



Improving the quality of public finance – an analytical framework

2018 Ludwig Erhard Lecture

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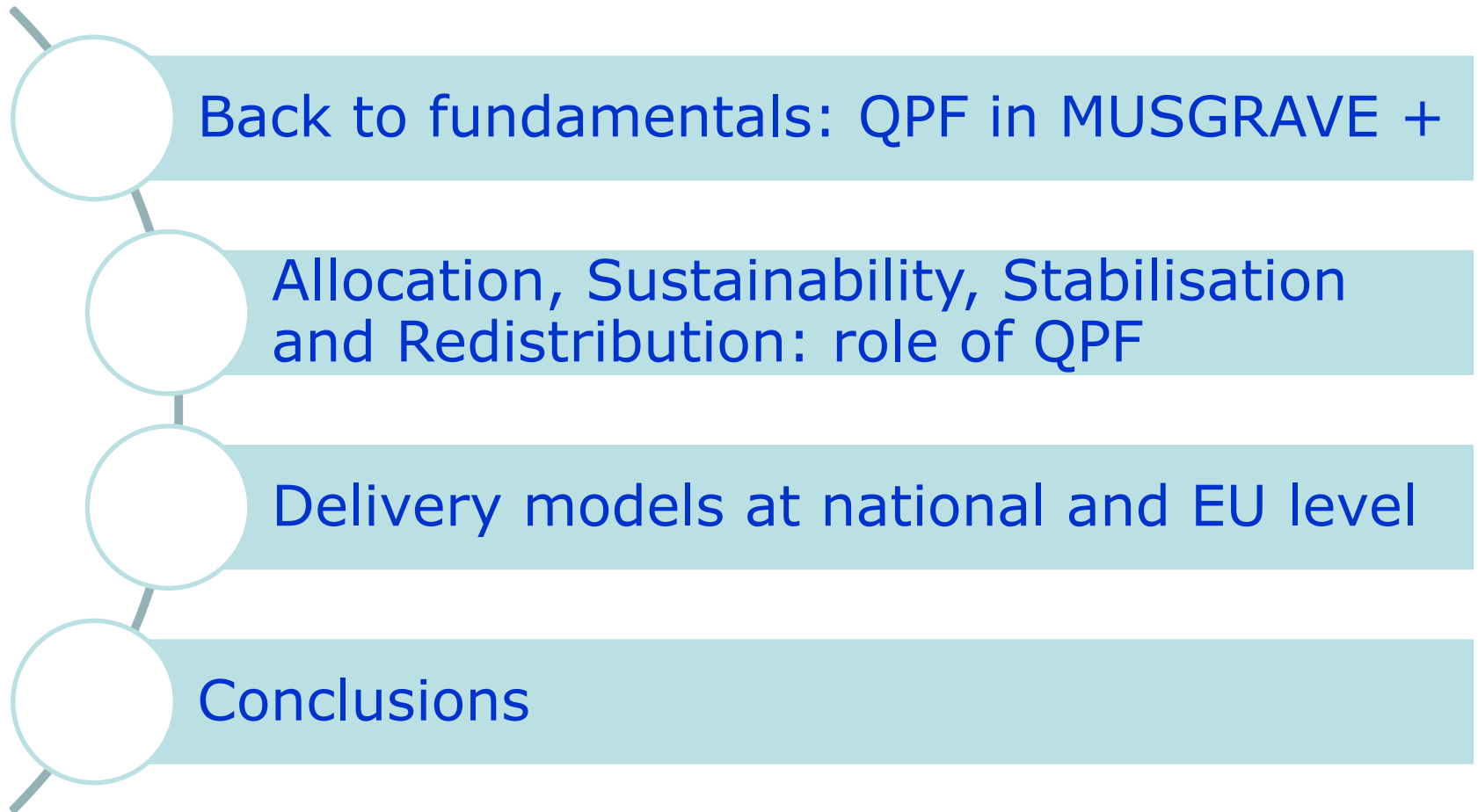
Economic and Financial Affairs, European Commission

Lisbon Council

*"The 2018 Euro Summit: Beyond Austerity: Why Quality Public Finance is Key to Prosperity – and
How Governments Can Deliver It"*

Brussels, 17 December

Outline



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)

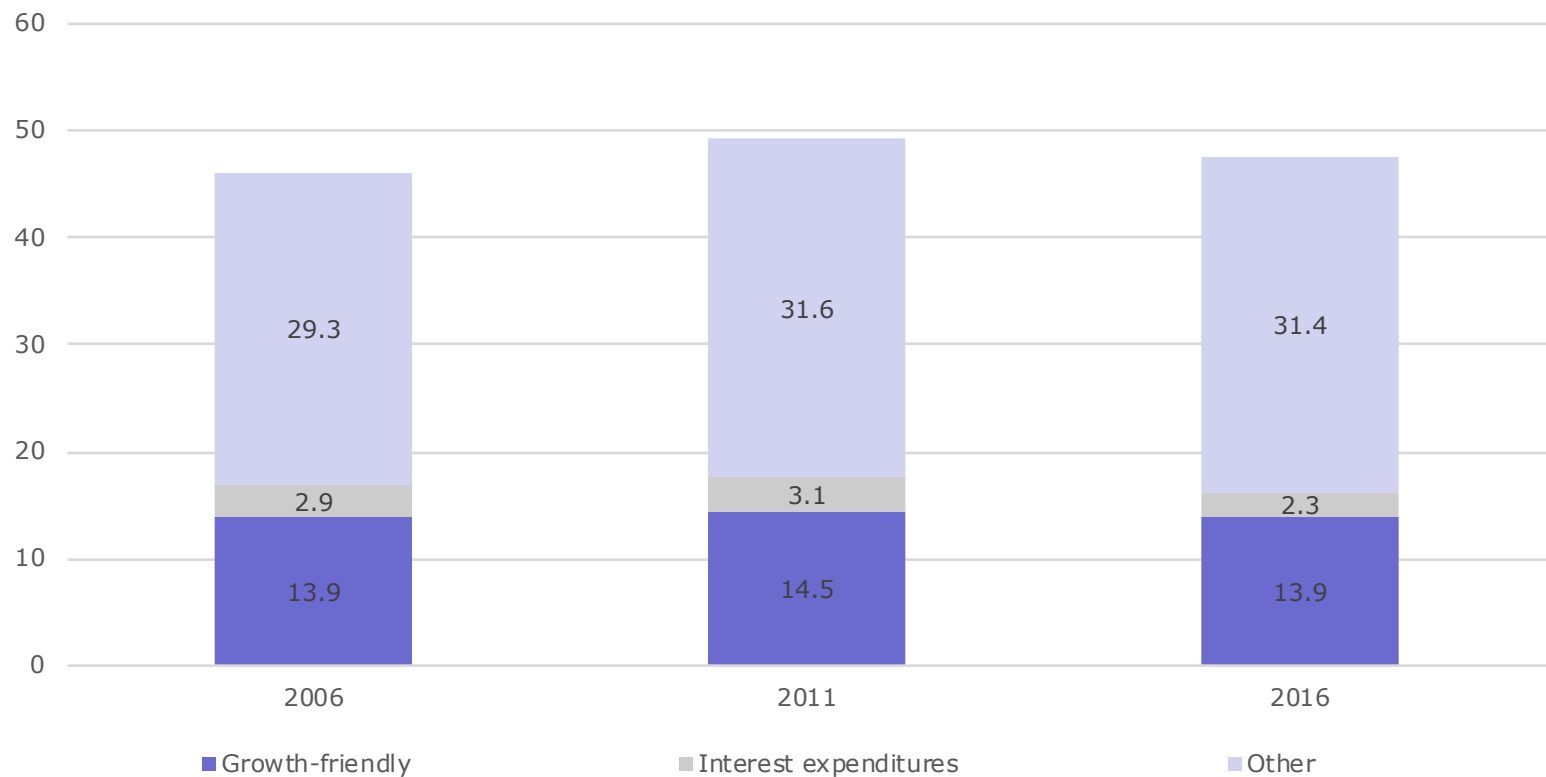
- **Redistribution**

(QPF for pre and post market policies)

