

Potential growth and Structural budget balance

CPB Approach

5 November 2015



Potential growth : CPB method and EC-method

- CPB-methodology : Potential growth , gdp growth medium term
 - Calculation only when update of medium term forecast
 - Before starting elections and coalition negotiations
 - Last exercise : 2014 Roads to Recovery
- EC-methodology : Cyclical component Emu-balance
 - Calculation every quarter for each short term forecast
 - Relevant for ministry of Finance



CPB's Potential growth in medium term

- CPB – methodology : Ces production function with labour and capital
- Main differences with EC-methodology
 - Production function market sector
 - Output gap government , health care = 0
 - Structural unemployment (no filter on unemployment)
 - > Replacement rate, wedge, relative prices
- Potential growth and medium growth GDP
 - Potential growth: labour supply, technological progress
 - Output gap closes in 4 or 5 years?
- Medium term projections based om potential and closure rule for labour market and tfp

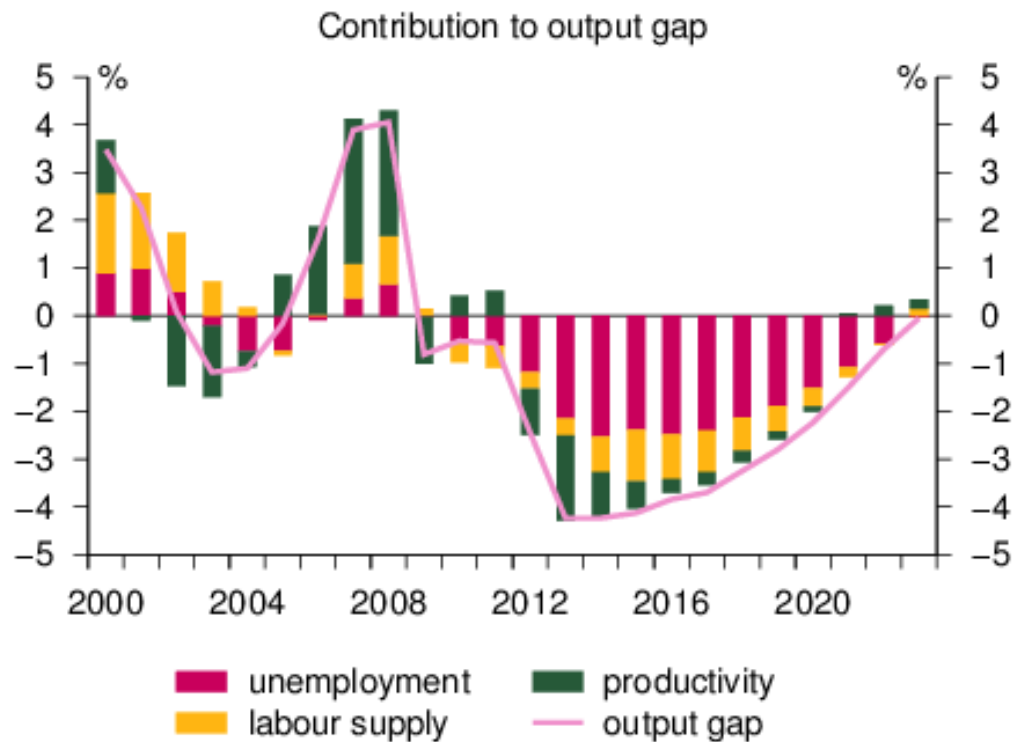


Roads to Recovery scenario's (published 2014)

- Some lessons from 2008-2009 crisis :
- Unemployment will return to 'normal' level ; can take some time
- Level-shift in productivity ? Hard to estimate
- Productivity growth will return to pre-crisis growth rates



