Parliamentary Library Lecture - Fiscal Sustainability - Stein Helgeby

15 September 2021

Slide 1: Fiscal Sustainability (title slide)

Introduction

Good morning and thank you for the opportunity to speak to you about fiscal sustainability.

Since I began in the PBO last November I have had many many discussions about Fiscal Sustainability. Regardless of where you begin the conversation on budget matters, it quickly gets around to sustainability. When we asked the PBO's expert panel for suggestions for analysis topics, one of them replied that there were three: sustainability, sustainability and sustainability.

This is hardly a surprise. The government's response to the pandemic has involved a lot of spending which translates into a lot of additional debt.

Slide 2: Australian Government gross debt (as a share of GDP)

As a share of the economy, commonwealth debt is higher than it's ever been outside of wartime, as you can see in this chart, so it is natural to ask if our finances are sustainable in the longer term. To reflect the need for information and analysis, in the space of nine months the government published two budgets and an Intergenerational Report,

Slide 3: (sequence of PBO reports – these will come in one by one automatically)

and the PBO has published a steady stream of information and analysis designed to assist parliamentarians and the public get their heads around what has been a 'rapidly evolving situation'.

So I am going to talk today about fiscal sustainability.

There is rightly not a single accepted definition of sustainability; it is a multifaceted concept, and we'll cover some of that later. But I want to start with a description that underlies much of our thinking on the topic so far in the context of government finances.

Slide 4: Sustainability

A sustainable position is one which can be maintained indefinitely, in the absence of dramatic shocks and without the need for similarly dramatic responses.

Slide 5: Fiscal sustainability

This means that a fiscally sustainable position is one which can be maintained while pursuing similar borrowing and repayment approaches over the long term, such as that taxation and spending can be expected to operate within reasonable and expected bounds.

While policies may vary significantly over time and between different political actors, a fiscally sustainable position increases the likelihood that governments maintain policies around predictable long-term settings that are recognisable to all.

A fiscally sustainable position is in some senses a familiar position.

Slide 6: Fiscal sustainability (sustainability = confidence)

It is one we do not need to spend considerable time puzzling about. Shocks will come and go. It is the reversion to a familiar trend that matters and which consequently enables the private sector – businesses and households – to make financial decisions with confidence in the fiscal settings that may affect them.

By contrast, an unsustainable fiscal position is one with potentially dire consequences for the ability of governments to operate, to borrow, to maintain the confidence of the population, for predictability and for the ability to invest, privately or publicly. It is a challenging and unfamiliar position, not because there are shocks to the system, but because the *responses* to those shocks and their long-term ramifications are unfamiliar and have high potential to erode confidence.

Limitations

Slide 7: Fiscal Sustainability: limitations and caveats

Anyone who lives in the world of policy costings and budget analysis knows that it is a land inhabited by caveats. There are some important caveats to consider in thinking about fiscal sustainability, particularly when it comes to trying to make real-world assessments of sustainability either quantitative or qualitative. And just like in costings, the caveats here are just as important as the central case.

Slide 8: Fiscal Sustainability: limitations and caveats (first caveat)

One is whether we are **measuring the right thing** when we consider a position sustainable. In focusing on *fiscal* sustainability alone we might be focusing on a concept that is ultimately too narrow. There is already a lively debate in the accounting world about 'extended external reporting', which tries to bring a wider range of considerations into the assessment of the viability of firms.

Slide 9: Fiscal Sustainability: limitations and caveats (first caveat – Dasgupta review)

At a broader level, it could be argued that the framework of economic thought needs to account for broader measures of economic, social and environmental progress and wellbeing. That is an argument recently made by the Dasgupta Review into the economics of biodiversity commissioned by the UK Government. This is one of many analyses from within the economics profession proposing that nature needs to be better integrated into economic thinking.

A related argument could be made that to focus on a sustainable set of fiscal numbers is to risk neglecting the institutional framework that sits around decision making, but that is a big topic beyond my theme today.

