Il dibattito sulle regole fiscali in Europa: le proposte dell'European Fiscal Board

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Plan of the talk

- EFB?
- Fiscal rules
- Junker’s questions – our answers
- Our proposals
- Where are we going?

What is the EFB?

- Independent advisory board of the Commission, established in November 2016, following a proposal of the “Five President Report” in 2014.

- Our main tasks are to report (annually) on the Commission’s implementation of fiscal rules, suggest improvements on fiscal surveillance, cooperate with national fiscal councils, offer advices on euro area fiscal stance and on specific issues when so asked by the Commission..

What is the EFB?

- “Independent”.. 5 members from 5 different countries, mandated “not to seek or follow advice” from either the Commission or member countries, plus a technical secretary (5 economists + one Head) who respond only to us.

- All our reports, including requested advices to the Commission, are made public.

What is the EFB?

- “Independent” does not mean isolated. Continuous interactions with the Commission (DG efin), the Council, the EU Parliament, member countries, academics and experts..
- Our proposals reflect (only) our opinions, but are also a part of a **more general debate** on the reform of the fiscal framework and more generally the Euro area..
- Decisions inside the Board taken unanimously, after lengthy (sometimes painful) discussion.

Fiscal Rules

- Should we reform the fiscal rules? Why and how?

- Is it urgent? Given all the problems that the EU & the Emu are facing, including a potential recession, is reforming the rules a priority?

Our answers ..(as EFB)

- Yes.
- Because the current setting presents a number of problems and reforming the rules (e.g. by adopting some of our proposals) might be useful even with no other changes in the Emu/EU architecture.

Our answers ..(as EFB)

- However, as it already happened with the 6-2 Pack reform (counterbalancing the ESM), it might well be that reforming fiscal rules might be *politically easier* as a part of a more general overhauling of EMU institutions.
- Building a “European fiscal capacity” and completing the remaining pieces (e.g. Banking Union) might be the other *essential elements* that allows for a revision of fiscal rules..

Our answers ..(as EFB)

- Proposed reforms of fiscal rules should then respect two constraints:

- a) to be compatible with a desirable reform of EMU institutions;

- b) not overburden them; not everything can be done with the fiscal rules.

Why should we reform the rules?

- **Our EFB assessment report (2019):**
- **Junker's questions: Have EU fiscal rules...**
  - ensured the long-term **sustainability of public finances**? (mah, perhaps..)
  - allowed counter-cyclical **economic stabilisation**? (No. At best, let things unchanged)
  - improved the **quality of public finances**? (definitely no, particularly in some countries)

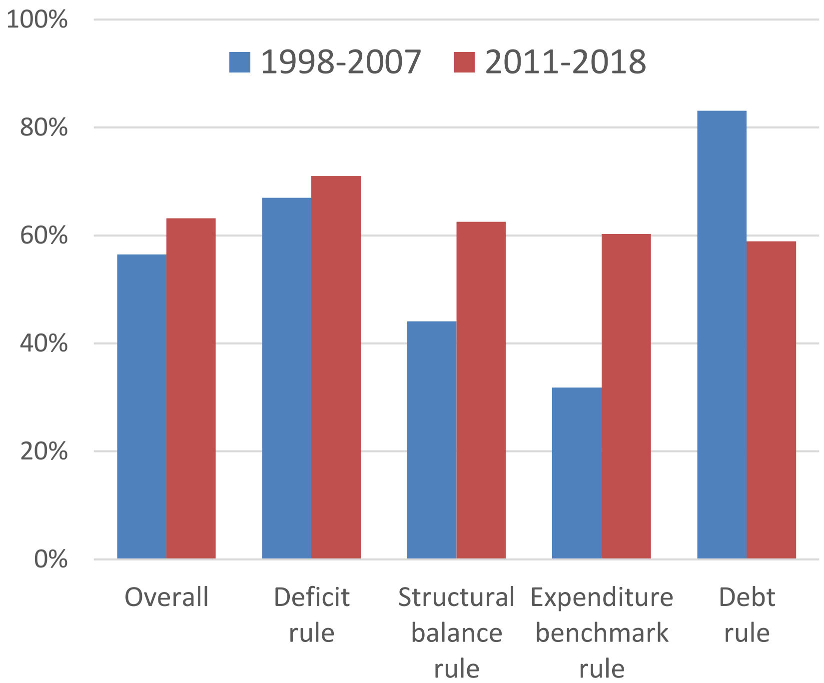
1. Have EU fiscal rules ensured sustainable public finances?

Positive developments

Outcomes

- **Compliance with fiscal rules** has improved on average since depth of crisis
- All EU Member States **out of EDP** in 2019; first time since 2003
- **Headline deficit** in the EU at lowest level since 2000, below 1% of GDP
- Over 40% of EU Member States **at their MTO**

Average compliance with EU fiscal rules, EU-28



Processes

- EU fiscal framework better equipped to **monitor expenditure growth** and **identify revenue windfalls**
- Better scrutiny of **macroeconomic forecasts**
- Involvement of national **independent fiscal institutions**

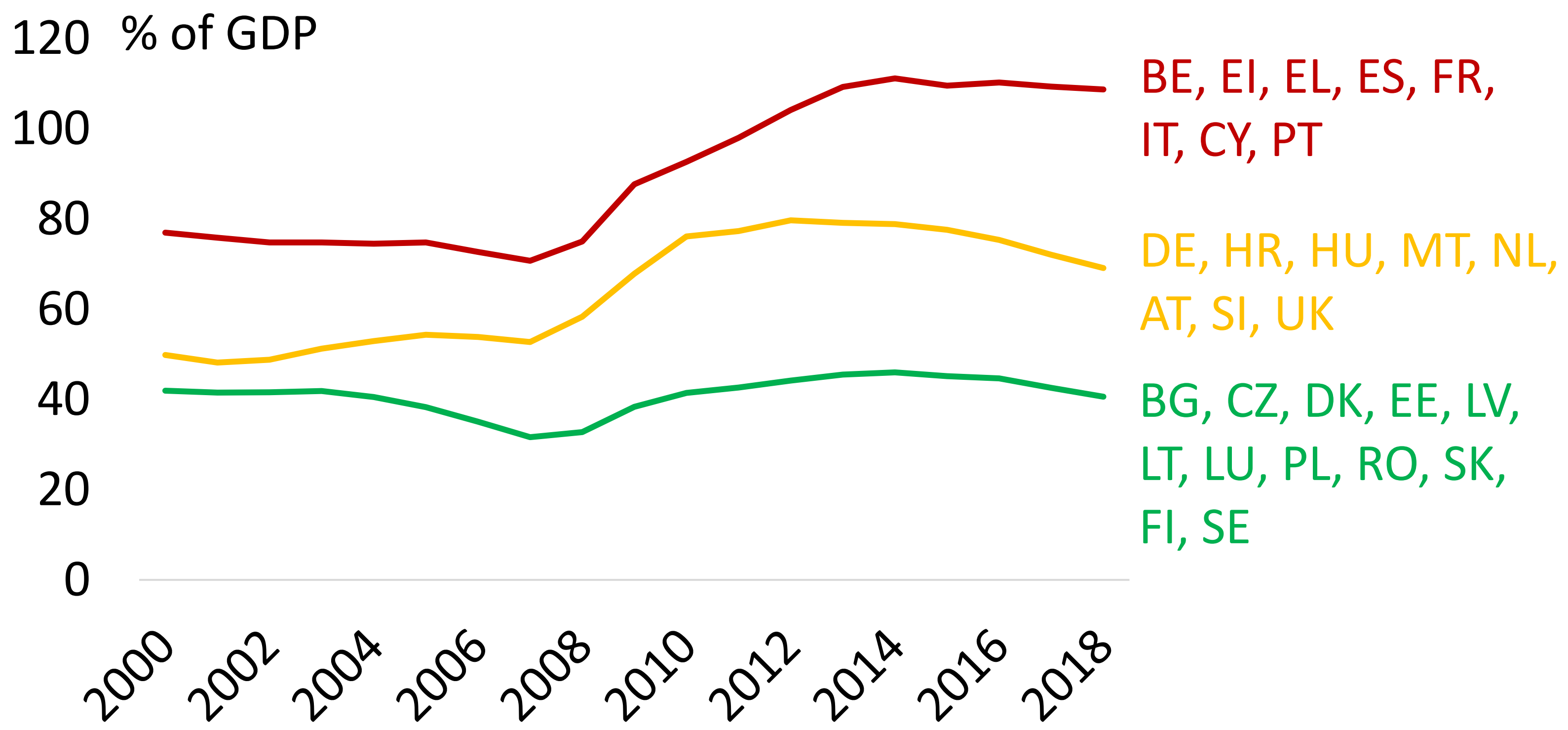
1. Have EU fiscal rules ensured sustainable public finances?

