

Fiscal Sustainability: Some Theoretic- methodological Issues

Ionel LEONIDA,
Victor Slăvescu Centre for Financial and Monetary Research, Bucharest,
ROMANIA

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Abstract: Fiscal sustainability is a well-known debated subject among scientific researchers and implies some ethic arguments like “fairness” or “equity” illustrated often from different theoretic and methodological perspectives.

In this framework the specific economic literature illustrates a large spectre of opinions for the general concept of economic sustainability and one of the most largely accepted definitions is related to the United Nations Brundtland Report statement: the capacity to meet the needs of present generations without compromising the ability of future generations to meet their own needs.

The present paper treats some theoretic-methodological aspects of sustainability applied in the case of fiscal-budgetary policies: the fiscal sustainability is oriented to diminishing the economic system distortions (like the explosive increasing of public debt, the growing of taxes, the drastic lowering of public expenditures or monetizing the public deficits).

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Fiscal budgetary sustainability is a well known debated issue within the scientific community. The importance of sustainability at the level of budgetary decision process is reflected with a lot of arguments.

In the context of sustainable development strategy that implies the economic, social and environmental convergence, the fiscal and budgetary policies determines positive externalities on sustainability of economic growth encouraging the sustainable investments in human capital.

The qualitative analysis of fiscal budgetary policies points out several possible plans of approach: in this respect, some of researchers consider that a good evaluation of fiscal and budgetary policies is not accurate evaluated only through a single general indicator¹, but also needs a closer attention to some other issues like:

- a) **The discretionary character of fiscal and budgetary policies** - the specific impact on fiscal position², the changes of economic environment or the new horizon of public policy targets;

¹ Chouraqui, Hagemann and Sartor (1990) respectively, Blanchard (1990);

² The fiscal position reflects the level and structure of taxes or budgetary expenditures

- b) **Fiscal and budgetary sustainability**, respectively the action directed to diminishing the economic system distortions (like the explosive increasing of public debt, the growing of taxes, the drastic lowering of public expenses or monetizing the public deficits);
- c) **The impact of fiscal and budgetary policies on aggregate demand side;**
- d) **The redistribute finality of fiscal and budgetary policies reflected in the decisional actions to encourage the saving-investment process at the macroeconomic level.**

A professional qualitative analysis of fiscal-budgetary policy performances must take into account also the aspects mentioned above, but in some interrelated approach of them.

For example, a discretionary fiscal - budgetary policy not related to economy trend cycles is not a sustainable policy.

That implies negative consequences on the dynamics on GDP, on allocation decisions of financial, material and human resources, in the context of the public debt raising that affects the financing of social public expenditures programs.

In the same time, the maintaining of stability of public finances requires to diminish the negative effects on the economy distortions but also an efficient fine tuning adjustment of fiscal and budgetary policies to the economic system evolutions.

In this framework, for a better understanding the sustainability of fiscal and budgetary policies in the context of public finances stability we propose an interrelated methodological-theoretic approach of the mentioned above issues.

Thus, fiscal budgetary sustainability requires activist measures of tax raising of budgetary expenditures reduction irrespective the evolution of economic cycle-the as so called discretionary policies conducting to fiscal position changing not related to economic ensemble evolution.

The main instrument for the management of discretionary components of fiscal and budgetary policies is the cyclically adjusted budget balance or structural balance³.

On that basis is measured the fiscal policy variability feed back of economic effects from one period to another of the size, which, in literature, bears the name of fiscal impulse⁴.

O. Blanchard (1990) defined fiscal and budgetary policies and as sustainable those that do not conduct to explosive growth of the public indebtedness or which do not adopt measures to increase taxation, limiting excessive public spending and monetization of the budget deficit.

Starting from this approach, you can interpret that a degree of indebtedness of 30% may reveal the promotion of sustainable policies, while a degree of indebtedness of 90% is determined to be non sustainable. Sustainability cannot be judged solely from the perspective of the size of the stock of public debt accumulated. Even with a degree of indebtedness of 20%, fiscal and budgetary policies can be non sustainable if, for example, the State has no ability to pay and obligations relating to public contracting loans, so if it is not viable.

Studies later⁵ have brought improvements to the approach of Blanchard, bring together the concepts of sustainability and solvency.

In this framework, it is considered a public policy is viable when the current primary surplus is equal to the level of public debt contracted, the solvency constituting a necessary but not a sufficient condition those fiscal and budgetary policies to become sustainable.