Slide 10: Fiscal Sustainability: limitations and caveats (second caveat)

A second caveat is that just because a position is **sustainable does not mean that it is desirable**. If fiscal sustainability alone was the presiding goal, we could not be certain that governments would take the actions necessary to improve citizen's livelihoods. There are many undesirable circumstances that can endure for a long time – poverty, oppression, ill-health, to name just a few - and we cannot always assume that we have the means to change them without presenting challenges for fiscal sustainability.

Slide 11: Fiscal Sustainability: limitations and caveats (third caveat)

The third caveat is an issue of **adaptation**. Will a given position be fiscally sustainable if circumstances change? Could a significant geopolitical shift or the consequences of climate change, for example, impact our ability to maintain our fiscal policy settings indefinitely? Could a change in values and priorities change the way we think about sustainability from a fiscal lens alone? In such cases, our view about what would be a sustainable position will change to reflect new realities.

A fiscally sustainable position therefore has limits – there is a point at which a situation ceases to be sustainable, all other things being equal, and there is a point at which we do not want it to be sustained. For example, because it has ceased to be as desirable as it once was.

So, fiscal sustainability is not everything.

But it is something.

And, for an organisation such as the PBO, fiscal sustainability is actually a lot. I am going to tease out a bit more about that.

The PBO and sustainability

Slide 12: The PBO's purpose

The PBO is one of around forty independent fiscal institutions around the world, the most famous of which is the US Congressional Budget Office. We were set up over nine years ago to provide the Parliament, and through it a broader audience, with information and independent fiscal analysis on key issues. This takes the form of confidential costings and analysis, public release of costings of election commitments, and making information more transparent and accessible. That information will, at least for the foreseeable future, particularly relate to fiscal sustainability.

Slide 13: (PBO cartoon)

Despite this cartoon, I can assure you that people are still very interested in the figures, perhaps more than ever.

Given the complexity, and the sheer volume, of financial information that is available for the Commonwealth, we provide some means of bridging the information accessibility gap that would otherwise exist between different participants on the political process. We are part of levelling up the capacity of Parliament to exercise its role in financial matters.

We are also about helping to keep that information in perspective – in a context.

Slide 14: The budget 'forward estimates' period

There are masses of financial information available, but much of that information has a relatively near-term focus. Considerable attention is paid to the Budget and MYEFO, which use a four-year focus in their economic forecasts and Budget estimates. You can see here the very first table which appears in every set of Budget papers.

It is understandable that the debate focuses on more immediate timeframes and data. That is what will affect us sooner, and the longer-term can seem far away, with many intervening decisions and events to change specific outcomes. Once it gets beyond the near term however, prediction seems a foolish errand, particularly as the population ages and different generations move through the education system and the labour market.

Slide 15: Looking beyond the forward estimates

We could leave it there and say that 'four years is a good period to allow us to think about the future', however, this would not allow us to consider if today's fiscal policy settings will remain sustainable or appropriate for future generations. As an independent agency, PBO looks across election cycles and considers this question closely.

When we do consider the future, particularly the fiscal future beyond a year or two, it is not about prediction. Forecasts will be wrong. Budgets are planning documents, not predicting documents.

Slide 16: (budget extract: Domestic economy – detailed forecasts)

This mass of numbers are the economic forecasts from the last Budget. They are the base assumptions from which the Government make its plans.

Slide 17: (PBO tile: Budget forecasts, medium-term projections, long-term scenarios)

We focus on the longer term to understand the underlying dynamics and therefore the sustainability of a position. Budgets and financial positions are really just maths.

When we go beyond the four year period in our work at the PBO, we are showing the maths, the dynamics, how the finances behave over time.

