



# **Fiscal Rules and Large Shocks**

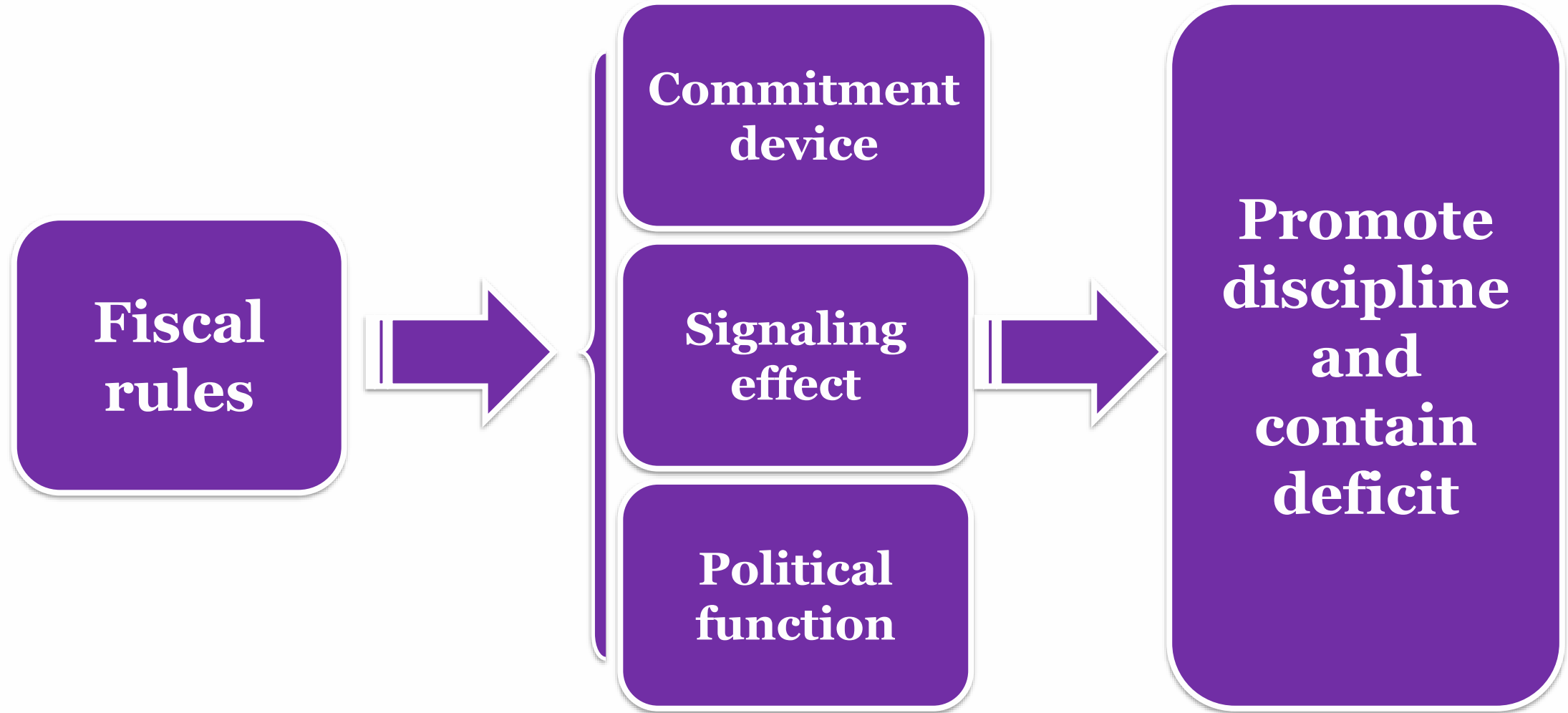