**National and
EU dimension**
(delivery models)

Allocation

Public spending and growth

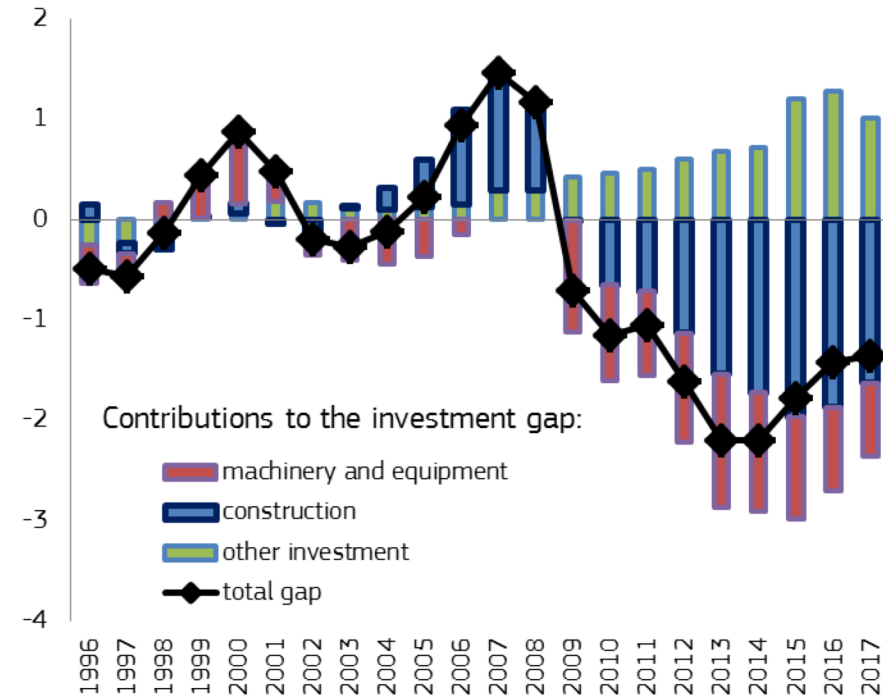
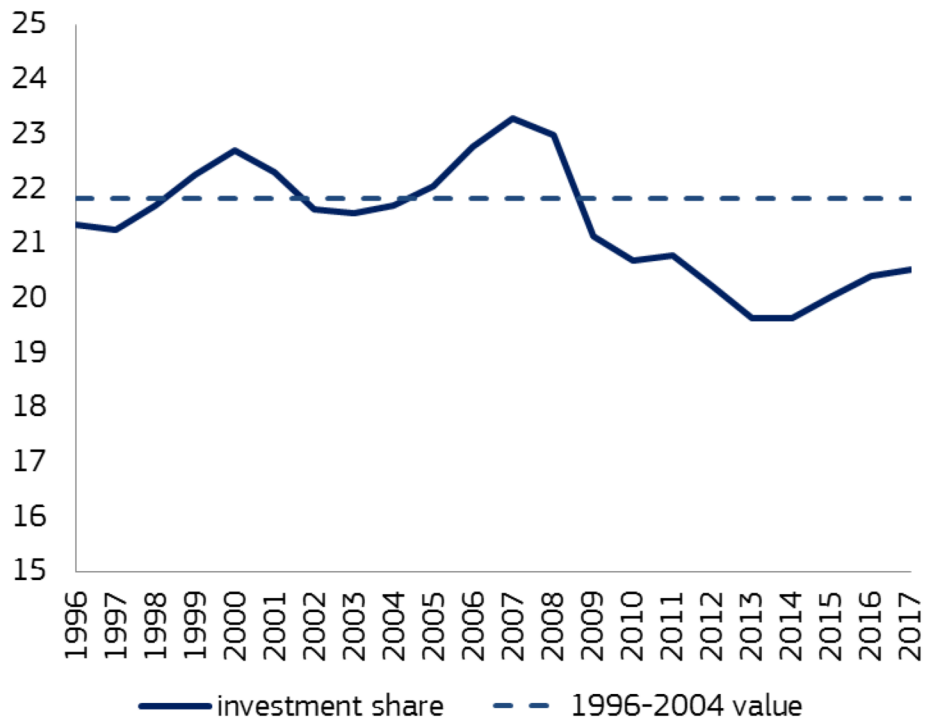


