

# The Budget – an Instrument for Forecasting. Multiyear Budgeting

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## Abstract

*The budget represents, by itself, a viable instrument for macro-economic forecasting, ensuring the harmonization of political interests with the financial resources of the state. Given its central role at the national level, the budget has been a veritable economic instrument. The economic forecasting – so necessary in establishing a coherent budget – both on a yearly and multi-year basis, is conducted by expert teams, which are usually independent of the public authority involved. This paper aims to achieve a theoretical analysis of budgetary forecasting and multi-annual budgeting, giving some examples from other countries such as United Kingdom, Germany and Holland, and how they acted in this field.*

**Key words:** *multiyear budgeting, budget forecasting, budgeting, governmental policy, yearly budget, economic policy*

## Introduction

The budget represents one of the most important aspects of public finances. Placed at the confluence between economy and policy, the budget has always controversies in what concerns the resources it makes up, but especially the destinations those resources follows to cover.

The public budget isn't an abstract notion of theoretical nature, but represents the most important instrument of social and economic policy at the entire country's level, which contributes to the achievement of economic policy and macro stability in concordance with established directions of political power for every year.

We may say that the state budget appears and increases from the necessity of public expenses correlated with available resources mobilized at the national level. In the public finances evolution the budget developed at the beginning of the contemporary period, as the main instrument of expenses projections.

In concordance with the public finances law, by budget we understand the document in which expenses and incomes are foreseen every year or sometimes only expenses in concordance with the system of public institutions.

The definition offered by Romanian law in the budgetary matter is compatible with the definition given to budget by the Financial Regalement of the European Community: the budget is "the act that foresees and authorizes every year preliminary expenses and incomes of the Community".

As far as the financial specialty legislation is concerned, we have adopted the model imposed by the French law on public book-keeping, according to which the state budget is the fundamentals of identification, establishment and incomes authorization and public yearly expenses of the state. This approval of the budget is valuable both from the theoretical and practical points of view: theoretically, because it shows the technical necessity of the budget, but also because of the importance of the authorization act that the budget shows; the practical one developed from the need of knowing the level of public resources and expenses.

## **The Main Role of the Budget in Covering Governmental Policy**

To speak about the budget includes a whole area of various elements from technical principles and book-keeping, moving to the quasi philosophical principles about human actions' responsibility and ending with the offered solutions to the conciliation of political and social purposes by means of the budget.

Through the public budget is established a ratio between public expenses, which are mainly taxes and duties and social needs aimed at avoiding the fiscal tasks of a society's members. Through a good and rigorous budget, the Parliament and Government can have a clear image of the relation between the value of material and immaterial goods made in economy and the value of the efforts made for their accomplishment. In the same way, the power of local organs and state administration can have this kind of image at the mezo-economic level. (Moșteanu, T. - *Buget and Public Treasury*, 2003)

The yearly budget reflects the accomplishment of governmental activities, being the result of a rich negotiation. It must succeed in giving a complete image of the exterior environment, of all economic and political factors. In other words, it should not only ensure the continuity of governmental actions projected on the years to come, and show control conditions. The budget must offer establishment and continuity to the state policy, showing rules and precise procedures to follow.

Foreseeing and budgetary planning are dealt with by the so-called budgetary offices. The budgetary offices have a rich culture resulted from the various tasks they must accomplish, e.g. guiding and watching the budgetary process in order to ensure the working of financial markets and guarantee the financial reputation of the state. The budgetary office is the guardian of the financial resources, being charge-d'affairs to ensure a stabile climate of policy for different governmental "clients".

The governmental policy shows the measures taken by pressure groups in order to change the policy adopted. The ministers and the others agencies are encouraged to come up with suggestions in order to help the centre foresee the financial matter. In this way the budget is a picture of all acts of foreseeing in financial matter, being the place of reconciliation of the resources with the social needs.

Public budgets are elaborated in most of the state in the world for a period of one year. However, their elaboration must also take into account the events that are outside the yearly budgetary cycle in general aspects concerning budgeters' incomes to the general costs in the long term, as well as the impact of those on internal environment.

A medium term vision of the budget is obligatory, because a period of one year is much too short to meet the requirements concerning public expenses. If taken into account, most of the expenses foreseen in the budget's elaboration are already involved.

