Budget Institutions in G-20 Countries: An Update

Fiscal Affairs Department
International Monetary Fund

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G-20 Budget Institutions: An Update

Outline of Presentation

I. Background

II. Methodology

III. Trends in Institutional Reform in the G-20

IV. Budget Institutions and Fiscal Performance

V. Priorities for Further Reform
I. Background:
  a. Motivation and Methodology

**Motivation**
- In the wake of the crisis many G-20 countries faced a large and long-term fiscal consolidation requirement. The paper was motivated by four key questions:
  - Can budget institutions help support the consolidation process?
  - Which institutions are particularly important?
  - Are these institutions in place in the G-20?
  - What are the institutional reform priorities for each G-20 country?

**Methodology**
- 12 budget institutions critical to 3 stylized phases of the adjustment process:
  - Understanding the fiscal challenge
  - Developing a consolidation strategy
  - Implementing the strategy through the budget process
I. Background:
a. Motivation and Methodology

Methodology cont’d

- Institutions evaluated in 2010 and again in 2013
  - Evaluation framework consisting of 52 dimensions to assess institutional strength
  - Set of 10 fiscal indicators used to assess impact of institutions on fiscal performance

- Extensive consultations with country authorities
  - Feedback taken into account in revising evaluation framework
  - Individual country specific factors highlighted in supplement to the paper

- Some limitations should be acknowledged. In particular:
  - The period under analysis is brief, just three years
  - Many countries plans for further reforms to their budget institutions not captured
  - The sample of countries, 19 in total, is small
  - While there is evidence that budget institutions can help shape fiscal outcomes, the analysis presented does not necessarily establish causality
II. Methodology for the Board Paper:
a. 12 Budget Institutions and 10 Fiscal Indicators

<table>
<thead>
<tr>
<th>Phase of Adjustment</th>
<th>Budget Institution</th>
<th>Fiscal Adjustment Indicator</th>
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</thead>
<tbody>
<tr>
<td>a. Understanding the Fiscal</td>
<td>1. Fiscal Reporting</td>
<td>1. Data Revisions</td>
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<td></td>
<td>4. Independent Fiscal Agency*</td>
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<tr>
<td>b. Developing a Consolidation</td>
<td>5. Fiscal Objectives and Rules</td>
<td>4. Fiscal Effort</td>
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<tr>
<td>Strategy</td>
<td>6. MT Budget Framework</td>
<td>5. Timeliness of Adjustment Planning</td>
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<td></td>
<td>8. Intergovt Fiscal Arrangements</td>
<td>7. Sub-National Adjustment</td>
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<td>c. Implementing through the</td>
<td>9. Budget Unity</td>
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<td></td>
<td>12. Budget Execution</td>
<td>10. Responsiveness to Shocks</td>
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Institutional reforms focused on strengthening consolidation planning…
…less focus on reporting, forecasting, risk management.

Concern over the growing gap in institutional strength between advanced and emerging markets
III. Overall Institutional Reform Trends:
b. Average Score by Institution
IV. Budget Institutions & Fiscal Performance:

a. Overall Fiscal Performance

Countries with stronger institutions overall have addressed more of their adjustment need...

...while those with weak institutions have not tended to plan or deliver much

Countries with stronger institutions were also better at sticking to their plans...

...while those with weaker institutions delivered less and had a more varied track record – some delivered while others missed by a wide margin

Source: MAP
IV. Budget Institutions & Fiscal Performance: b. Understanding the Fiscal Challenge

The relationship between the strength of understanding institutions and revisions to fiscal data is complex...

...But countries with stronger institutions for fiscal reporting, forecasting, and risk management saw smaller forecast errors impacting their plans.
IV. Budget Institutions & Fiscal Performance: c. Developing a Consolidation Plan

Having strong institutions seems to have led to earlier adjustment planning.

Countries with stronger institutions protected capital investment during consolidation.

*Months since January 2009.
IV. Budget Institutions & Fiscal Performance:

d. Implementation Through the Budget Process

Strong implementing institutions helped ensure budgets were respected and planned adjustments largely delivered.

Countries with strong intergovernmental arrangements also saw bigger falls in subnational deficits.
IV. Budget Institutions & Fiscal Performance:

   e. Response to Shocks

Many adjustment plans were hit by macro shocks...
...but countries with stronger institutions compensated with additional fiscal effort...
...and under-execution of approved budgets...

...while countries with weaker institutions were hit by revisions to their starting debt levels and macro shocks...
...but failed to compensate with additional fiscal effort...
...and overspent against approved budgets.
V. Priorities for Further Reform

<table>
<thead>
<tr>
<th>Institution</th>
<th>Advanced</th>
<th>Emerging</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fiscal Reporting</strong></td>
<td>Extend coverage to public sector</td>
<td>Gen. Gov and eventually public sector-independent fiscal statistics agencies</td>
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<tr>
<td><strong>Macro-Fiscal Forecasting</strong></td>
<td></td>
<td>Midyear updates, forecast vs outturn and L-T fiscal projections</td>
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<tr>
<td><strong>Fiscal Risk Management</strong></td>
<td>Improve reporting of specific fiscal risks</td>
<td>Produce alternative macro forecasts</td>
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<td><strong>Independent Fiscal Agencies</strong></td>
<td></td>
<td>Establish IFA’s</td>
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<tr>
<td><strong>Fiscal Objectives and Rules</strong></td>
<td>Rules should accommodate the business cycle and include escape clauses</td>
<td></td>
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<tr>
<td><strong>Medium-term Budget Framework</strong></td>
<td>Binding multi-year restrictions</td>
<td>M-T priorities and separate fiscal impact of current vs new policies</td>
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<tr>
<td><strong>Performance Orientation</strong></td>
<td></td>
<td>Comprehensive spending reviews</td>
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<tr>
<td><strong>Intergov’t Fiscal Arrangements</strong></td>
<td>Strengthen inter-gov’t coordination</td>
<td>Fiscal objectives cover all gov’t levels</td>
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<tr>
<td><strong>Budget Unity</strong></td>
<td>Annual budget covers all of central gov’t. Review mandatory exp. regularly</td>
<td></td>
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<td><strong>Top-down Budgeting</strong></td>
<td>All rev. and exp. decisions taken by executive during the annual budget process</td>
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<td><strong>Parliamentary Approval</strong></td>
<td>Annual budget approved by parliament top down and restrictions on parliament’s budget amendment rights</td>
<td>Annual budget approved by parliament top down, restrict ions on parliament’s amendment rights and parliamentary debate to endorse fiscal strategy</td>
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<td><strong>Budget Execution</strong></td>
<td>Restrictions on overspending during budget execution</td>
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