Budgets Report

Budgetary Policy

Sustainable Governance Indicators 2017

SGI Sustainable Governance Indicators

BertelsmannStiftung

Indicator

Budgetary Policy

Question

To what extent does budgetary policy realize the goal of fiscal sustainability?

41 OECD and EU countries are sorted according to their performance on a scale from 10 (best) to 1 (lowest). This scale is tied to four qualitative evaluation levels.

10-9 = Budgetary policy is fiscally sustainable.

8-6 = Budgetary policy achieves most standards of fiscal sustainability.

5-3 = Budgetary policy achieves some standards of fiscal sustainability.

2-1 = Budgetary policy is fiscally unsustainable.

Switzerland

Score 10

Budgetary policy in Switzerland is fiscally sustainable. Gross public debt (general government) rose from a low 29% of GDP in 1990 to a peak of 52% in 1998, but receded to 34% by 2015. Structurally adjusted budgets were balanced even during the crisis of 2008 and 2009. In 2016, the federal state ran a positive balance, spending less than it received.

This fiscal sustainability is mainly due to the political decision to have a low tax load and a lean state. In addition, keeping the public deficit and debt low has been a major concern of politicians at all levels of the political system. Various rules and means have been developed in order to avoid the dynamics of expanding budgets. For example, on the federal level, there is the constitutional debt brake (Article 126, Article 159): “The maximum of the total expenditures which may be budgeted shall be determined by the expected receipts, taking into account the economic situation.” Direct democracy offers another effective means of keeping the budget within limits. In popular votes, the people have proven reluctant (compared in particular to members of parliaments when elections are drawing near) to support the expansion of state tasks with a corresponding rise in taxes and/or public debt.

Notwithstanding a very favorable fiscal position, the Federal Council announced another austerity program for the coming years, expecting serious fiscal deficits. Even taking into account the fact that some individual cantonal and municipal governments do pursue unsustainable budgetary policies, the total (i.e., general government) budgetary policy achievement arguably puts Switzerland in the OECD’s top group in terms of fiscally sustainable national policies.

Chile

Score 9

Chilean budgetary policy has been very successful in terms of national debt reduction and reserve fund accumulation. The country's budgetary policy is based on a fiscal rule that explicitly – and relatively transparently – links overall government spending to an estimate of government revenue trends. This puts Chile at the international best-practice frontier regarding budget policies and fiscal regimes. Although temporarily suspended during the difficult 2009 – 2010 period, this rule's application since 2001 (and the adherence to fiscal orthodoxy even without comparative legislation since the mid-1980s) has allowed the government to reduce overall debt, accumulate sovereign wealth and reduce its overall financial liabilities to negative levels. This policy proved absolutely adequate in dealing with the global financial crisis. In order to improve fiscal transparency and the validation of the public balance, the Fiscal Consulting Council (Consejo Fiscal Asesor) was created in 2013.

Recent trends have been somewhat more worrisome. The country's budgetary policy has come under pressure due to declines in the price of copper, slowing economic growth, state spending that has risen faster than GDP, the continued presence of a structural deficit, and an increase in debt. This trend forced the Chilean government to significantly lower expenditures of some ministries and public services in the latter half of 2016.

Citation:
Cf. DIPRES, Política de Balance Estructural: http://www.dipres.gob.cl/594/w3-pro pertyvalue-16156.html

Denmark

Score 9

Budget policy is guided by fiscal norms: i) the actual budget deficit must not exceed 3% of GDP, ii) public debt must not exceed 60% of GDP and iii) the planned structural budget balance must not display a deficit greater than 0.5%. These norms are part of EU-rules and Danish budget law.

Fiscal policy has satisfied these norms, although in some cases it has come close, and maintained its budget due to ad hoc measures like forward lifting revenue from pension taxation. Both the current balance and the structural balance have been close to the limits. The actual budget balance was -2% of GDP in 2015, and the Ministry of Finance projects it to be -2.8% in 2016 and -2% in 2017. The structural deficit was 0.7% in 2015, and is projected to be 0.4% in 2016 and 0.4% in 2017. Satisfying the budget norm is thus a binding constraint in economic policy.

Analyses from both the Ministry of Finance and the Economic Council show that the criterion for fiscal sustainable public finances is satisfied. This is largely the result of a number of reforms aimed at increasing the labor supply and employment by increasing the retirement age (both early retirement and public pensions), reducing the early retirement period (from 5 to 3 years), and various other reforms of disability pensions, social assistance, and study grants.

In short, when compared to other OECD countries, public finances in Denmark are in relatively good shape. Still, analyses of fiscal sustainability show that the structural balance will display deficits for the coming 35 to 40 years. Although surpluses are expected far in the future, implying that the country's fiscal sustainability indicator looks reasonably favorable (and among the best within the European Union), it is very risky to base economic policy on a trajectory implying systematic deficits for such an extended period. There is thus an issue with the profile of public finances that needs to be addressed. Moreover, it should be noted that an assessment of fiscal sustainability considers whether it is possible to maintain current welfare arrangements, but does not include room for improvements in, for example, the standards and qualities of welfare services (e.g., health). Hence, some pressure on public finances can be expected.

Citation:
Danish Economic Councils, The Danish Economy, Various issues. Latest issue: Autumn 2016 report, English summary available at: http://www.dors.dk/files/media/rapporter/2016/E16/E16_English%20Summary_1.pdf (Accessed 23 October 2016).

Ministry of Finance, Økonomisk Redegørelse, August 2016. https://www.fm.dk/publikationer/2016/oer-aug-16 (Accessed 23 October 2016).

Ministry of Finance, Forslag til finanslov for finansåret 2016, https://www.fm.dk/publikationer/2015/forslag-til-finanslov-2016-sep (Accessed 23 October 2016)

Ministry of Finance, Budget Outlook 2, August 2014. http://uk.fm.dk/publications/2014/budget-outlook-2-august-2014/~/media/Publikationer/Imported/2014/BO2/budget%20outlook%202_august%202014.pdf (Accessed 16 October 2014)

Estonia

Score 9

Estonia has followed a strict fiscal policy for decades. As a result, the country has Europe's lowest public debt as a percentage of GDP, and is able to meet future financial obligations without placing extra burden on future generations. Yet maintaining a balanced budget has come with some costs. The government substantially cut municipal budgets during the economic recession, and has not yet restored these funds. As a result, many local governments are struggling under mounting debts, with insufficient resources to accomplish their tasks. Long-term debts accumulated by the health insurance and public pension funds also threaten the government's ability to secure citizens' welfare while adhering to the principles of fiscal sustainability.

Latvia

Score 9

Latvia’s budgetary policy has been recognized as prudent and fiscally sustainable by both the European Commission and the IMF. However, achieving medium-term structural-reform goals remains a challenge. For example, in 2013 and again in 2015, previously legislated reductions to income-tax rates were rolled back, while mandatory pension-contribution rates (part of the second pillar of Latvia’s pension system) had not rebounded to pre-crisis levels and are 2% short of the pre-crisis level.

The budget framework and government-debt cap of 60% of GDP, prescribed by the Law on Fiscal Discipline, has been maintained. Latvia remains broadly compliant with the principles of fiscal discipline. Though, in both 2014 and 2015, the government missed its budget balance target, as approved in the budget law.

In 2015, the budget deficit was 1.3% of GDP, above the target of 1.0%.

Citation:
1. IMF (2015), Article IV Consultation, Available at: https://www.imf.org/external/pubs/ft/scr/2015/cr15110.pdf, Last Assessed: 22.11.2015.

2. European Commission (2013), EU BOP Assistance to Latvia – Second Review Under Post - Programme Surveillance, Available at: http://ec.europa.eu/economy_finance/eu_borrower/balance_of_payments/pdf/lv_efc_note_2nd_pps_mission_en.pdf, Last assessed: 21.05.2013.

3. IMF (2016) Staff Report on Article IV Consultation, Available at: http://www.imf.org/external/pubs/ft/scr/2016/cr16171.pdf. Last assessed: 07.11.2016

Luxembourg

Score 9

From a position of relatively low public debt, consolidated public debt decreased from 23.3% of GDP in 2013 to 21.4% of GDP in 2015. After four years of fiscal consolidation and high economic growth, the 2017 government budget will include a €1 billion deficit, which will increase public debt. Supported by strong population growth and an investment boom, Luxembourg has the strongest economic growth rate along with Malta and Ireland among EU member states. Eurostat data suggests that Luxembourg’s fiscal situation will continue to stabilize. The cost of structural investments increased from €1.955 million in 2015 to €2.229 million in 2016, an increase of 14%.

Despite the loss of e-commerce tax revenue in 2015, Luxembourg’s government revenues increased significantly in 2015. In 2015, the banking sector accounted for 20% of government revenue. Furthermore, accounting for indirect taxes, such as income tax paid by banking sector employees, the overall contribution of financial institutions to government revenue is about 25%. This highlights the importance of financial services to public spending. In 2015, Luxembourg achieved a structural surplus. According to recent calculations, the general account reported a deficit of €176 million, against €841 million provided in the draft budget.

Recent legislation requiring financial institutions based in Luxembourg to provide information to U.S. authorities, which will take affect from 2017, will likely have a dampening effect on the country's financial sector. Nevertheless, individual tax rates and low indirect labor costs will continue to make Luxembourg an attractive base for international companies.

In 2017, public investments are expected to increase by €100 million to €2.3 billion. The government continues to increase investment in housing, education and research, which are key drivers of modernization and infrastructure development.

