Consejo Fiscal

Workshop on

“Marco fiscal peruano a 20 años de las primeras reglas fiscales”

INTERNATIONAL MONETARY FUND

Peru’s Fiscal Framework: An Outsider’s Perspective

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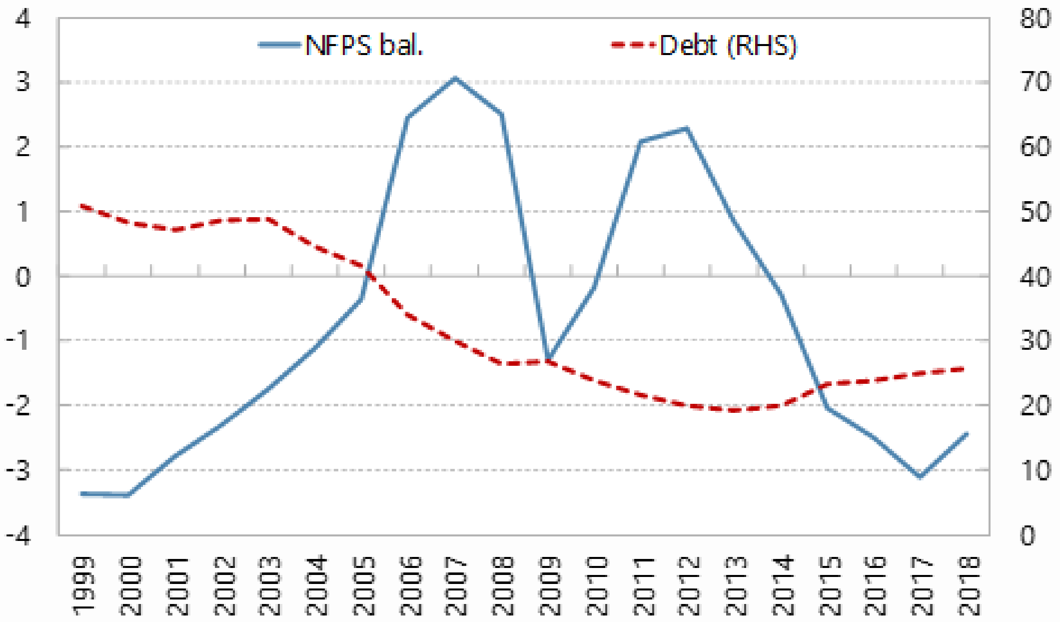
The analysis and policy considerations expressed in this presentation are those of the Peru team and do not necessarily represent the views of the IMF, its Executive Board, or IMF management.

Background

- **Strong fiscal outcomes**
  - Long period of fiscal surpluses
  - Manageable deficits
  - Public debt nearly halved
- Robust **economic growth** and **fiscal reforms** have been essential
- But the design of an **appropriate fiscal framework** has also been key

Peru. Fiscal Balance and Public Debt, 1999-2018
(in percent of GDP)



Sources: BCRP and IMF Staff calculaitons.