Composition of public spending, euro area, % of GDP

Allocation

Public investment: crucial for jobs and growth

Impact of the crisis in the euro area

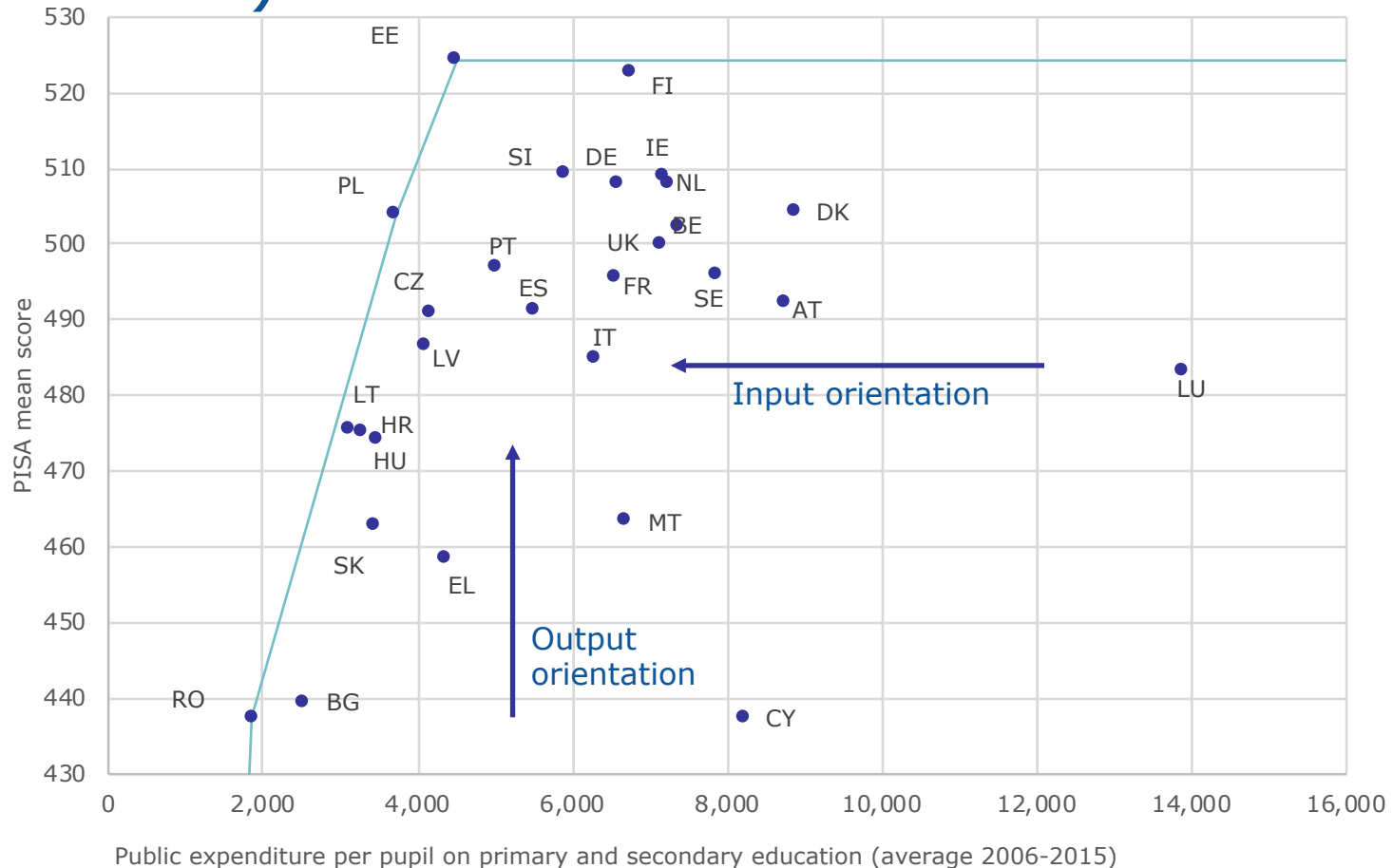


Source: AMECO

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

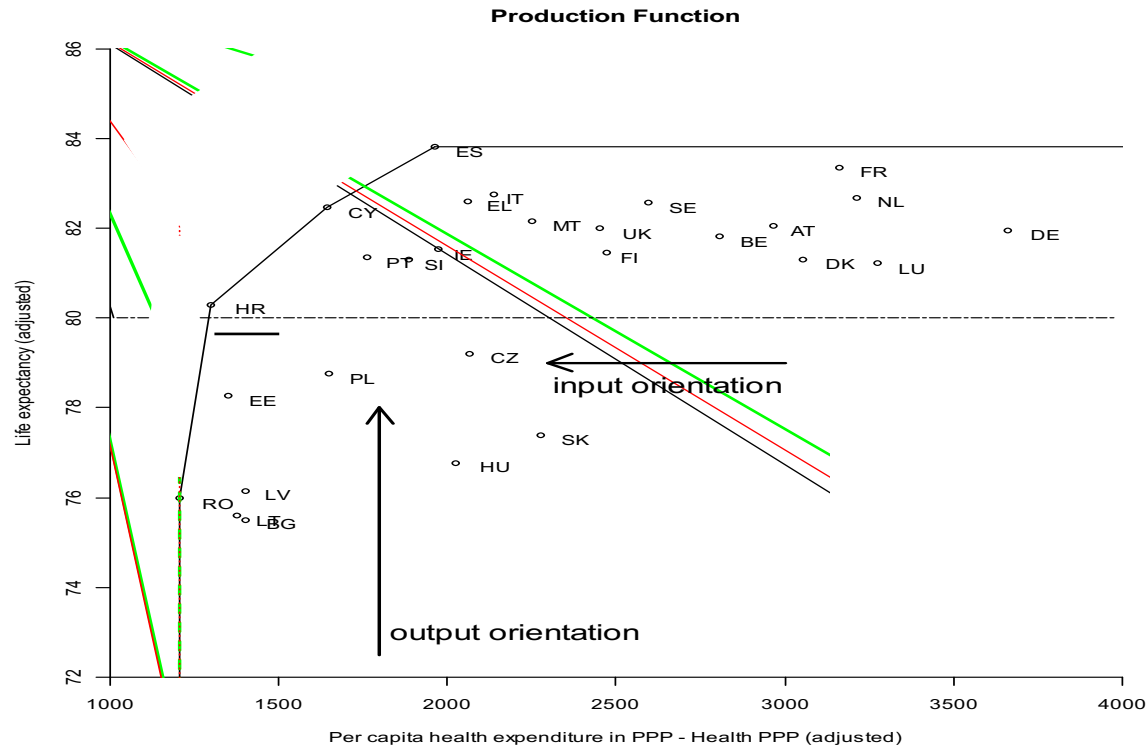
Allocation

Education: expenditure vs quality of education (Pisa scores)



Allocation

Health care: expenditure vs life expectancy

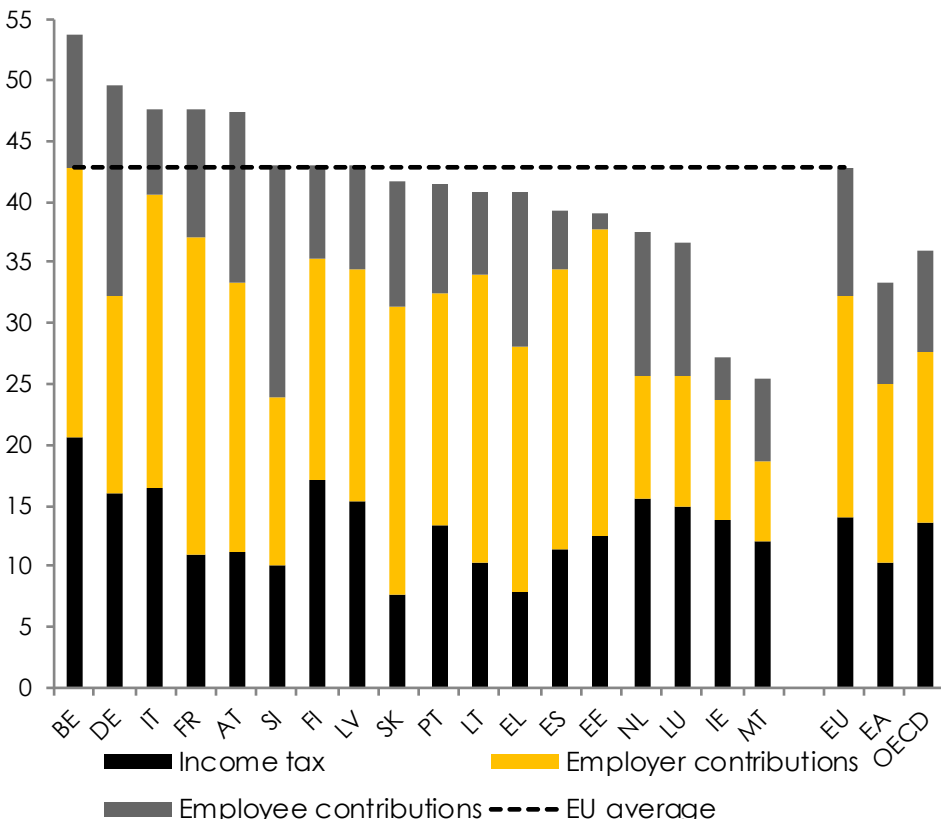


Output: life expectancy at birth (adjusted for lifestyle)
Input: per capita health expenditure in PPP (adjusted for lifestyle)

