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Πανεπιστήμιο Πειραιώς

**Σύμφωνο  
Ανάπτυξης και  
Σταθερότητας:  
Η επόμενη μέρα**

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Conference on the Future of Europe:

«Ο πόλεμος στην Ουκρανία και η επόμενη μέρα του Συμφώνου Σταθερότητας»,  
υπό την Αιγίδα του Υπουργείου Εξωτερικών της Ελλάδος και του Ιδρύματος  
Μεσογειακών Μελετών

Αθήνα, 17 Μαρτίου 2022, 19:00 – 20:30

# Reform of the EU Stability and Growth Pact (SGP)

- ❑ **SGP is a substitute for the missing fiscal union in EMU.** It is a set of rules on proper fiscal policy so that monetary policy is not over-burdened
- ❑ History shows the **European project keeps improving** over time **in small steps** and with continuous compromise
  - Same holds true for SGP
- ❑ **Jumps in policy occur only after crises**
  - The **Greek crisis** led to the beginning of the Banking Union, the establishment of ESM
  - The **pandemic crisis** pushed Europe into new fiscal territory:
    - i. Brought a large fiscal expansion, i.e., the implementation of the escape clause in SGP in the face of a large shock
    - ii. Brought a partial mutualization of debt, something that was discussed but did not materialize during the Greek crisis
    - iii. Opens the possibility of the establishment of a “central adjustment account,” previously advocated by academics

# SGP: A history of fiscal concerns and political friction

- ❑ **1992: Maastricht Treaty** sets the **3% deficit & 60% debt limits**
- ❑ **1997: Stability & Growth Pact**
  - Preventive arm (1998), Corrective arm (1999). Preventive arm included Medium Term Budgetary Objectives and Expenditure Benchmarks
- ❑ **2005:** Renewed discussions of the ideas of:
  - Medium-Term budgetary Objectives
  - Structural Balance
- ❑ **2010: European Semester** as an instrument of coordination & governance
- ❑ **2011: Six Pack:** Reduce public deficits and address macro imbalances
- ❑ **2012: Fiscal Compact:** Budgetary balance into Member States' constitutions
- ❑ **2013: Two Pack:** Prepare budgets with common standards and schedules
- ❑ **2015: Communication Flexibility**
  - European Commission describes how it will apply the rules of the SGP to strengthen the link between structural reforms, public investment and fiscal responsibility in support of employment and growth
- ❑ **2020:** Stability & Growth Pact **effectively suspended**

# A post Greek crisis “consensus”

- ❑ By 2015, the emphasis was on the structural deficit, as it is less procyclical than the ordinary deficit. Its size was decided to be smaller than 0.5% GDP (and for countries with low debt, 1% GDP).
- ❑ Lots of criticism & arguments on ...
  - The complexity of new rules, e.g., frequent ex-post revisions of structural deficits as large as 1% GDP, the proper definition of government expenditures, etc.
  - The time-inconsistency of penalties, advocating incentives in their place
- ❑ I can loosely summarize this consensus in the following prescription to a member state:

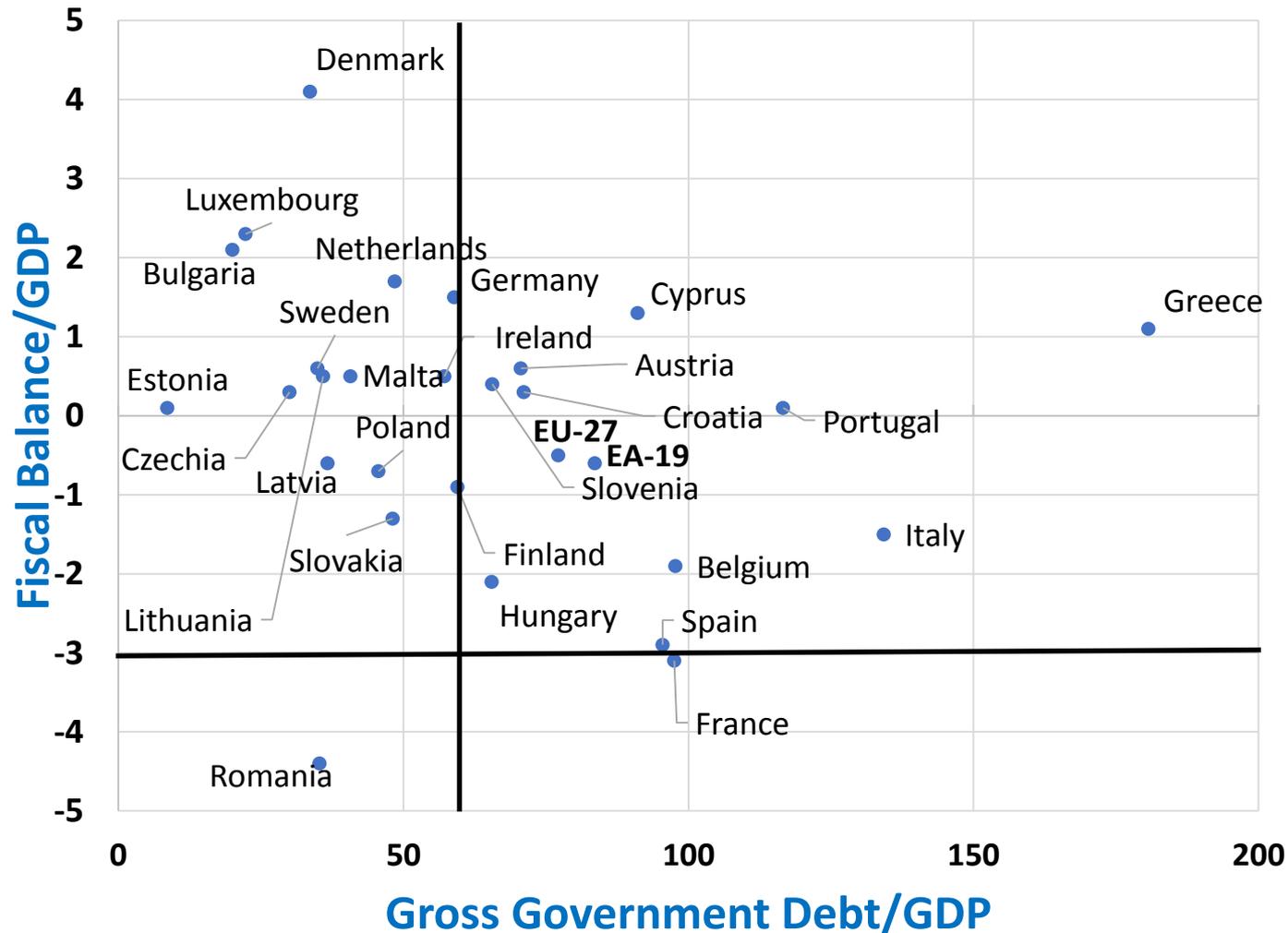
***“Utilize the good times to build a fiscal cushion in order to be able to follow a countercyclical fiscal policy on your own if a negative shock were to occur in the future”***

If the prescription is followed, then there would be no need for a central fiscal mechanism to do the fiscal stabilization, unless the shock is very large