Peru's Fiscal Framework: Two Pillars

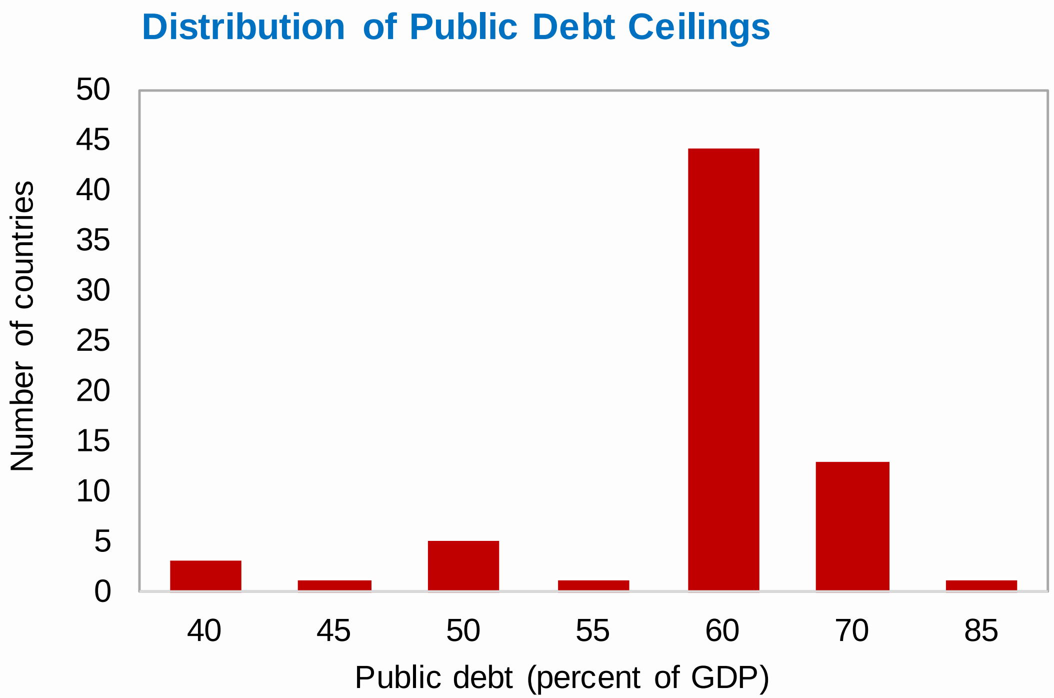
- **Institutions and procedures**
  - Law on Fiscal Prudence and Transparency (1999)
  - Multiannual Macroeconomic Framework (2003)
  - Fiscal Stabilization Fund (2003)
  - Fiscal Council (2013)

▶ **Worked well** and **evolved gradually** over time

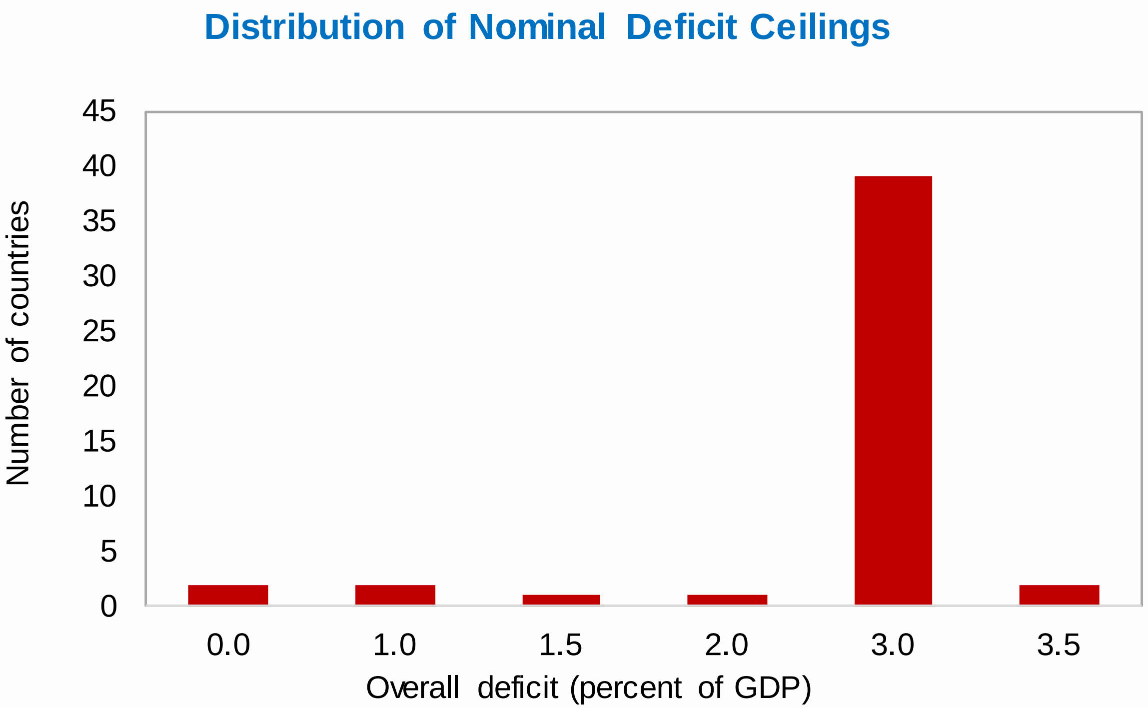
- **Numerical rules**
  - Ceilings for fiscal deficit, public debt, current expenditure, and primary expenditure
  - Rules for subnational governments (2009)