Citation:
Assessment of the 2015 Stability Programme for Luxembourg. European Commission, 2015. ec.europa.eu/economy_finance/economic_governance/sgp/pdf/20_scps/2015/16_lu_scp_en.pdf. Accessed 21 Feb. 2017.

Beffort, Bérengère. "Taking a critical look at the 2015 budget." Luxemburger Wort, 16 Oct. 2014, www.wort.lu/en/politics/finance-and-budget-commission-taking-a-critical-look-at-the-2015-budget-543f5981b9b39887080793a0. Accessed 21 Feb. 2017.

"De Budget 2016." Le gouvernement du Grand-Duché de Luxembourg, www.budget.public.lu/lu/budget2016/op-ee-bleck/bref-apercu/index.html. Accessed 21 Feb. 2017.

"De Budget 2017." Le gouvernement du Grand-Duché de Luxembourg, www.budget.public.lu/lu/index.html. Accessed 21 Feb. 2017.

"Europäische Union: Staatsverschuldung in den Mitgliedsstaaten im 3. Quartal 2016." Statista, Jan. 2017, de.statista.com/statistik/daten/studie/198377/umfrage/staatsverschuldung-in-der-europaeischen-union/. Accessed 21 Feb. 2017.

"Labour costs per hour in national currency." Eurostat, ec.europa.eu/eurostat/statistics-explained/images/4/41/Labour_costs_per_hour_in_national_currency_for_non-euro_area_Member_States,_whole_economy_excluding_agriculture_and_public_administration_2008-2013.png. Accessed 21 Feb. 2017.

"Le budget 2017 placé sous le signe de la qualité, de la solidarité et de la compétitivité." Le portal de l'actualité gouvermentale, 12 Oct. 2016, www.gouvernement.lu/6374544/12-gramegna-budget. Accessed 21 Feb. 2017.

"Luxembourg." OECD Economic Outlook, Volume 2015 Issue 1, OECD Publishing, 2015, pp. 155 - 157, www.keepeek.com/Digital-Asset-Management/oecd/economics/oecd-economic-outlook-volume-2015-issue-1/luxembourg_eco_outlook-v2015-1-29-en#page1. Accessed 21 Feb. 2017.

National plan for smart, sustainable and inclusive growth - Luxembourg 2020. Le gouvernement du Grand-Duché de Luxembourg, 2016. www.gouvernement.lu/5978972/2016-pnr-luxembourg-en.pdf. Accessed 21 Feb. 2017.

"National Reform Programme." European Commission, ec.europa.eu/europe2020/europe-2020-in-your-country/luxembourg/national-reform-programme/index_en.htm. Accessed 21 Feb. 2017.

OECD Economic Surveys: Luxembourg 2015. OECD Publishing, 2015, www.keepeek.com/Digital-Asset-Management/oecd/economics/oecd-economic-surveys-luxembourg-2015_eco_surveys-lux-2015-en#page1. Accessed 21 Feb. 2017.

"Propriété intellectuelle." Le gouvernement du Grand-Duché de Luxembourg, www.luxembourg.public.lu/fr/investir/propriete-intellectuelle/index.html. Accessed 21 Feb. 2017.

"Présentation du compte général 2015 – une amélioration sensible par rapport aux prévisions." Le portal de l’actualité gouvermentale, 26 Sept. 2016, www.gouvernement.lu/6333510/26-compte-general. Accessed 21 Feb. 2017.

“Une exécution du budget 2014 rigoureusement conforme aux projections.” Le portal de l’actualité gouvermentale, 14 Sept. 2015, www.gouvernement.lu/5225643/14-finances-gramegna?context=3423005. Accessed 21 Feb. 2017.

Winkin, René. “Die öffentlichen Finanzen aus Sicht des CSDD.” Forum.lu, Mar. 2010, www.forum.lu/pdf/artikel/6751_294_Winkin.pdf. Accessed 21 Feb. 2017.

Netherlands

Score 9

Budgetary policy was sound prior to 2008. The economic crisis, however, has put severe pressures on the government budget. In 2012 the government came €0.10 short on every €1 of expenditure. The national balance switched from a surplus in 2008 to a deficit of 4.1% of GDP in 2012, 0.3% higher than expected. Between 2008 and 2014, the Dutch government followed neoliberal austerity policies to the letter, carrying out several series of tax increases followed by expenditure cutbacks. From 2015 to 2016, the Dutch budget deficit decreased from -2.2% to -1.5% of GDP. During the same period, government debt decreased slightly to 66.2% of GDP, well above the EU recommended ceiling of 60%, but better than the euro zone average debt. All in all, the sustainability of state finances has considerably improved over the last few years. Although state income from gas exploitation decreased even more, higher tax and premium income compensated for this loss. For the first time in years, no further austerity measures were announced in September 2014. In 2016, the government allocated €5 billion to reduce taxes on labor to reduce the difference between labor costs for an employer and net income for the employee. These measures proved controversial, as some political parties and experts advocate priority for debt relief over economic stimulation by tax relief. Austerity measures are expected to be reintroduced in 2017 after the elections.

Citation:
Miljoenennota 2016 (rijksoverheid.nl, accessed 1 November 2016)

B. Giesbergen and M. Wijffelaars, Nederlandse begroting: na het jubeljaar 2016 dreigen zure bezuinigingen in 2017, Me Iudice, 12 January 2016

R. Gradusand R. Beetsma, Bezuinigingen voor volgend kabinet zijn onontkoombaar, Me Iudice, 7 July 2016

D. Samsom (2012), Keuzes die de samenleving versterken, in Socialisme & Democratie, jrg. 69, nr. 12, pp. 8-12

New Zealand

Score 9

New Zealand’s budgetary policy is fiscally highly sustainable. However, the world financial crisis ended 14 years of budget surplus. The National government stated very early on that a return to high-debt levels would be imprudent, and made decisions designed to ensure that gross debt peaked below 40% of GDP in 2010, well below the OECD average. Since then, the government has maintained its course of fiscal consolidation. According to an OECD forecast, general government gross financial liabilities as a percentage of nominal GDP will rise from 41.9% in 2015 to 42.0% in 2016 and then decline to 41.8% in 2017. Although opposition parties were highly skeptical of the way it was achieved, the government posted a modest budget surplus of 275 million NZD in 2015, the first such surplus since 2008. This trend continued into 2016. The longer-term aim of bringing net debt down to 20% of GDP by 2020 appears to be more and more realistic. The government announced that it would only be willing to reassess this course if the economy were hit by a severe negative shock that might imply that sticking to the current fiscal strategy would harm the economy by forcing a sharp reduction in demand. The proposed sale of shares in targeted state-owned energy companies will help offset the government's spending commitments.

Citation:
Fiscal Strategy Report 2016 (http://www.treasury.govt.nz/budget/2016/) (accessed July 4, 2016).
Government at a Glance 2013 – Country Note: New Zealand (Paris: OECD 2013).

Norway

Score 9

The Norwegian government has received a large flow of financial resources from the extraction of petroleum since the 1980s. This income is projected to remain substantial until around at least 2040, and in the case of natural gas, probably longer. However, the price drop in oil and gas markets led to a significant reduction in state revenue in 2014 and 2015. Due to technological changes and climate change, there is also more uncertainty regarding the long-term viability of oil and gas-based revenues. Fears of stranded assets are growing as carbon pricing approaches and the complexity associated with offshore oil fields could render extraction costs ineffectve. However, extraction costs have dropped significantly in Norway and the country's fields are competitive by international standards.

Gas has now passed oil as the most important source of income, and the production of oil has been in decline during recent years. For some time, significant drops in petroleum revenue have been expected at least by 2025, requiring significant budgetary changes. The recent oil-price declines have necessitated earlier reforms. In many countries, the abundance of natural resources has given way to corruption and irresponsible fiscal policies. Norway has so far avoided this resource curse. One important achievement has been the establishment of the so-called Petroleum Fund, created in 1990 by the Norwegian parliament as a means to share oil proceeds between current and future generations, as well as to smooth out the effects of highly fluctuating oil prices. This is today designated as a pension fund. The fund is administered by Norges Bank Investment Management (NBIM), an arm of Norway's central bank, and invests exclusively in non-Norwegian assets. However, the future value of these investments has taken a severe hit in the last several years as a result of the combined effect of lower petroleum revenues, lower interest rates worldwide, and the developments of international markets.

Public finances remain sound, but are notably more strained than in 2015. As revenues are expected to decrease, adjusting welfare spending and economic diversification will grow increasingly important. It is expected that marine industries and sea food production will play an increasingly important role for Norway.

Sweden

Score 9

Since the mid-1990s, fiscal, and budgetary discipline has been extraordinarily strong in Sweden and its tight budgetary regime has begun to yield benefits. In the wake of a financial crisis in the early 1990s, maintaining sound fiscal policy has been an overarching policy goal for both center-right and Social Democratic governments. Sweden is one of very few countries that targets a budget surplus and neither government nor opposition harbor any plans to abolish it. In 2016, a revised budget surplus goal of 0.33 % was negotiated between the two major blocs in parliament. The agreement also includes a commitment to a long-term reduction of public debt. Thus, while the surplus goal is somewhat relaxed, there is now a stronger commitment to addressing public debt. Indeed, the past two budgets have reduced the budget deficit. Overall, these developments indicate a continuing bipartisan commitment to maintaining fiscal and budgetary discipline.