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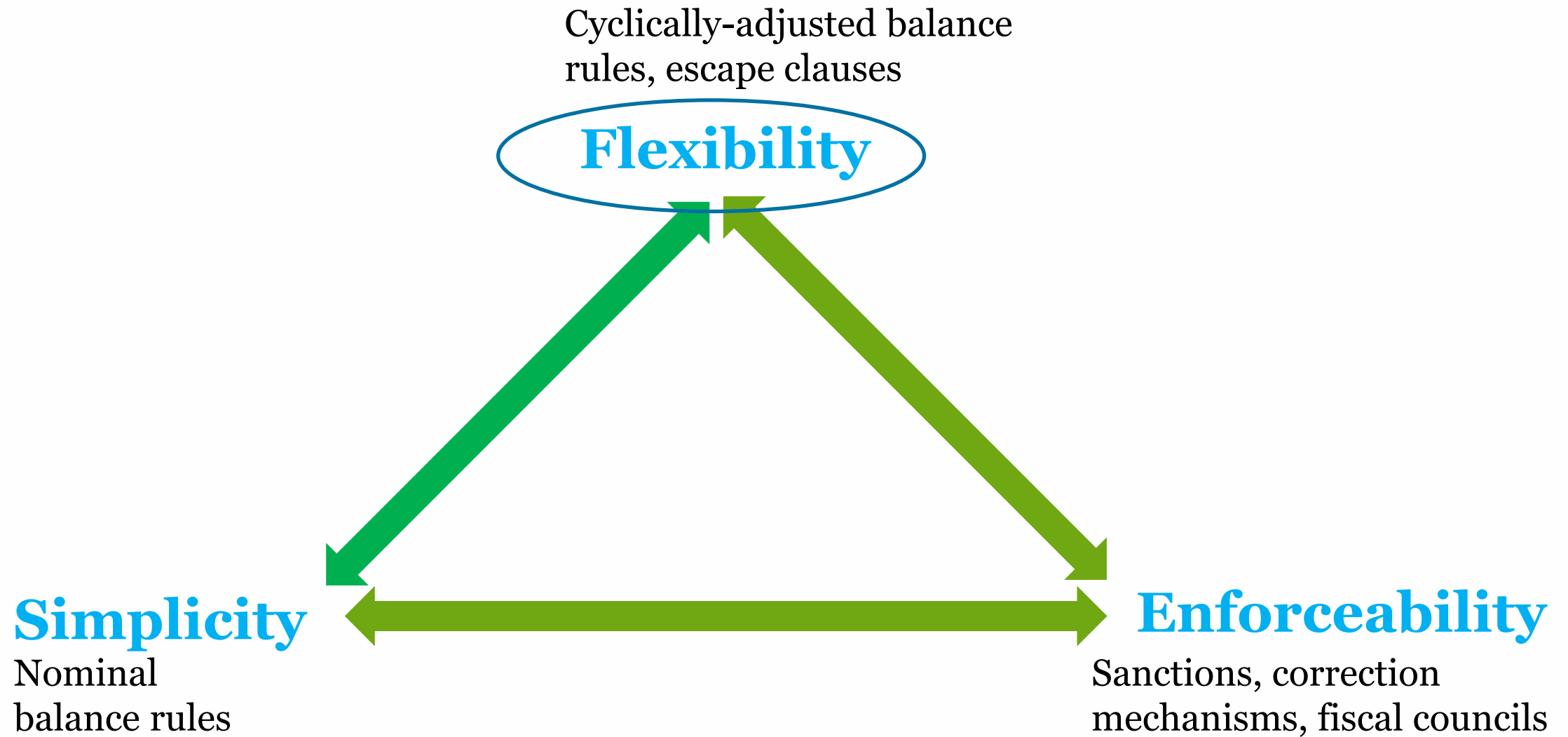
Fiscal Affairs Department