# European fiscal picture just before the pandemic

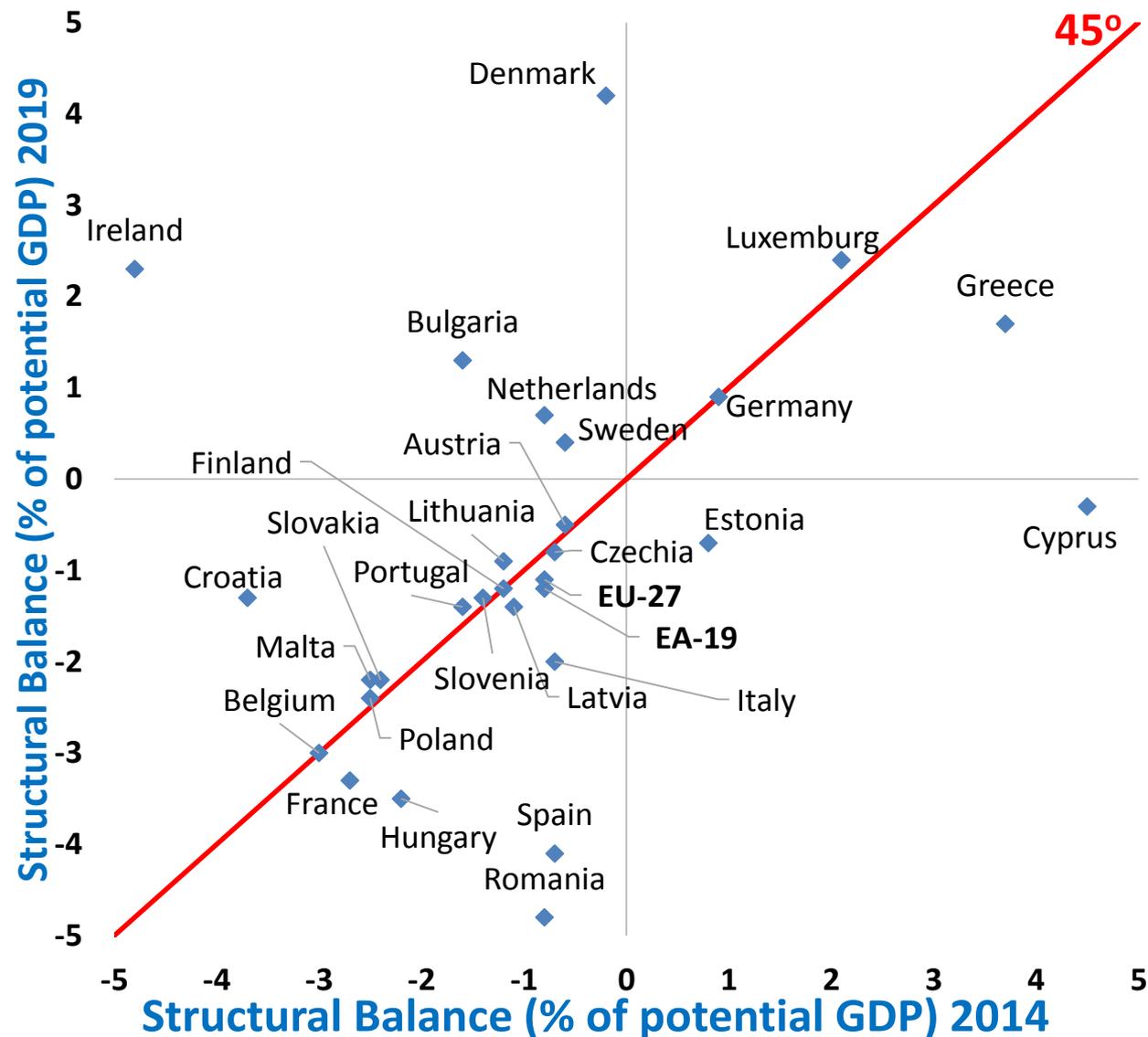
- ❑ In 2019, most countries **observed the Deficit limit**
- ❑ Yet half the countries **above the Debt limit**
- ❑ 2019 was preceded by a **period of growth** in all EU countries
- ❑ Did the countries build fiscal cushions for a future stress?

## The Fiscal Picture in 2019



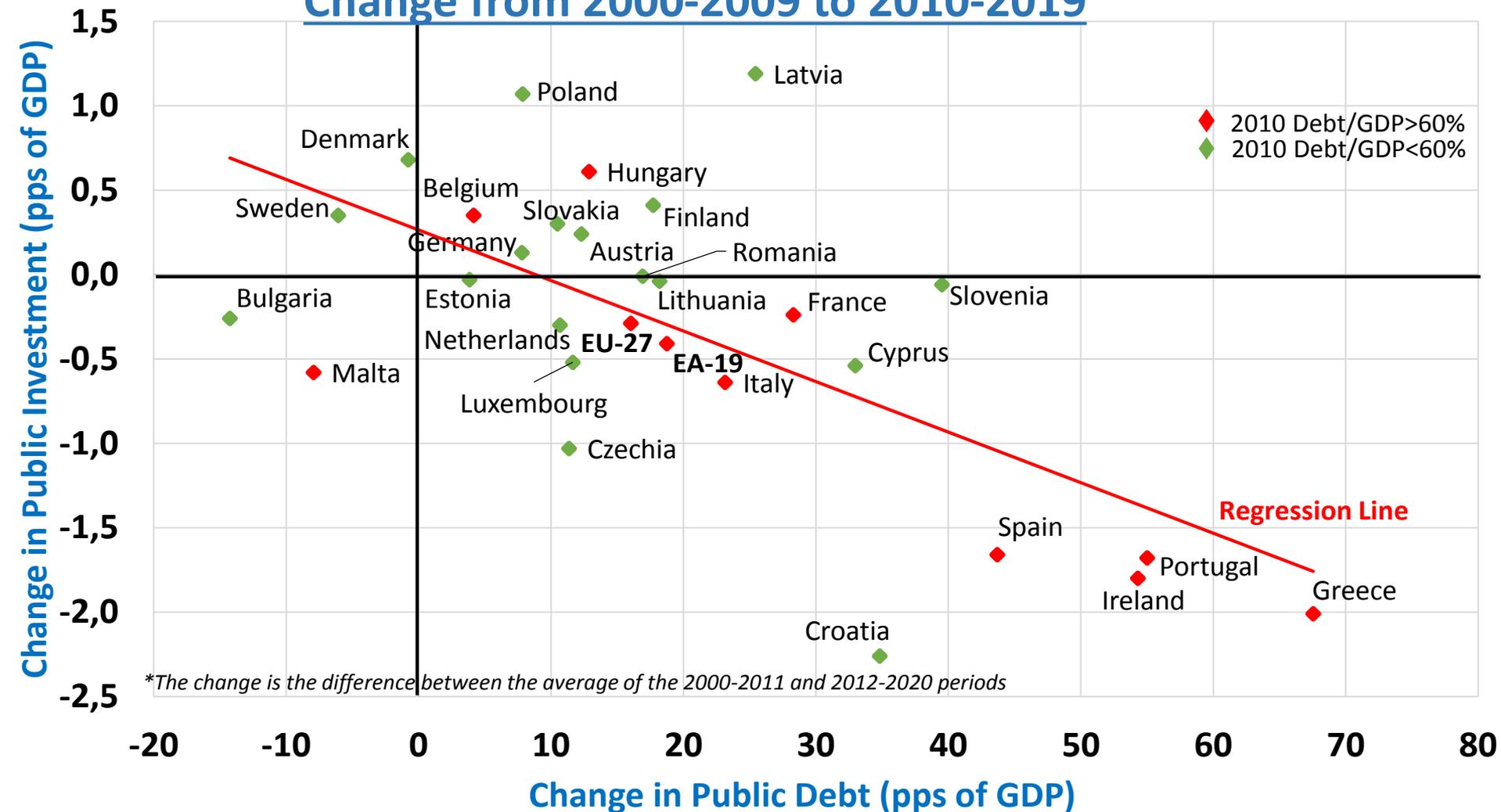
# Did the structural balance improve from 2014 to 2019?

