Finansdepartementet

Arbeidsnotat 2017/9

Analysis of Economic Developments in Budget Documents in Scandinavian Countries – A Comparison

Magnus Saxegaard

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Forord

Denne rapporten sammenligner de økonomiske analysene og hvordan de innvirker på politikkformuleringene i budsjettdokumentene i de tre skandinaviske landene. Rapporten legger særlig vekt på følgende spørsmål:

- Er det forskjeller i beskrivelsene av den økonomiske utviklingen og de økonomiske utsiktene mellom de tre landene?
- Hvilken rolle spiller økonomisk analyse for motiveringen av finanspolitikken?
- Hvilken rolle spiller tallfestede modeller i analysen av den økonomiske utviklingen og for utformingen av finanspolitikken?
- Hvilke faktorer forklarer forskjellene mellom landene?
- Kan det trekkes noen lærdommer for de norske budsjettdokumentene?

Rapporten er laget etter ønske fra Finansdepartementets modell- og metodeutvalg. Dette utvalget er opprettet for å bidra med faglige vurderinger og råd blant annet om utvikling og bruk av modellverktøy, med sikte på at analyseverktøyet som benyttes i departementet skal være effektivt og godt tilpasset formålet. Utvalget gir også råd om den faglige fremstillingen av makroøkonomiske problemstillinger i budsjettdokumentene. Utvalget består av fremstående norske akademikere, representanter fra Norges Bank og Statistisk sentralbyrå og forskere fra Sverige og Danmark. Finansdepartementet er sekretariat for utvalget.

Seniorrådgiver Magnus Saxegaard har hatt ansvar for rapporten. Rapporten har trukket på diskusjoner i Modell- og metodeutvalget, og særlig på kommentarer fra professor Torben Andersen som er med i utvalget.

Juni 2017

Hans Henrik Scheel

Finansråd

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1 Introduction

During the December 14, 2016 meeting of the Advisory Panel on Macroeconomic Models and Methods (MMU) at the Norwegian Ministry of Finance, it was proposed that a comparison of the economic analysis and its impact on policy formulation in the budget documents of the three Scandinavian countries would be useful. This report is a response to that request. In particular, this report aims to answer the following questions:

(i) How does the description of economic developments and the economic outlook differ among the budget documents of the Scandinavian countries?

(ii) What role does economic analysis play in motivating fiscal policy?

(iii) What role do economic models play in the analysis of economic developments and the macroeconomic impact of fiscal policy?

(iv) What factors explain differences in the analysis of economic developments across the three countries?

(v) What lessons can be learnt regarding the use of economic analysis in the Norwegian budget documents?

This note is not the first study that analysis the conduct of fiscal policy in Scandinavian countries. The OECD Journal of Budgeting has published reviews of budgeting in Norway (Anderson et al., 2006), Denmark (Blöndal and Ruffner, 2004), and Sweden (Downes et al., 2017), while there are several official documents that outline the fiscal frameworks of the three countries. In addition, a committee led by Professor Øystein Thøgersen prepared a report in 2015 on the Norwegian fiscal framework (Norwegian Ministry of Finance, 2015), while Andersen (2013) has published a paper on the Swedish fiscal policy framework and intermediate fiscal policy targets. The IMF has published Reports on the Observance of Standards and Codes (ROSC) on fiscal transparency in Norway (IMF, 2009) and Sweden (IMF, 2000 and 2002), while the International Budget Partnership regularly publishes a standardized set of transparency indicators for a broad range of countries in the context of the Open Budget Survey (International Budget Partnership, 2015). However, to the author's knowledge this is the first study comparing the analysis of economic developments, and how it relates to the fiscal policy formulation, in a cross-country context.

The information in the report is based on the author's reading of publically-available documentation, and comments from numerous people including Per-Mathis Kongsrud, Frank-Emil Jøssund, Kristine Høegh-Omdal, Kristin Solberg-Watle, Kari-Anne Haugen, Pål Sletten (all Norwegian Ministry of Finance), Mads Kieler (Danish Ministry of Finance), Åke Nordlander, Karl Bergstrand, Jonas Norlin (all Swedish Ministry of Finance), and Ylva Heden (NIER Sweden). Special thanks are due to Torben M. Andersen for his role as discussant during the presentation of a preliminary version of this report in the April 29, 2017 meeting of the MMU.[1]

[1] The views expressed in this study are those of the author, and do not necessarily describe those of the Norwegian Ministry of Finance.

2 Budget Process

As a preamble to the rest of this report, it is useful to compare the budget process in the three Scandinavian countries. Not only will this help identify in what documents, and at what stage of the budget process, the assessment of the economic outlook is made, but it may also help explain differences in the analysis of economic developments between the three countries.

Table 1 provides a stylized representation of the main elements of the respective countries' budget processes. Solid boxes indicate an event associated with the publication of a document, whereas half-shaded boxes represents steps in the budget process that are not accompanied by the public release of any documents.

It is clear from Table 1 that the budget cycle in all three countries is a continuous process. However, there are important differences in how often the economic analysis that lays the foundation for the budget is published.

In Denmark, this analysis is primarily presented in quarterly economic reports ("økonomisk redegørelse") that provide updates on the economic outlook for both the current and next fiscal year, and an analysis of the implications for the fiscal policy stance under the assumption of unchanged policies. In Sweden, the economic analysis underlying the budget is published in the spring budget bill ("ekonomiska vårproposition") and the budget itself ("budgetpropositionen"). In addition, as part of their commitment under the EU Stability and Growth Pact both Denmark and Sweden publish annual convergence programs that include an assessment of the medium-term economic outlook. Denmark also publishes an annual update of their medium-term plan (currently "DK2025"). In Norway, the economic analysis underlying the budget is published at the time of the actual budget in October ("nasjonalbudsjettet"). The revised budget in May ("revidert nasjonalbudsjett") also includes an updated macroeconomic assessment together with an assessment of fiscal space over the medium to long term, but the implications for next year's budget are not as spelt out as in Denmark and Sweden. Finally, it is worth noting that unlike in Sweden the economic analysis underlying the budget in Denmark and Norway is published separately from the actual detailed budget ("finansloven" and "statsbudsjettet").