▶ Reflected **tensions** (including a suspension of the deficit ceiling in 2009-10) and **changed frequently** (2003, 2008, 2013, 2016)

Fiscal Rules Across Countries (2014-15)



Source: IMF, Fiscal Rules Database.



Source: IMF, Fiscal Rules Database.

Credibility vs. Flexibility: The Right Trade-Off?

- With a *debt ceiling* of 30 percent of GDP and a *nominal deficit ceiling* of 1 percent of GDP, Peru is clearly on the **conservative** side of the spectrum

- Fiscal policy must be **conservative** owing to Peru-specific vulnerabilities
  - Large share of fx-denominated debt
  - Large share of debt held by foreign investors

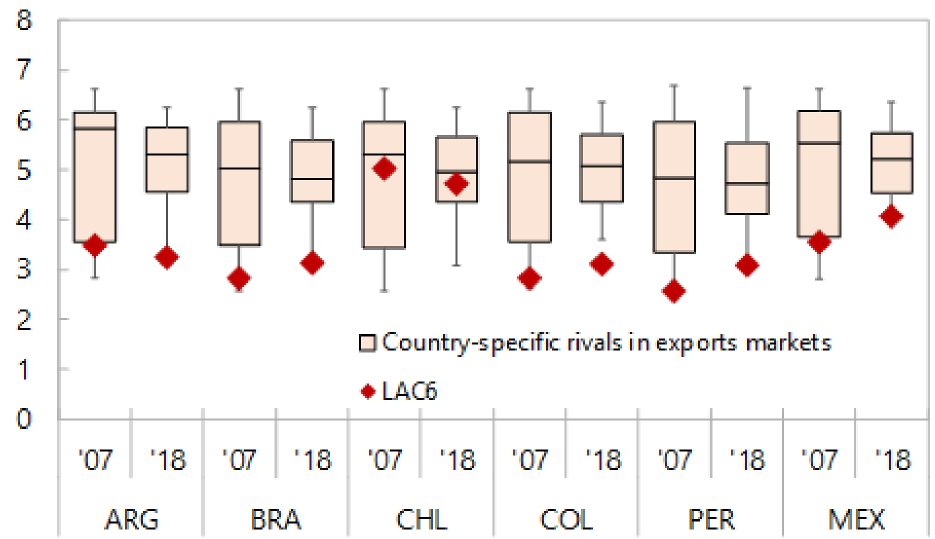
- What is the **max debt limit?**

- Is there enough flexibility for
  - A desirable **countercyclical** fiscal stimulus given the current growth slowdown
  - A substantial increase in public investment to **address the infrastructure gap** in the medium term

The Case For Flexibility

- **Preventing a procyclical stance** in the coming years is desirable
- **Addressing the infrastructure gap** is an important priority
- **The fiscal position is very strong** and confidence in Peru's government assets is high

LAC6 and Trade Competitors: Quality of Infrastructure, 2007-2018
(Index, 7 = best)



Sources: IMF Staff estimates with WEF and UNCOMTRADE data.
Note: Red diamonds represent the value for the corresponding LAC6 country. The box and whiskers correspond to the country-specific rivals.