The budget surplus goal issue ultimately relates to the Keynesianism-monetarism controversy. The government wants to use the budget actively to drive the economy while the coalition of non-socialist parties in opposition (Alliance) take a somewhat more monetaristic approach. Either way, the fiscal and budgetary regulatory framework helps sustain a course of strong and sustained economic development. Not even the 2008 global economic crisis nor the euro crisis have profoundly disrupted Sweden’s economic growth.

Since the 2014 elections, the issue in this context has been to what degree the two main contenders for power in Sweden (i.e., the four non-socialist-parties that form the Alliance or the Social Democrats with support from the Greens) still unconditionally subscribe to the surplus goal and other aspects of the financial regulatory framework.

Citation:
Finanspolitiska Rådet. Swedish Fiscal Policy. Fiscal Policy Council Report 2016 (http://www.finanspolitiskaradet.se/download/18.3a8070ba157c4f032a872f5b/1476880513278/Swedish+Fiscal+Policy+2016.pdf).

Finanspolitiska Rådet. Swedish Fiscal Policy. Fiscal Policy Council Report 2015 (http://www.finanspolitiskaradet.se/download/18.16952a1814faf01fc6a35444/1442578
125524/Swedish+Fiscal+Policy+2015.pdff).

Mehrtens, Philip (2014), Staatsschulden und Staatstätigkeit. Zur Transformation der politischen Ökonolmie Schwedens (Frankfurt/New York: Campus).

Regeringen (2016), Överenskommelse om skuldankare, nytt överskottsmål och förstärkt uppföljning

(http://www.regeringen.se/4a7bfa/contentassets/24a388a9a9994e67a706e0b91768bdd2/overenskommelse-om-skuldankare-nytt-overskottsmal-och-forstarkt-uppfoljning.pdf).

Turkey

Score 9

Total general government expenditures as a share of GDP stood at 40.7% in 2015, while interest payments on public debt amounted to 2.8% of GDP. During the period under review, there were some changes in the composition of government expenditure, such as the share of current expenditures, investment expenditures and transfer expenditures in GDP and current expenditures at 4%. Current transfers increased slightly to 18.5% in 2015.

As of the end of 2015, gross public debt declined to 32.9% and the net-public-debt-to-GDP ratio experienced a minor increase to 26.6%. In sum, Turkey's fiscal policy has been sustainable.

Austria

Score 8

Most of Austria's decision-making elite agree on the need to reduce the country's budget deficit. However, given the robust nature of the Austrian economy, at least in the European context, and the broad consensus across the two governing parties regarding social policies, there is comparatively little incentive to limit expenses. The political parties are reluctant to confront their specific clienteles (farmers and public servants for the Austrian People's Party (ÖVP), and unionized workers and retirees for the Social Democratic Party of Austria (SPÖ)) with policies that might undermine their particular interests.

In the past, Austrian budgetary policies have followed a biased Keynesian approach: In times of low growth, the government has engaged in extra spending regarded as investment in the improvement of growth. In times of high growth, however, available funds have not been used effectively to prepare the government for worse times. Nonetheless, in 2016, the government was able to pass a budget with only a very small structural deficit.

Austria recently enacted a new Federal Medium-Term Expenditure Framework Act (BFRG), which enables the government to plan the budget over the medium term. The BFRG prescribes binding ceilings on expenditures for four years in advance, on the basis of five categories that correspond to the main functions of the federal government. This multi-year approach should help improve the sustainability of the federal budget.

As hopes of future significant economic growth have grown increasingly out of reach, the contradicting interpretations of Keynesian policies have become sharper within the government: The SPÖ prefers using the deficit as an instrument to boost economic growth; the ÖVP argues that in the long run, deficit spending will result in disaster. But the gap between the main actors is still not dramatic.

Bulgaria

Score 8

Bulgaria has featured sound budgetary policy for most of the last 20 years. After the country's fiscal stance temporarily deteriorated in 2013 and 2014, though budgetary discipline was restored again in 2015-16. The Ministry of Finance achieved its targeted balanced budget in 2016 and stabilized the debt-to-GDP ratio, which had increased by about 10 percentage points in 2013-14, though it remained at a relatively low level of about 25%. Various fiscal rules, including the target of a medium-term balanced budget, a ceiling for public spending ceiling set at 40% of GDP and a public debt ceiling of 60% of GDP, have helped make budgetary policy sustainable. Adherence to these rules is observed by an independent fiscal council. The council, in operation since 2016, has already published a number of opinions and recommendations, including a review of the Bulgarian Convergence Program for 2016-2019 and of the 2017 draft budget.

Citation:
European Commission (2017): Country Report Bulgaria 2017 including an In-Depth Review on the prevention and correction of macroeconomic imbalances. SWD(2017) 68 final/3, Brussels (https://ec.europa.eu/info/sites/info/files/2017-european-semester-country-report-bulgaria-en_3.pdf), 20-21.

Canada

Score 8

Canada's government is in a relatively strong fiscal position. Private-sector employment is today above its pre-recession peak, indicating that the economy has recovered from the 2008 recession, although the Canadian labor market is not as strong as it appears by some metrics. Canada's budget deficit as a proportion of GDP is low by international standards, as is its public debt/GDP ratio. The fiscal situation is somewhat weaker in certain provinces, particularly Ontario, but budgetary balances are moving in the right direction.

The previous federal government had made balancing the budget a priority. In the October 2015 federal election, the Liberal Party of Canada won a majority, ending 10 years of Conservative rule. One of the campaign pledges of its leader Justin Trudeau, prime minister since 5 November 2015, was to keep spending in check with "a modest short-term deficit" of less than CAD 10 billion for each of the first three years and then a balanced budget by the 2019-2020 fiscal year. The 2016 federal budget outlined five consecutive years of deficits totaling more than CAD 113 billion, with a CAD 29.4 billion deficit in the 2016-2017 fiscal year, decreasing to CAD 14.3 billion in 2020-2021. However, in the 2016 Fiscal Sustainability Report from the Parliamentary Budget Office, federal net debt is on a sustainable path and on the current policy path, it will be eliminated in 50 years.

Rising health care costs associated with the aging of the population represent a potential challenge to long-run fiscal sustainability. The 2016 Fiscal Sustainability Report from the Parliamentary Budget Office suggests that while health care spending growth has slowed, subnational governments, which are responsible for the lion's share of spending, cannot meet the challenges of population aging under the current policy. A recent study by the Centre for the Study of Living Standards (Drummond and Capeluck, 2015) reached a similar conclusion.

Citation:
Parliamentary Budget Officer, Fiscal Sustainability Report 2016, posted at http://www.pbo-dpb.gc.ca/web/default/files/Documents/Reports/2016/FSR_2016/FSR_2016_EN.pdf

Don Drummond and Evan Capeluck (2015) "Long-term Fiscal and Economic Projections for Canada and the Provinces and Territories, 2014-2038," CSLs Research Report 2015-08. http://www.csls.ca/reports/csls2015-08.pdf

Finland

Score 8

The government agenda of the current Sipilä government builds on its predecessors' initiatives, structural policy programs and public-finance adjustment policies. Consequently, the government's economic policy program aims at strengthening the economy's growth potential, raising the employment rate, bolstering household spending power and improving international competitiveness. Accordingly, the government is committed to an active fiscal policy that supports economic growth and employment, aims at a reduction of the central government's debt-to-GDP ratio, and tries to strike a balance between long-run fiscal sustainability and the short-term need to support domestic demand. However, the unfavorable economic environment has impeded the government's goals and ambitions. The debt crisis in Europe has slowed economic growth, and the government's initial ambition to halt the growth in public debt by 2015 was not fulfilled. The Ministry of Finance's budget proposal for 2017 draws on the decisions made in the general government fiscal plan of April 2016. According to estimates, there has been no significant improvement in the economic situation. The 2017 draft budget total of €55.2 billion exceeds the 2016 budget by €0.8 billion. The European Commission's 2016 Stability Programme for Finland points to a risk of some deviation from adjustments targeting the medium-term objective of structural balance. The Commission's spring 2016 forecasts confirmed these fears, which implies a significant risk of deviation in the future.

Citation:
European Commission, "Assessment of the 2016 Stability Programme for Finland", http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/20_scps/2016/26_fi_scp_en.pdf

Germany

Score 8

For Germany, the 2009 global recession and its aftermath implied higher budget deficits and gross public debt following revenue shortfalls, anti-crisis spending packages, and bank bailout costs. Since then, however, Germany's budgetary outlook has considerably improved. Germany's debt-to-GDP ratio has continued to decrease from 74.6% in 2014 to 71.0% in 2016 (Global Competitiveness Report 2016). This decrease resulted from surpluses in the general government balances since 2014, stable growth and historically low government bond interest rates. In addition to this favorable environment, a constitutional debt limit was introduced (Schuldenbremse) that restricts the federal government's cyclically adjusted budget deficit to a maximum of 0.35% of GDP and requires German states to maintain balanced cyclically adjusted budgets from the year 2020 onwards.

Given the financial burdens associated with the refugee crisis, this positive development is even more astonishing. For 2016 and 2017, the German Council of Economic Experts estimates total expenses directly associated with refugees and asylum seekers to be €10 to €13 billion, roughly 0.3% to 0.4% of GDP (Sachverständigenrat 2016: 343). The Ministry of Finance stated that it would cover the cost of these additional funds through increasing tax revenue, the sale of mobile phone licenses and decreasing interest amortization spending.

