



Independent Authority
for Fiscal Responsibility

ANCHORING FISCAL POLICIES AND MANAGING FISCAL RISKS AT NATIONAL AND SUBNATIONAL GOVERNMENT LEVELS

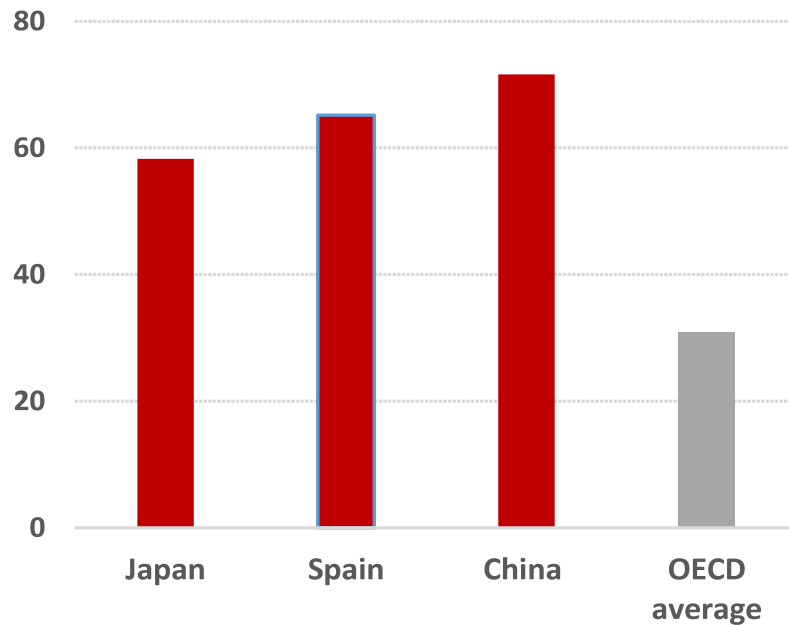
Tokyo Fiscal Forum
Tokyo, 10-11 June 2015

José Luis Escrivá

Fiscal local government overview

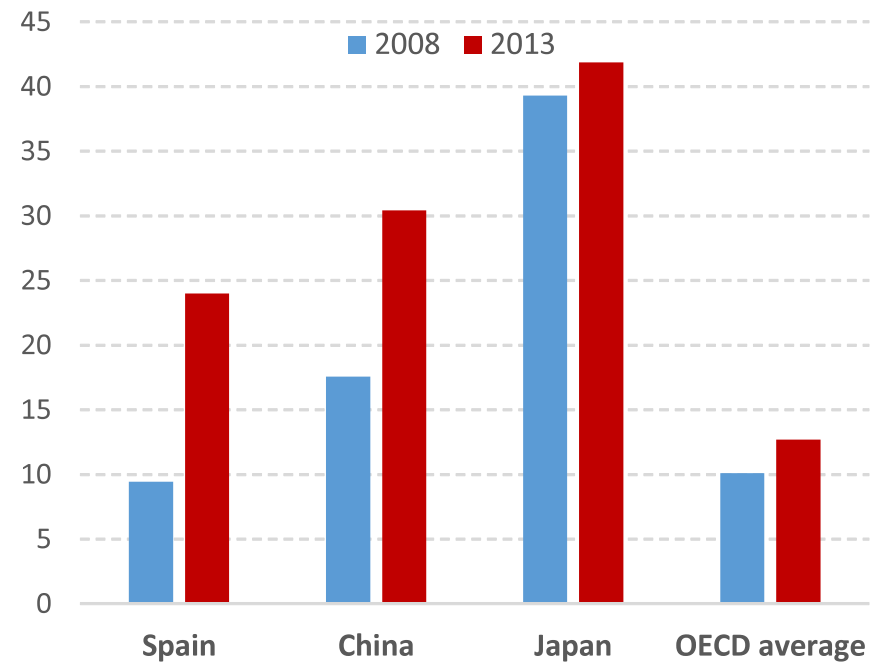
❖ Three highly decentralized countries with high level of local government debt

Local government share on total public expenditure (2013, %)



Sources: IGAE, Japan and China Ministries of Finance and OECD Fiscal Decentralization Database.