- Was the agreed by 2015 fiscal policy subsequently successful? Namely, did countries **build buffers in good times** for fiscal relaxation in future bad times?
- Lower left quadrant raises concerns:** Countries should have relocated to the top left quadrant
- Yet many are even **below the 45° line**, namely, despite the economy improving, they had a worse structural deficit in 2019



# Change in Public Debt & Investment across the Decades

## Change from 2000-2009 to 2010-2019



- From decade 1 to decade 2, **Debt/GDP increased** in most countries
- Countries with  $\Delta(\text{Debt/GDP}) > 0$  are typically the ones with  $\Delta(\text{Inv./GDP}) < 0$

# The current debate

## Three schools of thought:

- i. Current framework needs little reform
  - ii. Fiscal rules need to be adapted, yet within the current framework
  - iii. A complete overhaul of the rules; even a replacement of the numerical targets included in the European treaties
- ❑ See recent common position by Finance Ministers of Austria, Czech Republic, Denmark, Finland, Latvia, Netherlands, Slovakia, Sweden. Seems to lie between options (i) and (ii), closer to (i).  
*“De-activation of the General Escape Clause and the reform of SGP should not be linked.”*
  - ❑ Given the need of unanimity for final decisions and the history of EU policy-making, it is likely that **option (ii) would be followed**. Namely, an adaptation within the existing framework

# The current debate

## □ EU Fiscal Council proposes:

- 1) Set numerical targets for **debt reduction** in very high debt countries, at a moderate and differentiated pace
- 2) Implement an **expenditure benchmark** through a single, observable indicator, with one escape clause invoked on the basis of independent economic analysis
- 3) Maintain the 3% threshold for the headline deficit as a **backstop** in containing debt dynamics and as a **trigger** for the EDP for all MS

## □ **We are likely to see a debate** around the above proposal on items like:

- Definition of **public expenditure**: Net of interest payments, non-discretionary unemployment benefits, discretionary revenue measures, public investment (on an amortized basis?), Green investment
- Medium-Term Budgetary Objective as a preventive measure, rather than a corrective measure
- **Central fiscal capacity**, how large? A simple adjustment account or **RRF would transform into** a macroeconomic stabilization mechanism?

# Reform of the EU Stability and Growth Pact: Seeking the Golden Mean

## In conclusion:

- ❑ I am optimistic this crisis will lead to a better functioning EU and EMU
- ❑ The time to reform is now – before the escape clause expires
- ❑ Our European moto: The SGP reform ought to ...
  - Adjust the traditional dilemma: “***Rules versus discretion***” into “***Rules and discretion within a proper governance framework***”  
Namely, utilize both “discipline-improving” and stabilization-improving policies, like academic economists suggest
  - Take into account the pressing challenges of the next decades: climate change, digitalization, investment needs, ageing population

Thank you for your attention!

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