

## Discussion on “Sustainability of the Belgian public finances: an EU perspective” (EC)

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## The EC's fiscal sustainability assessment framework

- ▶ Impressive framework for assessing risks to fiscal sustainability
- ▶ Covers a wide range of factors/variables that affect fiscal sustainability
- ▶ Is theoretically and empirically well funded:
  - S0: based on empirical analysis of fiscal stress episodes
  - S1 and S2:
    - based on the intertemporal budget constraint / theoretical concept of solvency
    - Incorporate expected future ageing costs based on the AWG's projections
    - Incorporate consistent medium term forecasts on macroeconomic and fiscal variables
    - Homogeneous methodology across EU countries
- ▶ Provides policy makers with an overall score/colour which is easy to communicate enhancing policy impact
- ▶ The ESCB's methodology is similar to the EC's
  - See “Debt sustainability analysis for euro area sovereigns: a methodological framework” (Bouabdallah et al. 2017)
  - The ESCB results are not published, but very similar to the EC's result for the medium term



## Importance of the incorporation of a broad set of variables

Table 3.3: Financial-competitiveness variables used in the S0 indicator, 2016

	Yield curve	Real GDP growth	GDP per capita in PPP (%US level)	L.Net intern. invest. position (%GDP)	L.Net savings households (%GDP)	L.Private debt (%GDP)	L.Private credit flow (%GDP)	L.Short-term debt nonfin. corp. (%GDP)	L.Short-term debt households (%GDP)	L.Construction (%value added)	L.Current account (%GDP)	L.Change real eff. exchange rate	L.Change nom. unit labour costs
BE	0.5	1.2	79.0	61.3	2.2	166.3	4.5	41.1	2.6	5.4	-0.2	-2.5	1.5
BG	1.6	3.1	32.9	-60.0	-12.4	110.5	-0.3	16.9	2.3	4.3	0.6	-3.5	14.9
CZ	-0.2	2.2	59.2	-30.7	3.3	68.6	0.9	7.8	1.8	5.7	0.2	-3.1	0.5
DK	0.7	1.0	82.5	39.0	2.5	212.8	-3.3	25.6	4.3	4.5	8.8	3.4	4.9
DE	0.3	1.9	84.2	48.7	5.8	98.9	3.0	10.0	2.0	4.6	7.5	1.7	5.7
EE	1.1	49.7	-40.9	1.2	116.6	3.3	12.2	1.0	6.2	0.9	2.3	14.4	
IE	0.7	4.1	118.9	-208.0	2.1	303.4	-6.7	16.3	1.9	2.5	4.7	5.8	-18.1
ES	1.4	3.2	62.8	-89.9	1.4	154.0	-2.7	9.3	2.6	5.6	1.3	-1.0	-0.7
FR	0.6	1.3	71.0	-16.4	5.4	144.3	4.4	24.1	1.7	5.4	-0.7	-0.5	2.5
HR	1.9	2.6	39.9	-77.7	5.1	115.0	-1.3	10.5	3.8	5.2	2.7	-0.8	-5.0
IT	1.3	0.7	64.3	-23.6	1.9	117.0	-1.7	20.6	3.5	4.8	1.5	0.1	1.5
CY	3.9	2.8	56.4	-130.3	-8.4	353.7	4.4	34.7	12.5	3.6	-4.1	-0.6	-10.5
LV	0.3	1.9	44.0	-62.5	-6.9	88.8	0.7	13.5	2.1	6.4	-1.8	0.7	16.0
LT	0.9	2.0	50.9	-44.7	-3.5	55.0	2.2	4.9	1.2	7.3	0.9	-6.9	11.6
LU	0.0	3.6	180.1	35.8		343.1	24.2	9.5	2.9	5.1	5.3	11.2	0.6
HU	1.6	2.1	46.7	-60.8	2.2	83.9	-3.1	10.0	2.5	4.1	3.0	-5.1	3.9
MT	1.1	4.1	60.8	48.5		139.1	5.4	15.4	3.8	4.4	4.3	3.6	3.9
NL	0.4	1.7	86.4	63.9	2.8	228.8	-1.6	33.0	3.6	4.6	9.1	-5.1	0.2
AT	0.5	1.5	85.7	2.9	4.2	126.4	2.1	13.3	3.7	6.4	2.1	0.3	6.1
PL	0.9	3.1	47.4	-62.8	-0.3	78.6	3.1	8.3	3.0	7.8	-1.3	2.3	-0.4
PT	1.9	0.9	52.4	-109.3	-2.5	181.5	-2.3	21.0	2.9	4.1	0.7	-2.4	0.0
RO	2.1	5.2	39.9	-51.9		59.1	0.2	13.1	1.0	8.5	-1.0	-2.6	0.5
SI	1.1	2.2	56.3	-38.7	3.9	87.3	-5.1	11.4	2.5	5.5	5.4	0.3	-0.6
SK	0.4	3.4	53.3	-61.0	1.8	81.4	8.2	14.4	2.2	7.9	1.1	-5.6	2.2
FI	0.5	0.8	72.8	0.6	-0.4	155.7	9.5	6.0	4.0	6.3	-1.0	0.1	3.6
SE	0.9	3.4	84.4	4.1	8.8	188.6	6.5	39.8	14.3	5.9	5.0	-2.7	3.6
UK	1.0	1.9	74.2	-14.4	-0.1	157.8	2.5	26.1	9.9	6.2	-4.8	7.6	1.7

(1) Variables' names preceded by L are taken in lagged values.