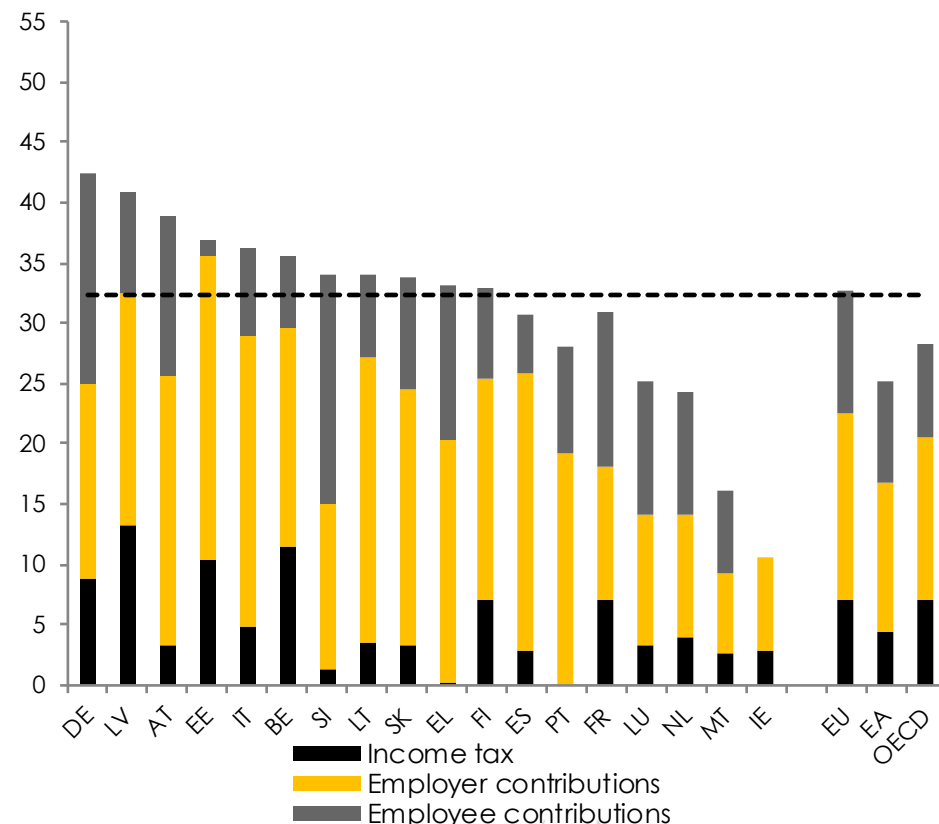
Allocation

Quality of public revenues: Tax burden on labour

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

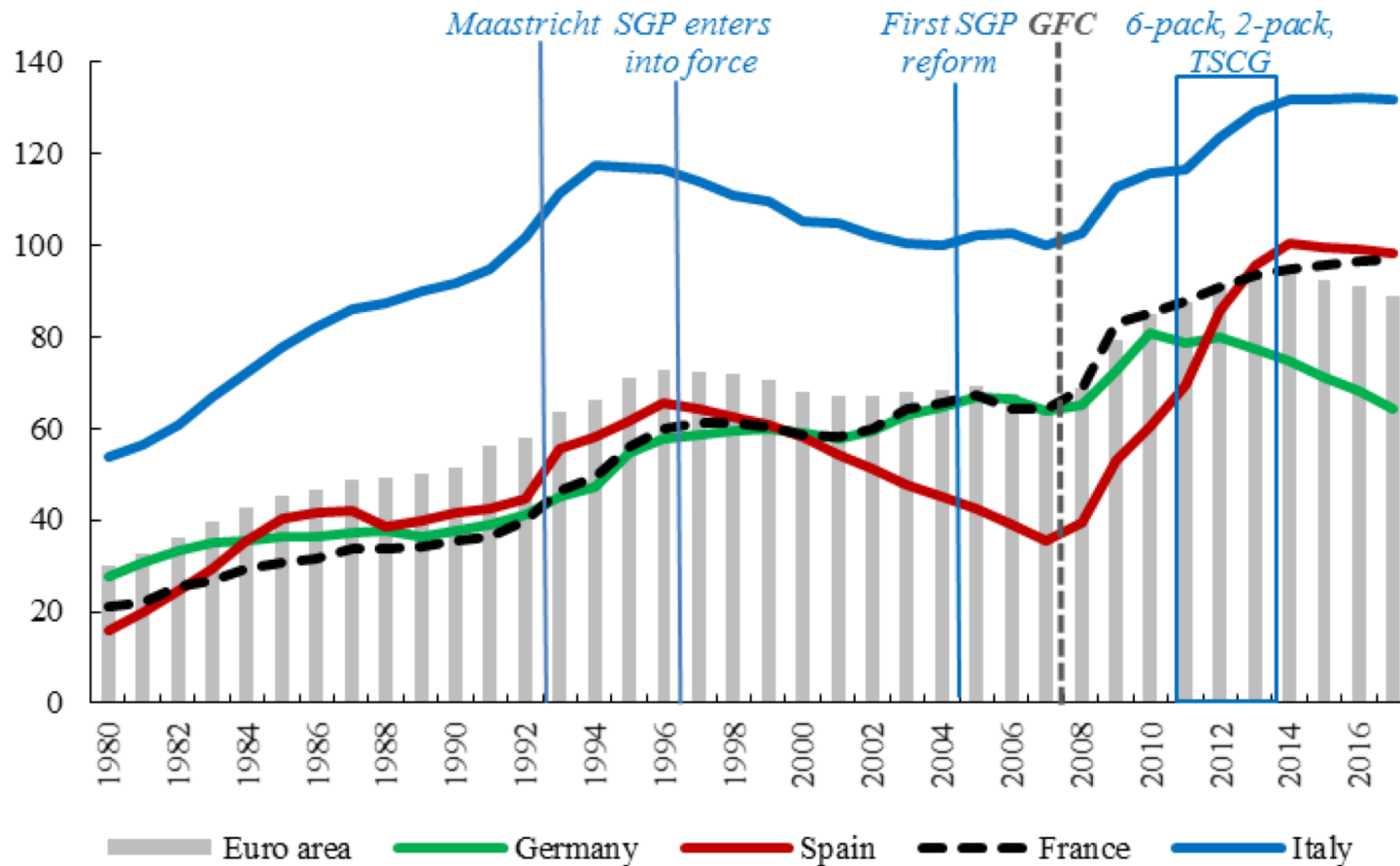


Tax wedge on labour, single earner, 50% of average wage (2017)