Presentation at the Joint Vienna Institute

# Main objective of fiscal rules is to contain excessive deficits



# A Balancing Act



# There have been several reforms since 2008

## Escape clauses

- ❑ Define conditions and period over which rule is suspended
- ❑ Adjustment to be applied to revert to the rules
- ❑ EU countries, Colombia, Georgia, Jamaica, Tanzania

## Other reforms

- ❑ Correction mechanisms (Grenada, Mongolia, Panama, Peru)
- ❑ Independent body monitoring rules (EU, Peru, Kenya, Uganda)

# When to activate the escape clauses?

## General principles

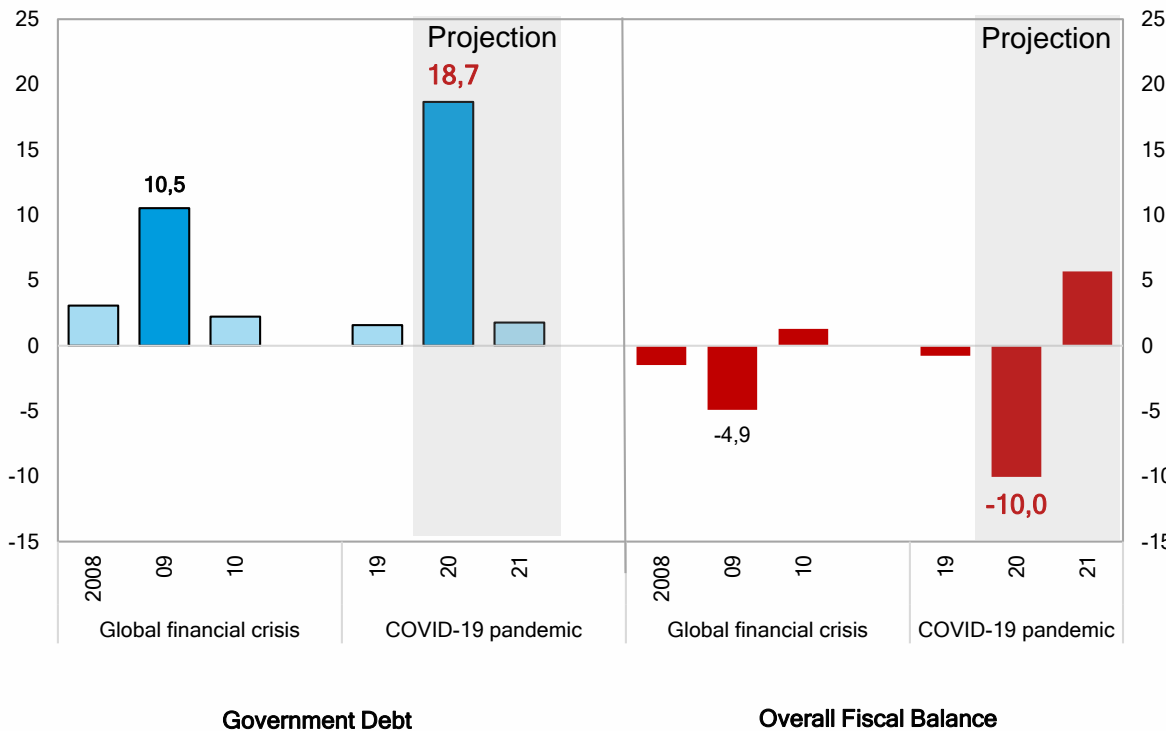
- Events triggering the activation should be outside government's control
- Severe economic downturns, large natural disasters, and states of emergency
- The size of the deviation should be linked to the policies directed at the crisis