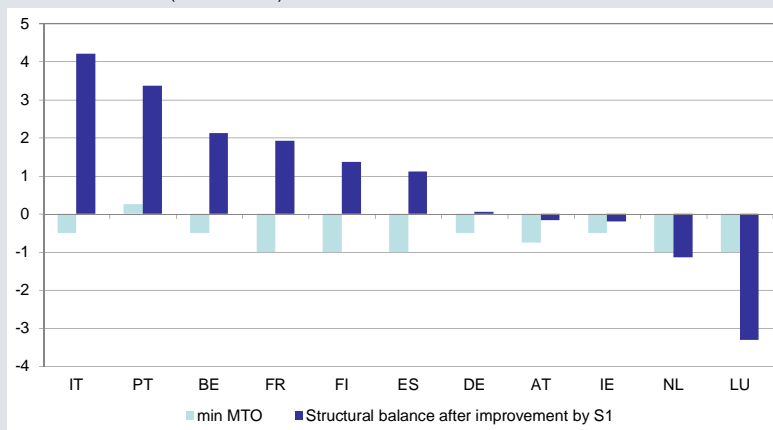
Source: Commission services

- ▶ S0 does not only reflect fiscal variables but also **macro-financial fundamentals**
- ▶ Financial-competitiveness variables also define sustainability in the **medium term** (cf. their use in the EC's **Macroeconomic Imbalances Procedure**)

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## S1-indicator vs. the Medium Term Objective (MTO)

Structural balance (in % of GDP)



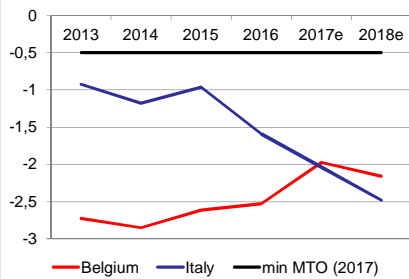
Source: EC, NBB

- ▶ For high debt countries, reaching the MTO is not sufficient to bring down debt to 60% of GDP in 15 years (cf SGP's debt rule wants this in 20 years)
- ▶ Why not calculate S1 based on reaching 60% debt threshold in 20 years?

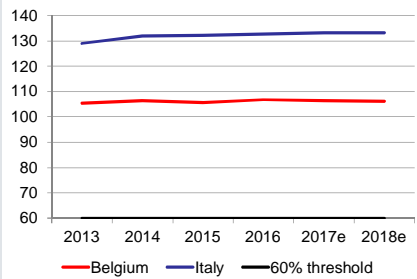
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## Sustainability indicators vs. implementation of the SGP's debt rule

Structural balance (in % of GDP)



Government debt (in % of GDP)



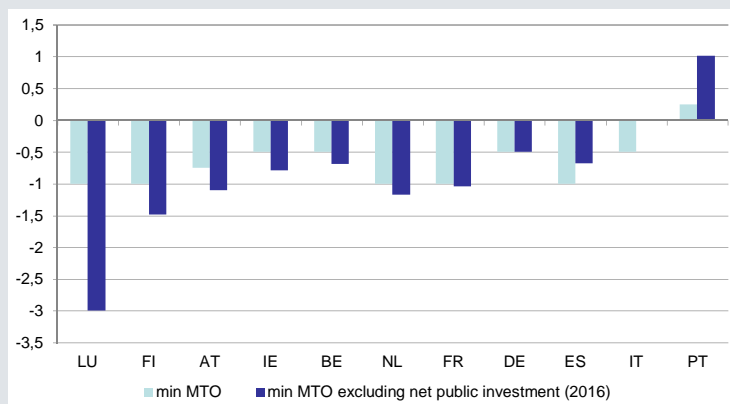
Source: EC winter forecast 2017

- ▶ BE and IT have a "high" medium term fiscal sustainability risk score
- ▶ BE and IT quit the excessive deficit procedure in 2014 and 2013 respectively
- ▶ Since then, the SGP's debt rule was de facto sidelined, because of:
  - Low nominal GDP growth
  - The implementation of growth enhancing structural reforms
  - Broad compliance with the required adjustment towards the MTO (cf flexibility clauses)
- ▶ In February 2017, IT was asked an additional effort of 0.2% of GDP in 2017

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## Fiscal sustainability vs. public investment

- ▶ "The intertemporal budget constraint (solvency condition) refers to the capacity of a country to meet its **net debt** obligations with a stream of future primary surpluses" (EC-DSM, 2016)
- ▶ **Net government investment** increases the government's stock of public capital => increases gross debt but not net debt (sensu latu)
- ▶ A case for correcting the MTO for net investment?



Source: EC, NBB

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**Thank you!**



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