The multitude of different documents and differences in the budget process obviously complicates any comparison between the three countries. In this report, a choice has been made to base the assessment on the documents that present the economic analysis underlying the near-term fiscal stance at the time of the budget. More precisely, the analysis in this report is based primarily on Norway's "nasjonalbudsjett", Denmark's August "økonomisk redegørelse", and Sweden's "budget-propositionen". For the sake of simplicity these documents will often be referred to as the budget. Other documents are referred to as needed.

Table 1: The Budget Process in the Three Scandinavian Countries

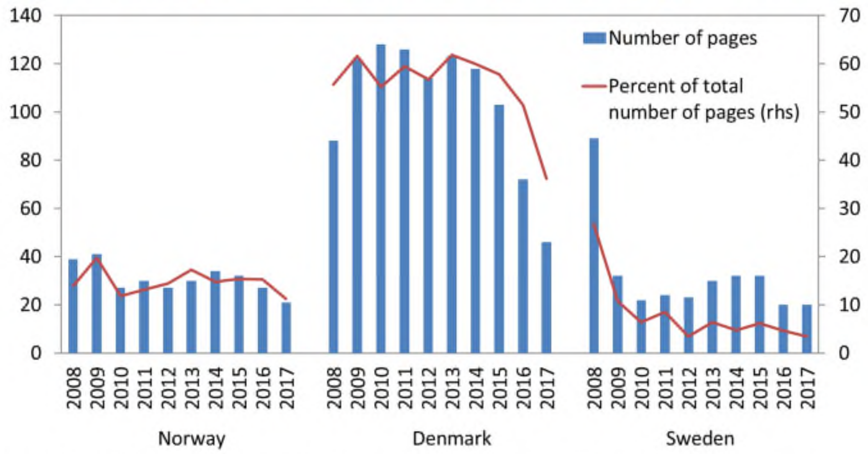
	Norway		Denmark		Sweden	
Budget	• Konsekvensjustert budsjett	January (t-1)	• Økonomisk Redegjørelse	December (t-2)	• Ekonomiska vårpropositionen	April (t-1)
	• First budget conference	March (t-1)	• Rammefastsættelse	February (t-1)	• Budget conference	August (t-1)
	• Revidert nasjonalbudsjett	May (t-1)	• Økonomisk Redegjørelse	May (t-1)	• Budgetpropositionen	September (t-1)
	• Second budget conference	August (t-1)	• Aftaler om den kommunale og regionale økonomi	June (t-1)		
	• Nasjonalbudsjettet • Statsbudsjettet • Skatter, avgifter, og toll	October (t-1)	• Økonomisk Redegjørelse • Finanslovsforslag	August (t-1)		
			• Avtaler om finansloven	November (t-1)		
			• Økonomisk Redegjørelse • Finansloven	December (t-1)		
Budget amendments	• Tilleggsbevilgninger	t	• Tillægsbevilgninger	t	• Vårändringsbudgetet	April (t)
	• Revidert nasjonalbudsjett • Regjeringens forslag til omprioriteringer og tilleggsbevilgninger på statsbusjettet	May (t)			• Höständringsbudgetet	September (t)
	• Nysaldert budsjett	December (t)	• Tillægsbevillingslov	January (t+1)		
Fiscal statement	• Statsregnskap	May (t+1)	• Statsregnskab	June (t+1)	• Statens årsredovisning	April (t+1)

1/ Solid (half) shaded boxes represent steps in the budget prosess (not) accompanied by the public release of one or more budget documents.
Source: National authorities

3 Description of Economic Developments

There is a significant difference among the three countries in terms of how much space they devote to discussing economic developments. As shown in figure 1, Denmark has traditionally devoted nearly three times as many pages to this purpose as Norway and Sweden, though the gap has declined recently. This gap is also reflected in the share of the total number of pages devoted to describing the economic situation and the economic outlook.

Figure 1: Description of Economic Developments in Budget Documents

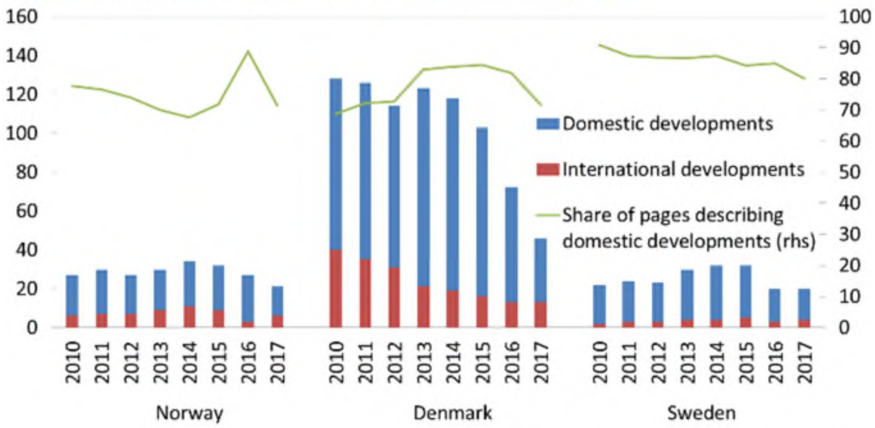


Source: Chapter on "De økonomiske utsiktene" in Nasjonalbudsjettet (Norway); chapter on "Den makroekonomiska utvecklingen" in Budgetpropositionen (Sweden); chapters on "International økonomi og finansielle markeder" and "Dansk økonomi" in August økonomisk redegørelse (Denmark)

Both domestic and international developments receive greater coverage in Denmark than they do in Norway and Sweden (see figure 2). The number of pages describing the domestic economic situation (in percent of the number of pages devoted to describing economic developments) is broadly the same across the three countries, implying that international developments receive three to four times as much coverage in Denmark as in Norway and Sweden.

