Improving the quality of public finance – an analytical framework

2018 Ludwig Erhard Lecture

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“The 2018 Euro Summit: Beyond Austerity: Why Quality Public Finance is Key to Prosperity – and How Governments Can Deliver It”
Brussels, 17 December 2018
MUSGRAVE + and QPF

• **Allocation**
  
  *(QPF for improving efficient resource allocation and insurance models (UB))*

• **Sustainability**
  
  *(Population ageing challenges, ensuring fiscal sustainability, DSA)*

• **Stabilisation**
  
  *(EA and national fiscal stance)*

• **Redistribution**
  
  *(QPF for pre and post market policies)*
Allocation

Public spending and growth

Composition of public spending, euro area, % of GDP
Public investment: crucial for jobs and growth

Impact of the crisis in the euro area

- Crisis legacy: large investment gap in the euro area
- A big part of the gap comes from construction
- Intangible investment makes the gap smaller

Source: AMECO

Contributions to the investment gap:
- Machinery and equipment
- Construction
- Other investment
- Total investment

Source: European Commission
Allocation

Education: expenditure vs quality of education (Pisa scores)

Public expenditure per pupil on primary and secondary education (average 2006-2015)
Allocation

Health care: expenditure vs life expectancy

Output: life expectancy at birth (adjusted for lifestyle). Input: per capita health expenditure in PPP (adjusted for lifestyle)
Allocation

Quality of public revenues: Tax burden on labour

Tax wedge on labour, single earner, average wage (2017)

Tax wedge on labour, single earner, 50% of average wage (2017)
Sustainability

Debt developments in large EU countries

Government debt ratio (% of GDP)
Sustainability

Pension spending vs pension adequacy

Overall index of adequacy incl. part rate 55-64 vs Relative public pension expenditures, %
Stabilisation

Fiscal stance: correcting pro-cyclicality

Fiscal stance, EA, 2011-2019
(Commission 2018 autumn forecast)
Stabilisation

Rebuild fiscal buffers and use fiscal space where it exists

The fiscal stance, fiscal sustainability challenges and the cyclical position in 2019 (Commission 2018 autumn forecast)
Stabilisation
Strengthening automatic stabilizers
Redistribution
Tax and benefit systems to reduce income inequality and poverty

Impact of taxes
Impact of transfers
Gini (disposable income, post taxes and transfers)
Gini (market income, before taxes and transfers)
Redistribution
Better performing welfare systems

At-risk-of-poverty rate vs. social protection expenditures excluding pensions (% GDP)

Gini coefficient vs. social protection expenditures excluding pensions (% GDP)

y = -0.4736x + 22.777
R² = 0.2473

y = -0.4161x + 35.681
R² = 0.1829

European Commission
Delivery models: national level

Spending reviews

How can spending reviews enhance the quality of public finance?

1. Promoting allocative efficiency
2. Improving value for money
3. Freeing up fiscal space

Eurogroup’s Common Principles on spending reviews (September 2016)

• Strong and sustained political commitment
• Best practices in design, conduct and implementation
• Monitoring and communication to the public
• Consistency with budget planning and fiscal framework
The European Semester as a tool to improve QPF

- Considerations about the quality of public finance play a prominent role in the Country-Specific Recommendations

- On the revenue side the main focus is on:
  - Lowering the tax burden on labour in a budget neutral way, especially by reducing tax wedge for low-wage earners combined with a shift to taxes least detrimental to growth - such as recurrent property and environmental taxes (directly recommended to 16 Member States)
  - Broadening tax base by removing distortive tax expenditures, broadening the tax base on consumption (20 Member States)
  - Improving tax compliance by applying specific measures and enacting broader compliance strategies (17 Member States)

- On the expenditure side we promote:
  - Safeguarding growth-enhancing expenditure such as on research, innovation and education. Making space for productivity enhancing investment (8 Member States)
  - Increasing effectiveness of public spending, including by recommending spending reviews (15 Member States)
The European Semester as tool to improve QPF

Delivery models: EU level

Level of implementation of QPF CSRs lags behind progress towards achieving the SGP-related targets and below the overall implementation of CSRs

Graph: Level of implementation of various groups of CSRs from the multiannual perspective (2011-2016)

- Average assessment for all recommendations
- Progressing towards SGP targets
- Fighting against tax evasion, improving tax administration and tackling tax avoidance
- Reducing the tax burden on labour
- Broadening tax bases
- Ensuring long-term sustainability of public finances

estimate of implementation in %
Conclusions

• Population ageing and the changing world of work call for strengthening the QPF.

• Well-designed public spending and taxes support growth, sustainability and inclusiveness for all.

• Composition matters for growth more than the deficit.

• Restoring investment is essential for jobs and growth.

• Spending reviews is a good way to monitor and evaluate policies at national level.

• How does the EU help to improve QPF?
  - Sharing best practices
  - CSR
  - Flexibility clauses in the SGP
  - New tools: New EU public good in MFF proposal, InvestEU, EISF, RDT
Thank you for your attention!