Pro-Cyclical Stance and Limited Room For Investment Under Current Rule

- **Negative fiscal impulse** when a stimulus would be desirable
- Multiannual Macroeconomic Framework: to accommodate investment increase
  - **compress current spending**
  - **strong assumptions about increases in revenues** from improvement in tax administration

Projected Fiscal Impulse under the Current Fiscal Rule
(in percent of GDP)

	2019	2020	2021
MMM Projections			
Fiscal Impulse	-0.1	-0.4	-1.0
Revenues GG	19.7	20.3	20.7
Primary Expenditures GG	20.3	20.5	20.4
IMF Projections			
Fiscal Impulse	-0.7	0.0	-0.4
Revenues GG	20.0	20.2	20.5
Primary Expenditures GG	20.1	20.2	20.0

Note: Fiscal impulse in percent of potential GDP.

How To Introduce More Flexibility

- **Using more flexible targets.** For instance, returning to a **structural deficit** target
  - More complex and less transparent, and recent experience not fully positive

- **Relaxing current ceilings** so that the government has more room to respond to both cyclical and structural challenges
  - Reputational risks
    - Too frequent changes
    - Reduced buffers
    - Exposure to foreign investors' sentiment

Relaxing the Deficit Ceiling Would Not Undermine Fiscal Strength

- With fiscal deficit ceiling of 1.5 percent of GDP debt would stabilize below the 30 percent of GDP ceiling

Peru: Growth, Fiscal Balance, and Public Debt (Long Term)1/

	(in percent)	d^*=30	b^*=1	b^*=1.5
g	nominal GDP growth	5.75	5.75	5.75
e	exchange rate depreciation	0.5	0.5	0.5
f	share of FX debt in total debt	33.0	33.0	33.0
b	deficit-to-GDP	1.58	1.00	1.50
d	debt-to-GDP	30.0	18.9	28.4

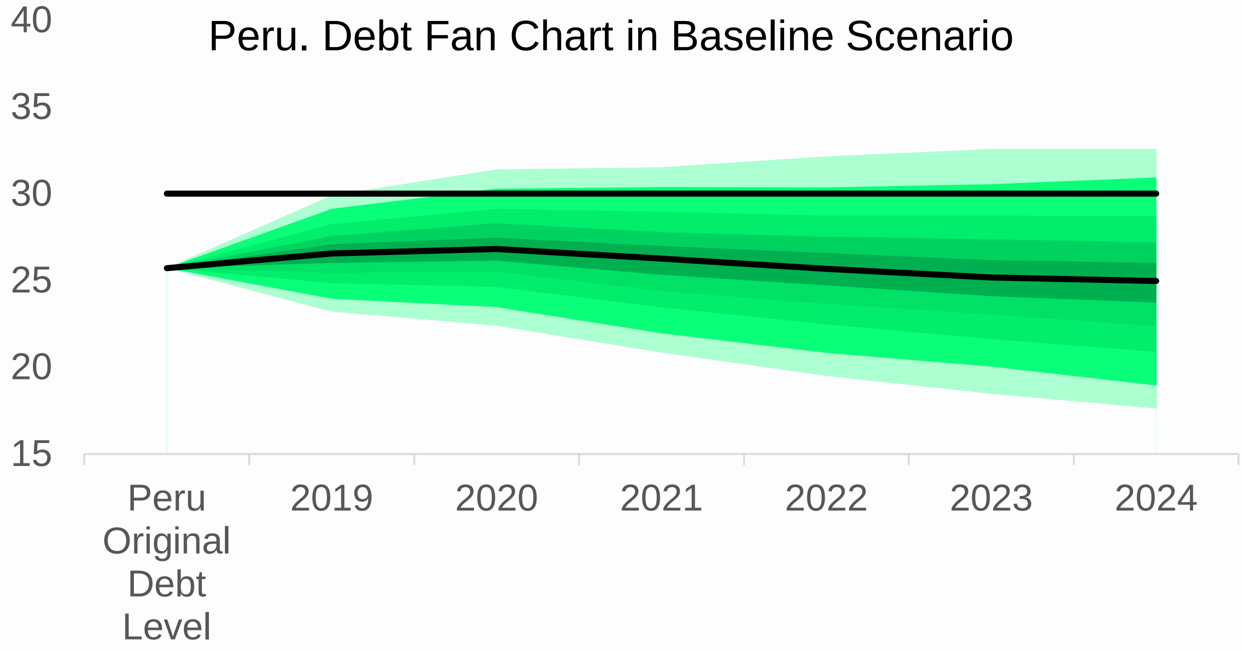
Source: IMF elaborations on the authorities' data

