Public Financial Management

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Motto

The multiple, intersected crises and the mounted responses at all levels have stretched public financial resources to the limits, with many or even most countries facing critical debt distress.

The question is: „How to ensure that fiscal limits won’t derail critical financing needed for the implementation of SDGs?

Background: crisis and public finance

- The standard (and common) problem related to public finance in times of a crisis is the disbalance between public revenues and public needs to finance „the state“ (its economic, social and administrative functions).
- Public revenues normally decrease, because of stagnation or even depression.
- The demands for public expenditure always increase, as the state needs to finance extra social and macro-economic actions.
- „Trade off“ is created between resources and needs.

How to manage the „trade off“: deficit?

- „Standard“ (for most streams of economic theory) solution is deficit budgeting.
- However, deficit budgeting has its strict limits (for example the EU Maastricht criteria expect that public deficit should be below 3% of GDP and public debt below 60% of GDP, to prevent fiscal crisis).
- Countries should utilize „good times“ to **create fiscal reserves** (but most of them do not do so!).

How to manage the „trade off“: inflation?

- Inflation is normally the result of a crisis, as deficit financing is inflationary in nature. However, for some governments it may „look“ as solution to limited fiscal capacity (printing money and relative decrease of the sum of public debt) – however, **inflation is „bad servant“.**
- In the early phase inflation may increase public revenues, especially via increased VAT collection. Some governments may appreciate this and use extra resources generated in this way – not recommended, as long term consequences of inflation are critical.

How to manage the „trade off“: cuts?

- Public expenditure cuts during the crisis may have two forms:
  - a/ „Cross-sectional“ cuts: cutting budgets but fixed percentage at all levels) – not best choice during the crisis.
  - b/ **„Selective“ cuts**: revision of all public expenditures and seeking for efficiency gaps – preferred! As example, improved public procurement is the path for most developing and transitional countries (may „save 2-3% of GDP!!!).

- States are advised to create and utilize „fiscal watch-dogs“, bodies which not only monitor fiscal discipline, but also pro-actively search for efficiency gaps.

How to make a difference? Through improved budget credibility to better SDGs achievement

Widespread budget credibility

- justified - sudden unexpected circumstances
- unjustified - poor administrative capabilities or policymakers pursuing own opportunistic interests

2030 around the corner → urgent actions by national governments, parliaments, fiscal councils, state auditing institutions (SAIs), civil society…

How to make a difference?

National governments:

- improve budget transparency and budget processes
- better target and prioritize spending for planned goals, and avoid unnecessary and unexplained deviations
- particularly governments of lower income countries where consequences are more pronounced
- however, all governments have to improve their VNRs to reflect both overall and sectoral deviations
- introduce or strengthen fiscal rules and fiscal councils
- ensure conditions for independent functioning of fiscal councils and accessible and inclusive public communication

How to make a difference?

Parliaments / legislatures

- strengthen their capabilities and establish competent budgetary committees and offices
- while MPs should educate themselves in budgetary issues to be able to keep governments accountable

Fiscal councils, where existing

- use their independence and competencies for hawkish control of budgetary figures.

How to make a difference?

SAIs

- The role of SAIs can’t be overemphasized.
- They should have everything under control, from prebudget statements to budget execution reports.

SDGs, budget transparency, participation, credibility, etc., are **not just constantly repeated mantras**.

- To make a difference → **steps to improve all of them**: budget transparency, participation and credibility.
- And **not gradual, but as fast as possible**.