There are number of possible explanations for these differences. A desire to constrain an already large document could help explain the relatively limited coverage of economic developments in Sweden where, unlike Norway and Denmark, the description of the economic situation is included in the detailed budget.[2] In addition, Andersen (2017) suggests the fact that authorship is often spread among several different ministries could help explain the greater number of pages devoted to describing economic developments in Denmark's budget. Finally, the greater focus on international economic developments in Denmark's budget probably reflects its relatively high trade openness (see figure 3) and its monetary policy regime which, unlike Norway and Sweden's inflation targeting framework, is centered on a peg to the euro.

Figure 2: Description of Economic Developments in Budget Documents
(number of pages describing domestic and international developments)

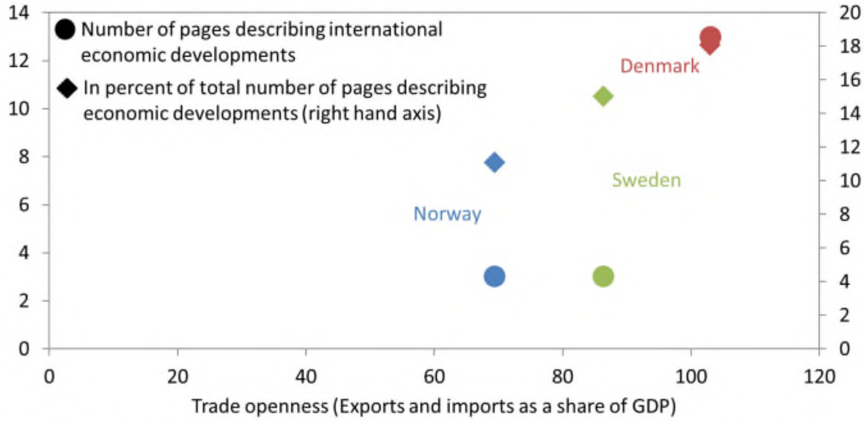


Source: Chapter on "De økonomiske utsiktene" in nasjonalbudsjettet (Norway); chapter on "Den makroekonomiska utvecklingen" in Ekonomiska vårpropositionen (Sweden); chapters on "International økonomi og finansielle markeder" and "Dansk økonomi" in August økonomisk redegjørelse (Denmark)

[2] The 2016 "Budgetpropositionen" in Sweden totalled 949 pages compared to 176 pages in Norway's 2016 "Nasjonalbudsjettet" and 130 pages in Denmark's August 2016 "Økonomisk Redegørelse".

The size difference is, to a certain extent, mirrored in the number of projected variables (see table 2). In particular, Denmark's August 2016 "økonomisk redegørelse" included projections of around twice as many economic variables as in Norway and Sweden's budget documents. Norway in addition stands out in terms of the relatively small number of macroeconomic annex tables included in the budget.[3]

Figure 3: Description of International Economic Developments and Trade Openness (2015)



Source: OECD and chapter on "De økonomiske utsiktene" in nasjonalbudsjettet (Norway); chapter on "Den makroekonomiska utvecklingen" in Ekonomiska vårpropositionen (Sweden); chapters on "International økonomi og finansielle markeder" and "Dansk økonomi" in August økonomisk redegjørelse (Denmark)

Again there are number of possible explanations for these differences. Andersen (2017) suggest that the large number of projected variables in Denmark could reflect the institutional setting, notably the existence of a fiscal watchdog that among other things produces its own economic forecasts. Another possible reason for the relatively large number of projected variables in the Danish budget could be the fact that the Danish central bank does not produce its own economic forecasts.

Interestingly, the coverage of topics in the main text of the budget is if anything inversely proportional to the number of pages (see table 3). In particular, Sweden covers a large number of topics in the least number of pages, while Denmark covers a more narrow set of topics in detail. For Norway, the comparison is complicated by the fact that the organization of the budget tends to vary more than in the other countries. For example, chapter 2 of the 2015 and 2016 Budgets cover inequality in great detail, while in the 2017 Budget this topic is moved to a separate chapter.

Table 2: Projected Variables in the Budget Documents

	Norway	Denmark	Sweden
Real GDP	17	29	12
Labor market	6	15	12
Prices and wages	3	6	4
Housing market	0	1	0
Interest rates	1	9	2
Exchange rates	1	4	2
External assumptions	21	28	17
Productivity	0	1	3
Other	2	11	15
Total	51	104	67
Memo item:			
Macroeconomic annex tables	7	21	20

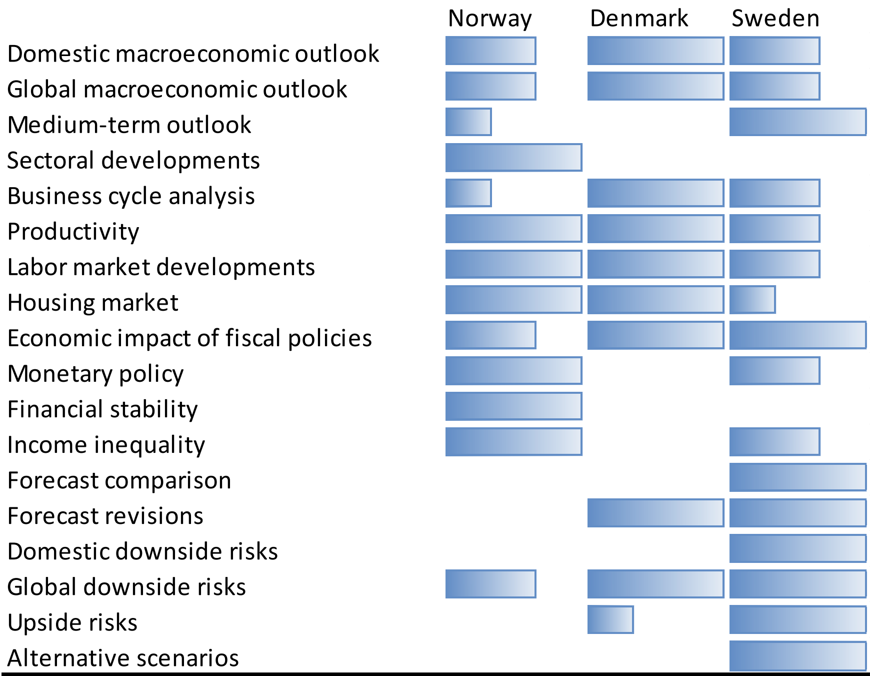
Source: Tables in national budget documents

In terms of the choice of topics Denmark and Norway put less emphasis on the medium term than in Sweden, while Norway stands out it terms of the relatively limited coverage of the business cycle. Norway, on the other hand, devotes more space to sectoral developments and to other areas of domestic macroeconomic policy, including monetary policy and financial stability. All three countries discuss structural challenges (e.g. productivity and the housing market) in some detail.