Sustainability

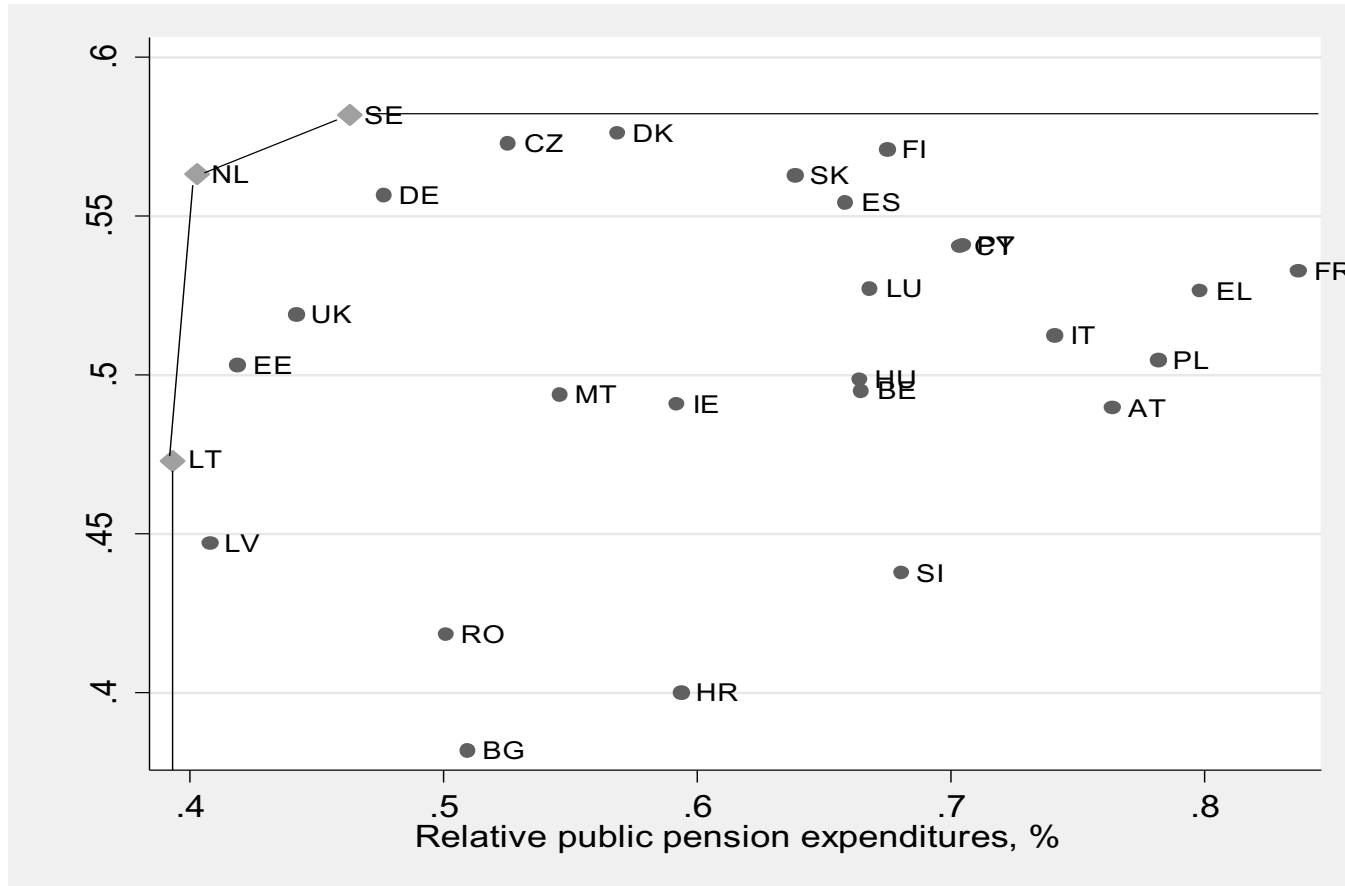
Debt developments in large EU countries



Government debt ratio (% of GDP)