By doing that, we are able to talk at a high level about trends – within a programme, between programmes, between taxes and spending, across the tax base itself, and at the level of the aggregates. These represent the top level, stylised, mathematics *of a Budget*

Slide 18: The budget in a nutshell - The reconciliation table

I'll start with the short term. If I were to pick a single table that simply captures any government Budget, it would be the reconciliation table. Here it is for the 2021-22 Budget, and for you Budget nerds out there this year is actually the 25th anniversary of this table appearing in the Budget.

This is the table that shows what the budget balance was last time, at the 2020-21 MYEFO …

Slide 19: The budget in a nutshell - The reconciliation table (start point)

… and the changes since then. First, the changes because of the changed view of the economy. We call these 'parameter variations'. Back in May the economy was thought to be stronger than was thought last December - so these numbers are all positive.

Slide 20: The budget in a nutshell - The reconciliation table (parameter variations)

If you want to know the reasons for those changes then you can find that in Statement 2 of Budget Paper 1.

The other reason for changes to the budget balance is government policy decisions, which you can see in the next line. The individual decisions are itemised in Budget Paper 2.

Slide 21: The budget in a nutshell - The reconciliation table (policy decisions)

In net terms, the government's policy decisions at the Budget reduced the budget balance, but you can see in the last line, which shows the new budget balance …

Slide 22: The budget in a nutshell – The reconciliation table (2021-22 UCB)

… that in some years the net effect of the parameter variations and the policy decisions is to improve the balance – the new numbers are less negative than the old numbers – and in some years the net effect reduces the balance. These figures will be the starting point for the same table at the next MYEFO later this year.

This is the maths of the budget.

We can look at the history of Budgets in this way. Here are all of the parameter variations since that first reconciliation table in 1996.

Slide 23: Budget variations over time (parameter variations)

These are changes to the budget because the economy was thought at the time to be going better or worse than previously expected. You can see the upwards variations during the mining boom and the downwards variations during the global financial crisis.

And here are the net impacts of the government's policy decisions for each year.

Slide 24: Budget variations over time (policy decisions)

You can see here the big personal income tax cuts through the mid-2000s, and the government's response to the GFC in 2009.

And here is the net impact of the changes.

Slide 25: Budget variations over time (total variation)

In many years, the parameter and policy changes offset each other, the big exception being during the crisis of 2009 when the government's policy decisions were in the same direction as the parameter changes. For most of the past decade there have been only small parameter variations matched by relatively small policies, usually in the opposite direction.

You might have noticed that the chart does not cover the full impact of the pandemic. Here it is:

Slide 26: Budget variations over time (total variation - expanded scale)

So, how does this relate to sustainability? As I said earlier, a sustainable position is a familiar one. While there have been very significant events, there are clear patterns of the interaction between economic events and government policy. This is a sustainable picture, even though the shocks are not predictable, and the government response varies in form.

Budgets are, of course, not all only reactive. The relationship between the economy and policy sets the maths of the budget in motion, but policy can also subtly change the maths.

I'll give a couple of examples, one for expenses and one for revenue. This first one is from our JobSeeker report released a year ago, where we explored how both gradual welfare changes as well as economic conditions have shaped the Budget and have affected men and women.

Slide 27: The budget is also shaped by gradual policy changes … like welfare payment reforms

During the period of falling unemployment from the end of the 1990s recession to 2007, JobSeeker recipient numbers tracked unemployment relatively closely for both genders.

[click for animation]

However, a growing divergence can be seen for women from around 2011 due to welfare changes, such as the closure of 'partner payments' and the removal of parenting payment exceptions.

The change in economic conditions played a strong role in this case too, with the global financial crisis leading to a rise in recipients of both genders.

Slide 28: … and changes to tobacco taxation (growth in tobacco prices)

A second example of how policy can change the underlying relationship between the economy and the budget is multiple actions governments have taken over many years to increase the price of tobacco products through excise rates.

Slide 29: … leading to behavioural changes (consumption changes)

The data shows how this has contributed to significant falls in consumption.