[3] The number of macroeconomic annex tables has been approximately halved since the 2015 Budget.

Sweden stands out in terms of its greater focus on forecast revisions and benchmarking against other forecasters, as well as its explicit discussion of alternative scenarios and upside as well as downside risks.

Table 3: Coverage of macroeconomic developments and policies



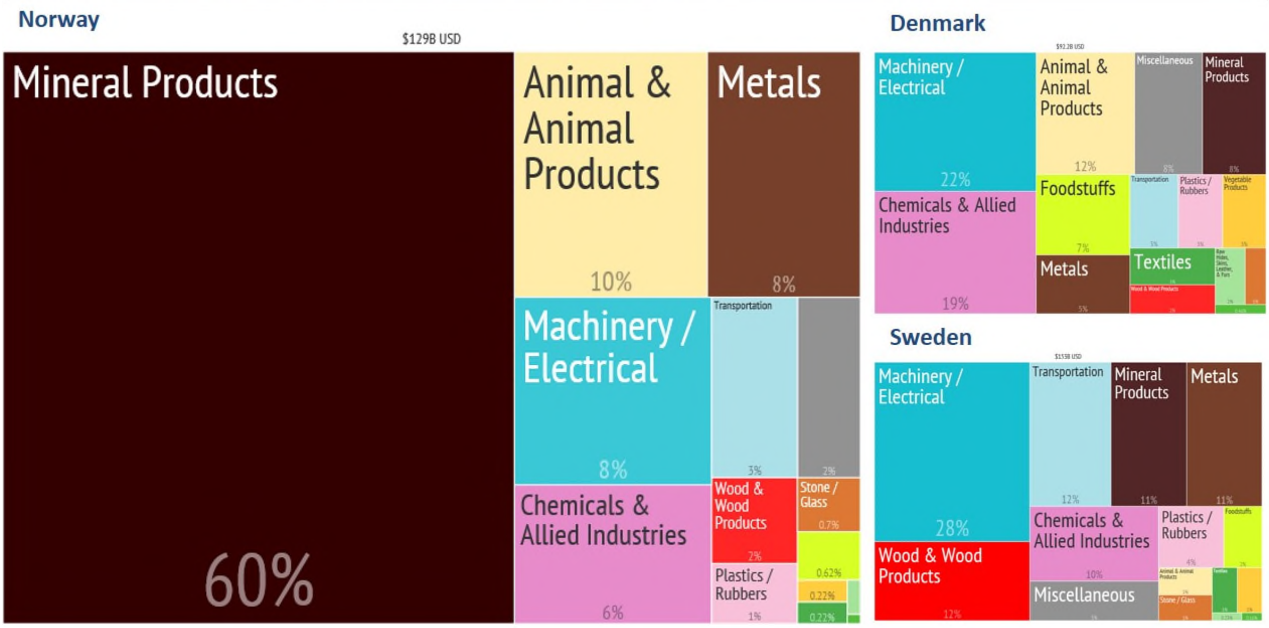
1/ Length of bar represents extent of coverage in each country relative to each other within the same area

Source: Author's assessment

Some of these differences in coverage likely reflect historical factors and are thus difficult to explain. However, others appear to reflect fundamental differences in the three economies, the fiscal framework, and the institutional structure of policymaking. For example, the greater sectoral focus in Norway is understandable given the outsized importance of the petroleum sector in the economy (see figure 4). Similarly, the greater emphasis on global downside risks in Sweden and Denmark could again be a reflection of the relatively high trade openness of these economies (see figure 3).

Differences in the structural challenges faced by the three countries also appear to play a role in the coverage of topics. Norway and Denmark, for example, have experienced weaker productivity growth than both Sweden and the OECD (see figure 5). However, despite similar challenges (see

Figure 4: Composition of gross exports from Norway, Denmark, and Sweden (2014)

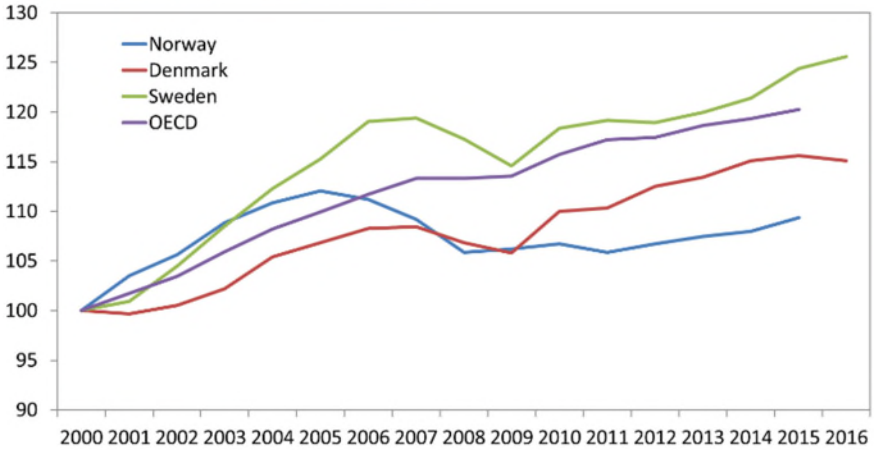


Source: Atlas of Economic Complexity

figure 6), the housing market receives significantly less coverage in Sweden than in Norway. One possible reason for this is the institutional responsibility for macroprudential policymaking, which in Norway lies with the Ministry of Finance whilst in Sweden this responsibility is shared between the central bank (“Riksbanken”) and the financial supervisory authority (“Finansinspektionen”).

