

International Seminar on
Strengthening Public Investment and Managing
Fiscal Risks from Public-Private Partnerships

Budapest, Hungary
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Fiscal Adjustment and Public Investment: Experiences in New Member States and Some Preliminary Policy Lessons

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Three key topics

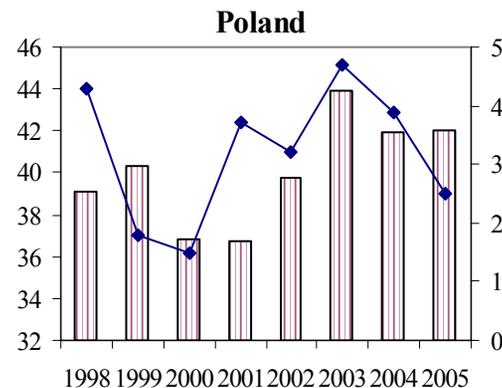
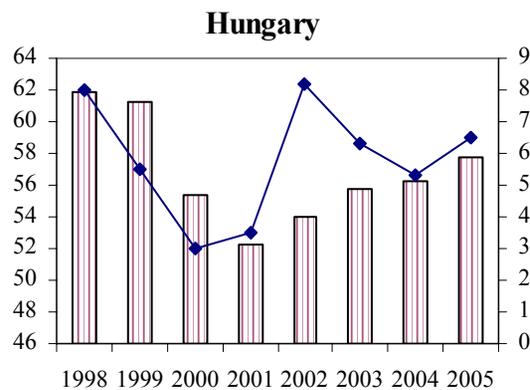
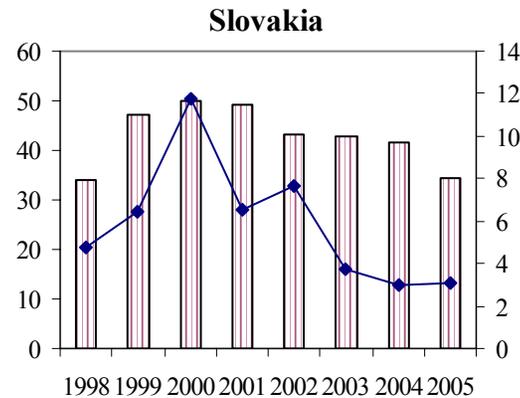
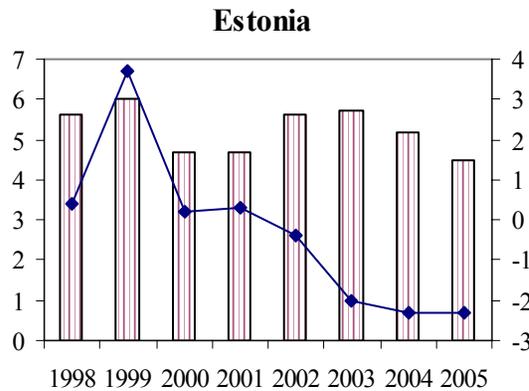


- Impact of fiscal adjustment on public investment
- Infrastructure in NMS
- Role of new available financing
 - EU Funds
 - PPPs

Public investment: The silent victim of fiscal adjustment?



- Sizable fiscal adjustment in some countries; volatile fiscal performance in others



■ Public debt (LHS)
◆ Fiscal deficit (RHS)

Public investment: The silent victim of fiscal adjustment?

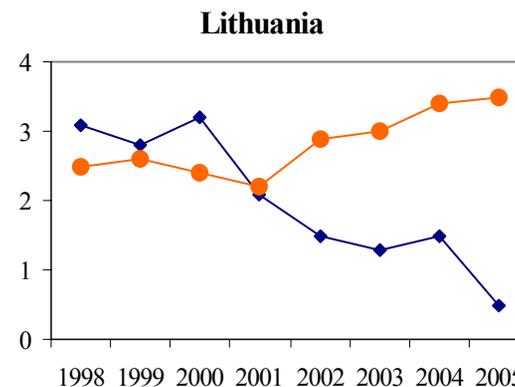
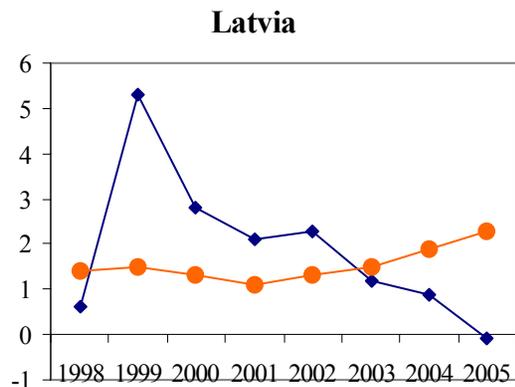
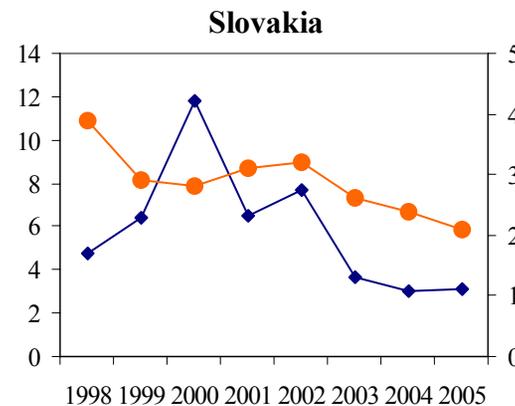
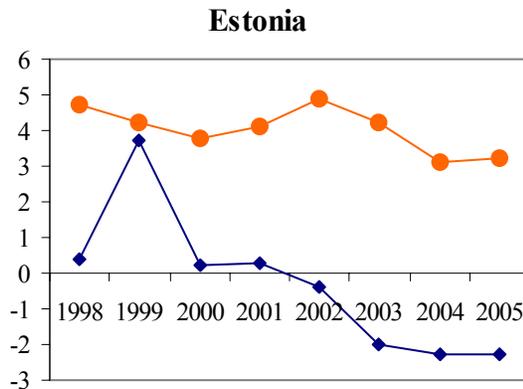