The elaboration of a yearly budget ensuring the countenance of projected government policy necessitates the elaboration of a macroeconomic frame in the long and medium term. The macroeconomic forecasting made does not represent only a simple estimate affecting the macroeconomic variable. The forecasting is based on a clear definition of the targets and

instruments specific to an area like: fiscal policy, monetary policy, trade and duty administration, especially the external one. The macroeconomic general background must include the government's forecasts of the financial and fiscal background in the medium term. Forecasts must cover a period of 5 years.

Establishing a clear policy represents the main task of budgetary offices in order to anticipate the future evolution of the national macroeconomic background. For example, the achievement of reducing policy inflation is complementary to the measures taken to maintain budgetary deficit and duty report at an acceptable level.

The elaboration of the yearly budget necessitates a clear and accurate action plan, and is defined by a series of objectives and priorities as well as by the establishment of fiscal and political objectives. Transposing these governmental political priorities into the budget depends on macroeconomic estimates as well as on fiscal and non-fiscal incomes estimates in the medium and long term. Therefore, the elaboration of a macroeconomic background in the medium and long term constitutes a *sine qua non* condition for a solid budget.

The elaboration of a coherent budget depends on a series of factors with multiyear influence, such as:

- the evolution's impact on fiscal deficit;
- the paying of pledges regarding public duty;
- the public institution's administrative capacity;
- the costs of investment projects in the long term;
- the future necessity to cover unexpected expenses.

At the same time, the budget is a powerful instrument of economic and financial administration, as well as a declaration of public policy and an area of expenses for various programs. Budget elaboration implies difficult selections for all the agents involved. These must make sure that the budget fully corresponds to the policy promoted by the government.

## **Budgetary Forecasting**

The expenses foreseen and the financial resources allotted make budget a really coherent instrument. An optimistic estimate of the budget will lead to confusions regarding complying with the rules. An apolitical budget is an oxymoron because almost always there is a scale of political compromise and negotiation in order to avoid trifles in financing programs.

The elaboration of some yearly budget started in the 70's and the beginning of the 80's, and later spread in the majority of the European states. In some states the multiyear estimates are shown in governmental problems. Perceived at the beginning as an instrument for identifying and creating new financing programs, budget planning is the most efficient method of blending the short-term objectives with medium- and long-term ones.

At the beginning it was very difficult to do multiyear budget planning. In Great Britain, for example, multiyear budgets were expressed mostly in real rather than nominal terms, while the expenses estimates were automatically adjusted, sometimes putting big pressure on public finances. At the opposite pole, at the beginning of the 80's Canada developed the so-called PEMS – the Administration System of Political Expenses, which includes a fiscal program running on a period of 5 years.

In 1995 an OECD report revealed the fact that the government reoriented the multiyear budget from planning to foreseeing. (OECD, 1997)

The estimates of the public financial resources focus upon public political pledges that lie at the basis of a coherent budget. Even if these represent only documents with informative title, they succeed in transcribing a limit for new expenses schemes.

The multiyear budgetary methodology varies from one state to another, from a period to another. However, what we should keep in mind is that it must be based on the accurate estimate of incomes, which is very hard to do in instable economic area.

In Germany the elaboration of the budget is realized on the basis of a financial plan drawn up and presented by the council of financial planning, which includes all govern pieces, structured on 40 major stages. These stages result from simultaneously making estimates over several years and calculating the yearly budget for every expense article. It is worth mentioning that every estimated feature year includes a foreseeing resource designated to cover new financial programs.

In general, budgetary forecasting includes:

- the current level of expenses;
- probability of supplementary expenses;
- accumulations achieved.

The control of expenses, as well as the income estimate lead to different approaches. Thus, countries such as Canada have replaced various medium-term plans with a two-year fiscal planning, which succeeded in offering an accurate image of a fiscal background. On the contrary, in Great Britain the long-term expenses plans are revised every 2 years.

Planning and control of public expenses in the medium term must meet the requirements of two strict *fiscal rules*:

- the golden rule according to which the government will use contracted borrowings only for investments and not for covering current expenses, as in Romania;
- the rules concerning investments must be held at a prudent level.

Concomitantly are made the estimates of public expenses, which describe medium-term background expenses. These are part of the medium-term budgetary background, which includes: incomes forecasting structured on major articles of standard GFS classification, expenses forecasting concerning the programs engaged or under way, as well as some estimates concerning other fiscal things.