Figure 5: GDP per hour worked

(USD PPP-adjusted 2010 Prices; index: 2000=100)

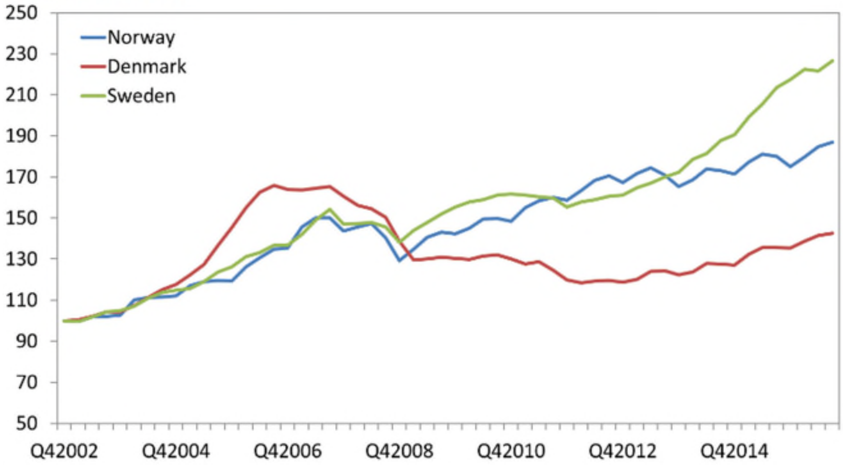


Source: OECD

The relatively detailed coverage of business cycle developments in Denmark compared to Norway could reflects differences in the methodology for calculating the structural fiscal balance (see table 4). In particular, Norway’s sophisticated methodology for estimating the structural balance relies on a relatively large number of cyclical indicators that can be difficult to present in a concise manner in the main text of the budget.[4] Sweden’s approach to calculating the structural fiscal balance was recently updated, suggesting that the detailed coverage of business cycle developments could be a legacy of the previous more simple methodology that relied primarily on the output gap.

Figure 6: Real House Prices

(index: Q42002=100



Source: Bank for International Settlements

The lack of focus on medium-term macroeconomic developments in Denmark and Norway likely reflects significant coverage in other documents (e.g. “Perspektivmeldingen” in Norway and the convergence plan and the medium-term plan in Denmark). In Norway it could also reflect the one-year fiscal framework (Sweden and Denmark both have multi-year fiscal frameworks including multi-year spending ceilings), though this is somewhat at odds with the emphasis on medium-term dynamic effects (e.g. crowding out) of fiscal policy as a motivating factor for the fiscal stance.[5]

Andersen (2016) notes a number of other institutional factors that may be important. Unlike Norway, both Denmark and Sweden have independent fiscal councils (“Det Økonomiske Råd” in Denmark and “Finanspolitiska Rådet” in Sweden). This could increase the burden on justifying the projections

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[4] A detailed exposition of the estimation of the structural balance in Norway is presented in an appendix.

[5] Section 3 includes a more thorough discussion of the role of economic analysis in explaining and motivating the fiscal stance.

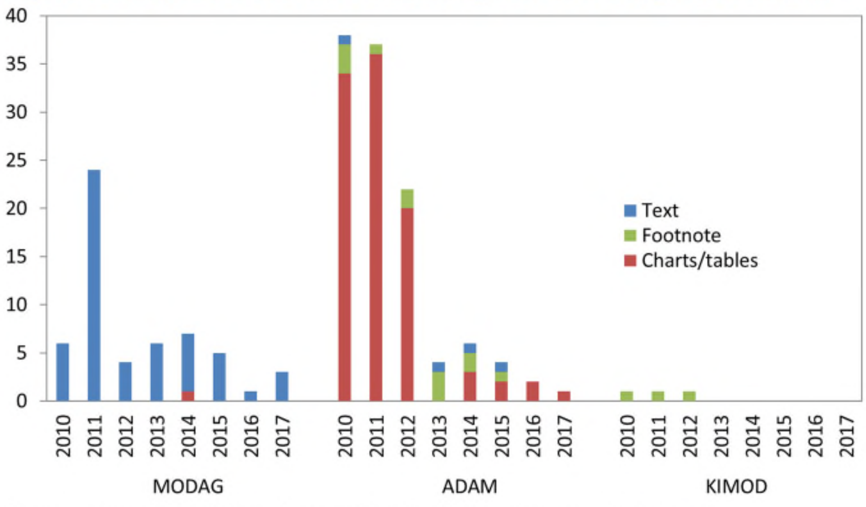
Table 4: Estimation of structural balance

	Revenue and expenditure categories corrected	Methodology	Cyclical indicators	Other corrections
Norway	Twelve revenue categories and unemployment benefits	Adjustment for cyclical deviations in revenue and expenditure base indicators followed by trend extraction using HP filter	• Mainland GDP gap • Full-time equivalent persons gap • Private consumption gap • Mainland private investment gap • Private investments in construction gap • First time motor vehicle registrations gap • Motor vehicle population gap	Revenues and expenditure items related to oil expenditure excluded. Trend correction of net interest payments and transfers from Norges Bank
Denmark	Eight revenue categories, six types of social transfers, public consumption and investment, and two categories of subsidies	Separate adjustment for impact of output and employment gap. Elasticities estimated using ADAM model	• GDP gap • Employment gap	Structural level of certain revenue categories (e.g. corporate taxes, car taxes, and tax on pension savings), as well as income from the oil sector and net interest payments estimated separately
Sweden	Seven different revenue categories and unemployment benefits	Trend level of each revenue category calculated as product of implied tax rates, the long-term level of the taxbase as a share of GDP calculated using an HP filter, and potential GDP. Structural unemployment benefits calculated by extracing an HP trend	• Potential GDP • Corporate profits trend • Household capital gains trend • Household income trend • Private consumption trend • Private investments trend • Household consumption trend • Total wage bill trend	One-off effects

Sources: National authorities

in the budget and thus contribute to a greater emphasis on forecast revisions and benchmarking against outside forecasters.Similarly, the explicit consideration of alternative scenarios in Sweden partly reflects the fact that this is a requirement under the EU's Stability and Growth Pact.[6] This, coupled with an extensive discussion of upside and downside risks, contributes to a clear presentation of the uncertainty surrounding the budget forecasts. As Andersen (2016) notes, the political process (e.g. the temptation for politicians to formulate policy on the basis of the most advantageous scenario) could be one reason why countries are reluctant to present and quantify the impact of upside as well as downside risks. Why this is not a constraint in Sweden, is unclear.