While the federal budget remains balanced, uncertainties concerning the medium- to long-term budgetary outlook have increased. Germany's aging population will mean that recent increases to welfare spending (e.g., increased pension payments for mothers and allowances for nursing care) combined with very dynamic increases in healthcare expenditures will pose a significant challenge to future federal budgets. According to recent calculations of "implicit debt" (i.e., future liabilities resulting from uncovered payment promises by the social security system and other government programs), the sustainability gap has increased (Stiftung Marktwirtschaft 2016). In this context, the very large increase in refugees claiming asylum in Germany in 2015 introduces an additional risk factor to future federal solvency. While long-term budgetary consequences are highly uncertain, the fiscal consequences will crucially depend on how well immigrants integrate into the labor market.

Citation:
Global Competitiveness Report 2016-2017: World Economic Forum

Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung (2016): Zeit für Reformen, Jahresgutachten 16/17, Sachverständigenrat: Wiesbaden. Online: http://www.sachverstaendigenrat-wirtschaft.de/jahresgutachten-2016-2017.html

Stiftung Marktwirtschaft (2016): EU-Nachhaltigkeitsranking 2016, Wenig Fortschritte in Europa, Konsolidierungsbedarf bleibt bestehen, Pressemitteilung 16. November 2016.

Czech Republic

Score 7

Improved economic performance has enabled the Czech government to retain its objective of reducing the central government budget deficit and thereby limit the growth in public debt while allowing some expansion of domestic demand. For the first time since 1994, and despite original plans for a deficit, the Czech Republic ran a fiscal surplus thanks to higher than planned revenues and EU funding, and lower government spending, especially on infrastructure projects. The government's attempt to push through parliament a constitutional law on fiscal responsibility was unsuccessful. The law, which envisaged the introduction of debt limits for all tiers of government, the adoption of a central government expenditure ceiling and the creation of an independent National Budgetary Council, did not gain enough support even among the deputies from the governing coalition. In 2016, public debt stood at about 40% of GDP, thus being lower than in most EU countries and clearly below the debt limits of 55% and 60% defined in the fiscal responsibility law.

Ireland

Score 7

Progress toward correcting budget imbalances has continued to outpace projections. The general government deficit fell to 0.9% of GDP in 2016 and is forecasted to fall to 0.4% in 2017.
The most recent data show that the national debt-to-GDP ratio, which peaked at 120% in 2013, fell to 76% of GDP in 2016. Moreover, this projection does not account for the sale of the government's stake in those banks taken into state ownership during the crisis.

Ireland's fiscal situation is now sustainable. Experience over the past four years has confounded the view that Ireland could not return to sustainable economic growth while undertaking a regime of fiscal austerity. The country's adjustment should be regarded as an example of successful "expansionary austerity."

Leaving aside the ever-present possibility of adverse external shocks, the main risk now facing the Irish economy is that the government, following record tax returns, will encounter increasing demands from public sector trade unions to increase public sector expenditure and in particular public sector remuneration.

Citation:
For projections of Ireland's national debt see:
http://www.ntma.ie/business-areas/funding-and-debt-management/debt-profile/debt-projections/

Israel

Score 7

After the economic crises of the mid-1980s, key steps were taken to reduce Israel's budgetary deficit and to build a set of objectives and guidelines enabling sustainable budgetary planning. Strict budgetary-discipline laws were enacted: The Budget Foundations Law set scrupulous spending procedure regulations and implemented deficit-reporting requirements, and another law prohibited the central bank from providing loans to the government, ensuring that future deficits would be financed by borrowing from the public and abroad rather than through direct monetary injections. Consequently, fiscal power was centralized, giving the Ministry of Finance's budget department the power to impose a policy of budgetary discipline.

Two crucial additional tools, the Arrangements Law (Hok Ha-Hesderim) and the Budget Deficit Reduction Law, redefined the financial and economic structure of the Israeli government. The Arrangements Law is an omnibus law passed together with each budget, consisting of numerous restrictions and amendments designed to secure the state's financial goals. In the last few years, the budget was converted to a biennial budget plan, which many regard has having a positive influence on planning capabilities.

This history of successful budgetary reform continues to contribute to the stabilization of the Israeli economy. Along with a prudent monetary policy, these measures helped the country weather the recent global economic crisis relatively successfully. The central government deficit came in at 2.1% of GDP and is well below the 2.9% target. Despite expansion of public spending in recent years and a rising deficit, it seems that the Israeli budget is still managed to insure fiscal stability.

Citation:
http://www.imf.org/en/News/Articles/2017/02/08/mcs02082017-Israel-Staff-Concluding-Statement-Of-The-2017-Article-IV-Mission.

Italy

Score 7

Italian governments have struggled to continue the budget consolidation process begun by the Monti government during an era of prolonged economic stagnation. Fiscal policies have gradually reduced yearly deficits and produced a strong primary surplus. Yet because of the recession environment, attempts to reduce the huge debt stock (by selling, for example, public properties or stocks of state-owned companies) have had little success or have been postponed. The improved climate on the international markets and ECB policies have yielded a sharp decline in interest rates for Italian long-term treasury bonds. This has eased the country's budgetary pressures. Toward the end of 2014, the recession ended and modest economic growth returned in 2015 and 2016, which has slowed the growth in public debt. However, the government's promise that the ratio of public debt to GDP would start declining in 2016 will have to be postponed to 2017.

Fiscal policies for 2016 have followed more or less those of 2015 and benefited from the slightly improved economic conditions. The fiscal consolidation, required by EU rules, has been modest, as the government has taken advantage of the greater flexibility allowed by the European Union for countries introducing significant structural reforms to promote economic growth. Tax reductions and incentives for entrepreneurial activities have only partially been offset by reductions in public expenditure. In general, cuts to public expenditure, proposed by the government's spending review, have been implemented more slowly than announced. This has been due to resistance from interest groups, but also because of a fear that such cuts would have recessionary effects.

Furthermore, the pace of privatization of public assets has been slower than anticipated, though the Italian post service (Poste Italiane) has been partially put on the market. The complete privatization of Poste Italiane and the Italian railways has been postponed because of unfavorable stock market prices.

The vast majority of regional and municipal budgets are fiscal sustainable, though not all.

Citation:
http://www.mef.gov.it/inevidenza/DEF_2016/intro.html
http://www.dt.tesoro.it/export/sites/sitodt/modules/documenti_it/analisi_progammazione/documenti_programmatici/Rapporto_evasione.pdf
http://ec.europa.eu/economy_finance/eu/forecasts/2016_spring/it_en.pdf

Lithuania

Score 7

During the financial crisis, Lithuania's fiscal situation deteriorated rapidly. The fiscal deficit grew to 3.3% of GDP in 2008, and to 9.4% of GDP in 2009. As a result of fiscal consolidation, the deficit dropped to 7.2% in 2010 and again to 5.5% in 2011. It was expected to continue falling to 3.2% in 2012. In 2014, the European Council adopted a decision allowing Lithuania to join the euro area as of 1 January 2015, in part recognizing its work in regaining control of the deficit. However, despite relatively high rates of economic growth and substantially reducing the budget deficit, the 2012 to 2016 government repeatedly failed to balance the budget as planned. Government debt also expanded during the crisis, reaching 38.5% of GDP in 2011 (from the pre-crisis low of 16% in 2008); this is expected to stabilize at around 40% of GDP over the coming years.

Despite these improvements in Lithuania's fiscal performance since the crisis, the country faces a number of challenges in terms of keeping its public finances sustainable. Factors such as projected expenditure related to an aging population, relatively high migration rates, and the vulnerability of its small and open economy to external shocks pose significant risks to the consolidation path projected by the government in its convergence program. The goal of introducing the euro in 2015 preserved the government’s determination to maintain the deficit at a level below 3% of GDP, while the fiscal-discipline law should provide an incentive to continue reducing the deficit even as the economy keeps growing. Although spending pressures are increasing, it has been difficult to increase total tax revenues (29.4% of GDP in 2015), in part due to geopolitical tensions, the impact of Russia’s import ban on the Lithuanian economy, and the ongoing stagnation in the euro-zone economy, which is the main export market for Lithuanian businesses. Moreover, in their opinions on the draft 2015 budget, the National Audit Office and the Central Bank of Lithuania stated that the draft violated the law on fiscal discipline by increasing expenditures too far. In autumn 2014, the government decided to postpone its convergence-program targets for achieving a budget surplus by an additional year, to 2017 (the year after the 2016 parliamentary elections). This increases the risk that even if the budget deficit remains below the 3% of GDP required under euro-zone rules, it might not be reduced further according to the strictures of the fiscal compact, and the structural deficit rule might not be observed. The 2016 budget to some extent confirmed those concerns, as no major effort had been made to further reduce the budget deficit. Instead, the government took advantage of economic growth and the recent improvement in tax revenues due primarily to an increase in domestic consumption. Geopolitical concerns prompted a major increase in defense expenditures, and some increase of social expenditures was also included. This leaves the job of balancing the budget to the next government, which was formed after the October 2016 parliamentary elections. The newly formed coalition government of the Lithuanian Farmers and Greens Union and Social Democratic Party of Lithuania postponed this objective until 2018.

