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Title: Cyclical Patterns and Sustainability of Fiscal Policy at Regional Level: the Spanish Case

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Abstract: [eng] Concerns over sustainability and the cyclical pattern of public finances have been especially great since the onset of the global financial crisis. This thesis comprises four essays which aim to examine those concerns with regard to the Spanish Autonomous Communities (ACs). The first paper analyses fiscal policy responsiveness of Spanish ACs over the cycle. We estimate fiscal reaction functions to analyze the response of ACs' fiscal impulse and fiscal stance. On the one hand, an analysis of the change in the primary balance (the fiscal impulse) suggests counter-cyclicality over the period 1987-2008, but afterwards an a-cyclical impulse until 2012. Foral ACs stand out from other ACs, as their response is much more counter-cyclical. We do not find evidence regarding any asymmetric behaviour of ACs in good or bad periods. On the other hand, the response of ACs' fiscal stance indicates that ACs' discretionary fiscal behaviour has been pro-cyclical. This pro-cyclicality has sharpened since the last crisis, which is especially worrisome as health, education and social services expenditures are within regional responsibilities. The second paper addresses the primary balance response to the debt of Spanish ACs from 1987 to 2015. Overall, the results of this study provide evidence of a nonlinear relationship between these variables, which points to a situation of fiscal fatigue and reduced fiscal space. The empirical framework builds mainly on the works of Bohn (1998) and Gosh et al. (2013), thereby also focusing on uncertainty issues. In 2015 the regional debt ratio stood at 26.8% of Gross Value Added, slightly above our lower estimate for the debt limit (24%) and well below the upper estimate (36%). A reduced fiscal space in ACs calls for measures to ensure a sustainable debt trajectory and regain some room to deal with potential negative shocks. The third paper deals with personal income tax (PIT) revenue elasticities, which is the most important revenue source for Spanish ACs. We apply an error correction model to estimate PIT revenue elasticities in common regime ACs. The stability of these elasticities is checked and short-run asymmetries are identified. A tax overreaction is identified when PIT revenue is above the long-run equilibrium while a typical error correction model response is obtained when PIT revenue is below. Some simulations are provided to evaluate the dynamic adjustment between short and long-run elasticities and their consequences for fiscal pressure. Some findings regarding cross-sectional variability should also be noted: short and especially long-run elasticities present a decreasing pattern in respect to per capita income. Another noteworthy contribution is the analysis of forecasting performance in the presence of an endogeneity relationship. Despite the OLS estimator bias, its superiority is made clear (analytically and empirically) in comparison to the IV estimator. The fourth paper examines potential GDP and structural budget balances at regional level, following the methodology of the European Commission (EC). These are instruments used to guide economic policy, widespread at state level but much less at regional level. Measuring the cyclical position enables us to make an appraisal of the Catalan fiscal stance since 2004. In short, the fiscal policy of the Generalitat of Catalonia has been pro-cyclical, except for the first budgetary response to the crisis and the recovery period beginning in the second half of 2013. In years to come, the available fiscal space (in terms of debt) can condition the fiscal stance. This paper also points out the main limitations of the EC methodology. Finally, alternative estimates of Catalan potential GDP based on unobserved components models are presented, as well as an assessment based on their reliability and usefulness for inflation and GDP growth forecasting performance.

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