Figure 7: References to Main Forecasting Model in Budget Documents



Source: Nasjonalbudsjettet (Norway); Ekonomiska vårpropositionen (Sweden); August økonomisk redegjørelse (Denmark)

A final difference that is worth highlighting relates to the use of economic models. As shown in figure 7,

[6] In Denmark, these alternative scenarios are reported in the annual convergence program.

references to the main forecasting model in Denmark (ADAM) has declined over time. Discussions with the Danish Ministry of Finance suggests this reflects both changes in how (and how much) the model is used, and also a perception that referencing the model may not be useful even in cases where it is still used. Similarly, in Sweden the current lack of references to the macroeconomic model KIMOD reflects the fact that the model is no longer being used by the Ministry of Finance. By contrast, in Norway references to the macroeconomic model MODAG have remained broadly stable, suggesting both that the model continues to be actively used and that referring to the model in the budget is perceived to add credibility.

4 The Role of Economic Analysis in Motivating Fiscal Policy

Economic analysis serves a number of purposes in the formulation of the budget. Most obviously, economic analysis plays a pivotal role in evaluating the current fiscal policy stance and in motivating changes to the fiscal stance over the budget horizon. Countries with fiscal rules that target a “structural” measure of the fiscal balance (including Norway, Denmark, and Sweden) are particularly reliant on quantitative business cycle analysis.

Economic analysis also plays a pivotal role in the formulation of the budget at a more detailed level. In particular, several revenue and expenditure components in the budget are linked explicitly to macroeconomic developments. This is particularly true in Scandinavia where automatic stabilizers are relatively high. Governments also use economic analysis to determine budget allocations across different programs and spending ministries, and to motivate targeted interventions in specific sectors or regions. Finally, the assessment of the economic outlook in national budgets often plays a key role in the budget process at the subnational level.

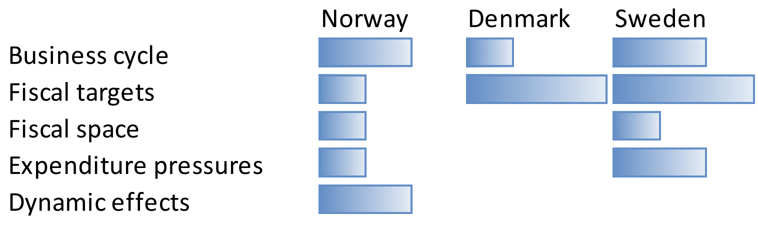
A complete analysis of the many ways economic analysis is used in the formulation of the budget is beyond the scope of this paper. In what follows we focus primarily on the role economic analysis plays in evaluating and motivating the aggregate fiscal stance.

Before we continue, it is useful to discuss briefly the meaning of the “fiscal stance”. Typically, the fiscal stance refers to the extent current fiscal policy positively or negatively affects economic activity. When measuring the fiscal stance it is common to use the structural fiscal balance in order to abstract from automatic stabilizers and isolate the impact of “discretionary” policy measures. An “expansionary fiscal stance” is usually associated with a fiscal policy that gives a “positive fiscal impulse” to the economy. However, in countries with a fiscal rule the absence of fiscal consolidation to correct deviations from target is sometimes also referred to as expansionary, even if there is no positive fiscal impulse. Finally, the terms fiscal stance and discretionary fiscal policy are often used interchangeably, even though it is debatable whether a contractionary fiscal stance to correct deviations from target should be considered discretionary policy. In the remainder of this note we abstract from these issues by focusing narrowly on what motivates the fiscal stance, regardless of whether it is expansionary/contractionary or discretionary.

It is also worth noting that the structural fiscal balance is affected not only by the current fiscal stance, but also by structural reforms. Structural reforms can affect the budget directly (e.g. raising the retirement age) or indirectly (e.g. higher labor force participation). In Norway, fiscal projections typically incorporate the direct effect (e.g. lower pension payments) but not the indirect effect (e.g. higher economic growth) which is usually hard to estimate. Denmark and Sweden typically also incorporate the indirect effect, albeit using conservative assumptions about the impact of any reforms. One possible reason for this difference is the delayed impact of most of these reforms, which means they are less of a factor in Norway’s one-year budget than in Denmark and Sweden’s multi-year fiscal framework. For the purpose of this note we focus narrowly on what motivates the near-term fiscal stance, which is usually driven by revenue and expenditure measures and unaffected by new structural reform initiatives.

Table 5 illustrates the factors used to justify the fiscal stance in the budget documents of the three Scandinavian countries.[7] In the author's assessment, the business cycle (i.e. the cyclical position of the economy) plays an important role in motivating the fiscal stance in Norway and Sweden, but less so in Denmark. Fiscal targets (e.g. a fiscal rule), on the other hand, play a key role in Denmark and Sweden, but less so in Norway. Expenditure pressures (e.g. from the recent influx of refugees) are particularly important as a motivating factor for the fiscal stance in Sweden. Finally, dynamic effects (e.g. the impact of current fiscal policy on the future structure of the economy) play a key role in motivating the fiscal stance in Norway, but do not appear to be a factor in Denmark and Sweden.