Sustainability

Pension spending vs pension adequacy

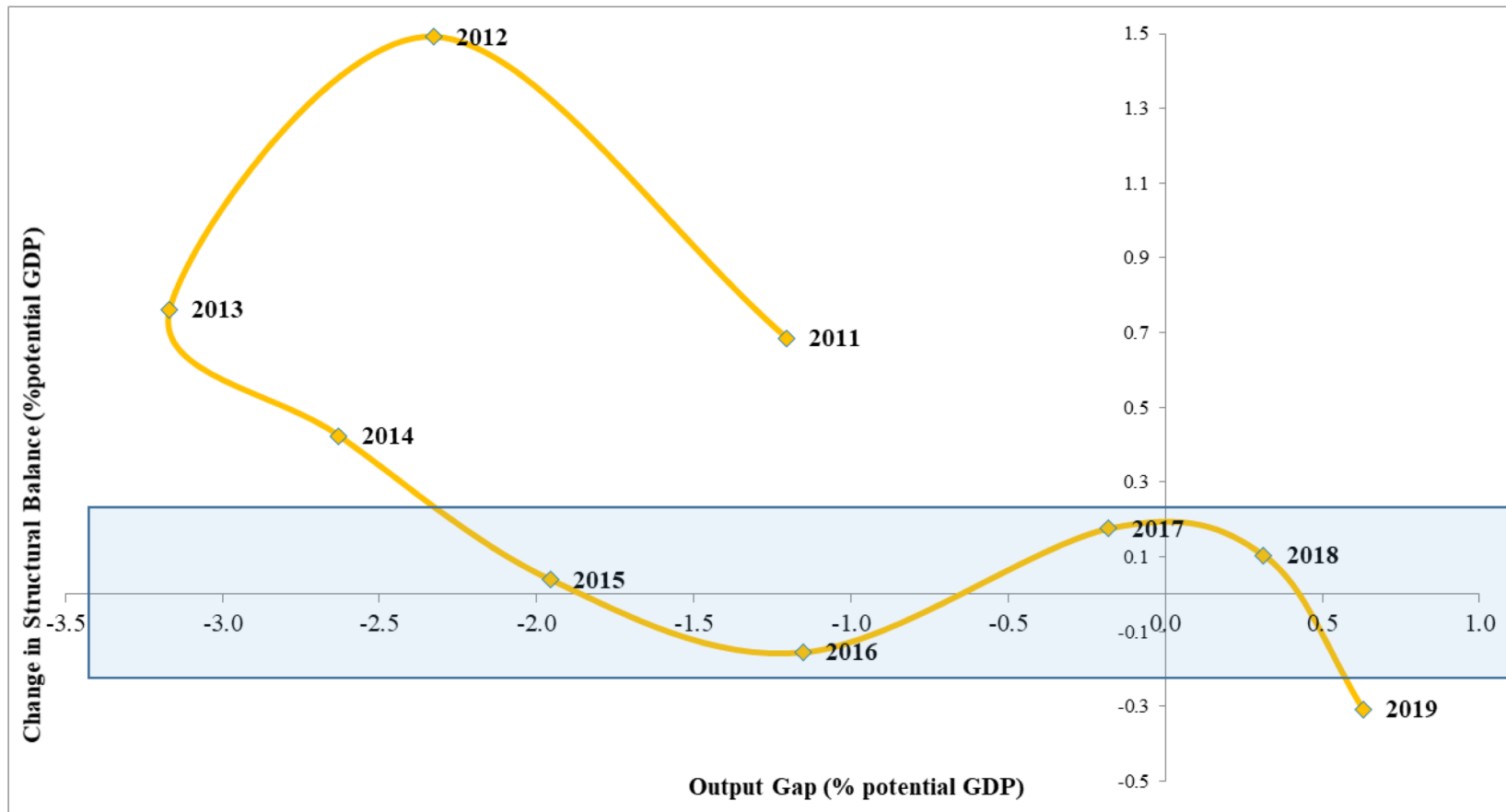


Stabilisation

Fiscal stance: correcting pro-cyclicality

Fiscal stance, EA, 2011-2019

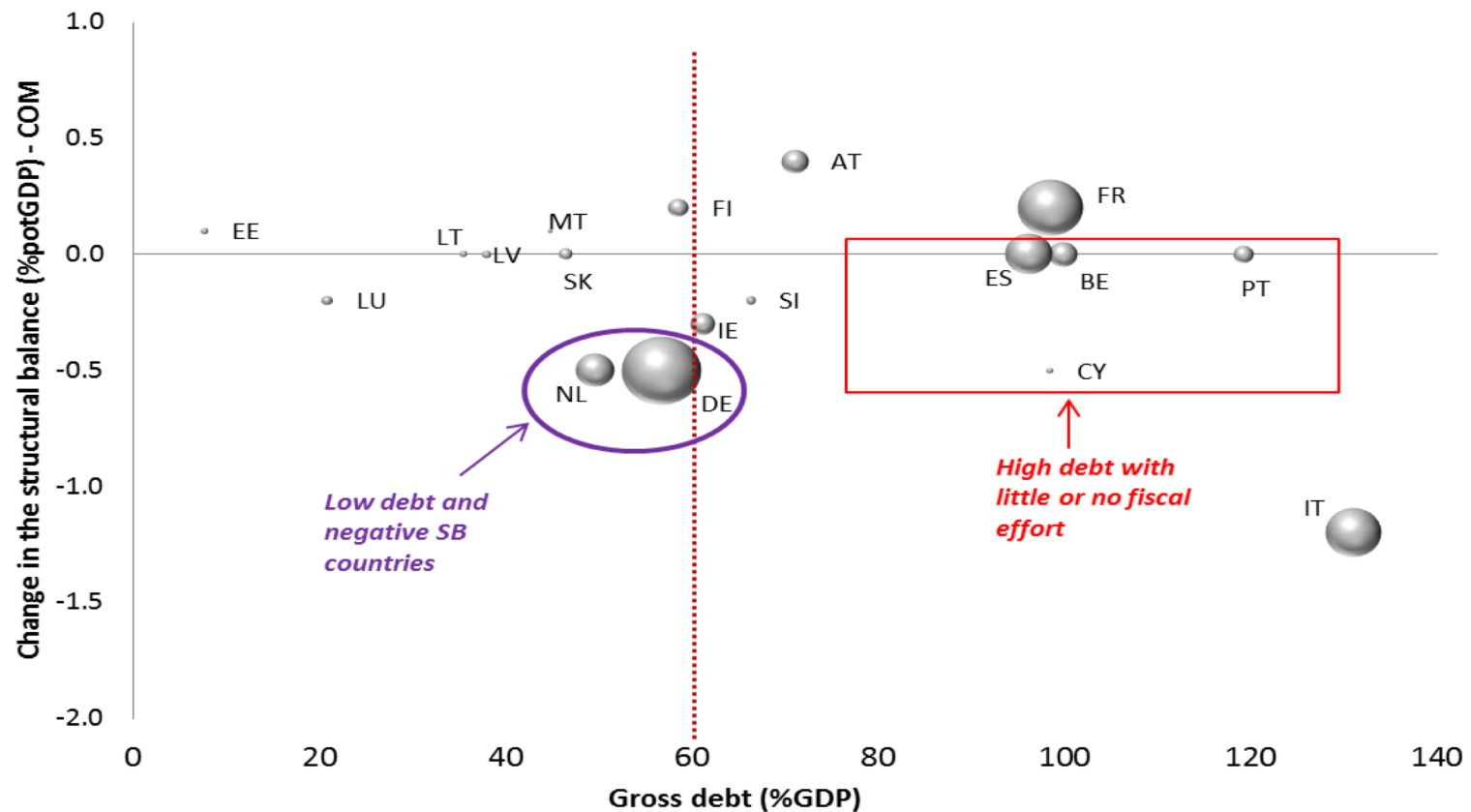
(Commission 2018 autumn forecast)



Stabilisation

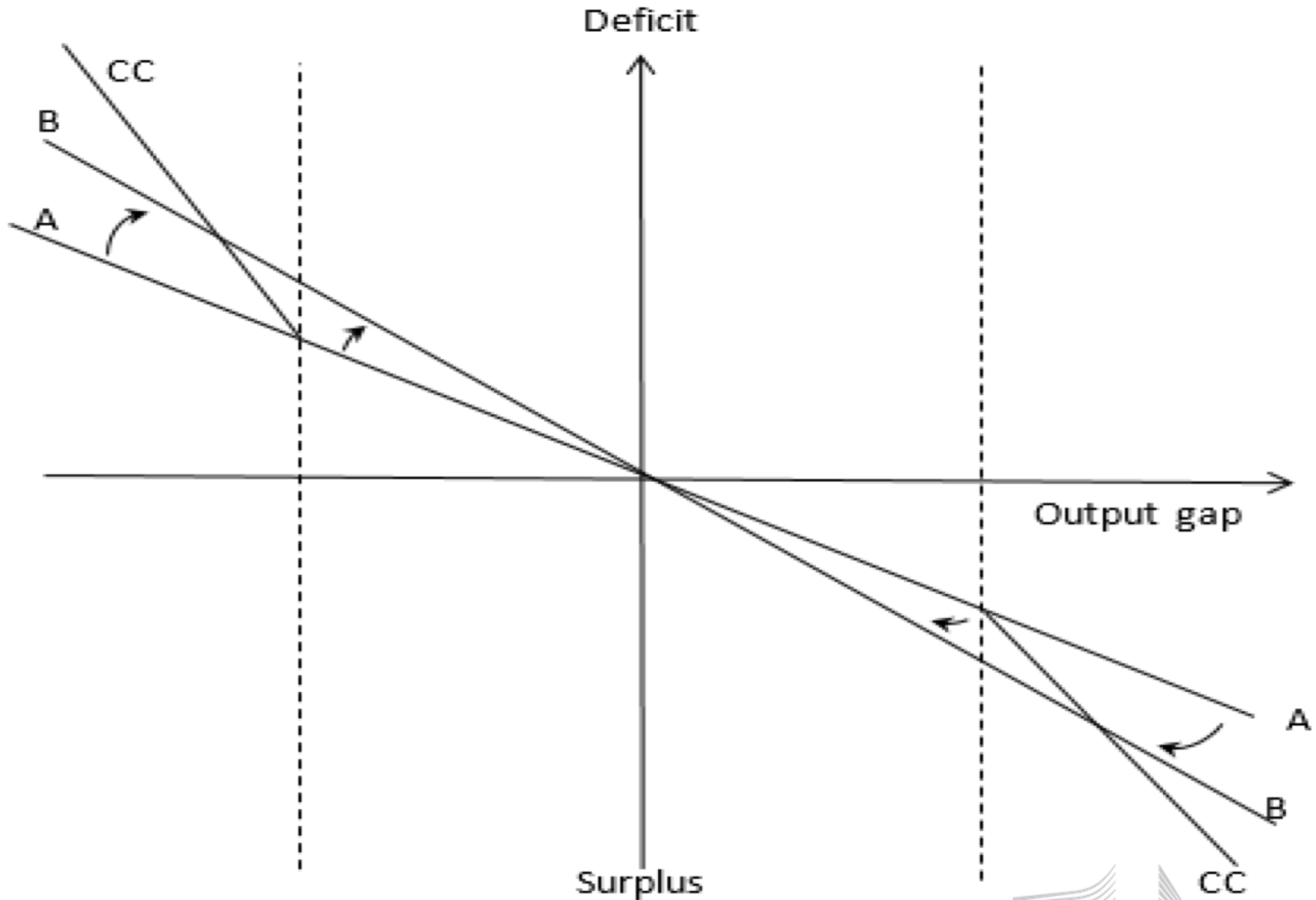
Rebuild fiscal buffers and use fiscal space where it exists

