

# The fiscal policy framework

– application by the Government in 2020

## Summary and recommendations

The Swedish National Audit Office (Swedish NAO) has audited the Government's fiscal policy in the fiscal policy bills in 2020. The audit compares the Government's reporting in fiscal policy bills with the fiscal policy framework. By reporting fiscal policy and its foundations in a transparent manner, the Government can contribute to strengthening citizens' and financial market participants' confidence in sustainable fiscal policy so that it can have the intended effect. The overall conclusion of the audit is that fiscal policy has been mainly designed and reported in accordance with the fiscal policy framework, but there are deviations. Among other things, the Government has raised the expenditure ceilings for 2021 and 2022 in a way that lacks support in the framework and that risks leading to less effective spending priorities, according to the Swedish NAO.

### **Audit findings**

The sudden and very severe economic downturn due to the ongoing COVID-19 pandemic has changed fiscal policy conditions in a short time. To counteract the deep economic downturn, the Government is pursuing an expansive fiscal policy, in which the active policy weakens public finances in 2020. The Government will therefore not achieve the surplus target. However, the Swedish NAO considers that the fiscal policy framework provides support to the Government to temporarily deviate from the surplus target for stabilisation policy reasons, even in the next few years. Since the surplus target applies over a business cycle, fiscal policy is in line with the fiscal policy framework.

Many of the Government's crisis measures are temporary, and as they are phased out, public finances will strengthen, cyclically adjusted, so that the structural net lending will reach the surplus target in 2023 according to the Government's calculations. At the same time, the Government considers, somewhat inconsistently, that it is not appropriate to present a plan at this point for a return to the surplus target other than at an overall level. In the event of an estimated deviation from the surplus target, the Government is obliged under the Budget Act to explain how a return to the target should take place. The Swedish NAO considers that the uncertain situation does not constitute a reason not to comply

with the provisions of the Budget Act. On the contrary, it is precisely in sudden downturns that deviations from the target level can be expected to occur.

The economic situation is of great importance in the Government's ongoing monitoring of the direction of fiscal policy in relation to the surplus target. This means that comparisons need to be made with other forecasters in order for an outside reader to get an idea of whether the Government's assessment is reasonable. As in previous audits, the Swedish NAO notes that the Government could be better at explaining the differences that exist compared with other forecasts.

The return from the expansionary fiscal policy in 2020, to a structural net lending in line with the surplus target, is supported by the Government's proposal for a new expenditure ceiling level for 2023. By returning to the same expenditure ceiling level in relation to GDP that applied before the crisis, the Government limits the scope for permanent spending increases during the period of the crisis. However, the Swedish NAO considers that the scope of temporary and permanent measures on the expenditure side of the budget should have been made clearer in the Budget Bill.

In 2020 the Government has proposed uniquely large increases of previously established expenditure ceilings for the period 2020—2022, citing fiscal policy reasons. In this way, the Government has great freedom of action to implement temporary expenditure increases in 2021 and 2022, if developments are significantly worse than has been assumed. The Swedish NAO considers that the raised level of the expenditure ceiling in 2020 is in line with the fiscal policy framework. The uncertainty regarding the fiscal year 2020 was very high at the time of the Government's proposal. Consequently, a sharp increase was justified without any clear explanation for the size of the increase.

However, the increases in the expenditure ceiling for 2021 and 2022 proposed by the Government are not in line with the fiscal policy framework, according to the Swedish NAO. The reason is that the levels have been chosen to create room for both the current fiscal readjustment and an alternative scenario of active fiscal policy that has not yet been announced. If economic development is in line with the picture otherwise drawn up in the Budget Bill, the sharply raised ceilings for 2021 and 2022 entail a risk that expenditures will not be tested against each other as the expenditure ceiling is intended to contribute to. All in all, the Swedish NAO assesses that the expenditure ceilings for 2021 and 2022 have been adjusted in a way that lacks support in the framework and that risks weakening budgetary discipline.

The fiscal policy framework also contains a balanced budget requirement for the local government sector and a benchmark for the general government

consolidated gross debt, called the debt anchor. The Swedish NAO considers that the Government's follow-up of these budget targets is transparent.

## **Recommendations to the Government**

The Swedish NAO recommends that the Government, at the latest in the Spring Fiscal Policy Bill for 2021:

- describes how a return to the surplus target is to be achieved
- returns to the Riksdag with new proposed levels for the expenditure ceilings for 2021 and 2022 that are consistent with the current main scenario for the development of expenditure
- clarifies the reporting of budget effects for proposed and announced measures to show the scope of temporary and permanent measures.