Negative developments

1) Fiscal performance varies across groups of countries

Debt reduction has stalled for important group of countries

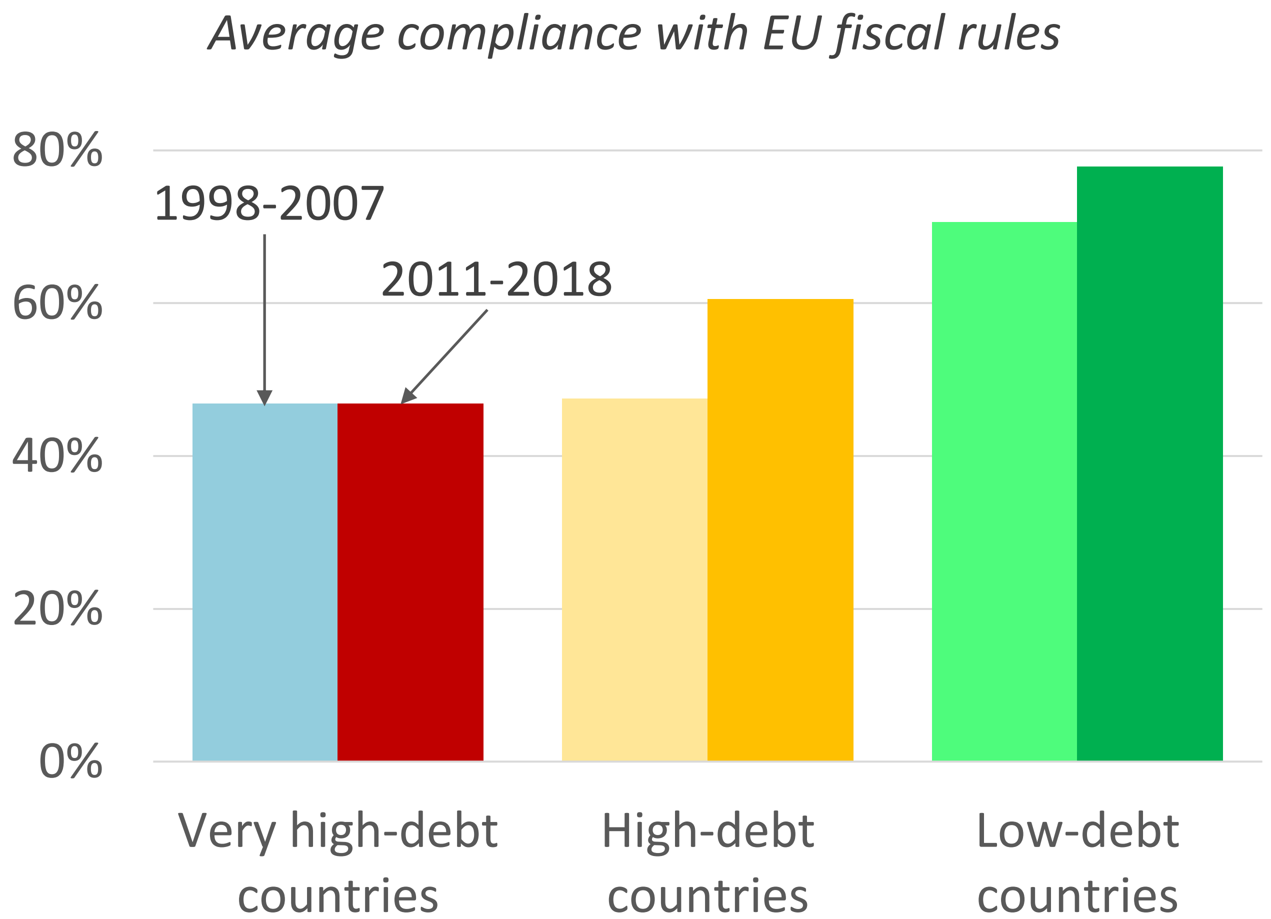
Average debt-to-GDP ratio



Note: Countries are grouped based on their average debt levels in 2011-2018.

