

Editorial

The reform of the fiscal rule in Colombia

Since the promulgation of the 1991 Constitution, public spending has increased due to a series of rights that the government must guarantee to the population. According to Mauricio Cárdenas, former Minister of Finance, this situation led to an increase in these expenditures, which in the nineties of the last century led to a notable fiscal deficit and forced the government to implement a series of reforms and measures to alleviate the fiscal situation. One of these initiatives was the signing of a macroeconomic adjustment agreement with the International Monetary Fund (IMF) in 1999, which led to the formulation of the Medium-Term Fiscal Framework (MTFF) and the Medium-Term Expenditure Framework (MTEF).

In Cárdenas' opinion although the fiscal situation improved in the first decade of this century, it was not enough to recover the level of investment that the country had lost in 1999. This situation forced the national government to propose additional, more demanding measures, while maintaining its constitutional character. For this reason, the Bank of the Republic, the Ministry of Finance and Public Credit and the National Planning Department formed an inter-institutional technical committee, advised by experts, and prepared a proposal for a fiscal rule, which was reflected in Law 1473 of 2011.

The objective of the said Law is to “adopt regulations that guarantee the long-term sustainability of public finances and contribute to the macroeconomic stability of the country” and the scope of the said Law is the fiscal accounts of the central government. Due to the coronavirus pandemic, this Law had to be modified in some aspects by Law 2155 of 2021. This last regulation states that “the fiscal rule will seek to ensure the sustainability of public finances, in such a way that the debt limit is not exceeded. The debt limit is equal to 71% of GDP and the debt anchor is equal to 55% of GDP”. It should be emphasized that the anchor mentioned in Law 2155 is considered the optimal level of debt.

Both the President of the Republic, the Minister of Finance and the Director of the National Planning Department have raised the need to open a debate on the fiscal rule, which could lead to its suspension or relaxation. For the President, given the 0.3% decline in the GDP growth rate in the third quarter of 2023, one way to reactivate the economy was to increase public spending. Ricardo Bonilla, Minister of Finance, belie-

ves that “the fiscal rule is an agreement that has been proposed for several years so that public spending is controlled and we do not have excessive debt. But the fiscal rule creates restrictions and prioritizes debt payments over investments. It stops the economy. Today, when we have this situation of negative growth, the discussion is that paying the debt does not reactivate the economy, investment does. (...) we are looking at where we can reduce 10 billion in debt payments and increase it in investments to reactivate the economy.” On the other hand, Jorge Iván González, director of the National Planning Department, has proposed the adoption of a green fiscal rule, arguing that “the part of public investment dedicated to environmental conservation could be excluded from the estimates of the fiscal deficit. This expenditure opens up budgetary space and would be justified because the resources allocated to the conservation and recovery of environmental assets are qualitatively different from other expenditure, so it is important to reiterate that expenditure is not uniform. Spending is not spending. The resulting fiscal rule could be called a “green fiscal rule.”

It should be noted that the approaches of the three officials sparked an intense debate in the country, since for some former presidents, former finance ministers and certain analysts, the proposals represented a threat to the fiscal rule. Former President Gaviria believed that modifying or suspending the fiscal rule would contribute to “scaring away investment,” said former President Santos: “What has to be said to President Petro, very respectfully, is that he would be shooting himself in the foot, because what it would mean is that later, in the long run, there will be no money for the social justice that interests us all.” Finally, former President Duque stated that “eliminating the fiscal rule would only destroy the value of the currency, make the debt more expensive and trigger more poverty.”

On the other hand, former minister José Antonio Ocampo stated: “Changing the fiscal rule is harmful and creates distrust in the economic management of the country.” Former Minister José Manuel Restrepo said: “Modifying it sends more messages of uncertainty and distrust, and therefore private investment deteriorates even more and closes the fiscal space due to the additional cost of financing. “This reduces the credibility of macroeconomic policy and is not a message of macro prudence.” Former ministers Alberto Carrasquilla and Juan Camilo Restrepo believe that “it would be a serious mistake to eliminate it”. Former minister Mauricio Cárdenas stated that “the growth problem is not the result of a lack of fiscal space, but of the low execution of the 2023 budget.”

Economic analysts such as Carlos Caballero Argáez, Luis Fernando Mejía, Marc Hofstetter, among others, are not in favor of proposing changes to the fiscal rule because, in the words of Caballero, “historical experience has shown that the barriers are necessary to control the spending appetite of politicians and governments, which leads to

catastrophic fiscal imbalances”. Mejía, Executive Director of Fedesarrollo, criticizes the changes to the fiscal rule: “Fiscal prudence is essential to continue reducing the cost of financing the nation, which would make room for an increase in public investment without affecting fiscal sustainability. Columnist Hofstetter says that the desire to spend on the part of Congress and the executive will always be present, and that is why he states: “Institutionalism –that is, the fiscal rule– is the ally in this struggle, which balances the short-term desires of each government with the sustainability of public accounts that is convenient for all citizens.”

It is appropriate to clarify that what the national government’s economic team is proposing is not the abolition or modification of the fiscal rule, but rather proposals aimed at opening the debate on the issue, which is just, appropriate and beneficial for the country. We must not forget that its modification is the responsibility of Congress, through a law; therefore, the ideal is that there is a prior discussion and, hopefully, that there are points of agreement that allow for consensual changes. In reality, what happens with the current government is that when faced with any proposal from the Executive, some mass media, opposition sectors and analysts magnify, minimize or ignore what is proposed, depending on the convenience of the moment.

The law on the fiscal rule provides for the possibility of suspending it in 2020 and 2021, as has been done in the past, due to the effects of the coronavirus pandemic in the country. Of course, certain conditions must be met. One legacy of this pandemic was the high level of public debt, which caused the central government debt to GDP ratio to rise from 48.39% in 2019 to 60.70% and 60.10% in 2020 and 2021, respectively. In 2022 and 2023, it fell to 57.90% and 55.80%, respectively, but at high levels compared to 2019.

This undoubtedly increases the debt service and agrees with Jorge Iván González when he states that “the country is experiencing a fiscal pandemic that will worsen in 2025, when the debt service could reach \$112.9 billion and investments only \$68.8 billion.” For this reason, the head of the DNP is in favor of suspending the fiscal rule or at least making it more flexible. Another worrying situation for 2024 is the El Niño phenomenon and its effects on the supply of agricultural products, energy production and forest fires, among other things.

In short, the high debt service and El Niño will affect the country’s economic growth in 2024 and 2025 and, consequently, it is advisable to encourage debate on the fiscal rule.

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