Policy changes need not be spectacular to change the relationship between the economic activity and the budget, the maths. You might call these structural changes to the budget. These will continue to impact on the budget.

COVID has had a substantial effect on debt levels and the trajectory of the mathematics.

I am going to use the framework we published back in April before the Budget to look at some possible long-term trajectories. What you are going to see here is a preview of our updated results post Budget that we will publish soon.

First, here is a diagram of how we have approached our analysis.

Slide 30: Fiscal Sustainability linkages

The trajectory of the future debt-to-GDP ratio will depend on three factors: interest rates, economic growth and the budget balance. We call them R, G and B.

Slide 31: Fiscal Sustainability linkages (R, G, B)

Economic growth will depend on growth in population, workforce participation and productivity. For those mathematically inclined, you can see the equations in our report.

Slide 32: Fiscal Sustainability linkages (budget policy: structural/cyclical)

Of course, the budget balance and debt scenario we are now faced with has structural and cyclical aspects. Not only have taxation receipts reduced due to the lack of economic activity, the Government has borrowed more in order to fund its policy response to the pandemic. The impact of immigration affects our long-term population.

The trajectory of the mathematics will shape the sustainability of government finances. We can measure that impact by looking at debt balances and debt to GDP ratios.

Slide 33: The debt-to-GDP ratio over 25 years

Debt and the servicing of debt are a cost that the past and the present impose upon the future. The benefits of that debt to the future depends on how it has been used – the balance to be struck between investing for the future and meeting short-term financing needs, although these are not mutually exclusive (keeping the economy viable in the short term leaves us with more options in the longer term, compared to the opposite circumstances).

Debt levels are now comparable only to WWII, and they will keep growing for some time to come.

Slide 34: The debt-to-GDP ratio over 120 years

There are many ways to understand the significance of this debt. It would be unwise to attempt to diminish the magnitude of it.

The fiscal sustainability challenge is how these debt balances can be managed over time and mathematics.

You can clearly do best with high economic growth, budget surpluses and low interest rates, but reductions in government debt have historically occurred through different combinations of these.

Slide 35: Reducing the debt-to-GDP ratio: post WW2

Here is our first example. It's the largest fall in the debt-to-GDP ratio in Australia's history. You might be interested to know that the dollar value of government debt hardly changed during the post-war years and the budget stayed in deficit, but because the economy grew so quickly and interest rates stayed so low, the debt-to-GDP ratio plummeted.

Slide 36: Reducing the debt-to-GDP ratio: the late '80s

The next example comes from the boom period in the late 1980s, where debt also fell but for a different combination of the three factors. In this case, interest rates were high – higher even than GDP growth – but budget surpluses drove debt down.

Slide 37: Reducing the debt-to-GDP ratio: 1996-2007

Moving on to the post-recession period, the combination of factors was similar to the late 1980s, but with a twist. Economic growth and interest rates both moderated as inflation came down. For the government, however, the interest rate being paid on debt was still largely locked in, an overhang from the ten and twenty year bonds issued in the 1980s. Through a combination of small operating surpluses and selling assets, the government's budget balance was positive enough to bring down debt, with much of the work done in the late 1990s.

Slide 38: Reducing the debt-to-GDP ratio: the next decade

Looking now to the years to come, the combination of factors is likely to be different again. The budget balance is projected to remain in deficit, but the relationship between GDP growth and interest rates is very different. Much of the current debt is locked in for decades at very low interest rates.

Going beyond the medium-term period in the Budget raises the question of whether we need to make dramatic changes in policy in order to deal with the debt.

Have we come to the end of an era where we knew the broad parameters within which Governments needed to respond, and do we now need to make a leap into a different approach to government? These are questions that sit behind some of our key recent publications as well as our next annual Medium-Term Projections Report, which are rebranding as *Beyond the Budget*.

Slide 39: Reducing the debt-to-GDP ratio: the next 40 years

Here is what we are calling our 'middle' scenario, out of twenty seven different scenarios that involve different combinations of R, G and B, which I'll come back to in a minute.

