COMMENTS ON SESSION 3
TAXATION, REGULATIONS AND PUBLIC SERVICES

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Comments on "Service Regulation and Growth: Evidence from OECD Countries" by Guglielmo Barone and Federico Cingano

Barone and Cingano argue that anti-competitive regulations go against growth in provision of services like energy, telecom and transportation in OECD countries. The authors also argue that such anti-competitive regulations impair price reductions in those services that would, otherwise, benefit consumers at large.

This lack of growth in service provision and the slow transmission of price reduction is due to three main factors, according to the authors. In the first place, setting regulation of prices and tariffs is a very complex issue, where even knowledgeable regulators tend to err. In the second place, by forcing "unbundling" of investments between generators and distributors, most economies loose opportunities to exploit economies of scale and scope in such services. Finally, the authors also argue that such excessive regulations hamper productivity gains at the inter-industry level, which is the main focus of their analysis.

This is very well crafted paper, where macro- and micro-analysis are carefully entangled and explained. In my opinion, the main conclusions against over-regulation in the service sectors could as well be extended to the health sector, where regulators have also requested "unbundling" of investments between the insurance component and the hospitals components, losing "economies of scale-scope", as explained before.

However, such conclusions seem to me a bit "counter-intuitive" when applied to the financial sector, where the recent financial global crises tells us that the lack of proper regulation prompted a severe and long-lasting mortgage and derivative crises. For instance, the Dodd-Frank Act in the United States and the Basle III regulations seem to be on the right track of strengthening regulations in order to avoid future "systemic risks".

Regarding their econometric work, their "working-horse" regressions focuses on the Real Value-Added Growth for the 1996-2002 period for OECD countries, as in equation (1):

$$VA_{j,c} = B_0 + B_1\ SERVREG + B_2\ SHARE + U_c + U_j + Error_{j,c} \tag{1}$$

where one of the main hypotheses has to do with finding $B_1<0$; in this case the argument is that higher regulation would imply lower growth in the provision of such services. Interestingly, the authors find statistical support, in a cross-country panel of a fixed-effect model, to argue that the rule of law (strong institutions) would permit that firms operate better in a deregulated framework, where markets conditions would benefit consumers.

Although the paper does not focus on emerging markets, let me suggest the authors to extend their analysis to those countries, since there seems to be a historical cycle regarding the regulation of services. In my experience as civil servant in Colombia, I have noticed that in many less developed economies the State moves late in regulating the provision of services. Hence, in order to catch up historically, then they move to the point of setting an over-regulatory framework which, indeed, might end up causing a lot of the problems stated here by Barone and Cingano.

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Comments on "Growth Implications of Structure and Size of Public Sectors" by Hans Pitlik and Margit Schratzenstaller

The main message of Pitlik and Schratzenstaller, in their interesting paper about structure of public sectors, is that there is not such a thing as "one-size-fits-all" both regarding public sector structure in promoting growth and concerning the topics of taxes and expenditure.

The authors analyze the "friendliness" indicators of growth for EU-12-15 and OECD countries and find, in the spirit of "endogenous growth models", that tax/expenditure composition is much more important that the size of revenue collections of outlays.

The authors take dispersion in the growth "friendliness" index as evidence of lack of policy coherence. Consequently, Pitlik and Schratzenstaller call for pursuing complementary policies to gain coherence, finding that over-regulation seems to play a role in growth stagnation (as in the case of Greece), while deregulation apparently promotes growth (as in the case of New Zealand).

On the issue of productive vs. unproductive expenditure, the authors explain that this continues to be an open debate matter. On the operative side, you could always argue about increasing expenditures in the "meritory ones" (education and health), while in the case of the "golden fiscal rules" you could as well argue that fixed capital formation is good to propel sustainable growth in the near future.

Let me suggest to the authors the adoption of an explicit theoretical framework in order to better organize this kind of discussion. For instance, the adoption of a model would allow the authors to better cast their hypothesis about growth promotion/retardyness, especially since productive/unproductive definitions are rather arbitrary. The second suggestion I offer is to include in their analysis cases of *ex ante*/*ex post* responses to the current European crisis, which I reckon could easily be introduced, given the complete research they have already conducted regarding both tax and expenditure structures.

Finally, let me pose two questions. How is it that well positioned countries such as Spain and USA ("friendliness index") have experienced so much macroeconomic pain recently (2010-12), lagging behind in the growth field and facing high fiscal tension? This is an example of how useful an analysis of *ex ante*/*ex post* experiences could be. My last query has to do with deepening their analysis with regard to the "effective tax burden", because clearly nominal or marginal rates do not tell the whole story regarding tax collections. On the expenditure side, it would be vital to include the impact of the so-called "contingent liabilities", which will significantly alter current expenditure structures, as discussed in previous fiscal workshops of the Banca d'Italia.