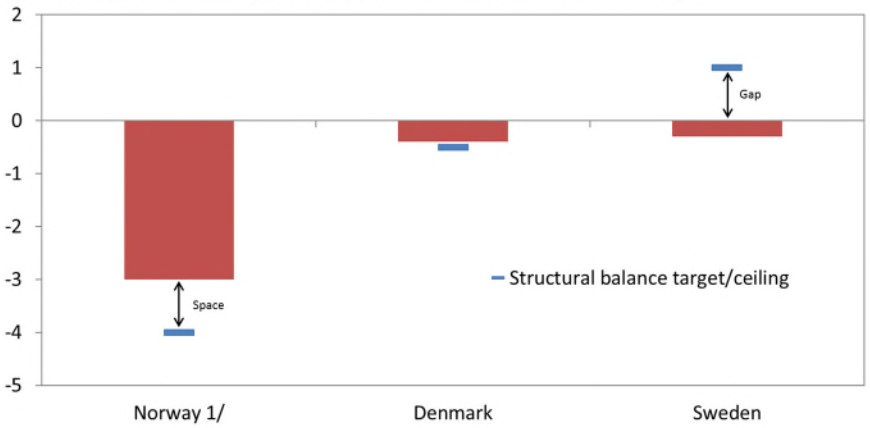
Table 5: Factors used to justify overall fiscal stance in budget



1/ Length of bar represents extent of coverage in each country relative to each other and other areas
Source: Authors assessment

It is important to note that these factors interact in important ways, and that their importance can change over time.[8] For example, the importance of the business cycle in Norway likely reflects that fiscal policy in recent years has not been constrained by Norway's fiscal rule (see figure 8). However, with the recent reduction in the expected real rate of return from the Government Pension Fund Global from 4 to 3 percent, fiscal policy in Norway is likely to become more constrained and increasingly guided by the fiscal rule. Similarly, the importance of the business cycle, fiscal space, and expenditure pressures in motivating the fiscal stance in Sweden likely reflects the fact that the structural fiscal deficit is currently significantly above the level dictated by the fiscal rule.

Figure 8: Distance to Fiscal Targets
(2017; structural balance in percent of potential GDP unless otherwise noted)



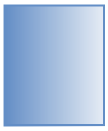
1/ Structural deficit measured in percent of the capital in the Norwegian Petroleum Fund
Source: National authorities

More broadly, it is clear that the fiscal framework in the three countries (see table 6) plays a key role in determining the factors that are used to motivate the fiscal stance. Specifically, the fiscal framework in Norway places greater emphasis on smoothing the business cycle than in Denmark and in Sweden, where fiscal policy is guided by a structural fiscal balance target and multi-year

[7] This analysis focuses narrowly on the factors that are mentioned in the budget documents. It is likely that additional factors are used in internal deliberations.
[8] The analysis in this note is based primarily on the 2017 budget in the three countries.

spending ceilings, as well as the fiscal targets in European Fiscal Compact. However, unlike in Denmark the fiscal framework in Sweden explicitly states that deviations from the target should be corrected in a manner that avoids a procyclical fiscal policy. In practice this implies that the economic situation plays a major role in motivating the fiscal policy stance in periods of deviation from target, as is currently the case (see figure 8). In Denmark, on the other hand, the fiscal framework only leaves space for countercyclical fiscal policy in periods where the structural balance is above target, which is not the case currently.

Table 6: Fiscal framework

	Norway	Denmark	Sweden
Fiscal rule	Handlingsregelen: Transfers from Government Pension Fund Global to budget limited, over time, to expected real rate of return of the fund	1. European fiscal compact including MTO of ½ percent of GDP 1/ 2. Maximum structural fiscal deficit of ½ percent of GDP 3. Medium-term Plan: Balanced budget in structural terms by 2025	1. European fiscal compact including MTO of 1 percent of GDP 1/ 2. Target for net lending to average 1 percent of GDP over business cycle (surplus target)
Other	Emphasis on smoothing out business cycles to ensure good capacity utilization and low unenmployment	Four-year rolling non-interest expenditure ceilings specified in real terms. Cyclically sensitive expenditure and public investments excluded from ceiling	1. Three-year rolling non-interest exenditure ceilings specified in nominal terms 2. Guidelines for correcting surplus target deviations aimed at avoiding a procyclical fiscal stance 3. Sizeable budget margin as buffer for unforseen developments
Scope for using fiscal policy to smooth the business cycle			
Symmetric 2/	Yes	Yes if below limit; No if above limit	No

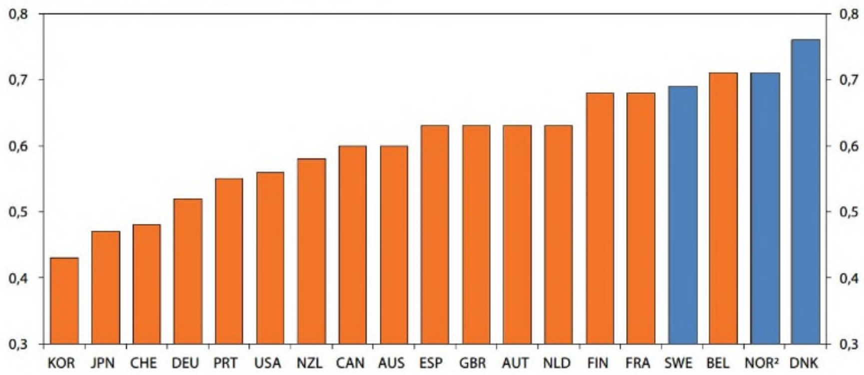
1/ The European Fiscal Compact stipulates a maximum general government deficit of 3 percent of GDP, a structural deficit not exceeding a country-specific medium-term objective (MTO), government debt below 60 percent of GDP, and automatic correction mechanisms
2/ Symmetric implies that deviations from target do not impose restrictions on whether fiscal policy can be expansionary or contractionary
Source: National authorities and author's assessment

Another potential reason for the lack of emphasis on using discretionary fiscal policy to smooth the business cycle could be the size of automatic stabilizers (see figure 9). Denmark, for example, has the largest automatic stabilizers among OECD countries, closely followed by Norway. This, coupled with structural fiscal targets that remove the effect of revenue and expenditure items that are sensitive to the cycle, means that fiscal policy automatically plays a significant role in stabilizing the economy even when there is no change in the discretionary fiscal stance. In conversations with the Danish Ministry of Finance, it was clear that there was a preference for relying on automatic stabilizers instead of discretionary fiscal policy to stabilize the economy, given that discretionary fiscal measures are often subject to time lags and can be difficult to unwind, and can increase uncertainty for the private sector. The same would normally be true in Sweden, though with interest rates at the lower bound the case for a more active use of fiscal policy becomes stronger.