Recent publications

Before that, I want to briefly touch on the five-yearly *Intergenerational Report*, released in July, which makes a significant contribution to these same questions, but taking a different angle to ours.

Both approaches picture a future financial position of the Commonwealth over the long term. First, the trajectory for debt in the IGR

> *Slide 40: The IGR projects higher debt levels than the PBO over the long term (IGR line)*

And then our middle scenario trajectory:

> *Slide 41: The IGR projects higher debt levels than the PBO over the long term (PBO line)*

On the surface, these seem very different pictures of the path of Commonwealth finances.

Perhaps the different results reflect people using different data, or different models, or different parameters?

In fact, they each use the same data and economic parameters. The PBO is under a legislative obligation to use the parameters as set out by the Government. So, we always start out from the same place.

Why, then, is there such a difference?

There is one critical difference between the two sets of results. The IGR shows what happens if the current Government fiscal policy settings are left to run indefinitely. That shows very clearly that a future without further decisions, the unchanged policy future, looks like an unsustainable future.

The PBO model, on the other hand, assumes that Governments will keep making decisions and that they will, on the whole, want to take actions to keep the finances sustainable.

> *Slide 42: The IGR projects higher debt levels than the PBO over the long term (additional text – no policy change / familiar policy continues)*

They will want, in fact, to continue within the long-standing expectations for political action in Australia. We base this not in hope but in the observations we saw earlier, that economic developments and policy interact in familiar ways.

If you put those two pictures together, you can get a sense of the level of focus that Governments, of whatever shape, need to do to maintain the fiscal sustainability we are used to.

While some of my colleagues will no doubt wince at this thought of nuances and qualifications being cast away, the gap between the IGR line and the PBO line is around 13 per cent of GDP by 2060.

That gives us a rough sense of the extent to which governments need to be able to continue to act over the longer term. To give this necessary action some context, this chart demonstrates the extent of fiscal consolidation that has taken place at various points in our history:

Slide 43: Previous fiscal consolidations

I should note that not all of the consolidation that has happened in our past has been driven by policy. We need to take into account what was happening in the economy at the time, and most recoveries in the budget balance have come about through a combination of the economy and policy.

A key point to make about the PBO's fiscal sustainability work is it is not focused on a central scenario alone – we are not trying to picture the future that we consider to be the most likely.

We take this approach because uncertainty is fundamental to thinking about underlying trends and dynamics.

Five years ago, even the most pessimistic of fiscal projections would not have resulted in the current levels of debt Australia has found itself in.

One way in which we can undertake analysis in the face of uncertainty is to provide confidence intervals around central scenarios.

Slide 44: Confidence intervals are one way of showing uncertainty

That gives a sense of the range of possibilities. The Budget papers include these around the Government's economic forecasts and Budget estimates. I have shown an example here.

A second way is to undertake scenario analysis.

Slide 45: We use fiscal scenarios to explore uncertainty

We take the second approach – scenario analysis. The Budget papers also undertake a version of this, analysing the sensitivity of projections of the underlying cash balance to assumptions for productivity growth, the terms of trade and the yield curve, looking at each in isolation.

Our analysis takes a slightly more complex approach over the longer term. As I said a bit earlier, we have run our 27 scenarios, with different combinations of high, middle and low levels for economic growth, interest rates, and budget positions. Our specifications for economic growth are built using a 'three-ps' framework, with different levels of population, participation and productivity. We assess fiscal sustainability under each of those 27 scenarios.

Here are the middle, downside and upside scenarios, where the extremes are simply a result of applying the maths to the combination of the best and worst scenarios for each of R, G and B.

Slide 46: By varying each assumption in turn we can project a range of scenarios for debt

The scenarios we have examined are built around historical variations to see how the various factors have behaved over periods that have included strong growth as well as recessions, reforms as well as periods of policy quiescence, periods of stronger fiscal consolidation as well as periods of fiscal expansion.

