Determinants of public investments in EU countries. Role and importance of fiscal rules

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Abstract

The goal of this study is to identify factors determining the size of public investment in relation to GDP in the European Union countries and to verify the hypothesis about the negative impact of fiscal rules on the public investment. Panel models estimated on the data from 1995 to 2019 confirmed the hypothesis. The increase in Fiscal Rules Index (which approximates the strength and restrictiveness of fiscal rules in each country) by one standard deviation is associated with the decrease in public investment by 0.2-0.4% GDP. The strongest impact on public investment has the existence of debt rules and the negative effect amounts to a maximum of 0.55% of GDP. The remaining significant determinants of the level of public investment are mostly consistent with the economic literature and intuition (debt level, GDP per capita, corporate investment, share of agriculture in GDP and government efficiency). Assuming that public investments are a desirable instrument of economic policy (e.g. supporting the recovery after a crisis or achieving long-term climate goals), obtained results are an empirical contribution to the current discussion on the reform of the fiscal framework in the EU, supporting addition to the fiscal rules investment clauses.

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