Citation:
COMMISSION STAFF WORKING DOCUMENT, country report Lithuania 2016: http://ec.europa.eu/europe2020/pdf/csr2016/cr2016_lithuania_en.pdf

Slovakia

Score 7

Slovakia managed to reduce its fiscal deficit from 8% in 2009 to 3% in 2015 and about 2.2% in 2016. As spending was higher than budgeted, the lowering of the deficit in 2016 was largely due to buoyant tax revenues on the back of strong economic growth and favorable labor market developments. For 2017, a further reduction of the deficit, this time largely achieved by tax increases, is projected. In order to accommodate new spending priorities, however, the third Fico government postponed the original deadline for meeting the medium-term objective from 2017 to 2019. The planned public-private partnership project to build a motorway ring around Bratislava has been associated with substantial medium-term fiscal risks.

Citation:
European Commission (2017): Country Report Slovakia 2017. SWD(2017) 90 final/2, Brussels, 15-16 (https://ec.europa.eu/info/sites/info/files/2017-european-semester-country-repor t-slovakia-en_0.pdf).

South Korea

Score 7

South Korea's national budgetary policies remain sound. South Korea continues to have one of the lowest levels of public debt and public expenditure among OECD countries, despite an increase in fiscal debt under the Lee Myung-bak and Park Geun-hye administrations. The ratio of public debt to GDP in 2014 was a relatively low 36%, but gradually increased to 40.1% in 2016. Previously known for extremely conservative fiscal policies, the Korean government has been much more pragmatic since the world economic crisis of 2008/09, when South Korea implemented some of the largest fiscal-stimulus packages in the OECD. Moreover, low overall government expenditure and tax rates leave considerable room for the government to take a more active role, for example by increasing spending for social security and education, both critical areas in addressing the problem of an aging society.

At the local level, budgetary problems have become more common due to the prevalence of prestige construction projects lacking substantial economic benefits. As local-government debt levels increased, the Park Geun-hye administration proposed the introduction of a bankruptcy system for debt-ridden local governments, which would hold them responsible for fiscal deficits and force them to cut their debt. Moreover, local governments such as Seongnam City and Seoul City have recently discretionally expanded their welfare budgets to include youth residing in the cities by providing so-called youth dividends or benefits. In 2015, Seongnam City was the first to adopt a policy of subsidizing young adults' living expenses and job-training fees in the form of gift certificates usable in Seongnam. In 2016, the Seoul Metropolitan Government started providing monthly activity subsidies of $440 in cash to youth selected through applications. The central government and the ruling party have consistently opposed both welfare programs, asserting that they were a waste of tax money and were politically motivated. The central government revised the Local Subsidy Act to slash the budget for Seongnam City in December 2015, seeking to put the brakes on the municipality's welfare programs. Seoul's subsidy program was later suspended, though the city has filed a lawsuit with the Supreme Court seeking to reverse the Welfare Ministry's decision to stop the program.

Citation:
OECD 2010, Preparing fiscal consolidation, Paris, http://www.oecd.org/document/23/0,3343,en_2649_34595_44829143_1_1_1_1, 00.html
OECD, OECD Economic Outlook No. 95, May 2014
"In financial pinch, Incheon under pressure to downscale Asiad plan," The Korea Times, April 4, 2012
Klitz, Walter, "Korea kaempft mit dem Defizit," Naumann Stiftung Seoul, http://www.freiheit.org/files/62/N_8_Korea_kaempft_mit_dem_Defizit.pdf
"South Korea Plans Record 2015 Budget as Spending Jumps," Bloomberg, Sep 18, 2014
"Time bomb ticking on local government debt," The Korea Times, March 31, 2014
"Seongnam at forefront of expanding welfare," The Korea Herald, February 4, 2016
"Seoul government to provide 500,000 won per month to young jobseekers," The Hankyoreh, April 12, 2016

United Kingdom

Score 7

The United Kingdom is a highly centralized state. As such, central government has considerable control over budgetary policy. Most public spending is directly or indirectly controlled by the central government, with few other influences compared to, for example, federal countries. This also means, however, that the central government has to shoulder the blame if things go wrong.

Under the previous Labour governments, the "golden rule" of UK fiscal policy was to limit deficit spending to investment over the business cycle. However, public spending as a proportion of GDP increased during the 2000s and, in hindsight, was too pro-cyclical. In 2009, adherence to fiscal rules was abandoned to cope with the consequences of the crisis. There is now a fiscal council, the Office for Budget Responsibility, and fiscal rules, including provision for surpluses in "good times," are being entrenched in a new Charter for Budget Responsibility.

Due to uncertainty about the economic consequences of leaving the European Union ("Brexit"), the government has postponed its goal of achieving a budget surplus by the fiscal year 2019 to 2020. Instead, a small increase in government debt is now forecast for the next two years before coming down again. While the public budget deficit has fallen from 10.2% of GDP in 2009 to 2010 - the postwar peak - to 3.4 % of GDP in the fiscal year of 2015 to 2016. According to the latest European Commission forecasts, it remains the highest in the EU after Croatia, Greece and Spain in nominal terms, and the highest in cyclically adjusted terms. Nevertheless, low interest rates and the extensive purchases of public debt by the Bank of England through its quantitative easing program has saved the UK from paying a high price for the period of high debt, with debt service payments only marginally higher than during the 2000s. Among the economies of the larger EU countries, public debt in the UK is now a little below that of France and Spain, and well below that of Italy. Yet, it is projected to be 20 percentage points above Germany's in 2016. Assuming that interest rates (at a record low 0.25% since 15 July 2016) remain low and the government sticks to its budgetary plans, the UK's fiscal policy is financially sustainable.

Citation:
European Commission Spring Forecasts 2016 (ec.europa.eu/economy_finance/eu/countries/uk_en.htm)
HM Treasury Autumn Statement 2016 (https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/571559/autumn_statement_2016_web.pdf)

Belgium

Score 6

Belgium was hit by several successive shocks in 2015 and 2016. The refugee crisis produced an unanticipated increase in spending that will continue in the medium term (successful integration of the migrants into the labor force should eventually compensate for this and prove a net benefit). Then, in March 2016 Brussels was hit by a terrorist attack. These events have significantly increased government spending.

In parallel, the government has introduced tax cuts that have reduced government income. As a result, the government deficit increased in 2016 in spite of a drop in interest rates. Cutting the structural deficit will require additional effort.

Notwithstanding, forecasts continue to point to Belgium's public debt peaking in 2016. However, it is projected to only shrink marginally over the next 5 years: from 107% of GDP in 2016 to 105% of GDP in 2021. One ticking time bomb continues to be the implicit pension debt related to entitlements that will be owed to current workers in 10 to 20 years.

Citation:
Macro imbalance procedure:
https://www.nbb.be/doc/dq/mip/en/mip_2015.pdf
http://ec.europa.eu/eurostat/documents/16624/0/SA-2016_ammend
http://www.plan.be/indicators/indicator-fr-t-mip-macroeconomic+imbalance+procedure+alert+mechanism+scoreboard
http://www.plan.be/admin/uploaded/201610111111110.FOR_SHORTTERM16_11332_F.pdf

Public finance sustainability: http://www.plan.be/admin/uploaded/201603311238220.Rapport_mars2016_FR.pdf

Croatia

Score 6

Croatia joined the European Union in July 2013 and almost immediately was placed under the EU's excessive deficit procedure. In March 2016, Moody's downgraded Croatia's issuer and bond ratings to Ba2 with a negative outlook, expressing doubts about the reform capacity of the Orešković government. At the height of the coalition crisis in June 2016, the government failed to issue government bonds. Eventually, however, the general government budget deficit was reduced: 2.1% in 2016, down from 3.3% in 2015 and far below the recent peak of 7.8% in 2011. The deficit reduction was largely achieved through windfall revenues stemming from stronger-than-expected economic growth. The Orešković government refrained from wage and pension cuts recommended by a number of prominent Croatian economists, instead allowing for a minor expenditure increase (in nominal terms) in the 2016 budget. The ratio of government debt remains high: 85% of GDP in 2016, a slight improvement over the 86.7% observed in 2015. Reduction in the debt is expected to continue this year and next as growth picks up. However, if the proposed tax reforms are implemented this may weigh on the revenue side of the budget, while public sector wage negotiations may yield pressures on the expenditure side. Overall, fiscal sustainability appears to be improving, though at a slow pace and significant risks remain on the horizon.

Citation:
European Commission (2017): Country report Croatia 2017 Including an In-Depth Review of the prevention and correction of macroeconomic imbalances. SWD(2017) 76final, Brussels, 19-21 (https://ec.europa.eu/info/sites/info/files/2017-european-semester-country-report-croatia-en.pdf).

Cyprus

Score 6

Budgets after 2014 have to conform with the provisions of the Law on Fiscal Responsibility and Fiscal Framework, which require basic planning within strategic targets set by the government under close scrutiny by the finance minister. Implemented gradually, this is expected to achieve strategic planning capacity and control and oversight from budget design to implementation in order to avoid past problems that nearly led to economic collapse. In fact, a positive balance of payments in 2008 with a significant volume of reserves was succeeded by structural economic imbalances that affected budgetary stability. Steadily rising expenditures continued even when state income was in decline due to decreasing tax revenue, the shrinking tourism industry and other developments, such as unpaid or uncollected taxes exceeding €1 billion in 2012. Expenditure increases were sustained by inflated public-service salaries and rising social outlays associated with higher unemployment rates, severance payments and other costs.

The above problems, combined with banks' losses linked to Greek debt, resulted in the exclusion of Cyprus from the markets and the need for ESM support. The country's obligations in the MoU required fiscal and budgetary reforms reflected in recent budgets design.