1. Have EU fiscal rules ensured sustainable public finances?

Overall compliance has not improved in the very high-debt countries

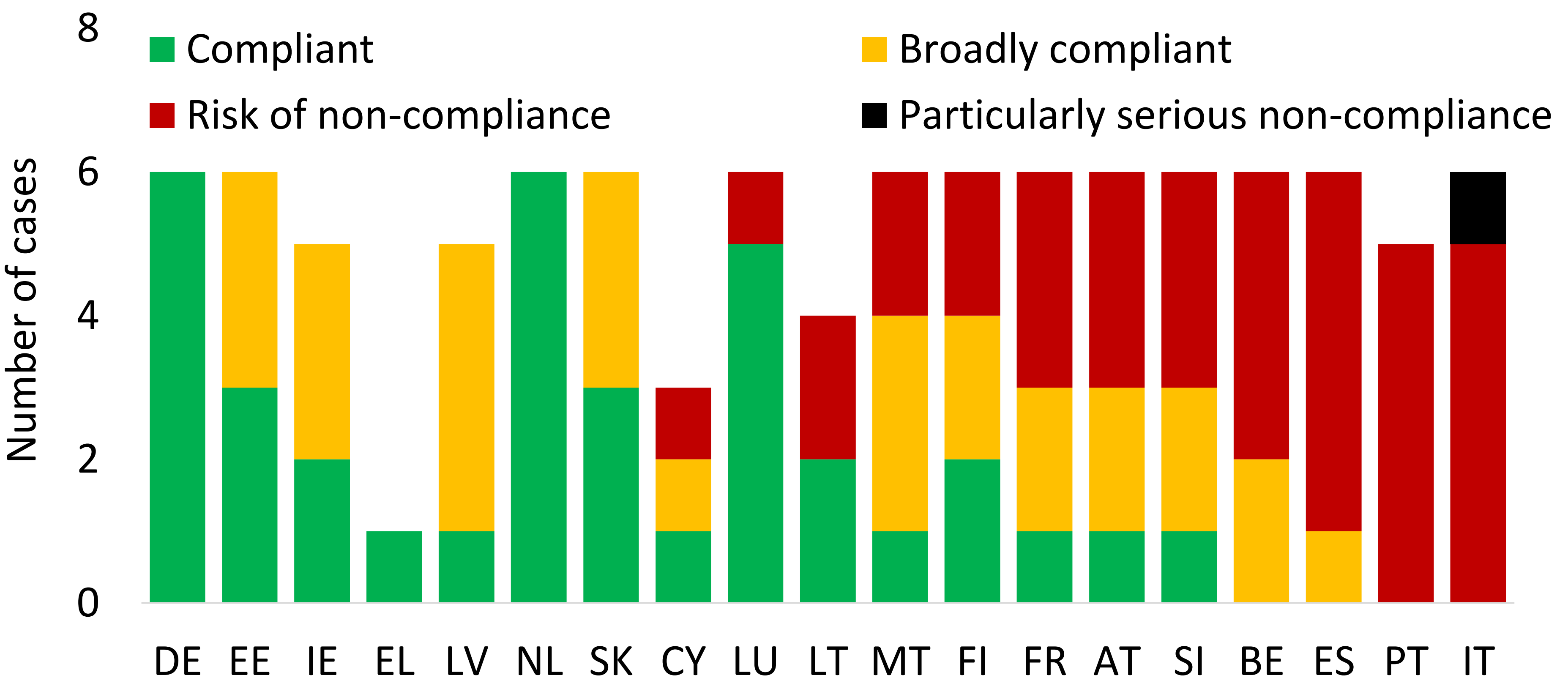


1. Have EU fiscal rules ensured sustainable public finances?

3) Problems already at planning phase

- **Draft budgetary plans** never (fully) compliant with SGP in 4 countries
- **Medium term**: consolidation back-loaded

Compliance of DBPs with the SGP, 2014-2019



Complexity of rules, indicators & procedurals

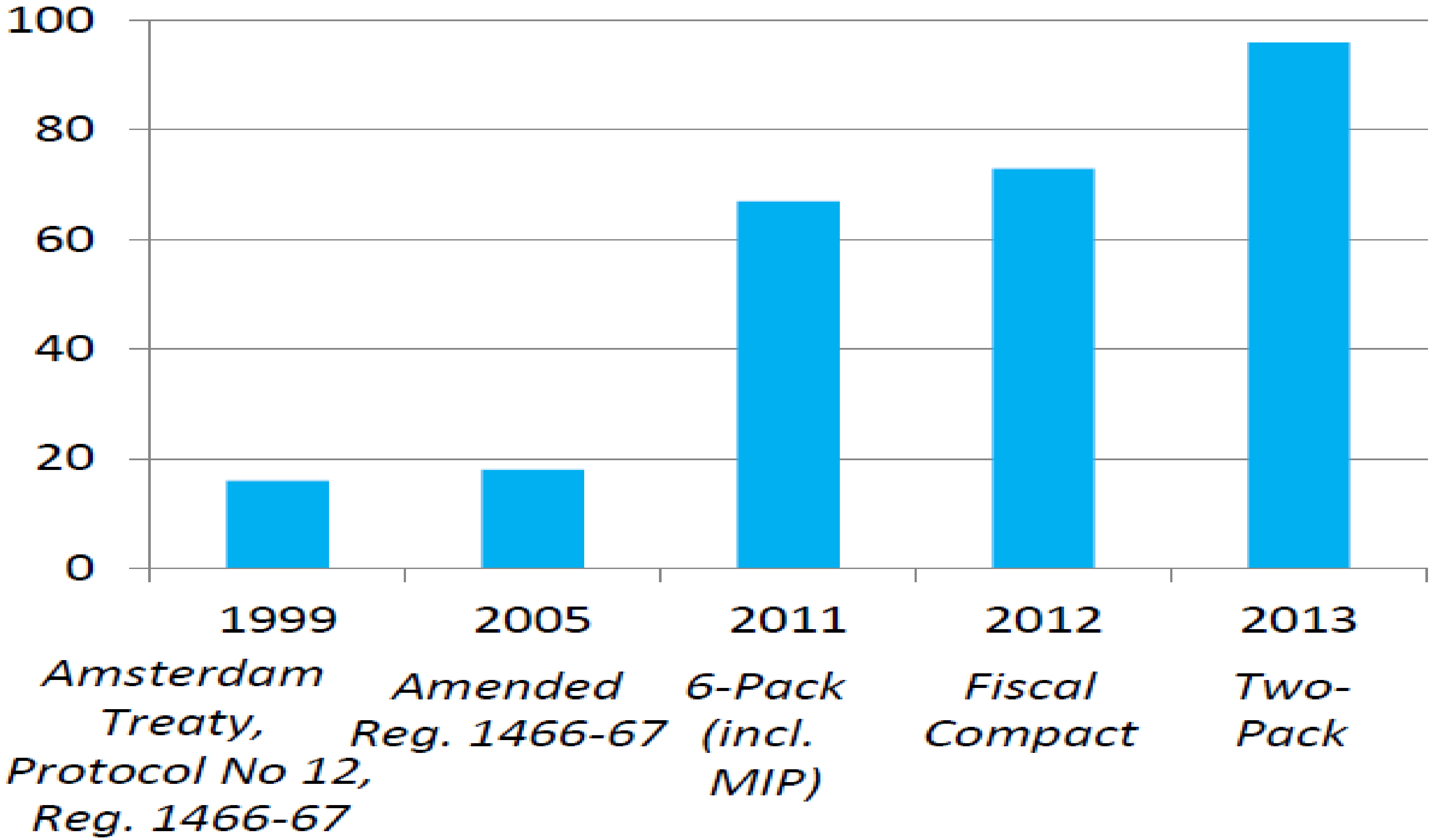
- Lack of trust (among countries and between countries vis Commission) has led to a continuous effort to *codify* any possible interpretation of the rules.. (Marco Buti’s myth of the “complete contract”)

- (interpretation of) rules have become increasingly complex and opaque.. “Code of conduct” & “VadeMecum on fiscal rules” cover hundreds of pages..

- with some obvious consequences..

