



JOINT WORKSHOP BY IMF FISCAL AFFAIRS DEPARTMENT AND OFFICES IN EUROPE

THE FUNCTIONS AND IMPACT OF FISCAL COUNCILS

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The views expressed are those of the presenter



Learning from limited experience

- Independent fiscal councils are widely advocated
- Experience is limited
- National approaches are diverse
- Irish Fiscal Advisory Council's (IFAC) experience is limited (18 months)
 - analytical work improves understanding of issues
 - operation confirms how council can help



Ex Ante case (1)

- Bias in forecasts
- Bias in setting of stance
- Councils can overcome by:
 - reducing information asymmetry
 - monitoring
 - making actions more observable
 - changing political incentives
- *Sufficient condition = only councils can achieve*



Ex Ante case (2)

- Quality of budget analysis
 - forecast accuracy
 - policy deliberation
- Strengthening public debate
 - informed analysis
- Councils can overcome by strong incentives under mandate to focus on these issues
 - technical expertise/capacity
 - transparency
 - dissemination



IFAC's mandate

- Assessment of:
 - macroeconomic forecasts
 - fiscal projections
 - compliance with Budgetary Rule and correction mechanism (subject to EU SGP)
 - overall fiscal stance
- No mandate to make forecasts
- Narrow remit on rules
- Very open mandate on “stance”



Ex post analysis of forecast record

Actual growth rate minus forecast growth rate

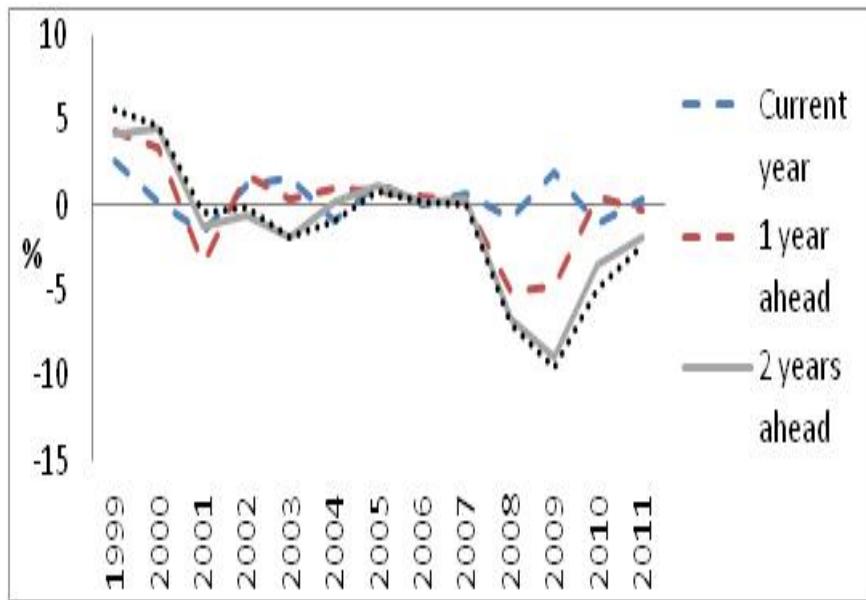
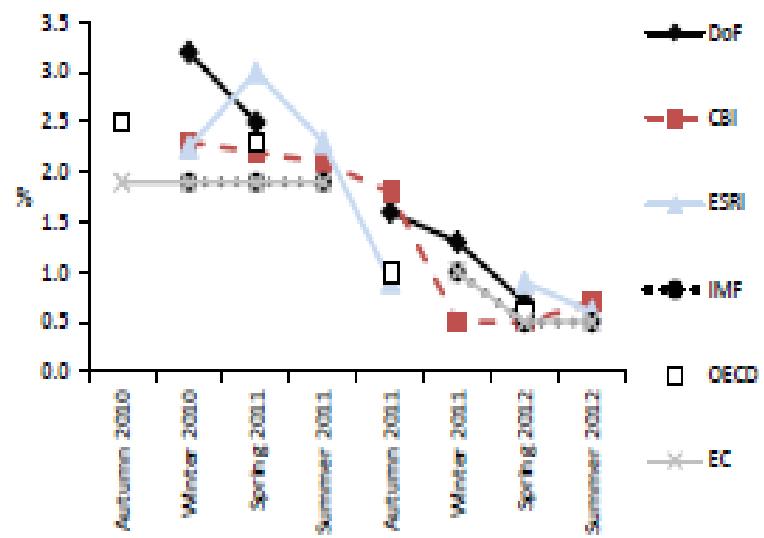