1/ Based on $b^* = -d^* \frac{ef-g}{(1+g)}$

Risks Under the Current Deficit Ceiling

- Under the current 1 percent deficit ceiling, the probability of breaching the 30 percent of GDP debt ceiling is only 14 percent in the medium term

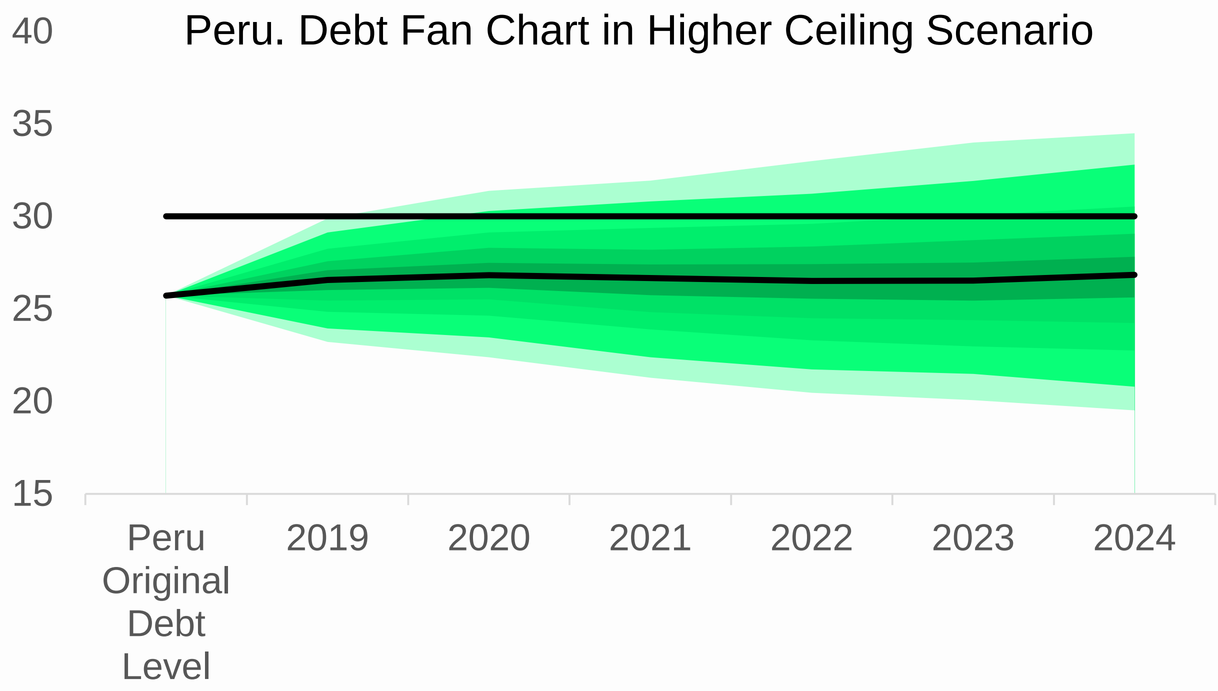
- The probability of debt exceeding 33 percent would be less than 5 percent



Risks Under the New Deficit Ceiling

- Under a 1.5 percent of GDP deficit ceiling, the probability of breaching the 30 percent of GDP debt ceiling would rise to 23 percent