Fiscal governance system became more complex

(pages of the entire framework in primary/secondary legislation by year, key innovation shown below in italics)



1. Have EU fiscal rules ensured sustainable public finances?

4) Multiple indicators weaken implementation

- **Preventive arm: cherry-picking** between change in structural balance and expenditure benchmark

- **Corrective arm: strategy of meeting the nominal deficit target** during the recovery thanks to higher revenue, rather than delivering the (more demanding) required structural effort

- **Debt criterion** superseded by compliance with the preventive arm (use of low nominal growth as relevant factor)

1. Have EU fiscal rules ensured sustainable public finances?

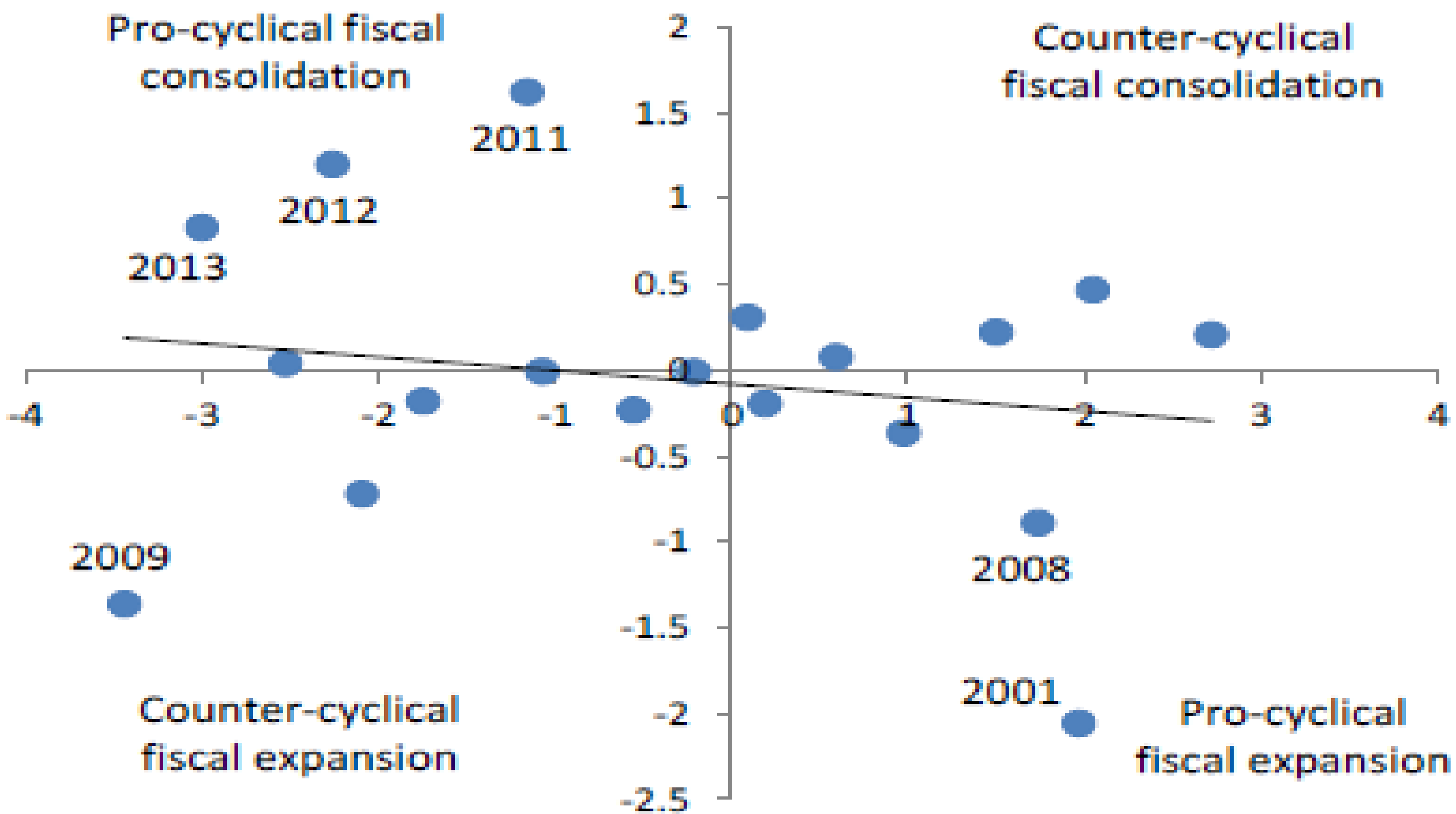
5) Governance issues

- **Fiscal surveillance** increasingly bilateral and less reliant on pressure by peers
- **Sanctions prove difficult to enforce**: contrary to expectations, RQMV has not helped imposing sanctions, because it has led the Commission to internalise the political consequences of its proposals

2. Have fiscal rules allowed for counter-cyclical **economic stabilisation**?

- One single example of counter-cyclical expansion (European Economic Recovery Plan: 2009)
- Two examples of conspicuous pro-cyclicality (2011-13; economic contraction; 2001; fiscal expansion)
- Fiscal expansion/consolidation more pronounced in very high-debt countries

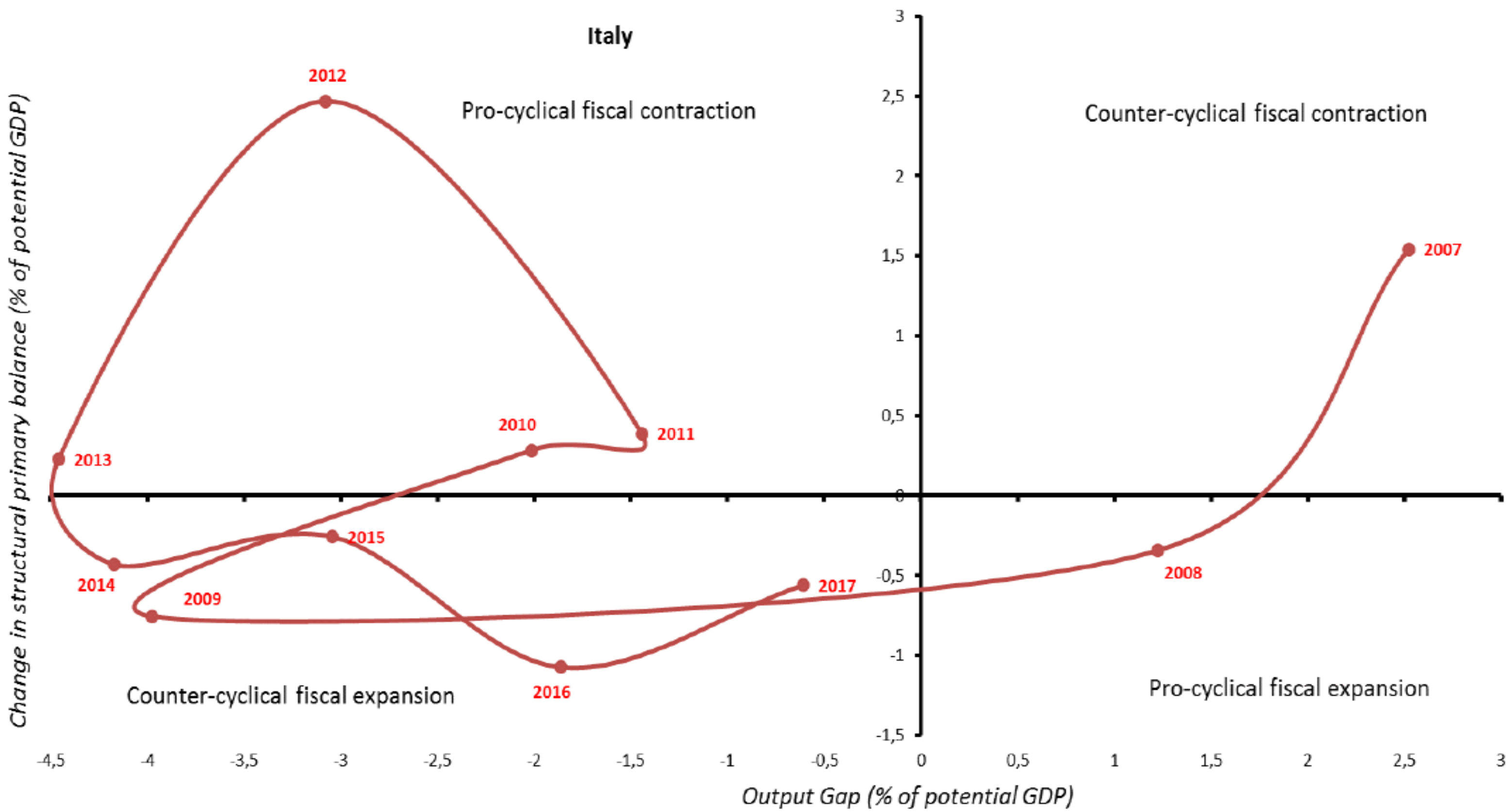
Graph 5.1: Change of the cyclically adjusted primary balance (vertical axis) vs. the output gap (horizontal axis), in percent of potential GDP



Source: European Commission.

