

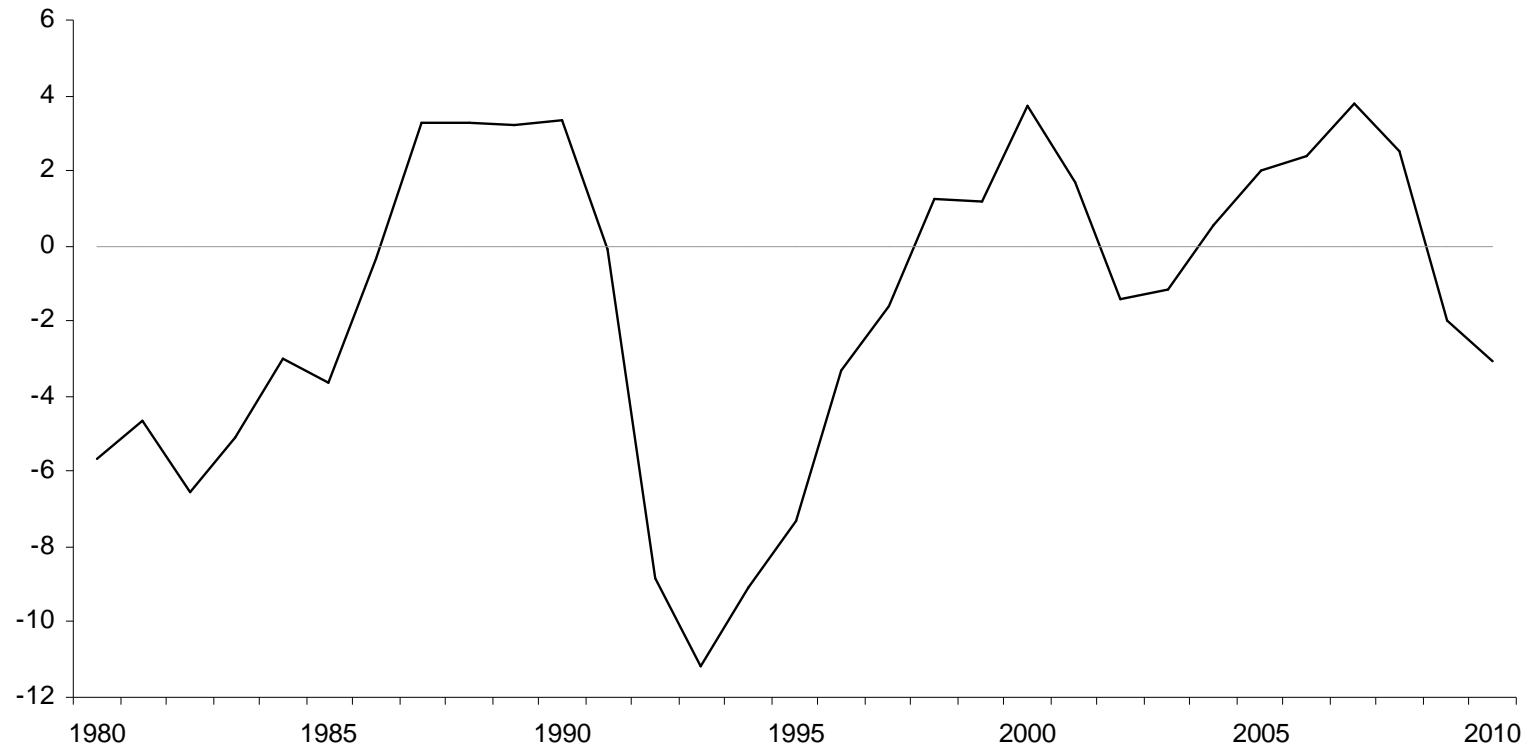
The Swedish Fiscal Framework and the Fiscal Policy Council

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Workshop on Fiscal Rules and Institutions