Another reason for differences in the emphasis on countercyclical fiscal policy could be historical. In particular, Andersen (2013) notes that Sweden more rigid fiscal framework has developed over the years in response to a “need to consolidate public finances after a period of deep crisis in the early 1990s… [when debt reached]… close to 90 percent of GDP”. In other words, a driving force behind the development of Sweden’s fiscal framework was concerns about fiscal sustainability.

Norway's fiscal rule, on the other hand, was introduced in 2001 in order to provide a framework for the gradual phasing in of oil revenues in a manner that would preserve macroeconomic stability and would ensure intergenerational equity. As a result, Norway's fiscal framework places greater weight on stabilizing the real economy than in Sweden and Denmark.

Figure 9. Size of Automatic Stabilizers

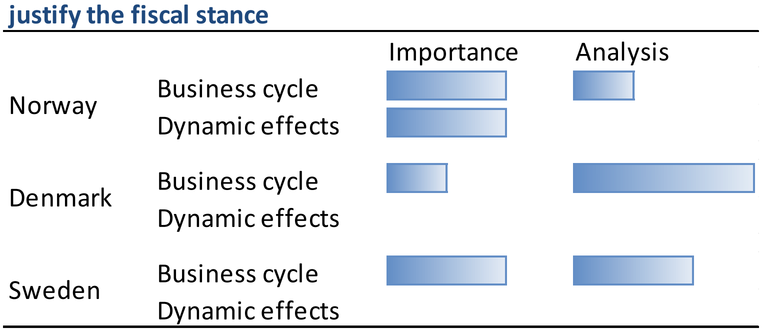


1/ The chart shows the automatic change in the fiscal deficit from a one percentage point change in the output gap
2/ Mainland Norway
Source: Thøgersen et al. (2015) using data from the OECD

What is perhaps surprising is that the emphasis on countercyclical fiscal policy does not appear to be related to the ability of the three countries to use monetary policy as a tool for macroeconomic stabilization. In particular, Denmark's peg to the euro means that monetary policy is largely delegated to the European Central Bank and driven by macroeconomic developments in the euro area as a whole. In Norway, on the other hand, the emphasis on countercyclical fiscal policy comes on top of a central bank mandate that, in addition to targeting inflation, calls for monetary policy to contribute to stabilizing output and employment.

Interestingly, the amount of emphasis placed on the factors used to motivate the fiscal stance often does not match the amount of analysis in the budget text. Table 7 shows the importance (as reported in table 5) and amount of analysis of the two factors most important for motivating the fiscal stance in Norway. It is striking that in the Norwegian budget there is comparably little analysis of the main factors motivating the fiscal stance, namely the business cycle and the dynamic supply-side effects of fiscal policy. By contrast, in Denmark the amount of analysis of the business cycle is disproportionately largely relative to its role in motivating the fiscal stance.

Table 7: Importance and amount of analysis of factors used to justify the fiscal stance



1/ Length of bar represents extent of coverage in each country relative to each other and other areas
Source: Author's assessment

As noted previously, the Ministry of Finance in Norway uses a sophisticated methodology for estimating the structural fiscal balance that relies on a wide range of cyclical indicators. It is difficult to present an analysis of all these indicators in a concise manner in the budget. However, it is worth emphasizing that the cyclical indicators used to estimate the structural balance are not necessarily the same as those that should be used to assess the economy's position in the business cycle for the purpose of motivating the fiscal stance. For example, it makes sense to use the motor vehicle population gap to estimate the structural level of motor vehicle registration fees, but not to assess the cyclical position of the entire economy. In the author's opinion, Norway's sophisticated methodology for estimating the structural balance should therefore not be a hindrance to a more quantitative analysis of the economy's position in the business cycle.

5 Some possible implications for Norway

The assessment of economic developments in the Norwegian budget documents is clear and concise, and broadly conforms to international best practice. International organizations that have reviewed Norway's fiscal framework, including the IMF and the OECD, arrive at similar conclusions, while Norway consistently scores high on the International Budget Partnership's Open Budget Survey.

The cross-country analysis in this report suggests, however, that there are some areas where changes could be warranted. First, in the author's assessment the analysis of economic developments in the budget would become more user friendly if the choice of topics and the organization of the document were more standardized and varied less from year to year. Special topics could be covered either in boxes or in special chapters. This would make it easier to compare the assessment of economic developments over time, thereby contributing to greater transparency.

In the same vein, the Ministry could consider including a comparison of its projections with those of outside forecasters and a discussion of the factors underlying revisions to the macroeconomic forecasts in the budget in the main text of the budget.[9] As noted by Andersen (2017), benchmarking against other forecasters would give a sense of the uncertainty surrounding the projections as well as the risks to the outlook. Benchmarking forecasts to those of other organizations and explaining the drivers of forecast revisions could also increase the credibility of the budget. The exposition in the Swedish budget could serve as a useful template.

Finally, it could be useful to consider ways to augment the analysis of the macroeconomic factors (i.e. the business cycle and the dynamic effects of fiscal policy) that are used to motivate the fiscal policy stance. Indicators commonly used to assess the economy's position in the business cycle include estimates of the output gap, the employment gap, and the productivity gap, as well as survey indicators of capacity utilization and the state of the labor market.[10] Analyzing the medium-term dynamic effects of fiscal policy, including on the industrial structure of the Norwegian economy, would also be useful. Such an analysis would benefit from the greater use of macro-economic models than is currently the case.

[9] A table comparing the budget forecasts with those of outside organizations is currently included as an annex table in the budget.

[10] The 2017 Supplementary Budget includes a greater analysis of the cyclical movements of the Norwegian economy.

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