Italy (Pisauro)

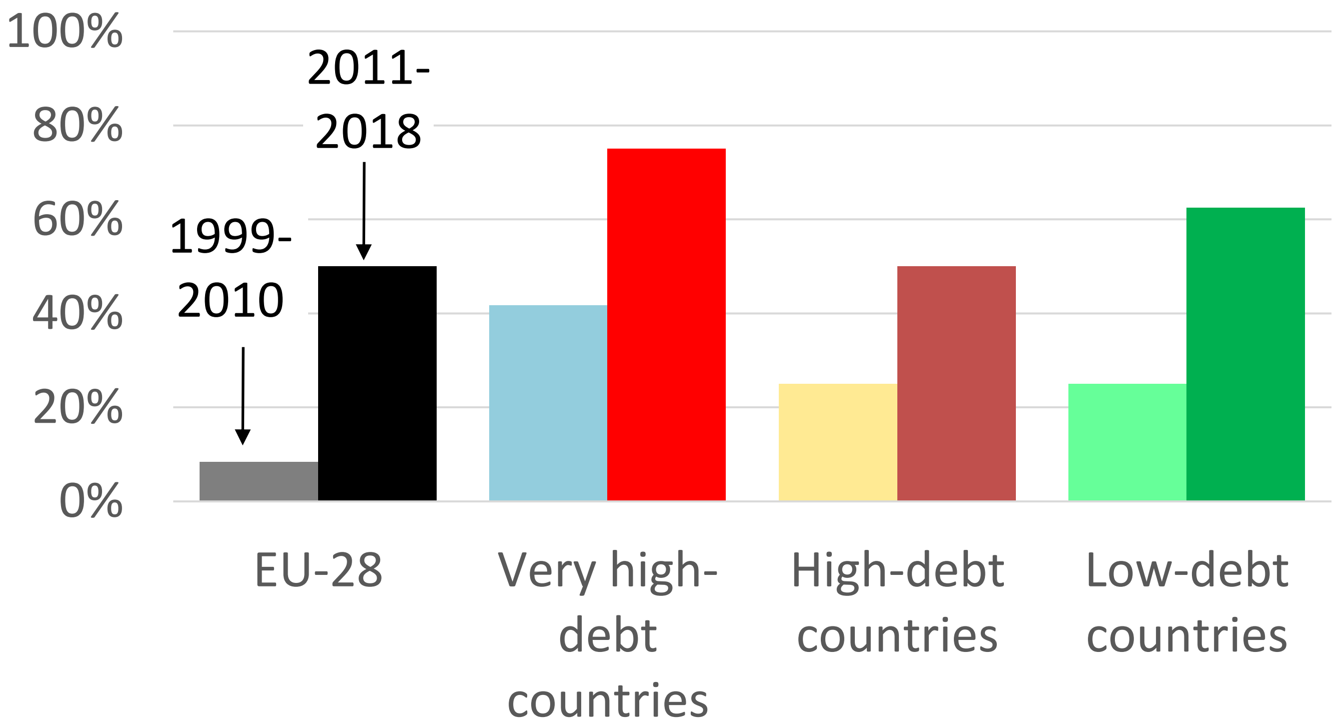
Overall results: fiscal stance



2. Have EU fiscal rules allowed economic stabilisation?

Pro-cyclical fiscal stances more frequent since depth of crisis

Frequency of fiscal policies in a pro-cyclical direction



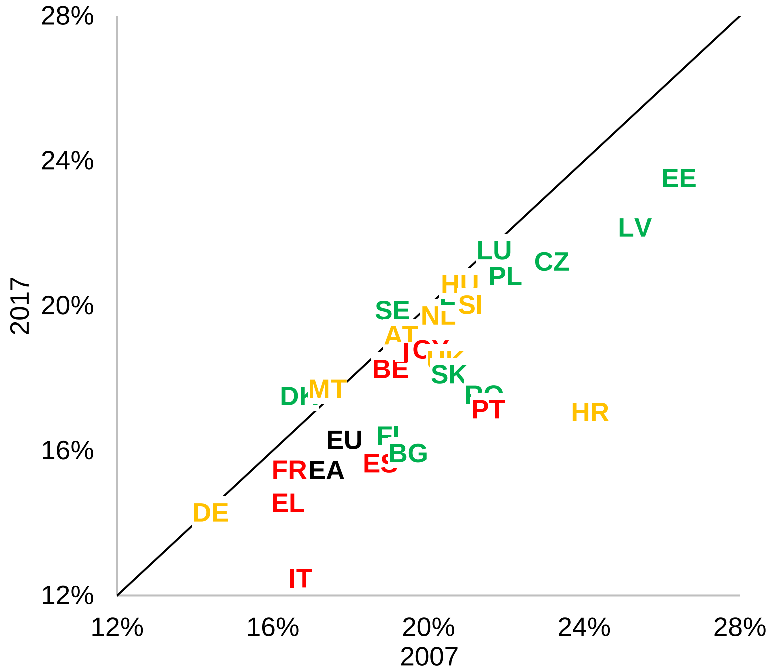
➔ **Pro-cyclicality not reduced over time**

➔ **Pro-cyclical tightening in bad times flip-side of not taking advantage of good times to build fiscal buffers; 2015-17 bad timing for increased flexibility**

3. Have EU fiscal rules improved the quality of public finances?

- **Productive public expenditure has borne the brunt of fiscal consolidation** especially in very high-debt countries and countries subject to EDPs

Productive public expenditure as share of total public expenditure, 2017 versus 2007