Thus, the sustainability of fiscal and budgetary policies requires the public authorities' ability and responsibility to run the same set of policies for an indefinite period.

The sustainability feature of fiscal and budgetary policies depends on the active measures taken in order to limit public budgetary deficits. Often, it is necessary to adopt measures aimed at increasing tax revenue or reduce certain categories of expenditures, independent of the business cycle or in the context of automatic versus discretionary stabilizers⁶.

³ Used for identification measures at the level of discretionary fiscal policies or budget, adjusted budget balance represents an indicator for cyclical fiscal performance in the opinion of many authors. But, have been formulated and many critics in this regard. Thus, Muller and Price (1984) believed that the budgetary balance cyclic adjusted (BBCA) is a good indicator by which amendments may be caught in the evolution of the balance due to budgetary policy and less due to economic fluctuations. Chouraqui, Hagemann and Sartor (1990) considered the usefulness of BBCA -as an assessment of discretionary degree for fiscal budgetary policies from the other following views: (i) on the one hand, because it allows the distinction between the cyclical and non-cyclical balances the budget, this indicator can be used to measure the incidence of policies fiscal and budgetary promoted by public authorities, in view of the public budget, (ii) on the other hand, given the long-term implications of public finance policies, this indicator can be revealed important information about future fiscal and budgetary policy orientation;

⁴ Alesina and Perotti, 1995;

⁵ Horne (1991) or Buiter (1997)

⁶ At the Centre for Financial and Monetary Research "Victor Slăvescu", a group composed of researchers Elena Pădurean, Emil Dinga, Camelia Băltărețu, Delia Nedu, Georgiana Chițiga, and Leonida Ionel, elaborate in course of this year 2008 the study "Fiscal Automatic Stabilizers Net values versus gross values"

Adjustments fiscal and budgetary policies play an important role in this regard ⁷.

Thus, a period of adjustment means that tax year in which cyclical adjusted primary balance improves by at least 2% of GDP or the interval between two consecutive years in which cyclical adjusted primary balance is improving with 1.5% of GDP in each of those two years. The fiscal adjustment episodes are associated with restrictive policies.

On the one hand, is seeking tax efficiency adjustments in the light of the effect you have on reducing public deficits, and on the other hand, are looking in their expansionist nature during and after adjustment this time. Adjustments fiscal and budgetary policies are considered to be effective, if:

- Over the next three years after adjustment episode in the share of GDP adjusted primary deficit is cyclical, on average, at least 2% below the deficit during the adjustment;
- Over the next three years after episodic adjustment in the GDP share of public debt is at least 5% below the level during the fiscal adjustment episode.

Periods of fiscal adjustment are considered expansionistic if the average growth of GDP during the adjustment the next 2 years is higher than the average value of the same indicator registered in all periods of fiscal adjustment.

The main issues to be pursued in connection with tax adjustments have in mind, at least, the following:

- Size of the adjustment;
- Structure adjustment, both through the prism possibility of opting either for reducing budgetary expenditures or to increase taxation and the light categories of spending or taxes to be used for this purpose;
- Efficiency adjustments of perspective how they contribute to the maintenance over time reduced the size of public deficits.

Studies on tax adjustments have revealed that the most effective and sustainable fiscal adjustment is based on reductions in budgetary spending, in particular, reductions in expenditures with wages in the social public sector, while measures based on growth budget revenues have not proved to be as effective in terms of reducing deficits and no less than that of stability in time.

As regards the composition of fiscal adjustment, studies have shown that the measures are based on tight criteria to accede at the benefits of social programs as well as reducing these benefits lead to lasting sustainable effects in terms of reducing public deficits, in comparison with measures aimed at reducing public investment.

The issue that arises in this context is to consider the effectiveness of episodes of fiscal adjustment, at least from the perspective of maintaining long-term results and sustainability of fiscal and budgetary policies, and the degree of public indebtedness.

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⁷ Many studies like those elaborated by (Alesina and Perotti, (1995), Alesina and Perotti, (1996); Perotti, (1996); Alesina and Ardagna, (1998) Alesina, Perotti, Tavares, Obstfeld and Eichengreen, (1998); Gupta, Clements, Baldacci and Mulas-Granados, (2002); Purfield, (2003) approached the issue of fiscal adjustments on the case of various countries to illustrate the most efficient activist measures and their impact on economic growth