Detailed estimates of the long-term expenses engaged (in the case of programs) are made concomitantly with the finance of the budget. The estimate is thus used for transmitting that the occurrence of a negotiation space or fiscal movement is impossible.

The multiyear budgetary planning implies a series of aspects of financial and political nature. The estimate must be based on conservative suppositions for fighting possible modifications of the budget structure but also for avoiding new confusions. In this way the expenses estimate must be equivalent with the multiyear budgetary estimate, but be lower than the expenses estimated in the macroeconomic scenario for other years.

The multiyear estimate has a levy reserve that might be implicit or explicit. Two types of *levies* are usually used at reserve establishment:

1. technical levies, which surprise the changes of key economic parameters;
2. a political reserve addressed to some new feature programs. The reserve has a purely indicative character, without giving anything to future resources.

The process of multiyear budgetary forecasting must be based on a series of *requests* such as:

- elaborating and outlining a coherent medium-term fiscal budget;
- defining and reanalysing the promoted budgetary policy;
- establishing the limits of expenses;
- establishing the limits of reserves and contingents for predicted years;
- budget programming.

In many countries the multiyear estimate is used for long-term engagement administration. The budgetary estimates and their drawing up in coherent programs make a disciplined budgetary space. In practice are used expenses estimates depending on the policy promoted by the government, by economic and financial priorities.

Multiyear estimates are usually elaborated in nominal terms or in constant price. If the estimate is elaborated in nominal terms, the Ministry of Finance must elaborate a set of rules that should be applied to current realities. Instead, the estimates made in current prices show that they are consistent with financial forecasting from governmental book-keeping accounts. Often budgetary background with multiyear development can develop opposite tendencies of some expenses categories, concomitantly contributing to competent estimates of countenance of the current policy.

## Conclusions

Budget is the principal instrument of materialization of a promoted policy developed at the governmental level. A general strategic background must ensure sectorial policy, together with the involvement of the main political administration vectors. The strategic budget planning isn't a static or casual event but it has continuity giving the working base for the agents who administrate or derive programs.

Any estimate must be based on a formal economic model, which implies an analytical description of the situation, a description based on national accounts and social country life. The degree of intricacy or the rank of forecasting models varies from area to area. The complex models of budgetary forecasting can give birth to the so-called "phenomenon of estimated illusion".

The elaboration of a coherent budget basis, either yearly or multiyear, is realized in most European countries by teams of experts. For example, in the United Kingdom forecasts are certified and validated by the Central Censor.

As we know, the budget focuses on three important rules: multilateralism, a multiyear perspective in budget elaboration and implementation monitoring.

Multilateralism supposes the fact that the budget series ensemble must give a complete image of the way in which the public area affects economy.

The rule can be reformulated. Thus every reallocation which is made via political process and not via market should be recorded and presented in budget for estimate (Lacsse, F. - *The elaboration of budgets and policy: problems and solutions*, OECD, 1999).

Although the budget execution is yearly, it must contribute to ensuring the government's policy and fiscal proposal. Multiyear budgetary solutions depend on our defining budget as an instrument for identifying the new programs costs.

The budget offers itself to the economic and political space, proving to be an important instrument of economic forecasting, and succeeding in controlling present problems.

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## Bugetul – instrument de previziune. Bugetarea multianuală

### Rezumat

*Bugetul public reprezintă, prin el însuși, un veritabil instrument de previziune macroeconomică, asigurând armonizarea intereselor de politică publică cu resursele financiare pe care statul le are la dispoziție pentru finalizarea acestora. Datorită rolului central pe care îl are la nivel statal, bugetul a constituit de-a lungul anilor o veritabilă pârghie economică. Previziunile economice atât de necesare fundamentării unui buget coerent, fie el anual sau, după caz, multianual, sunt realizate de către echipe de experți, care, de regulă, sunt independente față de autoritățile implicate în procesul decizional. Acest articol își propune o analiză teoretică a ceea ce înseamnă previziune bugetară și bugetarea multianuală, oferind câteva exemple din unele țări precum Marea Britanie, Germania sau Olanda, precum și felul în care acestea au acționat în acest domeniu.*