S*lide 47: The PBO is developing a fiscal sustainability dashboard which explores debt scenarios*

In order to illustrate the options, here is what we are calling an interactive dashboard, which we hope to have up on our website soon and will allow you to see what happens with different options.

S*lide 48: The dashboard can vary depending upon the assumptions chosen*

For example, if I select a lower interest rate option, with economic growth and the budget balance unchanged, the trajectory for debt is better.

We built these scenarios by looking at how R, G and B have varied over history, by using overall 25 -year historical averages, but this might seem quite problematic when it comes to discussing productivity, for example.

Productivity growth has been a significant part of the success of Australia's economy in distinct periods; and not in others.

Slide 49: Productivity is key to ensuring GDP growth returns to historical levels

The measurement of productivity growth is quite volatile, but it is clear that, in trend terms, it has now been low for a significant period of time.

cent.

Slide 50: Productivity is key to ensuring GDP growth returns to historical levels (additional IGR line)

The IGR assumption, as well as our 'middle case' assumption, is for yearly productivity growth of 1.5 per cent.

Slide 51: Productivity is key to ensuring GDP growth returns to historical levels (0.9% line)

Ongoing productivity growth at the recent historical lows is clearly conceivable. Recent reforms to return to higher productivity growth have been patchy. In undertaking scenario analysis, we question the likelihood of a return to historic long-term averages, and consider the alternatives. For example, what if productivity growth were to average only 0.9 per cent over the next forty years?

If we go back to our dashboard …

Slide 52: A low productivity scenario increases long run debt levels

… lower productivity growth would result in lower GDP growth, and therefore a higher debt-to-GDP ratio for longer.

A sustained decline in productivity growth would represent a failure on many levels. It would mean a long-lasting stagnation in the living standards of all Australians. It would also be significant on a narrower, budgetary, level.

We would also need to assume that no developments – policy choices, external economic drivers, technology – would occur to lift productivity back to even the lowest range of our 25-year averages.

That seems possible, but less plausible than the possibility that some developments will combine to lift productivity above that lowest range. This scenario leads to an important point in the R-G-B framework, which is that these things are not independent.

At the very least, a low productivity growth scenario would be accompanied by lower interest rates. While we don't know exactly how much lower, the lower interest rate scenario takes us in that direction, which of course improves our debt trajectory.

Slide 53: However, usually interest rates move with GDP, which reduces debt levels

There are, however, a wide range of productivity-enhancing reforms available to Australia, in health, skills and human capital, infrastructure, market functioning and the exploitation of data and digital strategies.

For our modelling purposes for our 'middle case', which like the IGR is based on longer term trends, we assume that some of these opportunities will be taken, sufficient to reflect our longer-term history, but we don't speculate on which opportunities they will be.

Let's look at all of our 27 scenarios in one hit

Slide 54: Only in our downside scenario does debt rise above medium term levels

Of the 27 scenarios, only our worst-case scenario does not maintain fiscal sustainability, in the sense that debt does not fall. This is a scenario of high interest rates with low GDP growth, maintained on a permanent basis.

Slide 55: Only in our downside scenario does debt rise above medium term levels (*with green line)*

This seems possible, but barely so. Our scenarios illustrate the degree of the gap required between economic growth and interest rates to produce an unsustainable scenario.

Another way of putting this point is to say that Australia currently has more paths that maintain fiscal sustainability than paths to unsustainability. It has more familiar paths available to it than not.

That is not to say that there might be good reasons to prefer some sustainable paths more than others – for example, because they reduce debt at a faster rate, or they strike a different balance between the contributions of economic growth and budget balance changes to debt reduction.

It is simply to say that more scenarios lead to a reduction of debt a share of GDP over time, rather than to further debt increases.