- Among NMS, during 1998-2005, there were 38 occurrences of improvements in the fiscal balance
- Out of these 38 occurrences...
 - 68% of times → cut in non-investment expenditure (2 percent of GDP)
 - 45% of times → cut in investment expenditure (0.5 percent of GDP)
 - 50% of times → increase in revenue (1 percent of GDP)

Public investment: The silent victim of fiscal adjustment?



- Overall, mixed experience. Investment even rose during fiscal adjustment in some countries



○ Public investment
◆ Fiscal deficit

Infrastructure: Where do NMS stand?



- Significant progress since the start of the transition
- But infrastructure still lags behind standards in OMS

Infrastructure Indicators, 1991-2002
(per 1,000 people)

	Electricity generation (kwh)		Fixed and mobile phone subscribers		Road networks (km)	
	1991-1995	1998-2002	1991-1995	1998-2002	1991-1995	1998-2002
Baltic states	4.5	4.1	247.5	587.0	7.7	16.8
CEEs	4.6	5.3	185.0	687.0	5.6	8.6
Bulgaria and Romania	3.5	3.7	199.5	391.3	3.7	4.4
EU-12 Average	5.5	6.5	473.1	1119.1	11.1	15.4

Source: The World Bank (2005) World Development Indicators Database; and staff estimates.

Infrastructure: How much investment is needed?



- Few estimates available. Not easy to provide concrete policy guideline at the country level

Infrastructure Investment Needs of NMS, 1995-2010

Sector	in € billion
Roads	44
Railways	37
Telecoms	63
Water/Sewage	180
Energy	110
Environment	71
Sum	505

Source: Brenck and others (2005).

Infrastructure: Policy options to increase investment



	Private Investment	Public Investment
Short- to Medium-Term	<p>Use PPPs. Provide government guarantees.</p>	<p>Reallocate public expenditure. Implement tax policy measures. Relax fiscal targets, financed by debt or the sale of state assets.</p>
Medium- to Long-Term	<p>Implement improvements in market-supporting institutions. Deepen financial markets.</p>	<p>Carry out structural reforms to help reduce current expenditure. Improve tax administration and expenditure management systems to enhance efficiency.</p>

Source: IMF (2005).

Infrastructure: Policy options to increase investment



- Appropriate strategy country specific
- Room to strengthen investment planning and efficiency
- Contingent on fiscal and macroeconomic environment
 - More flexibility in countries with stronger fiscal positions
 - Need higher public savings in countries facing imbalances (e.g., current spending reforms)

New available financing: Challenges to use EU Funds



- Co-financing and additionality
- Net fiscal impact could be negative
 - Recent estimate: fiscal drag of 0.5 percent of GDP¹
- Absorption has been relatively slow
 - Crucial given increasing size of EU Funds
- Changes in spending allocations can be expected

1/ Source: Rosenberg and Sierhej (forthcoming)

New available financing: Challenges to use PPPs



- PPPs can bring efficiency gains but also carry fiscal risks
- How ready is the institutional framework in the NMS?
 - Public investment planning: Generally weak frameworks; lack of use of CBA and VfM analysis
 - Legal and institutional framework: Legal frameworks not tailored to PPPs; inadequate role of MoF in PPP process; insufficient technical experience
 - Fiscal accounting and reporting: Lax standards; non-transparent disclosure of fiscal implications of PPPs

Concluding remarks



- Overall mixed experience regarding fiscal adjustment and public investment
- Upgrading infrastructure will require further efforts. No magic solution. Policy options country specific
- New financing presents opportunities and challenges
 - EU Funds: Net fiscal impact could be negative; absorption rates remain low
 - PPPs: Need to strengthen PPP frameworks to capitalize on efficiency gains and manage fiscal risks

Thank you!



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