## Pandemic

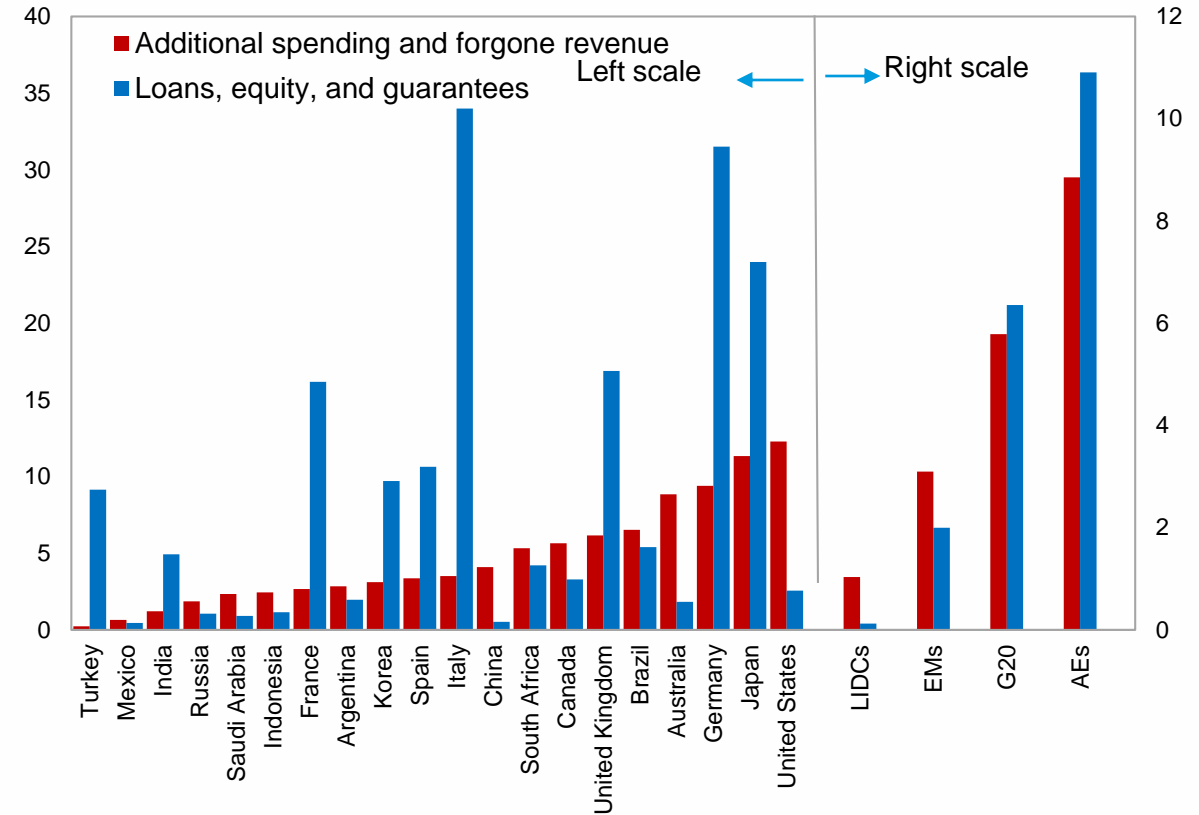
- Health costs due to crisis
- Large fall in economic activity
- The budgetary impact: automatic stabilizers and discretionary measures

# Debt and Deficits

## Change in Global Government Debt and Overall Fiscal Balance (Percentage of GDP)



## Country Fiscal Measures in Response to the COVID-19 Pandemic (Percent of GDP)



Sources: IMF World Economic Outlook, National authorities, and IMF staff calculations.

# How to activate the escape clause?

## The proposal should preferably explain:

- The reasons for activating the clause
- the period over which the rule will be suspended
- the adjustment to be applied to revert to the rules

## Parliamentary approval

- Budgetary impact
- Help ensure the escape clause is being used appropriately

## In practice, countries are using different approaches

- supranational mechanisms
- supplementary budgets
- using structural rules or declaring national emergencies

## Procedures to return to compliance

- ❑ Appropriate balance to avoid economic disruptions
- ❑ Some escape clauses define precise time or conditions to return to compliance with rule

## High uncertainty around the pandemic

## Effective monitoring and control

- ❑ Independent fiscal councils, audit institutions



## Credible medium-term fiscal strategy to anchor expectations

- ❑ Baseline scenario
- ❑ Risks and possible alternative scenarios

## Regular reports by the government

- ❑ Objectives of all the programs and measures, their fiscal costs, and potential risks to the budget (e.g. contingent liabilities)

## Reports by independent agencies

**In the absence of escape clauses: temporary suspend fiscal rules?**

- Impede appropriate response**
- Follow legal procedures**
- Parliament could establish the conditions**

**Revisions to escape clauses if not flexible enough**

**Revising fiscal rules?**

- Large shock**
- Make the rule-based framework more resilient**
- There are potential costs to change**

**THANK YOU!**