Local government debt (% GDP)



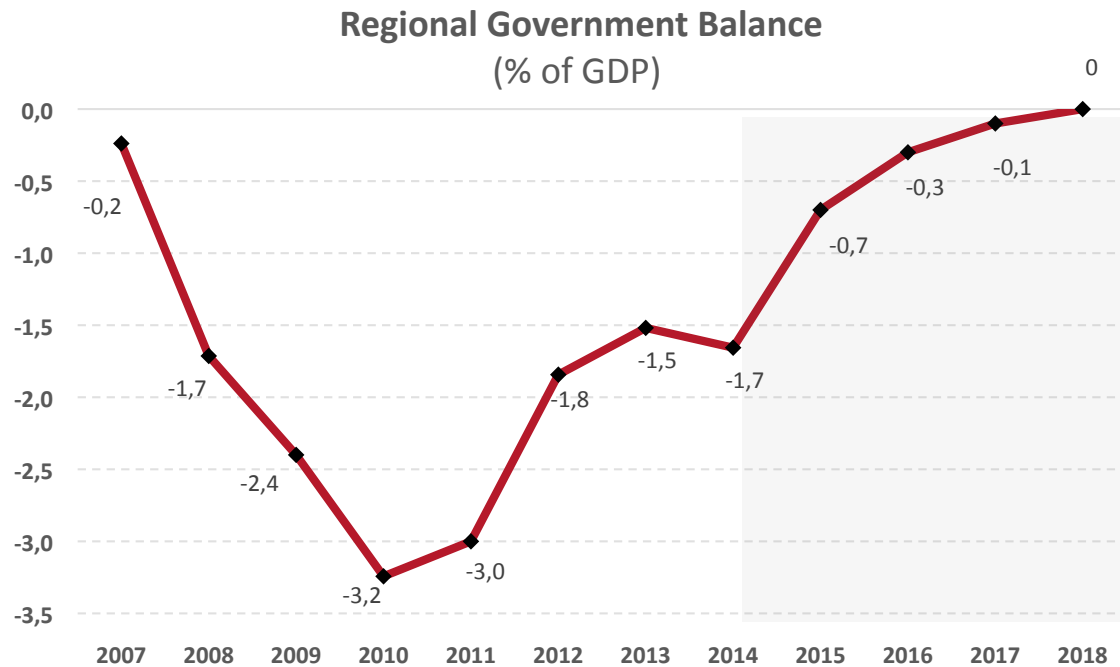
Notes: Spain gross non-consolidated debt; China: includes some contingent liabilities. OECD average for 2008 and 2012.

Sources: Banco de España, China National Audit Office, Japan Ministry of Finance and OECD Fiscal Decentralization Database .



A severe fiscal crisis of Spanish regions

❖ Half way of consolidation strategy: *towards budgetary balance in 2018.*



Note: adjusted by the regularizations of commercial debt operations in 2009 and 2011 and excluding in 2010 and 2011 the final settlement of the regional financing system.

Source: IGAE and AIReF's calculations.

How have these fiscal imbalances been addressed?

A comprehensive strategy based on 4 pillars ...

1. Stronger Fiscal Disciplinary Framework

- Budgetary Stability Principle at the **highest normative level**: Constitution + Organic Act.
- **ALL levels of public administrations** (regions and municipalities included) **subject to same rules**: budget balance (no deficits allowed- in structural terms for regions); debt rule; and expenditure rule. **Commercial debt and late payments included under the fiscal sustainability principle.**
- **Subnational enforcement mechanisms strongly reinforced**:
 - Preventive: risk of non-compliance ➡ early warning by central government.
 - Corrective: non-compliance ➡ automatic measures (ie, debt authorizations) + Rebalancing plans
 - Penalties: Gradually applied: expenditure freezing; interest bearing deposit; formal auditors missions or even regional administrations are put in receivership.