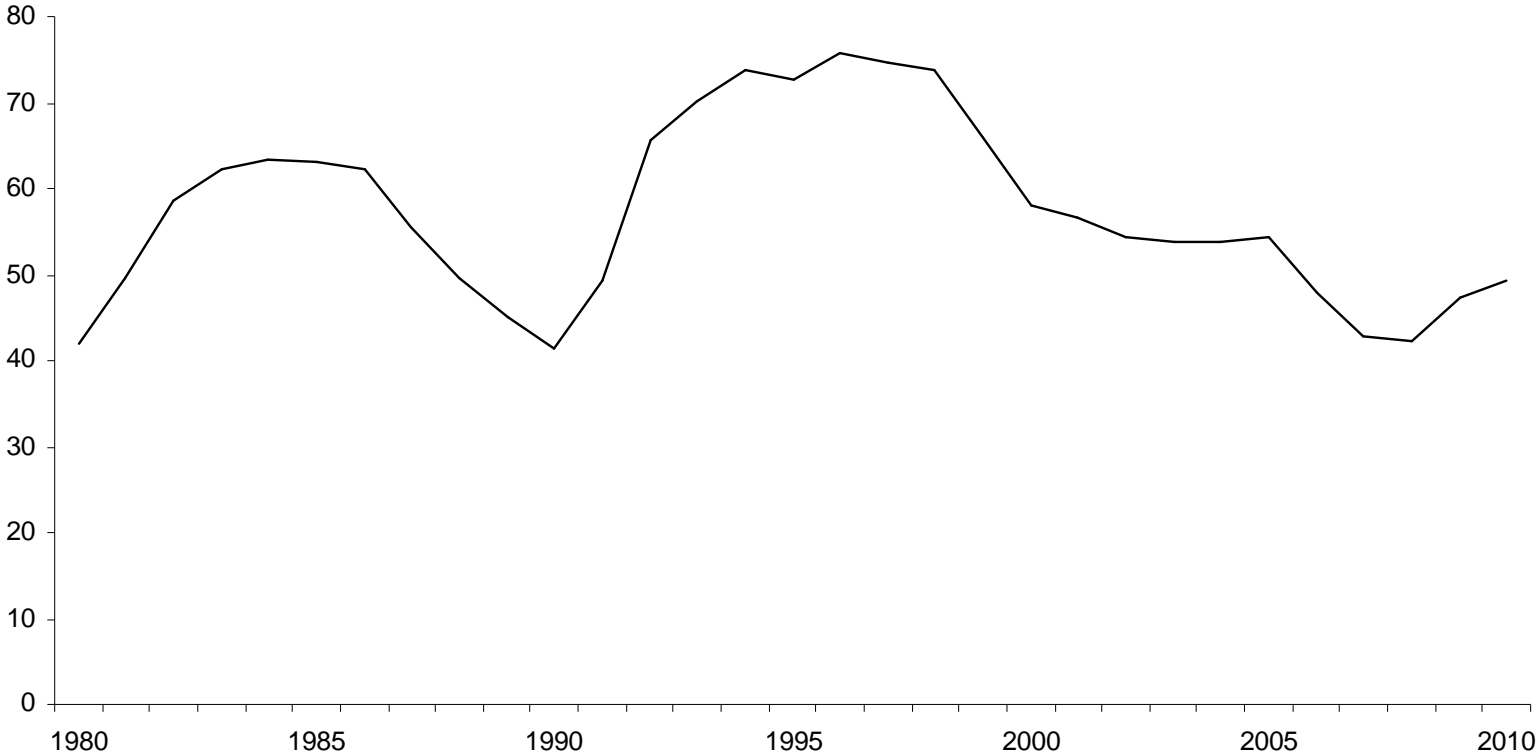
OECD, 22 March, 2010

General government net lending in Sweden, per cent of GDP



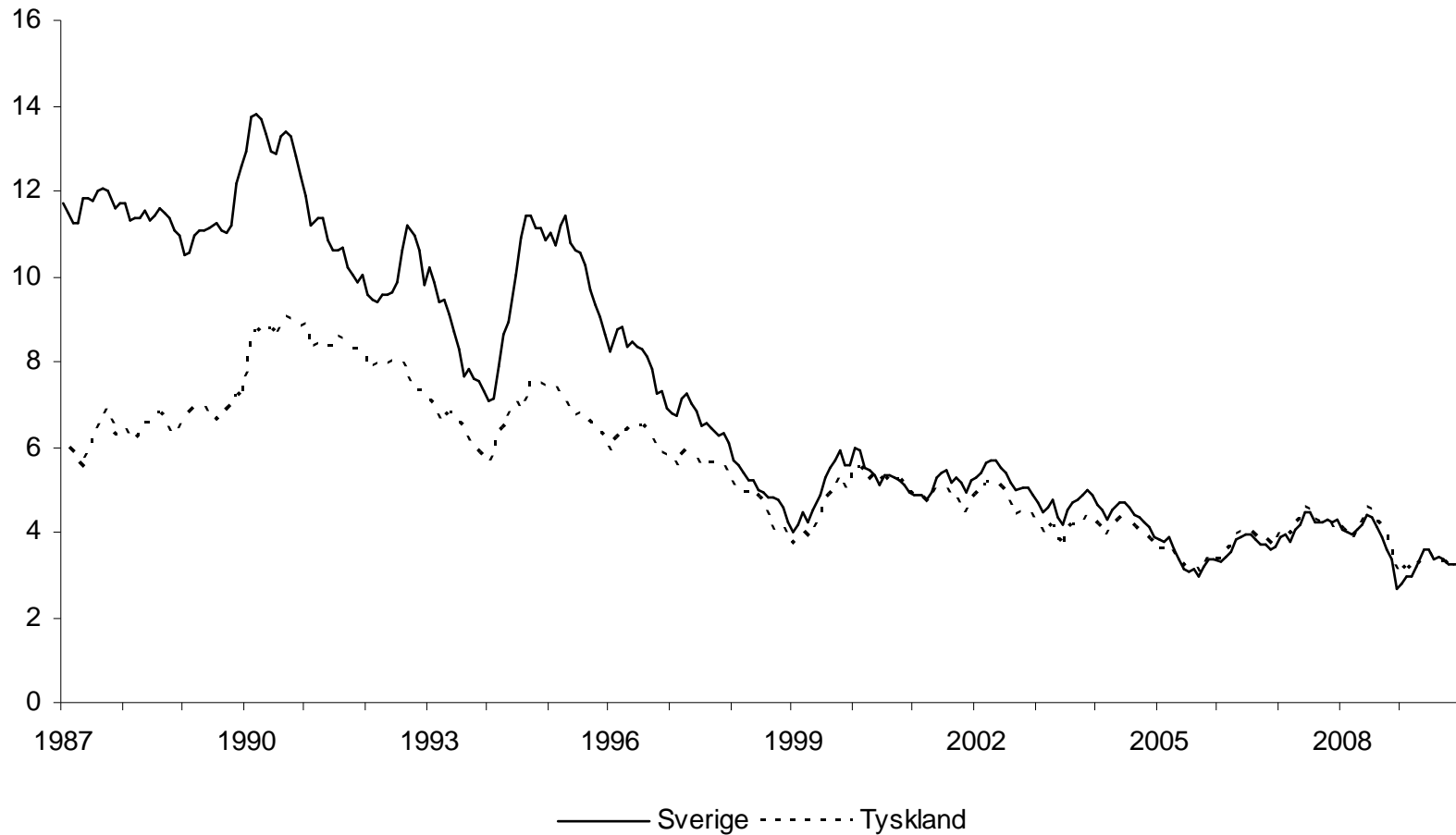
Source: OECD.

General government gross debt in Sweden, per cent of GDP



Source: National Institute for Economic Research.

Interest rates on ten-year government bonds in Sweden and Germany



Source: The Riksbank.

The S2-indicator on fiscal sustainability

Belgium	5.3
Denmark	-0.2
Estonia	1.0
France	5.6
Germany	4.2
Greece	14.1
Ireland	15.0
Italy	1.4
Latvia	9.9
Lithuania	7.1
Netherlands	6.9
Spain	11.8
Sweden	1.8
United Kingdom	12.4
Euro area	5.8
EU27	6.5

The Swedish fiscal framework

- Top-down approach for the central government budget
- Surplus target for government net lending
- Central government expenditure ceiling
- Balanced budget requirement for local governments
- Fiscal Policy Council

What has worked and what has not worked in the Swedish framework?

- Obviously a strong fiscal situation
- But there are also potential problem
 - budget tricks with the expenditure ceiling: tax expenditures and timing of payments
 - insufficient motivations for the choice of numerical target
 - the exact meaning of the surplus target

Fundamental objectives behind the intermediate surplus target

- Demography and sustainability
- Intergenerational fairness
- Social efficiency and tax smoothing
- Precautionary buffers
 - long-run developments
 - cyclical considerations

A surplus of one percent of GDP over the business cycle

- Is it a backward-looking target with memory?
 - compensation for past deviations
- Is it a forward-looking target without memory
 - no compensation for past deviations

Different indicators of the surplus target

Budget Bill for 2010, per cent of GDP

	2008	2009	2010	2011	2012
Actual fiscal balance	2,5	-2,2	-3,4	-2,1	-1,1
Historical average	1,6	1,2	0,8	0,5	0,4
Moving average	0,3	-0,1			
Cyclically adjusted balance	2,3	1,4	0,2	0,7	0,6
Historical average of cyclically adjusted balance	1,2	1,2	1,1	1,1	1,0
Moving average of cyclically adjusted balance	1,2	1,2			

Need for amendments?