The 2016 budget focused on deficit and public-debt reduction, while salary and benefit reductions in the public sector were sustained. Tax policies, along with a restructuring of public subsidies and other public expenses since 2013 bear results: deficits and the debt-to-GDP ratio have performed better than projected since 2014.

The GDP was expected to grow by 2.5% in 2016 (IMF) compared to 1.7% in 2015, with government estimates at 3%. The debt-to-GDP ratio improved to 106.7% in 2016 (down from 108.9% in 2015), and was expected to further recede in 2016, according to the IMF. A positive primary fiscal balance is projected for both 2016 (2.8%) and 2017 (2.2%).

Citation:
1. IMF expects Cypriot public debt grow slower, Cyprus Mail, press report, 5.10.2016, http://cyprusbusinessmail.com/?p=33559
2. IMF World Economic Outlook, Subdued demand - Symptoms and Remedies, October 2016, https://www.imf.org/external/pubs/ft/weo/2016/02/pdf/text.pdf
3. Georgiades sees expects 3 per cent growth this year, Cyprus Mail, press report, 17.10.2016, http://cyprusbusinessmail.com/?p=34160

Iceland

Score 6

The 2008 economic collapse dramatically increased the country's foreign debt burden. General government gross debt rose from 29% of GDP at the end of 2006 to 95% in 2011. Thereafter, it decreased gradually to 55% at the end of 2016, and is projected to decline further to 30% in 2021 (IMF, 2016). The government's net foreign debt – the government's foreign debt minus its foreign assets – rose from 18% of GDP at the end of 2007 to a peak of 66% in 2010, then fell to 46% in 2016 and is projected to decline further to 23% by 2012 (IMF, 2016). Reflecting a reduction in debts which stems in part from a stronger króna, interest payments on the public debt have declined from 4.5% of GDP in recent years to 3.5% in 2016. There is, however, a significant possibility that excessive wage increases will boost inflation as the Central Banks forecasts and weaken the currency. This, in turn, would cause an increase in the foreign debt burden again, other things being equal. Still, Iceland's foreign debt burden would remain sustainable. However, fiscal sustainability remains a serious concern for the government given the dire financial situation of several key public institutions, including the State University Hospital and the State Broadcasting Corporation (RÚV) among others. Fiscal balance is not on a firm foundation when vital public institutions and infrastructure continue to suffer from long-standing financial neglect.

Another factor that increases the complexity of Iceland's fiscal situation is uncertainty concerning the availability of foreign exchange. During 2016, foreign entities, owning considerable funds locked up in Iceland due to capital controls in place since 2008, were allowed to transfer these funds out of Iceland through a special arrangement with the government. Before, if the government had removed these capital controls, it would have led to a shortage of foreign exchange and, consequently, a significant depreciation of the Icelandic króna. The government was keen to avoid such a situation. From 2013 onward, several government announcements promised to lift these capital controls. However, it was not until mid-2015 that the first credible steps were taken toward relaxing these controls. Furthermore, the decision to relax the capital controls under strict conditions was based on agreements between the steering committees representing creditors and the respective government task forces. The fiscal implications of these agreements remain to be seen.

Citation:
IMF, October 2012 World Economic Outlook.
IMF (2014), Country Report No. 14/19, Iceland Staff report, http://www.imf.org/external/pubs/ft/scr/2014/cr14194.pdf.
IMF (2016), Iceland: Staff Report for the 2016 Article IV Cconsultation, June, https://www.imf.org/external/pubs/ft/scr/2016/cr16179.pdf, accessed 12 January 2017.

Malta

Score 6

Developments since 2013 have demonstrated that fiscal policy is now expected to meet most standards of sustainability. In 2014 the deficit fell to 2.0% of GDP, to 1.5% of GDP in 2015 and is estimated to fall to 0.7% of GDP in 2016 and 0.6% of GDP in 2017. In June 2015, Malta was no longer subject to the EU's Excessive Deficit Procedure and was placed under the preventive arm of the Stability and Growth Pact. The November 2016 EU Commission report stressed that both revenue and expenditure have been revised upwards for 2017 and should contribute to a deficit reduction in 2016 and 2017. Government gross debt ration is expected to decrease to 61.9% of GDP by 2017. However, the EU's recommendation on the 2016 Maltese National Reform Program and Stability Program continues to stress that age-related expenditure and health care costs could pose a threat to the long-term sustainability of public finances. The introduction of legislation to enhance the transparency of government finances also represents a step forward. The Malta Fiscal Advisory Council advised the government to introduce an appropriate framework for the monitoring and issuing of government guarantees. The 2016 European Commission Staff Working Document on Malta's Country Specific Recommendations also notes the fact that public expenditure as a share of GDP was below the euro-area average. Nonetheless, the document noted that higher average wages and higher employment rates (particularly in the education and health sectors) led to an increase of 6.1% in compensation during the period 2012-2014. Measures to improve pension income and the sustainability of the health sector may ameliorate the situation but are not considered adequate as yet. This is coupled with the fact that the average subsidy rate increased by an average of more than 28% as a result of increasing subsidies to the energy and public transport sectors. State-owned enterprises, namely Enemalta and Air Malta, were also regarded as a source of concern that pose a significant risk to the government's deficit target. It was also noted that Malta had not made progress with the structural part of the fiscal recommendations issued by the Council in 2016.

Citation:
The Politics of Public Expenditure in Malta in Journal of Commonwealth & Comparative Politics, Vol. 46, No. 1, February, 2008, Routledge, U.K. Maurice Mullard, University of Hull & Godfrey Pirotta.
European Economic Forecast Spring 2016 p.100, p.101
European Commission Recommendation for a COUNCIL RECOMMENDATION on the 2016 national reform programme of Malta and delivering a Council opinion on the 2016 stability programme of Malta, SWD (2016) 86 final p. 4
Commission Staff Working Document Country Report Malta 2016 COM (2016) 338 final p. 15, p.17
Commission Opinion of 16/11/2016 on the Draft Budgetary Plan of Malta C(2016) 8013 final

Mexico

Score 6

Given the country's history of severe macroeconomic imbalances until the 1990s, fiscal stability has been a very strong policy priority for the past several administrations. Just as Germany would do anything to avoid a repetition of the hyperinflation of the 1920s, Mexico badly wants to avoid repetition of its debt crisis of 1982 or the "Tequila Crisis" of 1994. Southern Europe's recent financial difficulties have also been a cautionary tale to the President Peña Nieto government of the dangers of fiscal profligacy. Consensus among the major political actors is significant on this matter. In fact, all the major parties in Mexico support policies of fiscal stability. In 2008, Mexico accepted a domestic recession as the necessary price to pay for avoiding inflation.

However, Mexico’s fiscal stability continues to be under threat as a result of the collapse in global oil prices through 2014 and 2015. Although most oil production is consumed domestically, oil exports are a significant source of public revenue given the state-owned structure of Mexico’s oil industry. Consequently, there is a direct relationship between global oil prices and public revenue. In this environment of international constraints, the government continued to put high priority on fiscal stability in 2016, prioritizing budgetary discipline at the cost of domestic growth. Even so, increasing tax revenue in 2015 and 2016 allowed for a growth in public spending. Public borrowing requirements were reduced to 3% of GDP.

One key shortcoming of the current administration is the lack of consistency between planning and implementation. In 2015, the government announced a spending cut but actual spending increased 5% in real terms. There are few reasons to believe that spending cuts for the coming years will be implemented: according to Mexican researchers, public spending has increased more than 4% every year in real terms since 2012. Even when the goal has been to maintain a primary surplus at the beginning of the year, the trend is reversed by the end of the sane year. That is, spending surpasses revenues even before interest payments.

Government debt has increased more than 10% during the Peña Nieto administration. Moreover, not all debt is clearly accounted for: there are items classified as “non-oil revenues,” non-tax revenues, and “returns” (aprovechamientos), ambiguous categories that include worker pensions and PEMEX assets. These spending patterns along with growth deceleration have increased the value of sovereign debt as a share of GDP. Rating agencies lowered Mexico’s sovereign credit outlook from stable to negative in 2016, which will further increase the country’s interest payments. In 2017, Mexico will pay more toward debt interest payments than toward capital.

A second key shortcoming of Mexican budgetary policy is the opacity surrounding spending decisions. More than half of spending increases have gone to subsidies and transfers, surpassing the amount approved by Congress by more than 10%. Of this increase, around 40% was spent in programs without monitoring, audits or impact evaluations. This opacity allows for the political use of resources, which may partly explain state-level variations on per-capita spending that seem to be associated with changes in the party holding the executive office.

Citation:
http://mexicocomovamos.mx/new/md-multimedia/1476288726-748.pdf
http://www.cnbc.com/2016/08/23/sp-lowers-mexicos-sovereign-credit-outlook-to-negative.html
http://mexicoevalua.org/2016/11/15/las-dos-caras-de-tu-moneda/
http://mexicoevalua.org/2014/04/14/descifrando-la-caja-negra-del-gasto/

Poland

Score 6

Thanks to the combination of robust economic growth and restraint in spending, Poland successfully reduced its fiscal deficit from its 2010 level of 7.9% of GDP to less than 3% in 2015. This allowed Poland to exit the EU's excessive deficit procedure one year ahead of schedule. Ths PiS government has pursued a more expansionary fiscal policy. According to the minister for development and, since September 2016, finance, Mateusz Morawiecki, a stable budget is "not a holy cow.".While the fiscal deficit actually fell in 2016 because of one-off revenue from the sale of radio frequencies for mobile internet and a significant drop in public investment, increases in social spending and the uncertain implementation of the PiS government's tax plans, as well as increasing interest rates on government debt, will raise fiscal deficits. The modification of the official expenditure rule in December 2015, which created additional space for spending in the 2016 budget, has reduced the credibility of the country's fiscal framework. While the PiS government has announced it will improve medium-term budgetary planning, it has not addressed the lack of an independent fiscal council, so that Poland still is the only OECD country without such an institution.

