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Fiscal Risk Management

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Fiscal Risk

- **“To expose to a *chance* of loss or damage”**
 - Unexpected event adversely impacting an already established fiscal framework
- **Fiscal risk is not same as fiscal sustainability**
 - Ageing populations

Categories of Fiscal Risks

- **Economic Assumptions**
- **Structure of Government Debt**
- **State Guarantees**
- **Public-Private Partnerships (PPP's)**
- **Natural Disasters**

Economic Assumptions

- **By far, the most significant fiscal risk**
 - Commodity prices
- **Full disclosure**
 - Sensitivity analysis
 - Forecasting track-record
 - Comparison with private forecasters
- **Use of Independent boards / agencies**
- **Prudency factors**
 - Systematic and explicit downward revisions
 - Reserve funds

Structure of Government Debt

- **Level of Debt = Sustainability**
- **Structure of Debt = Risk**

Structure of Government Debt

- Key Risk Characteristics

- **Short-term debt vs. long-term debt**
- **Variable rate of interest vs. fixed rate of interest**
- **Foreign currency dominated debt vs. local currency denominated debt**

Structure of Government Debt - Risk Management

- **Explicit debt management strategy**
- **Transparency of debt structure**
- **Sensitivity analysis**

- **Financial markets create discipline**

- **Debt Management Offices**

State Guarantees

- **Two Types**
 - Institutional Guarantees (student loans, housing)
 - One-off Guarantees (individual projects)
- **Key Risks**
 - Default
 - Lack of transparency
 - Undermining budget process (“escape route”)

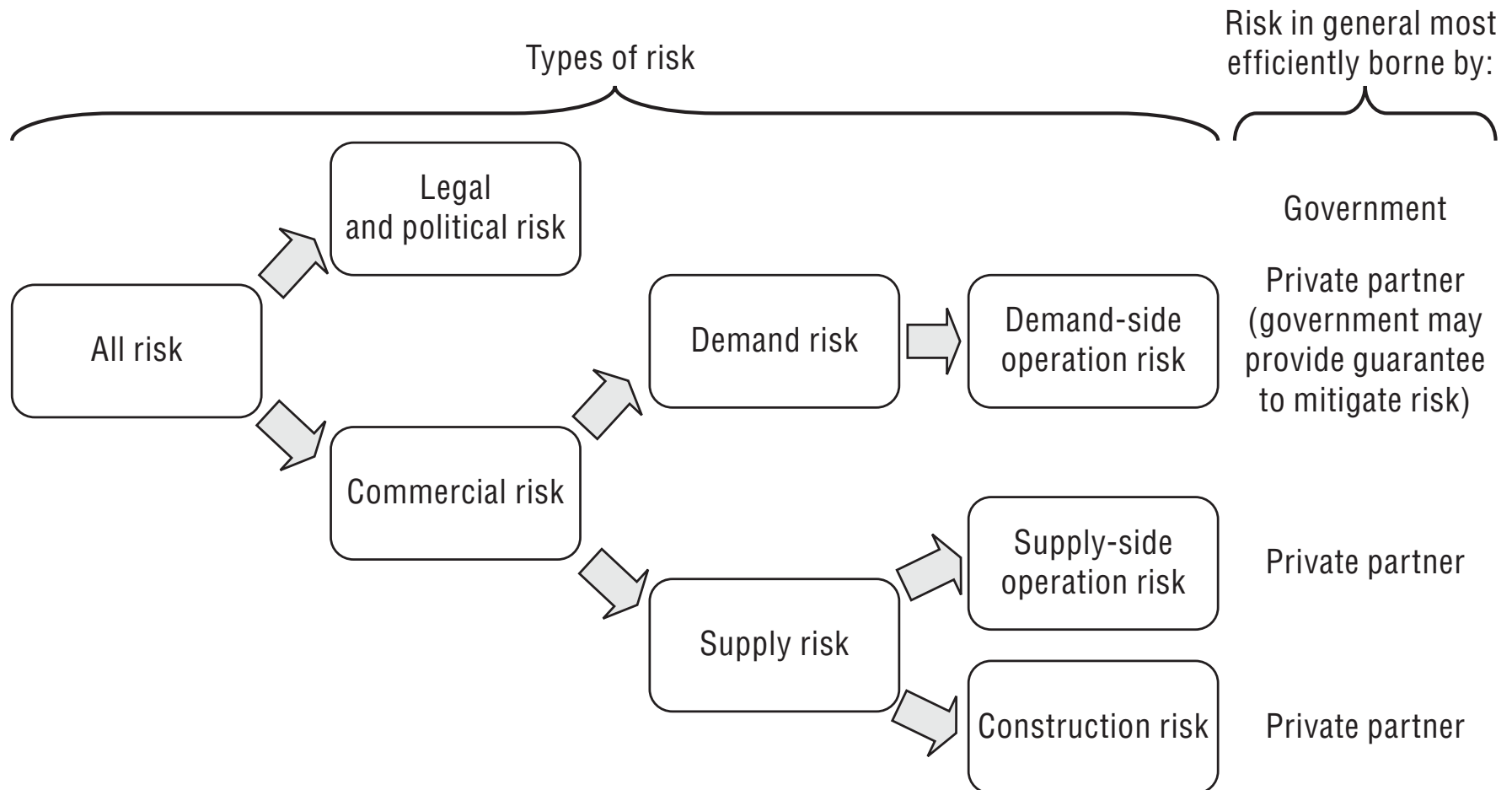
State Guarantees - Risk Management

- **Transparent reporting of all guarantees**
- **Authorisation by legislature**
 - Permanent within aggregate limits
 - Case-by-case
- **Risk sharing**
 - Partial guarantees, collateral
- **Integrate with annual budget process**
 - Estimate default risk
 - “Front”-fund default risk
 - Guarantee fees

Public-Private Partnerships (PPP's)

- **Same issues as with State Guarantees, but more complex**
- **Integrating PPP decisions with annual budget process essential**

Categories of PPP Risk



Assessing Risk Transfer

- **Very Difficult**
 - Legal complexity of PPP contracts
 - Implications of renegotiations
 - Special risks in case of providers of essential services & those “too big to fail”
- **Very Important**
 - Determines viability of PPPs
- **Need for specialized PPP Units**

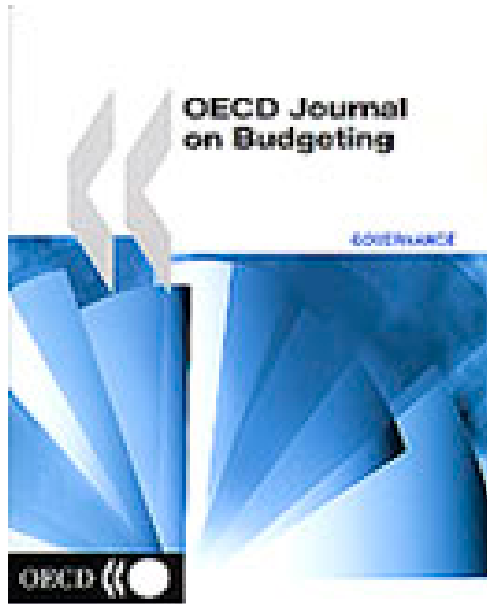
Natural Disasters

- **Emerging area ... linked with increased attention to very long term budget forecasts**
- **Options**
 - Mandatory insurance
 - Government contingency funds
 - Prevention measures
- **OECD project currently underway**

Conclusion

- **Implicit Guarantees – Systemic Faults**
 - Current financial crisis
- **Disclosure is Not Enough**
 - Needs to be integrated with the budget decision-making process

For further information



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