Keeping the focus

Slide 56: Fiscal sustainability linkages

To the extent that we focus on debt, we should therefore focus on economic circumstances – on interest rates and payments, on economic growth. We therefore need also to focus on population, participation and productivity, which leads us back to our diagram and the maths.

The high-level maths would suggest that the focus on economic growth (on population, participation and productivity) as well as Budget policy and interest rates is key to the predictable and sustainable delivery of services and benefits through the disaggregated budget.

To the extent that any of these head in an undesirable direction, the remaining drivers will need to do more of the work to keep debt sustainable.

Slide 57: Fiscal sustainability linkages (policy and growth)

In particular, budget policy has a harder role to play if these factors move away from their sustainable long-term trends. I have mentioned that policy can play a role, for example in enhancing productivity growth, leading to stronger economic growth and therefore fiscal sustainability.

That said, we may also be comforted that other linkages work to stabilise things, and I've looked at economic growth and interest rates in this context.

Slide 58: Fiscal sustainability linkages (growth and interest rates)

Budgets, though, are not just about aggregates, and not just about the maths. They are also about services, benefits, incentives and a whole range of non-financial outcomes.

In cases where fiscal settings move too quickly and result in year-to-year policy unpredictability, they frustrate the achievement of those non-financial goals. Budget flexibility seems a good thing at the aggregate level, but it comes at a cost at the disaggregated level.

How can these multiple objectives be squared away, to strike the right balance between fiscal sustainability and service predictability?

We think it is important to keep those considerations regularly in mind and to check, from time to time, how many fiscally sustainable paths we still have available to us.

If, as events progress and decisions are made, more paths lead to unsustainable financial positions, it will be important to know that, sooner rather than later.

So we will keep growing our focus on fiscal sustainability.

Slide 59: Our dashboard focuses on key variables

Our simple dashboard, updated a few times a year, will give data on the key variables – interest rates, economic growth and the budget position; and, population, participation and productivity.

The dashboard will also show our most recent modelled scenarios so you can see how many of them lead to sustainable long-term finances.

While a dashboard like this will not change very quickly, it will provide a base of information to suggest if we are keeping open our paths to a sustainable fiscal future, or starting to narrow the range.

There is value in keeping pathways open.

Early actions to respond to options having closed will come at a lesser overall impact than allowing even more paths to close before action is taken.

Slide 60: Fiscal sustainability has its limitations (1)

Conclusion

I said at the outset that there are limitations to the concept of fiscal sustainability.

Firstly, there is the limitation of scope.

Secondly, there is the limitation of desirability and the constraints for decision making.

Third, there is the limitation of adaptation.

These limitations are real and important.

Fiscal sustainability needs to be seen in the context of these limitations. We need to see the maths, but we also need to be attentive to broader debates.

If the movement towards extended external reporting takes the form of common standards, and as social and environmental conditions become more integrated with economic analysis, the way in which financial statistics are framed and presented will evolve too. Organisations such as the PBO will be asked to bring different perspectives to bear in our future analysis.

Slide 61: Fiscal sustainability has its limitations (2)

Nor should we confuse data and models about fiscal sustainability with the debate about what we as a polity wish to achieve.

Fiscal sustainability is a servant, but the risk of being fiscally unsustainable turns it into the master. There is an asymmetry in that multiple forms of fiscal sustainability are possible, but unsustainable finances are always problematic.

Finally, the fiscal system sits within a broader set of systems. Where circumstances or values change, the fiscal system needs to change too.

Those limitations do not detract from the importance of fiscal sustainability. They say we need also to see the broader context.

Slide 62: Thank you (end slide show)

So, have we come to the end of an era where we knew the broad parameters within which Governments needed to respond, and do we now need to make a leap into a different approach to government?

Our own work would suggest that the answer is ‘not necessarily’.

The central question is whether our polity can do again what it has shown it can do before – keeping an eye to the big drivers of the budget and financial position, pursuing reforms for their longer-term benefit and creating the conditions favourable to productivity.