2. Improving Transparency

- **Information requirements become mandatory** (previously not binding): Oct 2012 Ministerial Order.
- **Extremely detailed regulation on**:
 - who provides what and how (electronic means) .
 - Information becomes public and available in a single database:
[The General Government Financial Information Center: Ministerio de Hacienda y Administraciones Públicas](#)
 - Non-compliance is made public and could trigger automatic corrective measures.
- **Some examples of informational gains**:
 - Ex- ante control: annual draft budgets; medium-term budgetary frameworks.
 - Budgetary execution: monthly (cash and national accounts) for regions and quarterly for municipalities.
 - EFP and its follow up reports. ○ Human resources (expenditure, structure, staff size)
 - Since May 2015: monthly information on the subnational financing system in national accounts terms.

How have these fiscal imbalances been addressed? A comprehensive strategy based on 4 pillars ... (cont')

3.
Central Government Financial Support to Face Liquidity Constraints

- **Subnational governments suffer severe financing problems:**
 - Loss of access to financial markets
 - Arrears to suppliers

Requiring central government financing
- **Strict financial and fiscal conditionality in exchange for this extraordinary financing.**
- **Average period of payment starts to be closely monitored.**

4.
Voluntary Agreements between Central and Subnational Governments

- **To rationalize the regional public sector:**
 - 2010 and 2012 agreements adopted within the Fiscal Council (25% reduction in the units of the regional public sector since 2010)
- **Looking for efficiency gains in the regional administration:**
 - Measures to remove duplicities (Commission for the Reform of the Public Administrations).
- **On relevant sectoral policies such as health-care :**
 - Working group on efficiency and rationalization of health-care expenditure (in progress)