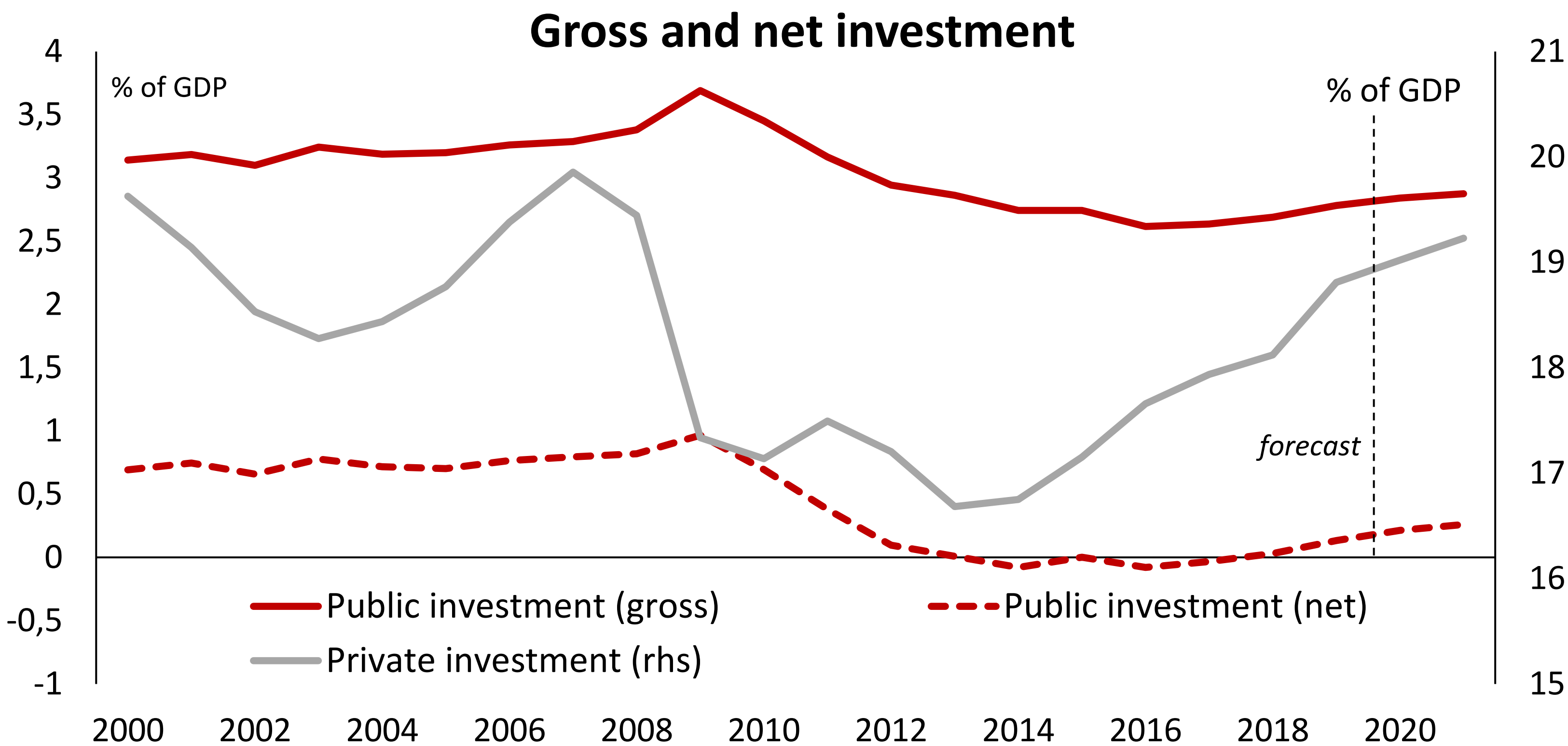


Note: Productive public expenditure includes expenditure on R&D, education and transport (COFOG classification).

- **2015: investment clause** meant to shield investment in bad times, **structural reform clause** to incentivise reforms
- **Only few countries qualified for the flexibility clauses**, even fewer have benefitted from them
- **Weak progress** with CSRs on the quality of public finances

➔ **Need to better protect growth-enhancing public expenditure that reinforces sustainability of public finances**

Public investment in the Euro area



Reforming fiscal rules

- What do we propose?

Simplified SGP: 2018 Annual Report proposal still relevant

ONE fiscal anchor:
debt ceiling at 60% of GDP

- Focus on sustainability
- Simple and observable

ONE operational indicator:
expenditure benchmark

- Largely observable
- Built-in anti-cyclical effects
- 3-yr ceiling: medium-term perspective
- Annual monitoring with compensation account

ONE escape clause replacing all existing flexibility provisions

- Flexibility without current complexity and "complete contract" approach
- Triggered based on independent analysis

Demarcate policy decisions from economic analysis

- Isolate underlying staff analysis from political considerations

Possible extensions: rules

Limited Golden Rule

- Protects investment by exempting specific categories of growth-enhancing expenditure from the expenditure rule
- Exemption applies to EU spending programmes
- Classification monitored by IFIs and national statistical offices

Differentiated national debt targets or adjustment paths

- In function of key socio-economic indicators: differences in saving, pension systems, borrowing costs, current account balance etc.
- To be agreed within Council over a period (say, 7 years) following a proposal of the Commission and subject to legal enforcement.

Possible extensions: institutional arrangements

Full-time President for the Eurogroup; neither a sitting national Finance Minister nor a member of the Commission

- More stable governance and stronger continuity
- Strengthens political debate and peer review
- Weakens potential conflicts of interest

Reconsider RQMV

- Moves political responsibility of enforcing rules back to Council
- Reinforces multilateral surveillance
- Reinforces Commission's role as guardian of the Treaties

Replace sanctions by conditionality

- Gives strong positive incentives
- Makes access to future CFC conditional on compliance with EU fiscal rules

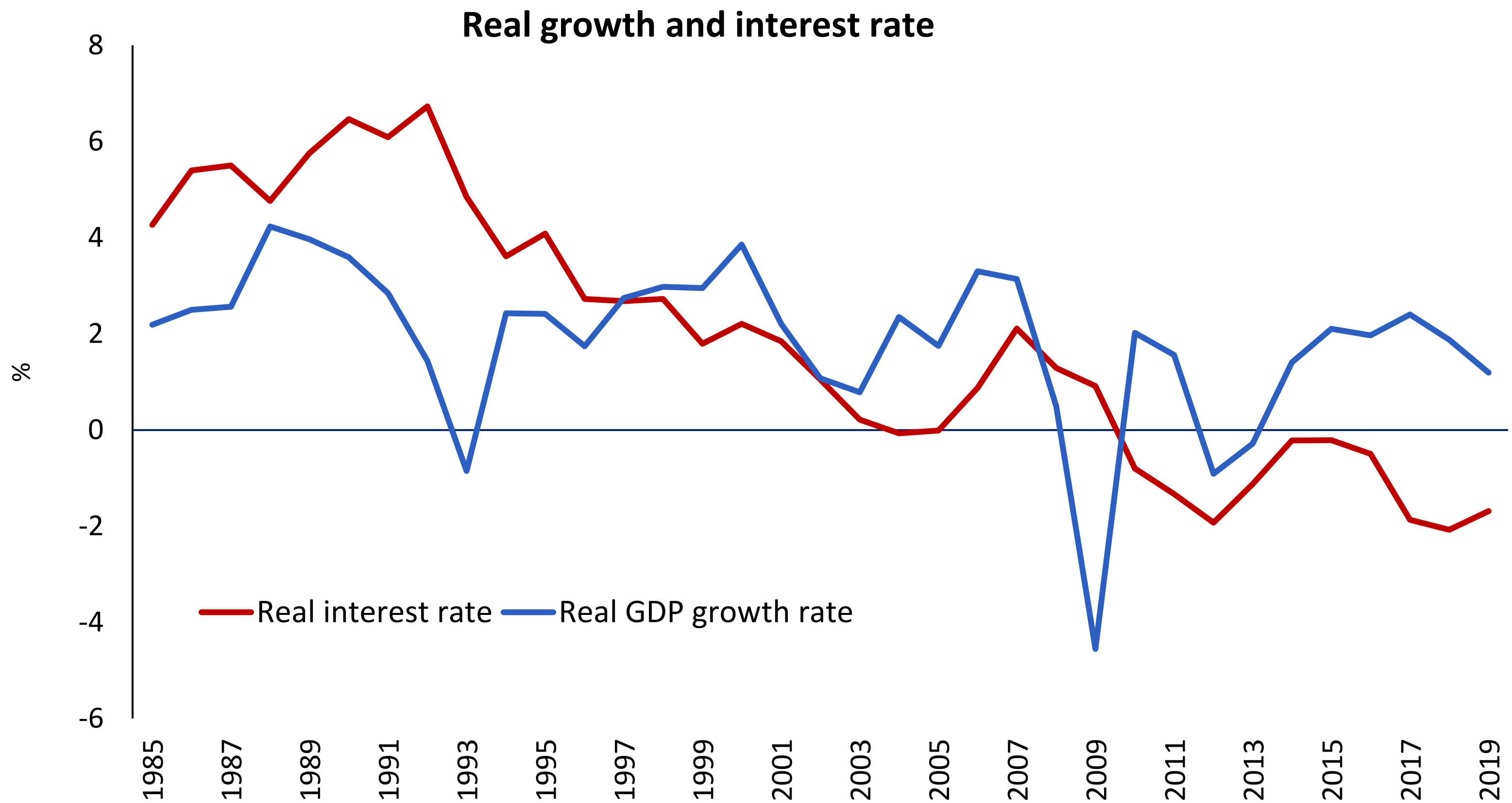
Do our proposals have some hopes to be implemented?