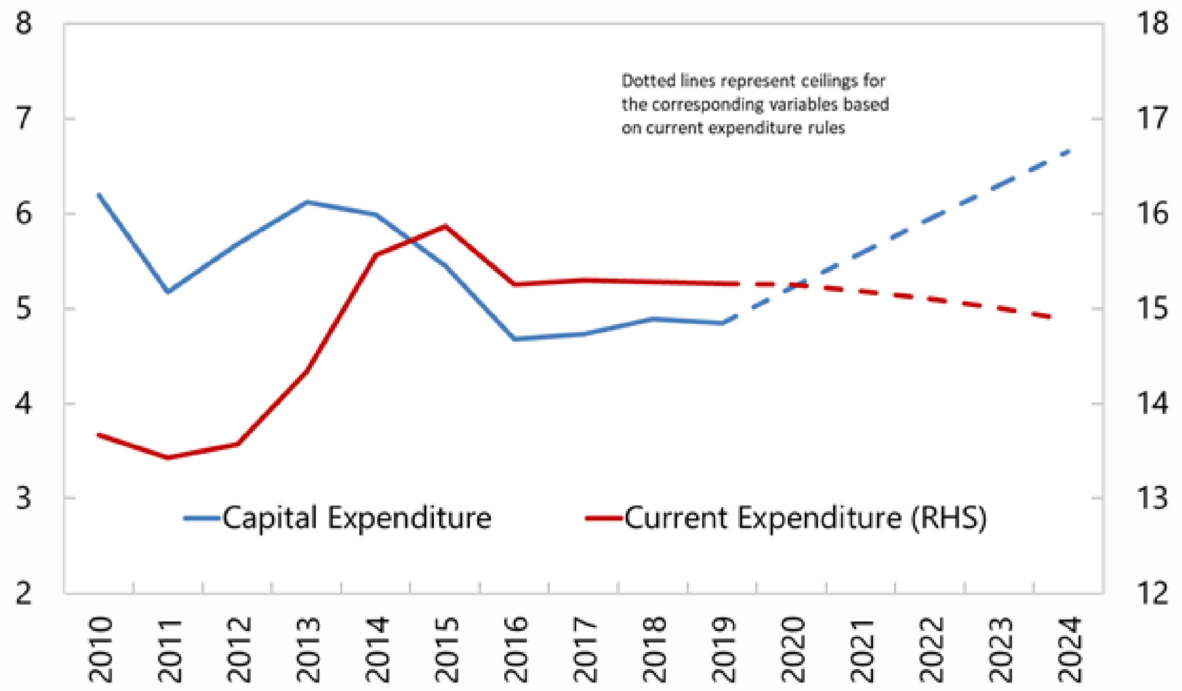
- The probability of debt exceeding 35 percent of GDP would remain less than 5 percent



Expenditure Ceilings Would Help Limit Reputational Risks

- The extra fiscal space could not be used to finance higher current spending
  - Real growth of current expenditure would be capped at 3-4 percent during 2020-24
  - The higher ceiling on total expenditure (2 percent higher) would preserve space for higher capital spending

Peru. Capital and Current Expenditure of the General Government
(in percent of GDP)



Sources: BCRP (historical data) and IMF staff calculations (projections).

Conclusions

- Peru's fiscal framework has been instrumental in achieving strong fiscal outcomes. However, numerical rules are quite conservative, ensuring robust fiscal buffers but lacking flexibility

- This is apparent at the moment, as the consolidation required by the fiscal rule clashes with the desirability of a countercyclical fiscal stimulus and the government's objective of increasing public investment to address the country's infrastructure gap

- A relaxation of the fiscal deficit ceiling to 1.5 percent of GDP could provide added flexibility without a significant increase in fiscal risks. Public debt would remain at low levels and expenditure rules would prevent the added fiscal space from being used to finance current spending, thus limiting reputational risks

Thank You