Citation:
European Commission (2017): Country report Poland 2017. SWD(2017) 86 final, Brussels, 9, 19 (https://ec.europa.eu/info/sites/info/files/2017-european-semester-country-report-poland-en.pdf)

Spain

Score 6

Despite 2016 being an interim year in Spanish politics, with a caretaker government in office after the December 2015 inconclusive elections, the budget for 2016 had been passed before the elections taking advantage of the previous absolute majority enjoyed by Prime Minister Rajoy's party. This has been the first year since his arrival to office in 2011 in which budgetary policy has somewhat softened the austerity measures. Nevertheless, despite four years of public spending cuts, neither the deficit (approximately 4.5% GDP at the end of 2016) nor public debt (99% of GDP) have been significantly reduced. Spain has the highest deficit in the European Union (France, with 3.4%, is the second), and its public-debt-to-GDP ratio is the seventh-highest in the EU (after Greece, Italy, Portugal, Ireland, Belgium and Cyprus). Thus, even if the fiscal restraint since 2011 has succeeded in reducing long-term public-sector borrowing costs, it would be premature to conclude that Spanish budgetary policy has realized the goal of fiscal sustainability. However, the spending cuts have been achieved with great effectiveness both by the central and regional governments (see "Task Funding"). This fiscal policy was implemented through a scheme introduced by the Organic Law 2/2012 on Budgetary Stability and Financial Sustainability of Public Administrations. The commitment to a balanced budget and the creation of the Independent Authority for Fiscal Responsibility (AIReF) in 2013 have allowed Spain to regain fiscal credibility abroad. By the end of 2016, Spain's risk premium had reached its lowest level since early 2010, and the Commission appeared likely to grant additional flexibility delaying achievement of the deficit objective of 3.0% of GDP until the end of 2017. In any case, financial stability today depends more on the ability to increase revenues than on new austerity measures. If economic growth consolidates, and the ECB continues its current expansionary monetary policy, the long-term sustainability of Spain's public finances will continue to improve.

Citation:
European Commission Economic Forecast Autumn 2016:
http://ec.europa.eu/economy_finance/eu/countries/spain_en.htm

Australia

Score 5

Australia's fiscal position continued to deteriorate during the review period. Corporate tax revenue has not recovered from the 2008 to 2009 economic downturn, resulting in eight successive budget deficits averaging over 2% of GDP and forecasts of continued deficits under unchanged policy settings. However, the government will introduce a diverted profits tax, which will increase the tax rate to 40% on profits offshored by multinational corporations. Considering the widespread criticism of tax avoidance by large companies, the government is attempting to maintain popular support for an open economic system.

With net federal government debt standing at approximately 19% of GDP at the time of the review period, the fiscal position is still relatively healthy, but the consensus is that Australia has a "structural deficit." This means that, averaged over the business cycle, existing revenue streams will not adequately meet ongoing expenditure needs given current tax rates and expenditure levels. The reasoning is that commodity prices will not return to pre-2008 levels, and expenditure demands are projected to increase over coming years, in part because of population aging. Today, Australia's high primary deficit requires substantial adjustment, but political factors have made reform very difficult. Treasurer Scott Morrison has adopted a moderate approach to reducing public spending. Severe spending cuts would have resulted in a further deterioration of economic prospects, primarily because of poor national infrastructure.

Citation:
Australian Government Treasury historical budget and net worth data: http://www.budget.gov.au/2016-17/content/bp1/html/bp1_bs10-03.htm

http://www.abc.net.au/news/2016-05-03/budget-2016-winners-losers/7338448

http://infrastructureaustralia.gov.au/policy-publications/publications/files/Australian-Infrastructure-Audit-Executive-Summary.pdf.

Greece

Score 5

After achieving fiscal consolidation in 2013 and 2014, the state finances of Greece were put at risk in 2015 owing to economic uncertainty related to government turnover in January 2015. Fiscal problems grew as state funds were depleted in the course of protracted negotiations (February-August 2015) between Greece and representatives of the EC and the ECB regarding the last tranche of the loan extended to Greece through the second economic adjustment program (2012). The aforementioned strain on public finances also grew as a result of the sudden referendum called by the Syriza-ANEL government in July 2015 on the EC's reform proposals. Further, the imposition of capital controls, just after the referendum was called, did not contribute to streamlining the budget implementation or the timely collection of tax revenues.

In 2015, the Syriza-ANEL government was consumed in negotiations with the country's creditors and essentially only started collecting direct taxes in August. In 2015-2016, the government was late in paying private suppliers for some goods and services, which resulted in the near collapse of some private businesses.
The new draft budget, announced by the Ministry of Finance in early October 2016, forecasts robust growth for 2017 (2.7%). The budget adds more than 1 billion euros in mostly indirect taxes on items from phone calls to alcohol. It also cuts spending by over 1 billion euros. It predicts a primary budget surplus of 0.6% of GDP at the end of 2016, rising to 1.8% of GDP at the end of 2017, and to 3.5% at the end of 2018. Clearly the growth rate predicted is not attainable: the parliament's own budget office has said that the combination of extra taxes and spending cuts will "in the short term" have "a recessionary effect." International organizations seem to agree that the growth rate will probably be closer to 0.6%.

The government insisted that it achieved a 2016 primary surplus of more than double the original forecast, excluding debt servicing, and defended its decision to give an extra €617 million to some 1.6 million low-income pensioners. This announcement took Greece's creditors by surprise.

In other words, the new government, elected in 2015, eventually followed throughout 2015-2016 the road of its predecessors, as far as budgetary policy and fiscal sustainability are concerned.

Citation:
Information on the Greek state budget is drawn on the official site of Greece's Ministry of Finance, available at http://www.minfin.gr

Hungary

Score 5

After exiting the European Commission's excessive deficit procedure in June 2013, Hungary has managed to keep the fiscal deficit below 3%. The Orbán government has been keen on escaping the strict fiscal EU oversight. However, fiscal adjustment has been accomplished by ad hoc measures rather than by structural reforms, so that its sustainability is questionable. In 2016, budgetary policy started to loosen. Given the tax cuts and expenditure increases adopted in 2016, the deficit will further increase in 2017, thereby slowing the decline in Hungary's still relatively high debt-to-GDP ratio. Hungary's fiscal framework has suffered from a lack of credibility. Contrary to legal requirements, the government largely ignored the official medium-term fiscal framework when drawing up the 2017 budget. The Fiscal Council, with its uniquely strong constitutional power, has neglected its watchdog role. In October 2016, Eurostat expressed worries about the official Hungarian data on the public debt, since some expenditures, e.g. those of state-owned Eximbank, were not included.

Citation:
European Commission (2017): Country Report Hungary 2017. SWD(2017) 82 final/2, Brussels, 6, 16-17 (http://ec.europa.eu/info/sites/info/files/2017-european-semester-country-report -hungary-en_1.pdf).

Portugal

Score 5

The Costa government faces a difficult challenge regarding fiscal policy. On the one hand, it has committed to turning the page on austerity following its deals with several left-wing political parties. On the other hand, it has also reaffirmed its euro-zone commitments to fiscal consolidation.

Portugal's budget deficit of 4.4% of GDP in 2015 was very high. However, this was inflated by the one-off bailout of the Banif bank in December 2015. Without the Banif bailout, the 2015 deficit would have stood at around 3%. Eurostat estimates the deficit would have been 2.8% without this bailout, Portugal's National Statistics Institute estimates 3% and the European Commission estimates 3.2%.

For 2016, the government's budget, approved in March 2016, forecasts a reduction of the deficit to 2.2% of GDP, allowing Portugal to withdraw from the existing Excessive Deficit Procedure. While most external assessments consider this value to be optimistic, they nevertheless expect the deficit to be below or around 3% in 2016. Data for the first half of 2016 is consistent with these expectations, with a deficit of 2.8% of GDP until June 2016. The budget for 2017, approved by parliament on 4 November 2016, targets a deficit of 1.6%.

While this trajectory is very positive, it remains vulnerable to external shocks. Portugal's fiscal policy is vulnerable to several risks, notably a slowing economy, external shocks on export demand (a driver of recent GDP growth), a rise in the interest rates on government bonds and a vulnerable banking sector (government bailouts of private banks considerably inflated the 2014 and 2015 budget deficits). This vulnerability explains the IMF's cautionary statements about Portugal's fiscal consolidation, which expect Portugal to have the worst budget deficit within the euro zone in 2021 (albeit, at 2.9%, below the euro zone's 3% threshold).