- Hard to say. It depends on where the new Commission intends to invest its political capital and what is also put on the table together with a revision of fiscal rules…
- Reforming the rules difficult because it implies changing pieces of legislature (from secondary up to the Treaties), although something could be done in terms of interpretation..(for example, on the expenditure rule..)

Do our proposals have some hopes to be implemented?

- However, our proposals fit well the current situation characterized by :
- 1) low investment rate, particularly in new technologies;
- 2) very low interest rates;
- 3) risk of deterioration of economic activity in the euro area;
- 4) still persistent surplus on external current balance….

Low interest rates & Debt; for how long?



Note: based on Eonia (and reconstructed)
Source: Blanchard et al. (2019)

Do our proposals have some hopes to be implemented?

- It might well be that some of our solutions will be implemented through other means (i.e. the French proposal for a temporarily limited suspension of the rules to allow for investment and exploit zero interest rates..)
- French-German conference: European public goods and to how to revise the rules so as to finance them..
- (Blanchard-Zettelmayer; Fuest-Pisany Ferry etc.)

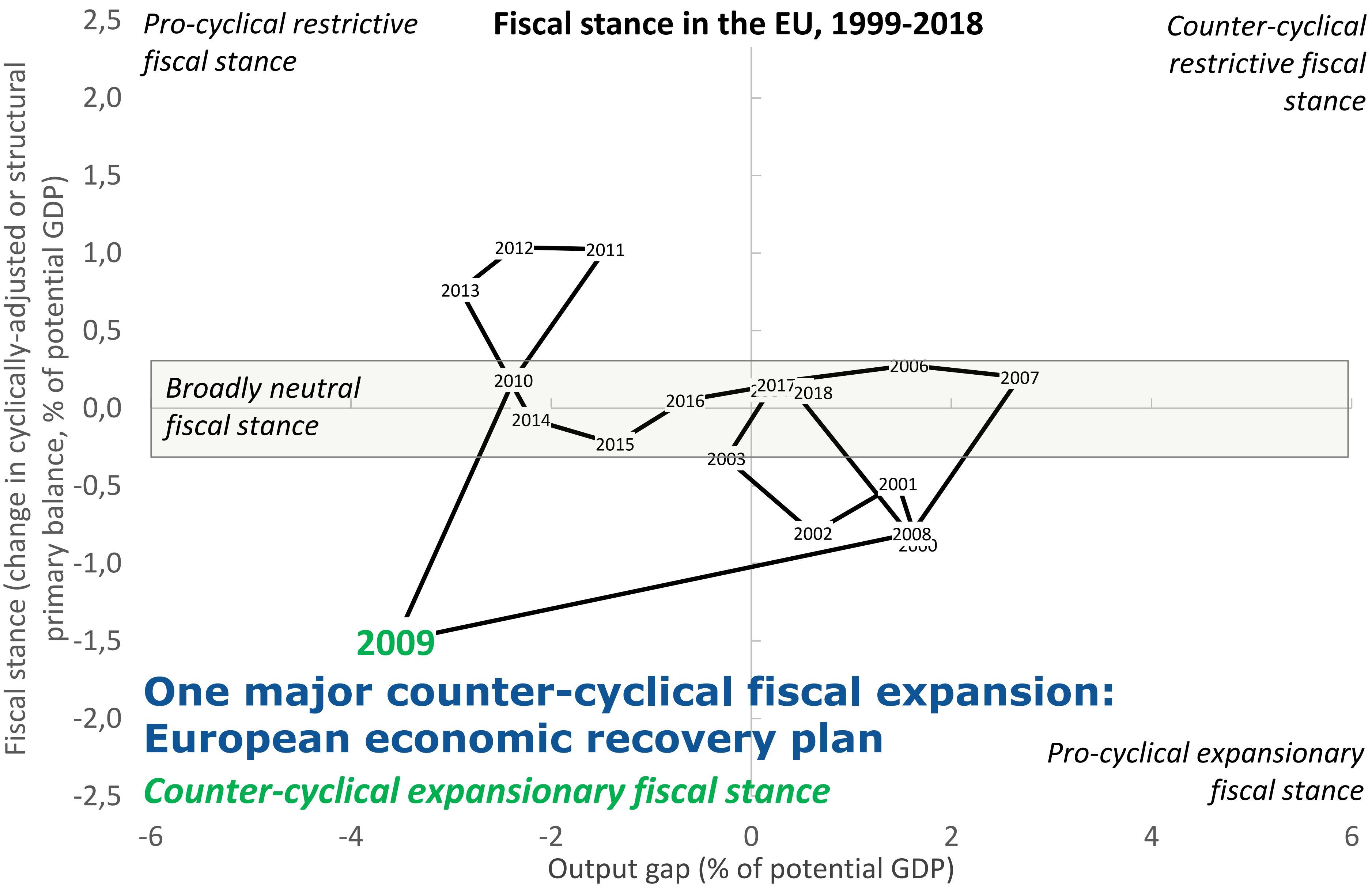
Do our proposals have some hopes to be implemented?

- Similarly, for the “common fiscal capacity”: stabilization halted (by Nordic countries) with the new Budgetary Instrument for Competitiveness and Convergence..
- but European unemployment benefits re-launched in the Von Der Leyen’s program (in the social pillar..)