...and a key role to be played by AIReF



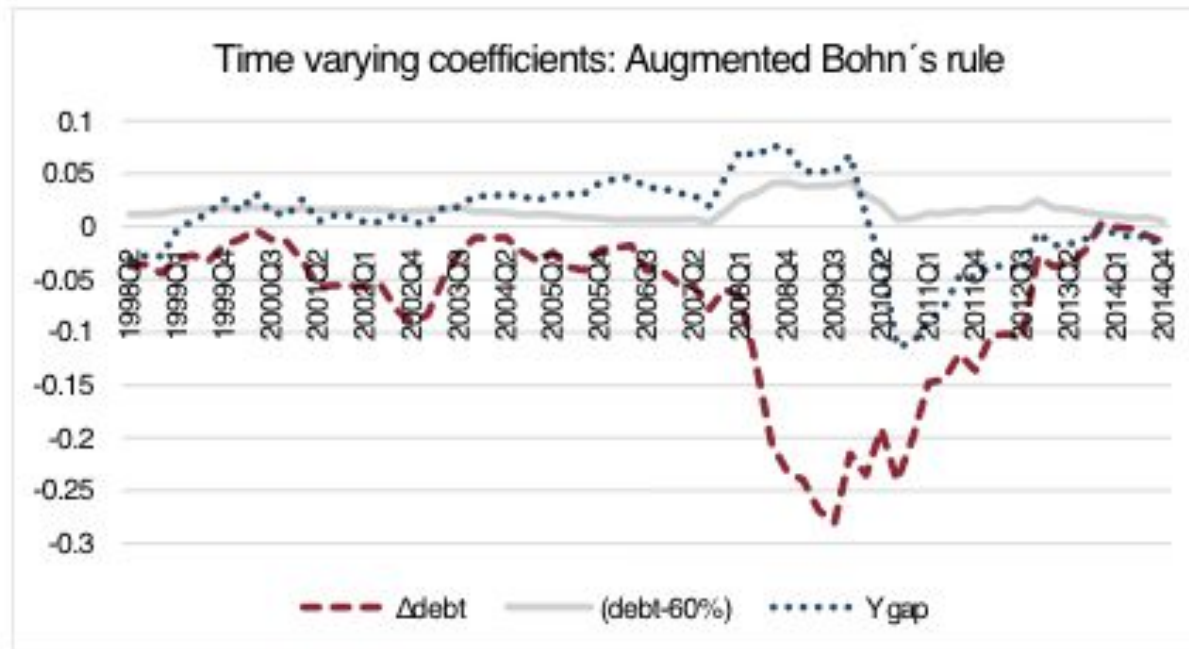
AIReF contributes to 3 of the pillars

Pillars	AIReF's contribution
<p>1. Stronger Fiscal Disciplinary Framework</p>	<p>Monitoring the whole budgetary cycle:</p> <div style="display: flex; justify-content: space-around;"> <div style="border: 1px solid #800000; border-radius: 15px; padding: 10px; width: 30%; background-color: #f08080;"> <p style="text-align: center;">Fiscal Policy Planning</p> <div style="border: 1px solid #800000; border-radius: 10px; padding: 5px; margin-bottom: 5px; text-align: center;"> Regional Budgetary Targets </div> <div style="border: 1px solid #800000; border-radius: 10px; padding: 5px; text-align: center;"> Regional Macroeconomic Forecasts </div> </div> <div style="border: 1px solid #800000; border-radius: 15px; padding: 10px; width: 30%; background-color: #f08080;"> <p style="text-align: center;">Budgetary Monitoring</p> <div style="border: 1px solid #800000; border-radius: 10px; padding: 5px; margin-bottom: 5px; text-align: center;"> <u>Ex ante</u> Draft budgets Approved Budgets </div> <div style="border: 1px solid #800000; border-radius: 10px; padding: 5px; text-align: center;"> <u>In year</u> Identification of risks </div> </div> <div style="border: 1px solid #800000; border-radius: 15px; padding: 10px; width: 30%; background-color: #f08080;"> <p style="text-align: center;">Enforcement</p> <div style="border: 1px solid #800000; border-radius: 10px; padding: 5px; margin-bottom: 5px; text-align: center;"> Asking central gov to activate all the preventive, corrective and enforcement mechanisms (7 regions in 2014) </div> <div style="border: 1px solid #800000; border-radius: 10px; padding: 5px; text-align: center;"> EFP </div> </div> </div>
<p>2. Improving Transparency</p>	<ul style="list-style-type: none"> • Reports are public. <u>AIReF - Autoridad Independiente de Responsabilidad Fiscal</u> • Recommendations directly aimed at reinforcing transparency. (ie regions must make explicit their assumptions and methodologies to estimate the economic impact of their measures). • Comply or Explain principle.
<p>3. Central Government Financial Support to Face Liquidity Constraints</p>	
<p>4. Voluntary Agreements between Central and Subnational Governments</p>	<ul style="list-style-type: none"> • Attending meetings of the two coordinating bodies between the central government and subnational governments • Studies requested by: <ul style="list-style-type: none"> ○ the coordinating bodies. ○ individual regions and municipalities provided their scope does not go beyond their powers. In such a case, the request must be made by the coordinating bodies. • Close dialogue with regions and municipalities.



Augmented Bohn's rule for Spain

- ❖ What role for economic recovery and fiscal sustainability in determining the primary balance?



Sources: INE, IGAE, AIReF

$$pb_t - pb_{t-1} = \theta_1 * (b_t - b_{t-1}) + \theta_2 * (b_t - 60\%) + \theta_3 * Ygap$$

Quarterly data, 1986q1-2014q4



Augmented Bohn's rule for Spain

- ❖ What role for economic recovery and fiscal sustainability in determining the primary balance?

$$pb_t - pb_{t-1} = \theta_1 * [(b_t - b_{t-1})] + \theta_2 * (b_t - b_t^*) + \theta_3 * Ygap$$

- ✓ Are the resulting signs in line with theoretical priors?

θ_1 : + vs. - θ_2 : + vs. + θ_3 : + vs. -/+

- ✓ Are the coefficients stable throughout the sample **no**
- ✓ What was the status quo before the crisis? **Countercyclical FP**
- ✓ How did FP respond to the negative shock? **Continuation of countercyclical FP (exacerbation), eating up the previous buffer and leading to a procyclical FP, later on dominated by sustainability concerns**
- ✓ How to spot institutional changes? **2012 onwards, recovery of sustainability as a primary goal, reaching a somewhat neutral tone**

La importancia de la sostenibilidad de las finanzas públicas



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