COMMENT

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Being the last who is scheduled to speak at the conference, allows me some licence to take an overall, more philosophical stance and to pose some general "existential" questions: Why are we all here? What is the use of the kind of work, which was presented in this session and in the conference?

The answer is simple. The role of the public finance analyst is to provide information so that the Government may do what individual households do as a matter of course: To incorporate a budget constraint in their decision processes.

The difficulty of attaining this should not be underestimated. Casual empiricism reveals that many Governments behave as if they believed, fervently, that they were Irish and "had time on their side". In contrast to the Irish paper's sombre Old Testament quotation, most European governments seem to pay more heed to the opening lines of the Koran which refer to "God the Compassionate, the Merciful", believing instead that "God will provide".

There are *structural* reasons for this attitude. Understanding the bases for them is important in being able to overcome them. I will offer two:

1. Governments are organised on sectoral, "vertical" lines, where individual ministries are responsible for only one aspect of people's

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overall well-being. Yet, as we heard these days, the problem impacts the welfare of entire generations, in a multi-dimensional, "horizontal" manner. Some countries, such as Finland, have dealt with this coordination problem through an ad hoc committee of the Prime Minister's Office. In the UK this approach has been formalised in the case of issues which are of "interministerial significance" by setting up special units with a semi-permanent structure. The Social Exclusion Unit is a case in point. Whichever way is chosen, the key issue is how to bring together at the same point those spending and those facing the budget constraint.

2. However, there is a deeper reason for the public finance problem. Much of social security consists of transfers from one group of people to another. In the course of this transfer, nothing is produced; hence the system is essentially a "zero-sum game". But, while this is true if *all* affected are taken together, for any combination of *part* of those affected, the game is *positive-* sum. When one party leaves the table, those remaining can, very simply, agree between themselves that the one missing will foot the bill. The missing party in the case which our conference examined, is the future generation, to whom all the bills will be sent in the form of postponing needed measures. Indeed, one can make a cogent case that the reason we may be facing a problem now, is because we have been sent the unsettled accounts of our fathers and grandfathers.

These observations serve to motivate some of the discussion of rules and straightjackets, which the papers of this session examined. Decision rules are useful in providing clear signals and as shortcuts to what can be quite elaborate arguments. That, however does not mean that they should become substitutes for thinking. Decision makers must ultimately understand the reasons for their actions and decisions. They must know what the results of their decisions are for variables and welfare targets which are (or should be) their ultimate goals. I will illustrate this point with three examples:

- In the discussion of contingent liabilities, the case of private pensions was mentioned. In their case the public finance implications depend on whether there exists an (implicit) guarantee formulated on the basis of income adequacy for the aged. Low rates of return on capital could reduce the values of private pensions decisively. This may lead to (political or social) pressures to intervene to increase living standards

of the old. In this way, public finance pressures in systems relying to a greater extent on private pension provision may mirror developments in public, PAYG, systems.
The ways in which this may happen, though are not captured symmetrically in projections. The *technical* implication for public finance projections, is that in simulations we should attempt to provide information to track not only accounting magnitudes, but also information on incomes and purchasing power, on which government decisions will be based. Otherwise simulations as a policy tool may mislead.

- A similar problem of contingent liabilities is not yet appreciated. A number of pension reforms rely on changes which are pre-announced a long way before. These changes can be quite drastic in the sense of altering perceived rights and entitlements. Much of post-reform simulations' improved picture reflects the full effect of these pre-announced changes. However, the drastic difference in entitlements between cohorts has led, in some countries, to some of the pre-announced changes to be overturned in the courts. In this way some of the more optimistic public finance expectations can be forcibly overturned. An adverse judicial decision is obviously not easy to model. Nevertheless, there *are* lessons to be learnt in terms of explaining the legislative decisions, grounding them on solid welfare motivation. Above all, it is important to design adequate transition periods, so that legislation does not affect closely comparable individuals in very disparate ways.

- The third example of where blind rule following can violate thinking was provided by the Irish paper. The Stability Pact was not designed to cover countries which need to invest fast in order to change development and growth paths. What is true for Ireland and Greece today will apply with greater force to transition countries currently attempting to join the EU. This point implies that consumption and investment (as in Keynesian thought) ought to be treated separately. To some extent the force behind this argument has been already acknowledged by the EU in setting up and maintaining the Community Support Frameworks, which explicitly recognise that real convergence requires separate treatment.

In the final analysis our attempts to quantify, define and provide transparent measures for the government budget constraints and to affect the political economy of policy formation must have three objectives:

1. Illustrate that policy can have no free lunches. To deal with real problems, real behaviour has to change. Masking inactivity behind accounting changes, as the accounting of pension in certain cases does, cannot lead to solutions.

2. Convince governments that time cannot *always* be on their side. In this respect the practice of calculating the marginal cost of delaying reform can be a powerful tool. We must remember, that age cohorts are not uniform in number. Given the long lead times in transition periods, delaying reform could mean that the reform could "miss" these large cohorts, leading to the cost of the reform being borne by far fewer individuals.

3. Create a constituency for change. On this count, policy prescriptions should be wary of erring on the side of being too apocalyptic. Economists, on the basis of some of their past forecasts, may be accused by policy makers of having "cried wolf" too often. The area of pensions (and often the lack of transparency is to blame) is too easy to manipulate so as to shift the solution of a problem in the future, hence often "disproving" predictions.