Citation:
Diário de Notícias, “FMI. Portugal terá o pior défice orçamental da zona euro em 2021”, 5 October 2016. Available online at: http://www.dn.pt/dinheiro/interior/-portugal-tera-o-pior-defice-orcamental-da-zona-euro-em-2021-5425731.html

Expresso, “Eurostat: sem ajudas ao sector financeiro défice de 2015 ficava em 2,8%”, 21 April 2016. Available online at: http://expresso.sapo.pt/economia/2016-04-21-Eurostat-sem-ajudas-ao-sector-financeiro-defice-de-2015-ficava-em-28

Observador, “INE. Défice de 2015 ficou em 4,4% do PIB, com o Banif a pesar mais que o previsto”, 24 March 2016. Available online at: http://observador.pt/2016/03/24/ine-defice-2015-ficou-44-do-pib-banif-pesar-previsto/

Diário de Notícias, “Bruxelas reitera que défice sem Banif foi 3,2% do PIB em 2015”, 3 May 2016. Available online at: http://www.dn.pt/dinheiro/interior/bruxelas-reitera-que-defice-sem-banif-foi-32-do-pib-em-2015-5155268.html

Romania

Score 5

Budgetary policy was procyclical in 2016. Despite the strong economic growth, the general government fiscal deficit is estimated to have increased from 0.8% of GDP in 2015 to 2.8% of GDP in 2016, and is expected to widen further to 3.6% in 2017. As a result, the debt-to-GDP, which stands at about 40%, but is sensitive to ageing costs and exchange rate risk, increased. As highlighted by the Romanian Fiscal Council, the original 2016 budget, prepared by the former Ponta government, as well as the budget amendments in August and November 2016 violated rules enshrined in the 2010 Fiscal Responsibility Law, thereby reducing the credibility of the country’s fiscal framework. The preparation of a 2017 budget by the Ciolos government proved controversial, with opposition representatives criticizing it as unconstitutional since the December 2016 parliamentary elections could bring in a new government with new policy priorities. On a positive note, the transparency of budgetary policy substantially increased under the Ciolos government.

Citation:
European Commission (2017): Country report Romania 2017. SWD(2017) 88 final, Brussels, 7-8, 15-16 (https://ec.europa.eu/info/sites/info/files/2017-european-semester-country-report-romania-en.pdf).

IMF (2017): Romania. Country Report No. 17/133, Washington, D.C., 8-11 (http://www.imf.org/en/Publications/CR/Issues/2017/05/25/Romania-2017-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-by-the-44944).

Slovenia

Score 5

The Cerar government succeeded in bringing the fiscal deficit down from 3.4% of GDP in 2014 to 2.9% in 2015 and about 2% in 2016, thus exiting the European Commission’s excessive deficit procedure in June 2016. However, the improvement in the fiscal stance has largely stemmed from the recovery of the Slovenian economy and a number of one-off measures such as wage and promotion freezes in the public sector. Given the solid economic growth, trade unions were less cooperative in 2016 and refused the extension of wage restraint in the public sector. Slovenia's structural deficit has remained relatively high, the debt-to-GDP ratio reached more than 80% in 2016 and, according to the European Commission, Slovenia has the largest long-term sustainability gap of all EU member states. In order to stress its commitment to a sustainable budgetary policy, the National Assembly, in line with the EU's Fiscal Compact, enshrined a "debt brake" in the constitution in May 2013. However, the adoption of the corresponding legislation didn't occur until July 2015 and the government and the opposition have not yet agreed upon the three members of the Fiscal Council in charge of supervising fiscal developments, which requires a two-thirds majority in parliament.

Citation:
European Commission (2017): Country Report Slovenia 2017 Including an In-Depth Review on the prevention and correction of macroeconomic imbalances. SWD(2017) 89 final, Brussels, 17-25 (https://ec.europa.eu/info/sites/info/files/2017-european-semester-country-report-slovenia-en.pdf).

IMF (2017): Republic of Slovenia. Country Report No. 17/125, Washington, D.C. 7-11 (http://www.imf.org/en/Publications/CR/Issues/2017/05/15/Republic-of-Slovenia-2017-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-44921).

Slovenia Times (2016): Slovenia yet to appoint Fiscal Council. December 28, 2016 (http://www.sloveniatimes.com/slovenia-yet-to-appoint-fiscal-council).

United States

Score 5

The condition of budget policy in the United States is complex and raises different concerns depending on the time perspective of the assessment. In the depths of the 2008 – 2009 recession, the budget deficit, enlarged by the fiscal stimulus, reached $1.4 trillion, or 9.9% of GDP. While the deficit shrunk to a projected 2.5% of GDP by 2015, recovery has been too slow to stimulate vigorous economic growth. At the same time, long-term deficits are by all accounts seriously beyond acceptable levels. As the Congressional Budget Office testified in 2013, "Under current law, federal debt appears to be on an unsustainable path." The primary cause of this condition, in addition to the severe limits on revenues, is the growth of the elderly population and the generous terms of the Medicare and Social Security programs.

In short, U.S. budget policy has provided too little current stimulus to promote robust growth; has failed to balance revenues and spending over a 10- to 20-year period; and has nevertheless underfunded most government services – from infrastructure and border security to environmental regulation and R&D. In comparison to recent years, budget policymaking in 2015 and 2016 showed some significant improvements, resulting partly from (perhaps temporarily) more accommodating Republican leadership. The current deficit was reduced (to 3.2% of GDP in fiscal 2016), some modest reductions in the future growth of Medicare and Social Security were achieved, and authorization for required increases in the debt limit was assured until 2017. Political gridlock has locked in the unfortunate combination of insufficient short-term stimulus and serious lack of long-term discipline.

France

Score 4

France’s budgetary situation is unsustainable in the long term. Over the past year, some slight but insufficient improvements have been observed under pressure from the European Commission and partners. The deficit remains above the 3% ceiling and the number of civil servants, which had slightly decreased since the Sarkozy election in 2007, has grown again. Many new commitments (public servants’ salary increase, security or military expenses, disputable rescue operations such as Alstom’s purchase of trains to avoid a plant closure in Belfort) will further increase public spending in spite of public declarations and commitments.

The Hollande government’s major mistake when coming to power in 2012 was to increase taxes on all fronts rather than to cut spending, which, in fact, increased. The outcome has been rather catastrophic: revenues were much lower than expected due to the economic crisis, lack of growth, tax evasion and growing black market, while at the same time the collective morale of French individuals and companies plummeted. Though it announced cuts in public spending (relative to the government’s spontaneous spending increase) amounting to €50 billion for the period 2015-2017, the government made very few real cutbacks. The 2015 and 2016 budgets have foreseen expenditure cuts but failed to respect the 3% deficit limit set by European rules. The Court of Accounts as well as the High Committee on Public Finance (Haut Comité des Finances Publiques) have expressed serious doubts about the economic forecast and the estimates of the 2017 budget which foresees a 2.7% deficit. Similarly, while the structural deficit was reduced in 2012, 2013, and 2014, the government has abandoned the objective to balance the structural budget, postponing this target to 2017. The savings resulting from the review of policies are disappointing: €400 million, while the government committed more than €500 millions to rescue an industrial plant in Lorraine. As a result, France’s comparative performance on budget consolidation is still disappointing. In this context, there is very little chance that the objectives set by European treaties will be met by the end of Hollande’s term in 2017. As well, the Presidential elections in May 2017 and the coming to power of a new team will make official objectives more fragile and difficult to reach. There are serious doubts about the improvement of the 2017 and 2018 budget outlook.

Japan

Score 2

Gross public indebtedness in Japan amounted to 248% of GDP in 2015, the highest such level among advanced economies. The budget deficit, while currently declining, also remains high at 4.9% in 2015, making it the highest among Japan´s peer group. In its August 2016 Article IV staff report, the IMF (like others) urged the government to more seriously address the deficit problem and present a determined and realistic medium-term consolidation strategy. The Abe government has reiterated its intention to achieve primary budget balance by 2020, despite the postponement of the consumption tax hike. This is based on very optimistic and, as the IMF argues, unrealistic assumptions. It has even been suggested to create an Independent Fiscal Institution for Japan to create more reasonable outlooks.

Nominal interest rates have been and remain low. A major factor producing these rates is the fact that more than 90% of public debt is held by Japanese, mainly institutional investors. The government and institutional investors obviously have no interest in lower bond prices, and this oligopoly of players can thus sustain the current price level of Japanese government bonds for the time being. However, should national savings fall short of domestic needs – a foreseeable development given the aging Japanese population – future government deficits may be difficult to absorb domestically. In this case, government bond prices could fall and interest rates could rise quickly, which would create extremely serious problems for the Japanese government budget and the country's financial sector.

In addition to such structural longer-term concerns, the unprecedented presence of the central bank in the financial market, which absorbs more than the new issuance of government bonds, can lead to short-term liquidity shortages in the availability of Japanese Government Bonds (JGBs). This can lead to considerable short-term swings in JGB prices and may thus cause significant concerns regarding the stability of the financial system.

Citation:
International Monetary Fund, Japan 2016 Article IV Consultation - Staff Report; and Press Release, IMF Country Report No. 16/267, August 2016

Address | Contact

Bertelsmann Stiftung
Carl-Bertelsmann-Straße 256
33311 Gütersloh
Germany
Phone +49 5241 81-0

Dr. Daniel Schraad-Tischler
Phone +49 5241 81-81240
daniel.schraad-tischler@bertelsmann-stiftung.de

Dr. Christian Kroll
Phone +49 5241 81-81471
christian.kroll@bertelsmann-stiftung.de

Dr. Christof Schiller
Phone +49 5241 81-81470
christof.schiller@bertelsmann-stiftung.de

Pia Paulini
Phone +49 5241 81-81468
pia.paulini@bertelsmann-stiftung.de

www.bertelsmann-stiftung.de
www.sgi-network.org

BertelsmannStiftung