- Legal requirement on a surplus (fiscal) target
- Requirement that the government should explain how it will act when there are deviations of a certain magnitude according to pre-specified indicators
 - letter to the parliament
- Regular reviews of the target
 - co-ordination with pension rules
- Stricter rules prohibiting circumventions of the expenditure ceiling
 - instead well-defined *escape clause*
- Automatic cyclical adjustments in central government grants to local governments

The Swedish Fiscal Policy Council

- Established in 2007
- Agency under the Government
- Independent evaluation of fiscal and other economic policy
- Annual report to the Government
- Public hearing in the Parliament
- Eight members
 - six academic researchers
 - two ex-politicians
- Small secretariat

Background

- International discussion of Fiscal Policy Councils/Committees
 - advisory group giving recommendations
 - government obliged to base budget bill on forecasts of independent council
 - delegation of actual decision-making
- Proposal on Fiscal Policy Council by Government Commission on the EMU in 2002
- The earlier Social Democratic government did not like the idea
- Council established by liberal-conservative government in 2007 (Minister for Finance: Anders Borg)
- The Left Party: *“another body providing false scientific clothing for the government’s right-wing policy”*

The council's remit

1. To assess if fiscal policy objectives are met
 - long-run sustainability
 - surplus target
 - expenditure ceiling
 - cyclical situation
2. To evaluate long-run employment and growth developments
3. To examine the clarity of the budget bills
 - grounds and motivations for policies
4. To evaluate the government's forecasts and the underlying models

The council "should work to achieve an increased public discussion in society of economic policy"

A broad remit

- Trade-off between breadth and depth
- Risk that fiscal policy watchdog role is weakened
- But important "supervisory" role of economic policy discussion
- Prime objective: the fundamentally democratic one of raising the standards of the economic policy debate
- Why this remit?
 - other pre-existing bodies
 - "institutionalise" strong Swedish tradition of high-profile academic participation in economic policy debate

Themes in the reports

- Increase the clarity of the surplus target: net lending of one percent of GDP over a business cycle
 - underlying fundamental objectives
 - too many indicators
- Criticism of circumventions of expenditure ceiling
- Critical evaluation of fiscal sustainability calculations
- More discretionary fiscal stimulus in the current recession (but less of permanent measures)
- Evaluation of the government's labour market reforms
- The economic reporting of the government

The council's impact

- Extensive media coverage
- Formal response in the spring fiscal policy bill
- Impact on actual policy
 - what is the counterfactual?
 - fiscal stimulus in 2010
 - less effect on "budget tricks"
 - some effect on surplus target
 - some effect on economic reporting

The council's role in the fiscal policy debate

- On average a fiscal policy council should be expected to advocate more fiscal discipline than the government
- But this need not always be the case: credibility gain
- The council must make its own judgements
- Stronger fiscal framework allows more discretionary stimulus in recessions
- The government's focus on fiscal discipline and the existence of the council are explained by the same factors



The council and the standing of the finance ministry

- Unclear effect on the standing of the finance minister vs spending ministers
 - finance minister could be backed up
 - but other ministers get access to alternative analyses
- Effect within the finance ministry
 - technocrats are strengthened relative to politicians

The council in the general political debate

- Political bias against the government
 - evaluations of government policy but not of opposition proposals
 - smaller problem in the long run
- Members are free to express their own views in the economic policy debate

The council's independence

- Members appointed by the government: three-year renewable periods of office
- Risks balanced by:
 - appointments after council proposals
 - low pay
- Budget has to be negotiated with the government
- Main guarantee of independence: academic economists have their main activities in another arena
- But potential problem that everyone knows everyone in a small country

The council's survival

- Too much power to independent academics?
- Initial reaction of the opposition: "experts should not evaluate the elected representatives of the people"
- Less clear today