Thank you for your attention

Background slides

2. Have EU fiscal rules allowed economic stabilisation?



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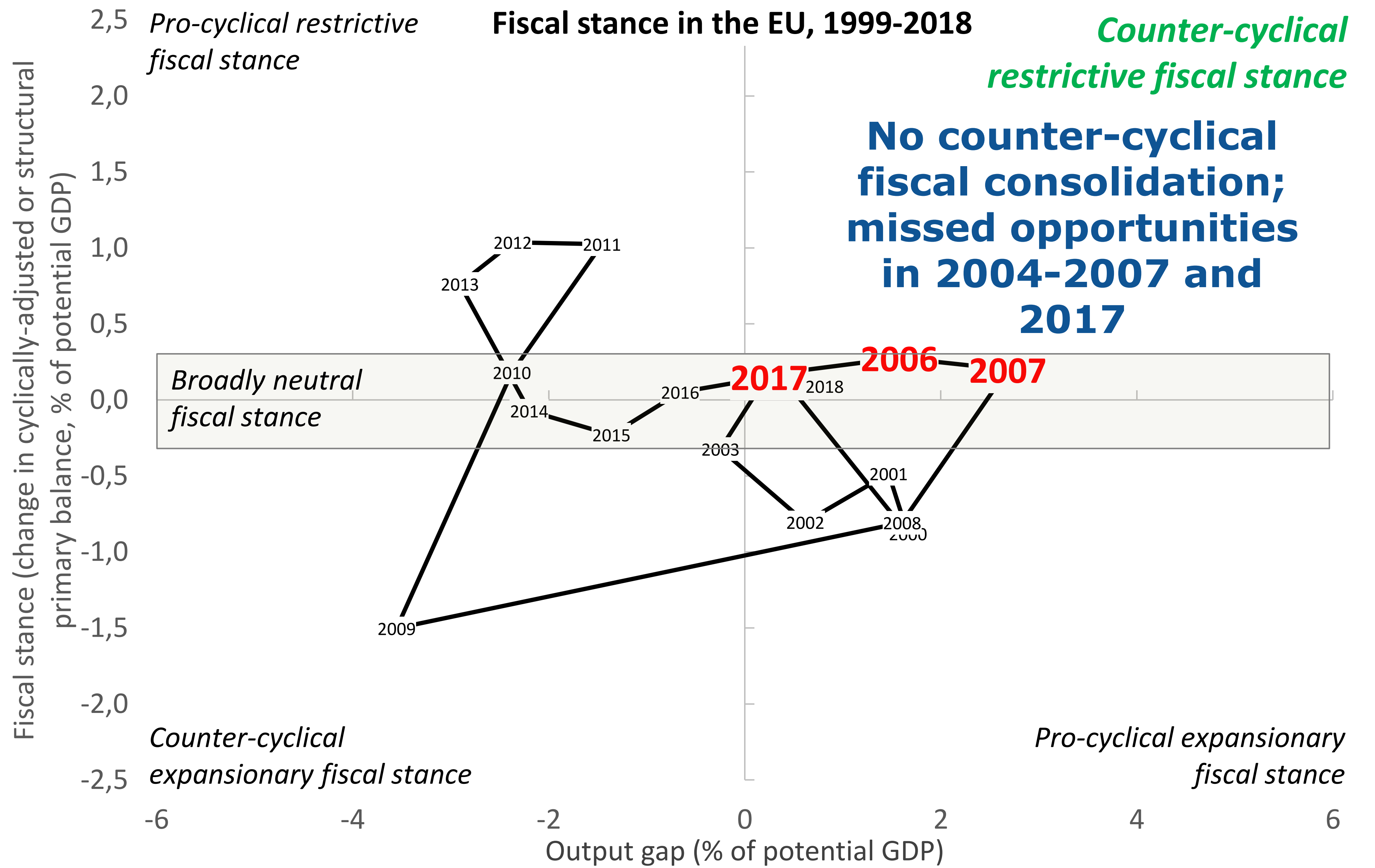

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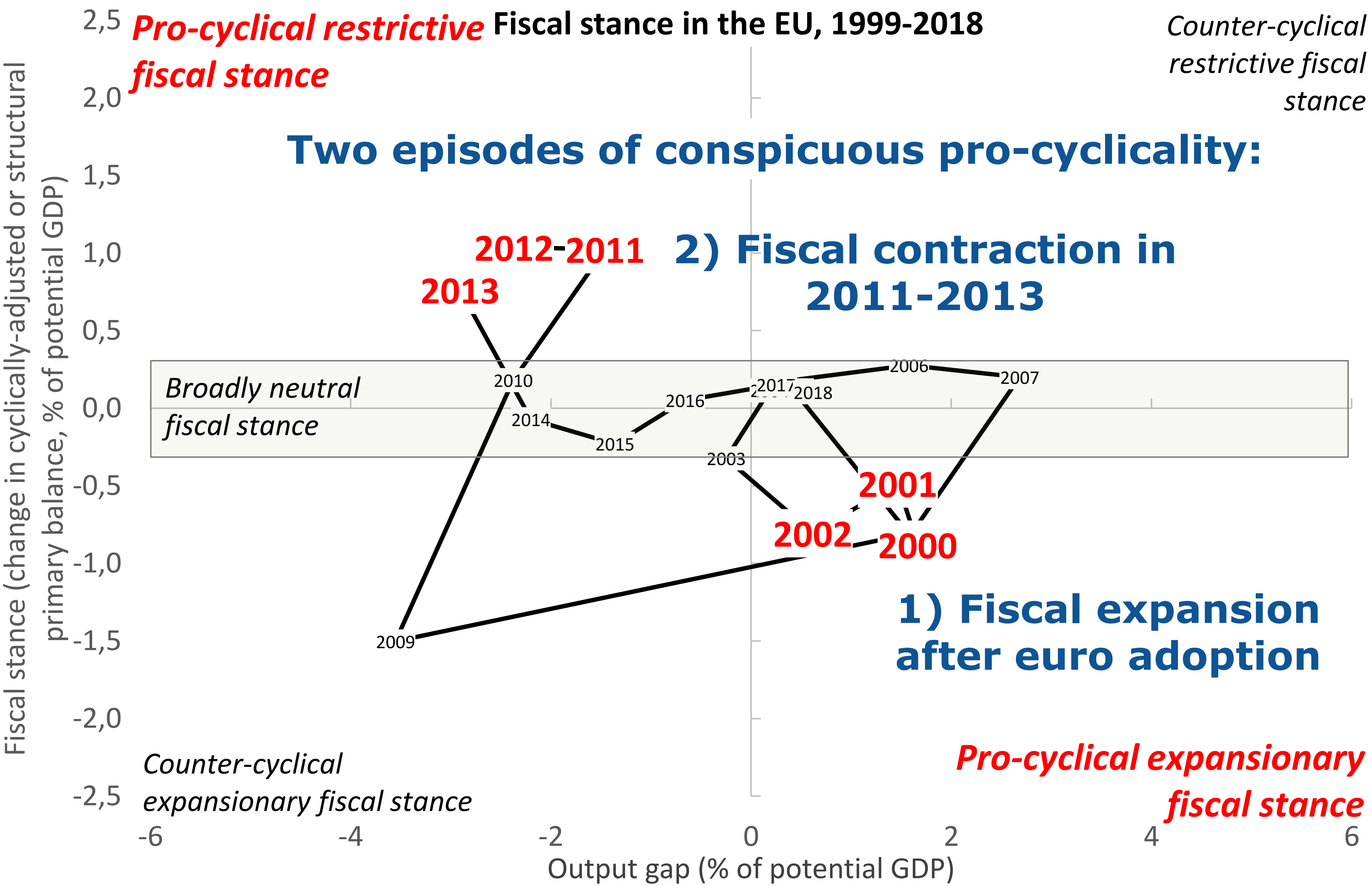

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Fiscal expansion/consolidation more pronounced
in very high-debt countries