Closing gap 2014-> 2023





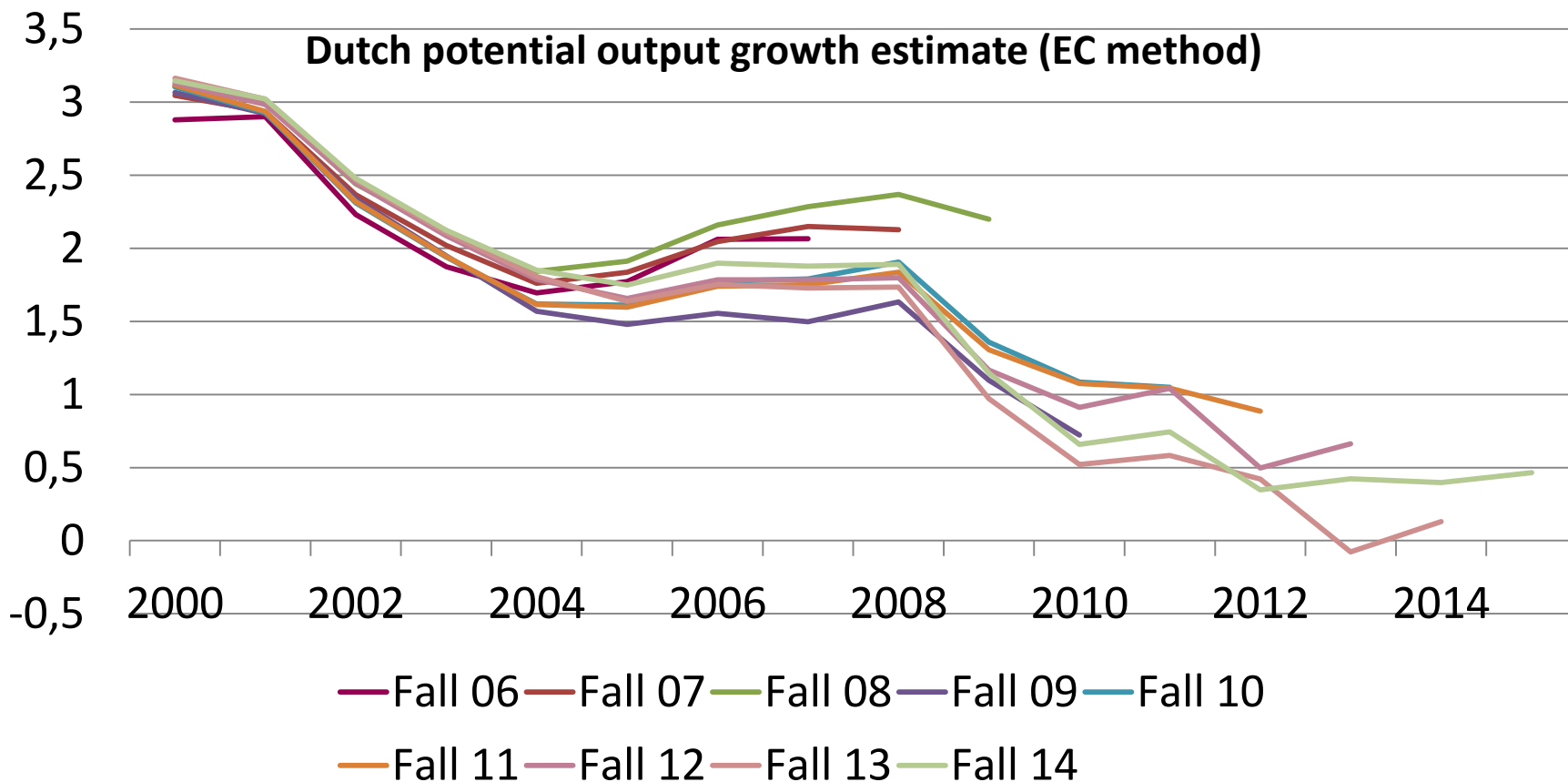
My opinion on EC-methodology

- Many improvements last ten years
 - Tfp-filter depends on capacity utilization
 - Alternative nawru specifications tested
 - Budget elasticity's recently updated

 - Structural indicators for extrapolation T+10
- But
 - Nawru remains pro-cyclical
 - Sensitivity potential growth for new projections remains
- Role of structural budget balance in EC-recommendations
 - A lot of policy debat going on



Significant 'revisions' of potential growth





Structural budget balances

- Using EC-methodology for output gaps
 - that's the one relevant for policy analysis
- Main problem: significant revisions in potential growth and output gaps
 - and level of structural budget balance
- CPB Policy brief on Structural budget balance (October 2014)
 - Volatility is problem because this a basis for recommendations
 - > room for judgement in development budget balance
 - Reduce volatility by stricter filters or structural indicators
 - > for structural unemployment and factor productivity
 - Apply additional indicators for recommendations
 - > Ex ante effect of fiscal packages



'Solution' of CPB to reduce revisions in potential growth

- Nawru : structural indicators
- End-point : adding additional years (medium-term forecast)
 - Short –term looks like Stability Programme (additional years)
- Output gap in year t is the same for projections for the short term and medium term
- Otherwise structural budget balance changes when adding additional years to projection
- 'Disadvantage' : result depends on projection medium term

=> But : we also have revisions