Fiscal policy under rules and restrictions

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In the last fifteen years, several countries have adopted fiscal rules and restrictions in order to guarantee fiscal discipline. This thesis discusses some of the main motivations, forms, and effects of such restrictions. Restrictions on public debt are compared with restrictions on primary deficit, showing that economies with the former type of sanctions feature higher social welfare than economies with the latter type. The incentives of a government facing electoral uncertainty to implement structural reforms in the presence of a deficit restriction are also explored. In designing a reform package, the government faces a trade-off between enhancing its electoral chances by compensating individuals and the cost of violating the restriction. Regarding Europe’s Maastricht Treaty and Stability and Growth Pact, we find that they have been relevant to reduce deficits, although none of them have altered the cyclical behaviour of fiscal authorities in the Eurozone. We also conclude that the recent reform of the SGP has given more room for the implementation of necessary structural reforms in Europe. Overall, this thesis demonstrates that rules and restrictions can be effective in curbing excessive deficits and to guarantee fiscal sustainability. Nevertheless, their design deserves careful attention in order to avoid providing the wrong incentives to policymakers and negative economic spillovers.