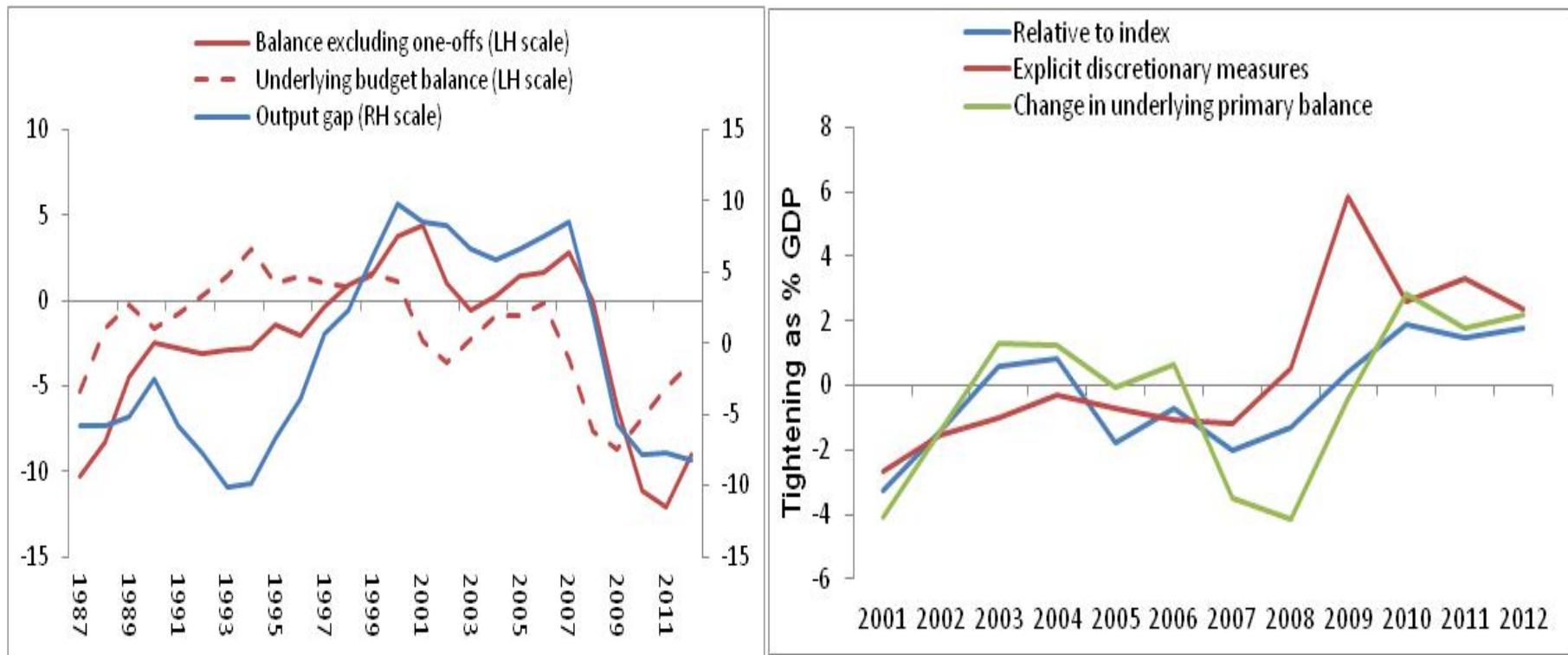
Figure 2.4a: Evolution of 2012 Real GDP Growth Forecasts¹²



- No bias on average
- Large and persistent errors
 - Revisions are key part of the picture