The fiscal stance, fiscal sustainability challenges and the cyclical position in 2019
(Commission 2018 autumn forecast)



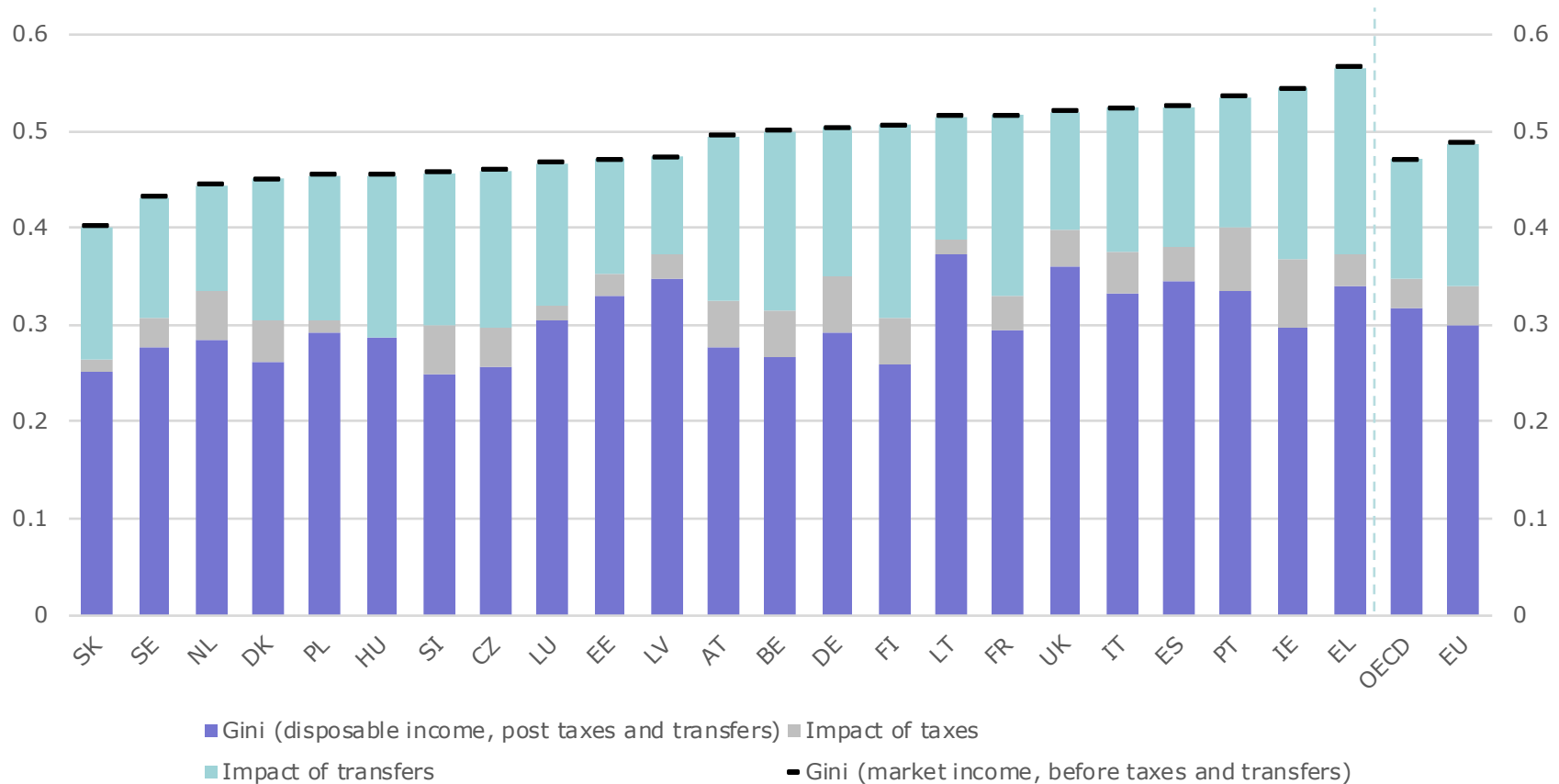
Stabilisation

Strengthening automatic stabilizers



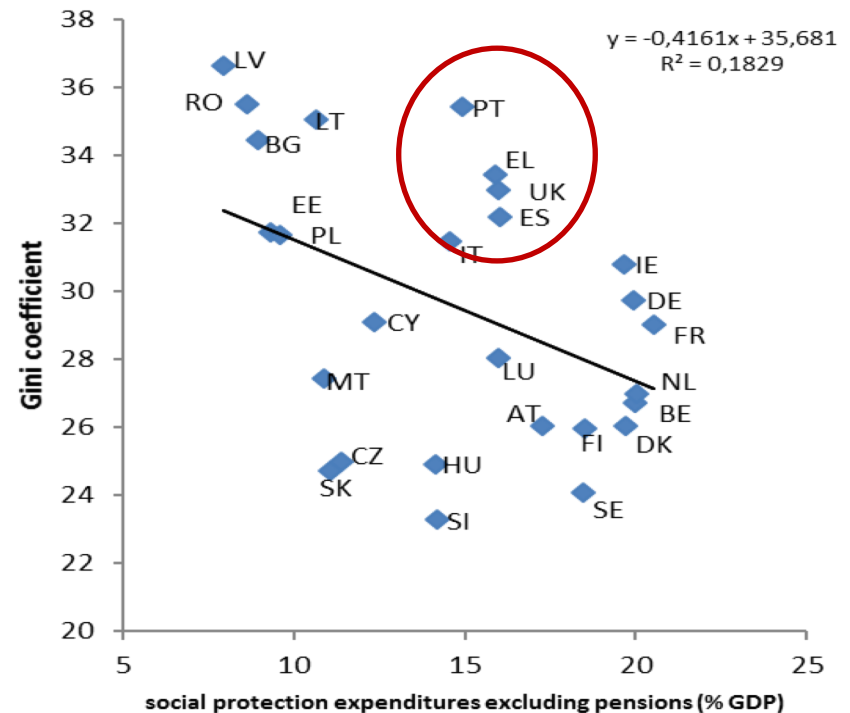
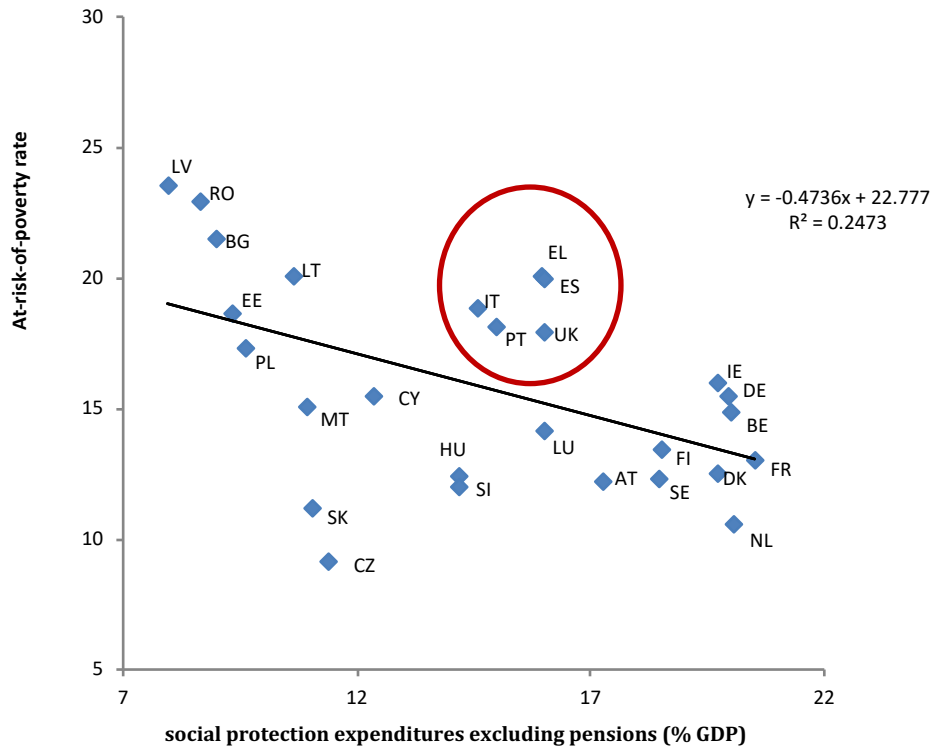
Redistribution

Tax and benefit systems to reduce income inequality and poverty



Redistribution

Better performing welfare systems



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

Delivery models: EU level

The European Semester as a tool to improve QPF

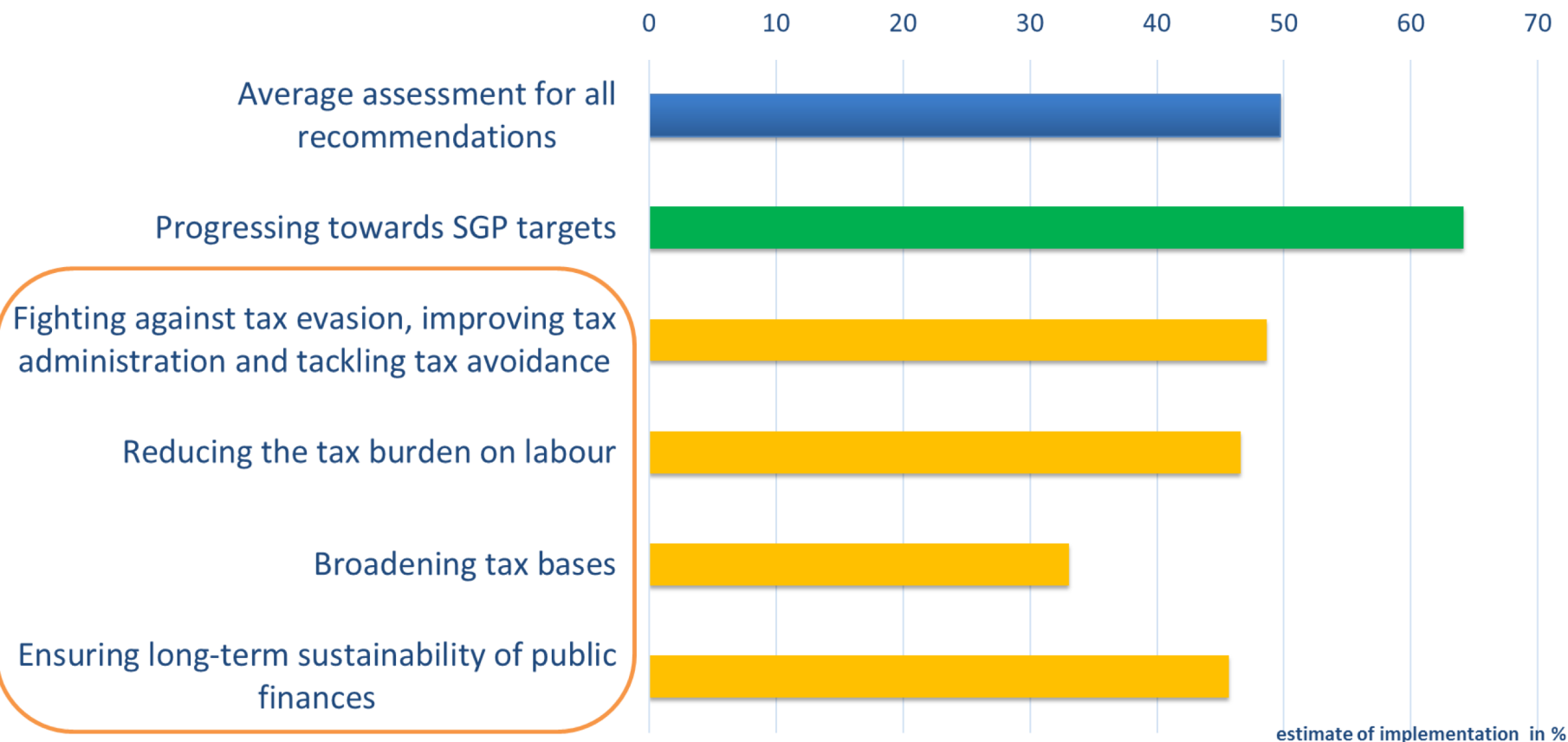
- **Considerations about the quality of public finance play a prominent role in the Country-Specific Recommendations**
- **On the revenue side the main focus is on:**
 - **Lowering the tax burden on labour** in a budget neutral way, especially by reducing tax wedge for low-wage earners combined with 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*)

Delivery models: EU level

The European Semester as tool to improve QPF

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)



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
 - CSRs
 - Flexibility clauses in the SGP
 - New tools: New EU public good in MFF proposal, InvestEU, EISF, RDT

Thank you for your attention!