

Improving fiscal policy in the EU.
The Case for independent forecasts.
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Two types of comments

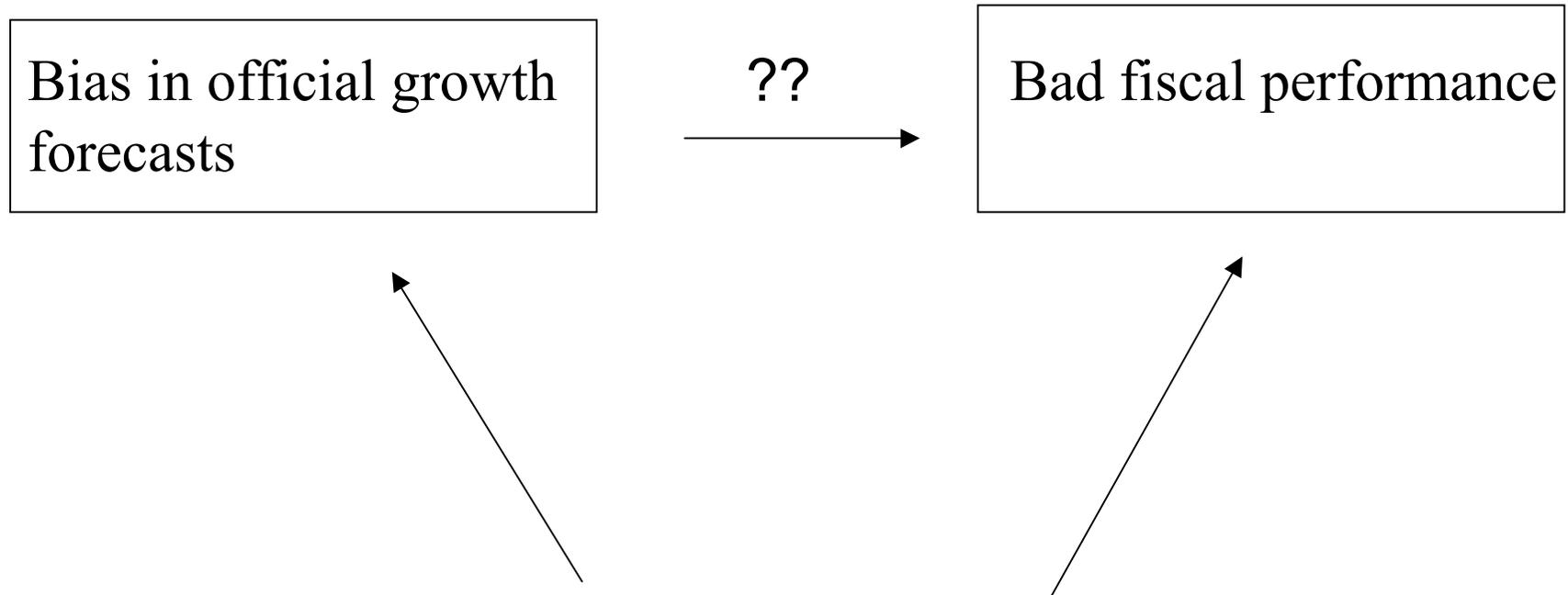
- on the analysis of the present situation
- on the policy recommendation itself

- Main message of the positive section of the paper:
 - official growth forecasts are biased (over optimistic)
 - The positive bias affects the cyclically-adjusted primary deficit
- Some questions on the empirical section
 - Paper is persuasive on first point, less so on the second
 - Why so few countries (4)? In more comprehensive study, Strauch et al. (2004) have the EU15

–The message that Commission is much better than governments at forecasts is overstated except for Germany Table 1b

Country	Mean bias	No bias (proba)
Germany (official)	-0.95	0.00
Commission	-0.24	0.52
France (official)	-0.45	0.23
Commission	-0.18	0.57
Italy (official)	-0.94	0.01
Commission	-0.58	0.01
UK (official)	0.02	0.96
Commission	0.16	0.63

What is exogenous and causal?



Fundamental political and institutional features: political instability, electoral rules, fragmentation/centralization of budget process

- The explanation of the better forecast record for UK is not in terms of independence of forecast institution
- To be convinced that quality of forecast matters, need to control for these fundamental institutional features (not affected by independent forecasting institution) and see whether the forecast error still has an impact on the fiscal outcome
- There is data (see work by von Hagen for example) on the extent of centralisation/fragmentation of the budgetary process + electoral rules (Persson and Tabellini)

- The proposal of independent forecasts
 - what is the view on the political-economy problem that causes the deficit bias?
 - 1) public spending involves delegation + principal-agent relations with issues of asymmetric information between the public and the politicians?
 - independent (better) forecast would improve information, accountability and politicians incentives to deliver policies preferred by voters but then there is already quite a lot of competition on forecasting business (see lately French debate)

2) Is it a problem of “common pool” property of public budgeting : politicians do not internalize fully the true marginal cost of public spending

– Empirical evidence (Poterba+Von Hagen) that institutional reforms that lead to less fragmented and more centralized (strong role of Ministry of Finance) budget process helps

– In what sense would independent (unbiased) forecasts help?

What is the mechanism through which independent forecasts help resolve deficit bias?

- The content of the proposal: independent forecasting institution
- Much less radical than proposal by Wyplosz for independent fiscal authority on the model of independent central banks
- Certainly more politically acceptable. More difficult for politicians to argue that forecast should remain a political decision
- Is this interpreted as a first step towards independent fiscal authority?

- The parallel with independent central banks is interesting but also reveals some conceptual weaknesses of proposal: can you go only halfway?
- Would we want an independent institution that forecasts inflation with a (dependent) central bank that decides interest rates/money supply?
- Is it sensible or feasible to distinguish fiscal policy decisions and growth forecasts?
- Growth forecasts are dependent on fiscal policy decisions
- Fiscal policy decisions are dependent on the growth forecast

- How do you make the forecast and decision process logically consistent?
- Should the forecast institution assume unchanged fiscal policy?
- Danger that fiscal policy becomes too inflexible ?
- Would large fiscal contractions or expansions (non linear effects) be possible in such a framework?

- The authors need to be more precise on the institutional framework: e.g. proposal that Ministry of Finance is obliged to adopt forecasts in the planning of budget
- Could there be some cooperation/ coordination between forecast institution and the government?
- A possibility would be that the government “feeds” the forecast institution with fiscal policy choices and the independent institution generates forecasts of both growth and deficits

- No need for this institution to be European
- What is the European externality in forecasts production?
- If main advantage is more transparency and accountability in fiscal debate, this should be done at the national level: subsidiarity principle should apply
- Other reforms of fiscal process may be much more important: e.g. check ex-post spending by independent court