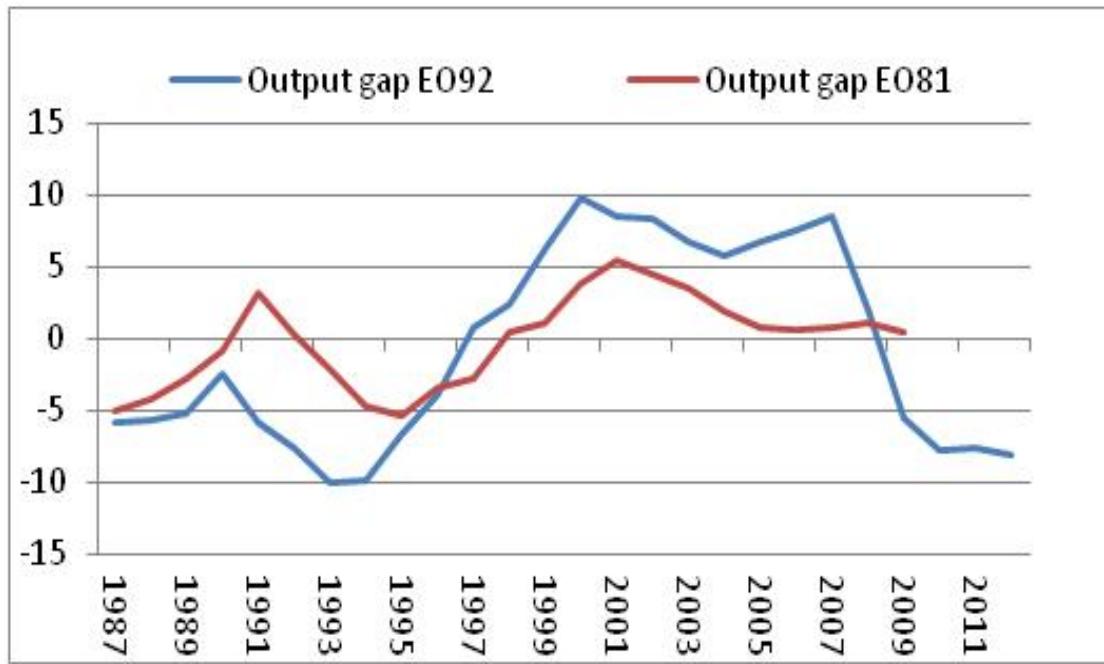
Ex post analysis fiscal stance (1)



- Stance appears too *loose* during boom
 - Too little to *tighten* policy against the cycle
 - True position less favourable



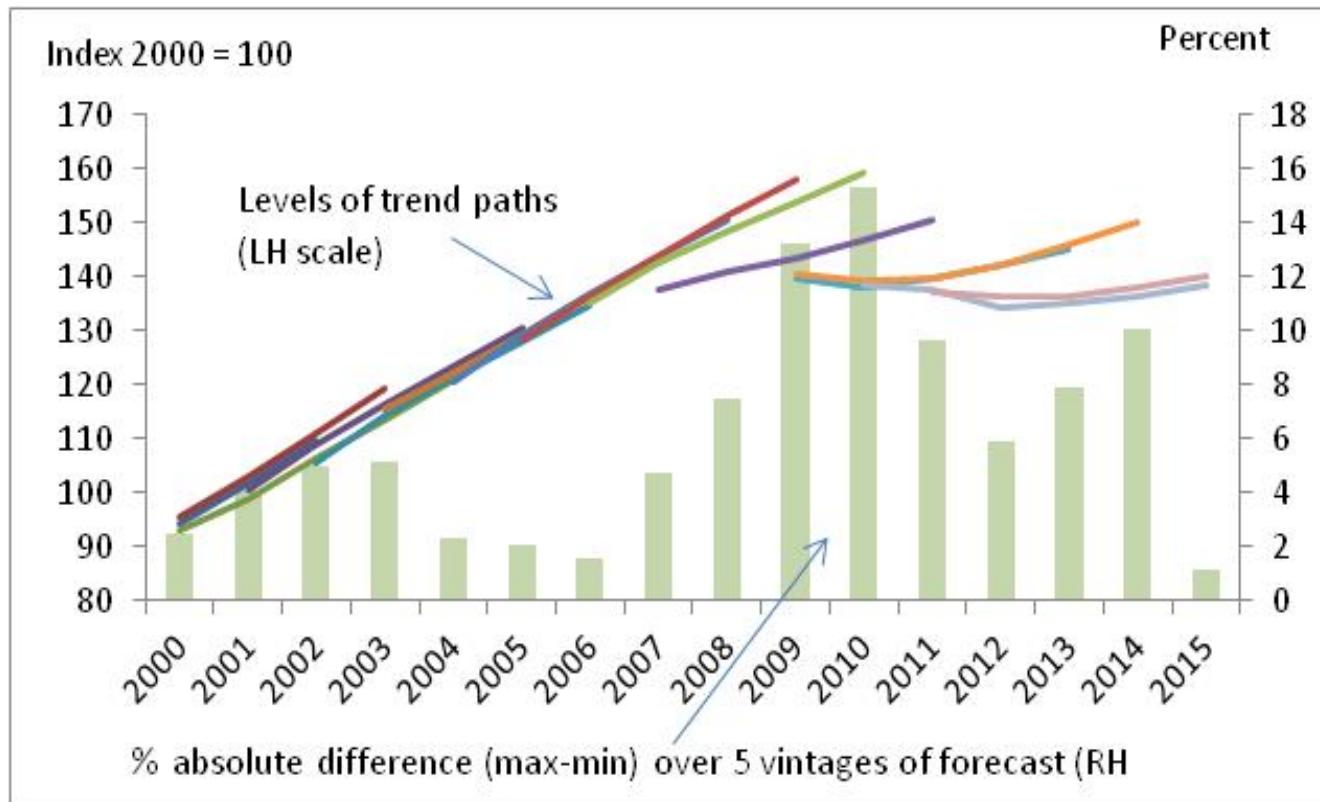
Ex post analysis fiscal stance (2)



