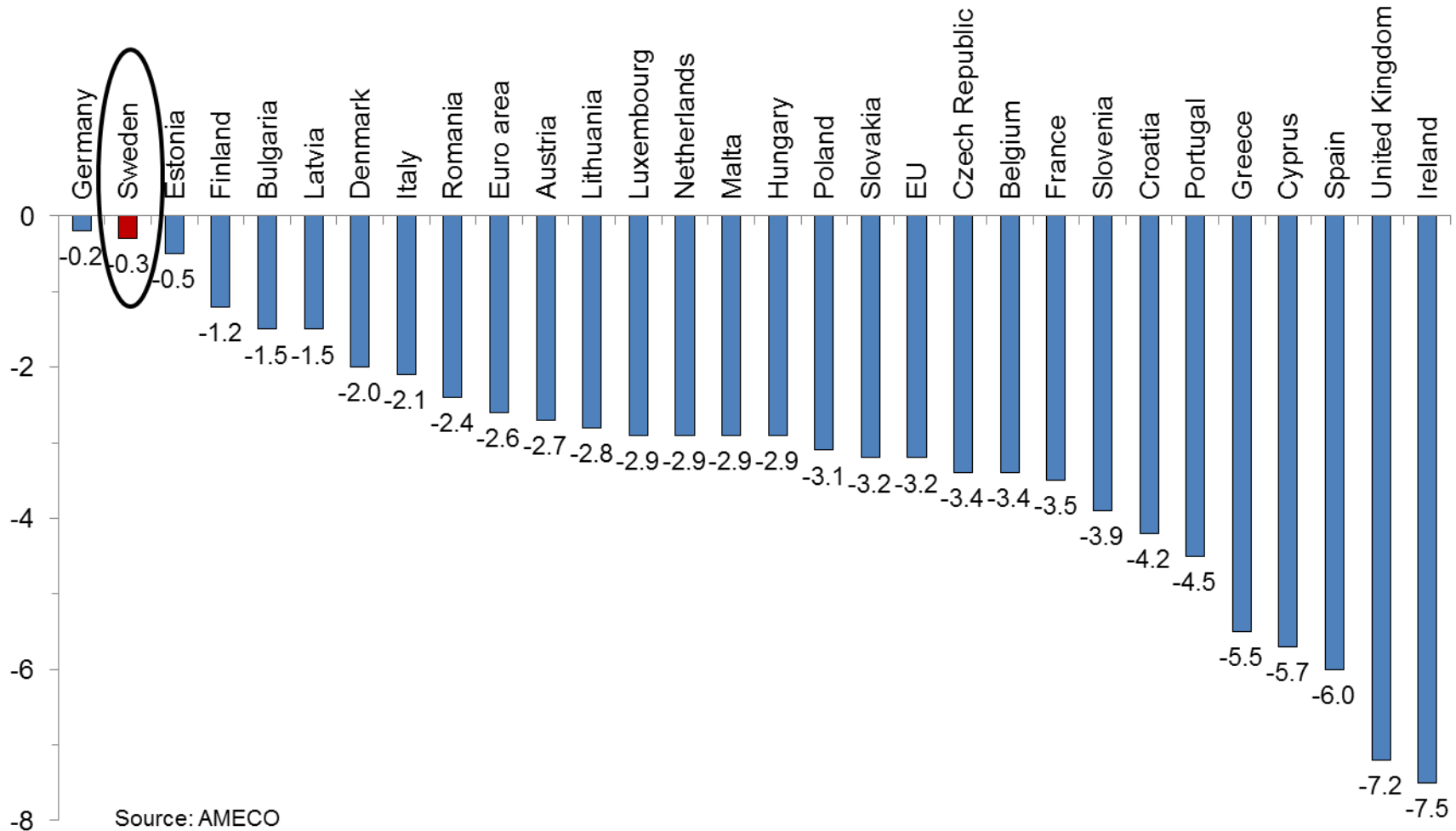


General government gross debt (% of GDP) 2013



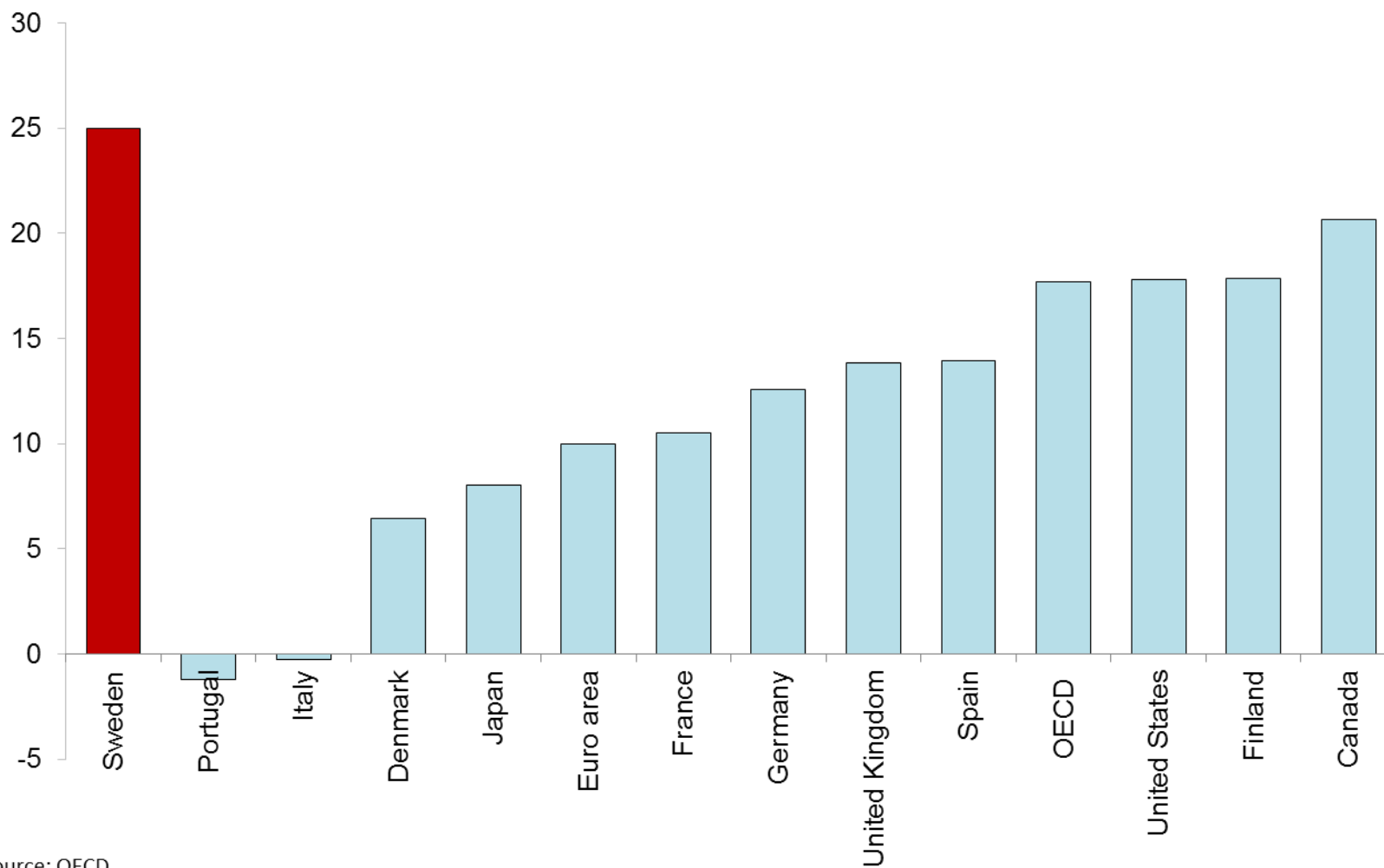
Source: AMECO

General government net lending (% of GDP) 2013



Source: AMECO

Total real GDP growth (%) 2002-2012



Source: OECD

What are the lessons from Sweden?

Lesson 1:

Sweden adopted a fiscal framework, including a fiscal policy council, *after* the severe fiscal shock during the crisis in the early 1990s.

The task of the framework including that of the council should be to keep the memory of this shock alive in present and future fiscal policy debates. The fiscal framework should thus serve as an inoculation making the political system more resistant to fiscal profligacy and deficit financing.

What are the lessons from Sweden?

Lesson 2:

The fiscal consolidation process started *after* the financial and fiscal crisis of the 1990s and continued for many years.

Timing is important when introducing a fiscal framework and a fiscal policy council. It should *not* be established in such a way that it prevents an effective response by the fiscal authorities during an acute economic crisis, although steps to put a fiscal framework and a fiscal council in place can be taken during the crisis when there is a feeling of emergency in the political system.

What are the lessons from Sweden?