- In real time, analysis did not signal
 - 2005 SPU had output 1.3% *below* potential
 - Small headline budget balance not unreasonable



Ex post analysis fiscal stance (3)



- Level and path of trend output misjudged
 - Cyclical/permanent spilt is critical



Forecast assessment

- Pre-IFAC assessments very limited
 - 1-year ahead, domestic comparisons, limited data
 - forecast errors not analysed systematically internally
- Difficult information problem to overcome
 - curse of dimensionality
 - limited data and transparency
 - difficult to communicate
- Need for local knowledge
 - forecasting GNP might be more useful?

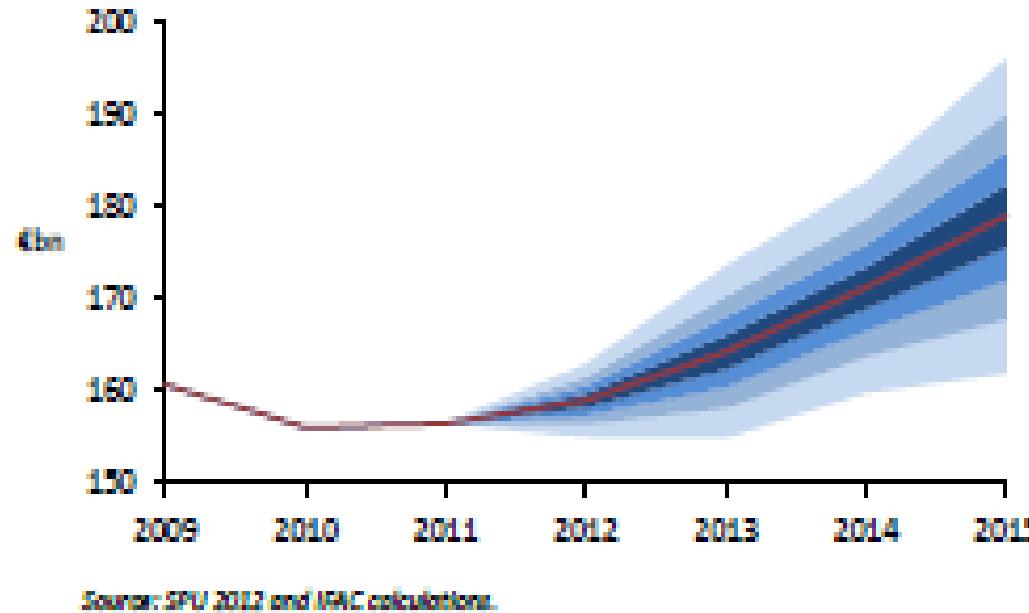


Open discussion of forecast errors

- Conflict of interest for forecasters
 - reluctant to discuss errors
- Herding tendency
 - all forecasts uncannily similar
 - outside forecasts no different
- Lack of analysis of errors limits learning
- IFAC not making forecasts is crucial
 - needs some tools



Open discussion of uncertainty



- Transparency around uncertainty
 - need to recognise errors/uncertainties
 - important for discussion of stance



Transparency

- Too little information published to assess
 - Annual data, selected components (volumes only)
 - No explanation of cyclical adjustments
 - Some tax bases not published
- More credibility than authorities
 - VAT forecasts were reasonable, but not believed



Fiscal stance

- IFAC policy line impossible to evaluate
 - Stance appropriate
 - Additional consolidation warranted
- Increasing response from government
- This message most prominent
 - little interest in forecasting work



How the council can close the gap

- **Specialised capacity to address**
 - 3 more analytical staff
 - Council – 5 members
 - Deliberative process
- **IFAC gets public attention and viewed as credible**
 - expert
 - independent
 - mandated (“government’s own watchdog”)
- **This cannot be easily replicated by other bodies**
 - attention to domestic factors



Conclusion

- Political bias problem not central
- Technical/transparency roles are key
- Council does meet a need
 - needs resources/credibility/legitimacy
- Hints for future direction of council
 - Examining forecast *process*
 - Focus on medium-term
 - Communication is difficult but critical