Lesson 3:

The fiscal consolidation process has been accompanied by falling long-term interest rates. Thus policy-makers have been rewarded by the financial market for their efforts.

The task of a fiscal framework including a fiscal policy council is facilitated by a well-functioning financial system that serves as a signaling device concerning the fiscal policy stance of the government. The government's adherence to a fiscal framework will inform financial markets about fiscal developments. A fiscal framework will under these circumstances represent a pro-market device.

What are the lessons from Sweden?

Lesson 4:

A fiscal framework is likely to consist of a number of quantitative fiscal targets and constraints covering various time horizons. Here nominal government spending ceilings given on an annual basis are likely to be more efficient from a political economy point of view than over-the-business cycle (a.k.a medium term) defined constraints and targets.

What are the lessons from Sweden?

The effectiveness of a fiscal policy council depends on several factors.

Lesson 5:

The task of a fiscal council is facilitated by the existence of a fiscal framework founded in law and/or in practice. The council can use such a framework as a benchmark for its analysis and recommendations concerning fiscal policy. Without a fiscal framework, a council faces a much more difficult mandate. It is forced to decide on proper fiscal rules to use by itself, when judging the performance of the government. Whatever it chooses, it will be more open to criticism and counter-arguments than in the case of an existing fiscal framework.

What are the lessons from Sweden?

Lesson 6:

The independence of a fiscal council is facilitated by the council being at a distance from the government.

Independence is promoted by not being directly involved in policy-making, for example by supplying the ministry of finance with forecasts or other recommendations.

By providing only *ex post* analysis of the government's economic policy proposals and measures, a fiscal council can avoid being dragged directly into the policy process in a way that risks its independence.

What are the lessons from Sweden?

Lesson 7:

Independence is fostered by recruiting a majority of the members of the council from academia, preferably also foreign members to foster independence and allow for intellectual import into the domestic policy analysis.

Members could also be selected from policy-makers who have left active engagement and are expected to have no further career plans in the political system.

What are the lessons from Sweden?

Lesson 8:

Consensus in society about a council is facilitated by a strong position of the economics profession in public discourse. The council will then be recruiting members who by themselves have a respected background.

What are the lessons from Sweden?

Lesson 9:

A fiscal council can be a strong voice in the public debate, serving as an educator of the public and the political system on fiscal policy, if the existence of a council is supported across party-lines. A council that is viewed as partisan will find it hard – if not outright impossible - to gain credibility.

A consensus society like the Swedish one is likely to serve as a better background for a council than a country deeply divided across political party lines.

What are the lessons from Sweden?

Lesson 10:

The impact of a fiscal policy council depends on the economic policy culture or traditions of governance of a country. If a country has a culture where the public holds a strong trust in public institutions, in government effectiveness and honesty, in the accountability of elected politicians, in the democratic process and in the rule of law, as in Sweden, such an environment probably makes a fiscal council more effective. These prerequisites concerning governance are not always available. In addition, they are difficult to establish in the short run. Although an open society with strong public trust in the political system and in the role of experts makes it easier for a fiscal policy council to have an impact, we should not expect the opposite line of causation to hold: a fiscal council per se does not bring about immediate trust in public governance. However, a council may, in the long run, contribute to trust in the political system.

Trust in the political system in EU member states

Country	The government		The political parties		Satisfaction with the way democracy works	
	<i>Tend to trust</i>	<i>Tend not to trust</i>	<i>Tend to trust</i>	<i>Tend not to trust</i>	<i>Very/Fairly</i>	<i>Not very/Not at all</i>
Sweden	59	38	35	61	86	13
Finland	62	35	36	60	78	21
Denmark	42	56	36	61	90	9
UK	25	70	12	83	60	38
Germany	41	53	21	73	70	29
France	30	65	12	83	60	38
Spain	11	86	6	91	32	66
Portugal	22	74	17	79	25	74
Italy	17	77	8	88	27	72
Greece	7	91	5	94	11	89

Source: European Commission, Eurobarometer 78

What are the lessons from Sweden?

Lesson 11:

Finally, creating new institutions and making them trustworthy in the eyes of the public is a time-consuming trial-and-error process. Mistakes will be made. We should not expect a new fiscal policy council to have an immediate impact regardless of where it is established. We should also expect that the new council being erected in

Conclusions

Fiscal frameworks and fiscal policy councils can play an important role by strengthening weak governance structures.

This role is facilitated by a strong backing by the political system of fiscal frameworks.

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