

# **The new EU fiscal governance framework: a quantum leap or only small steps ahead?**

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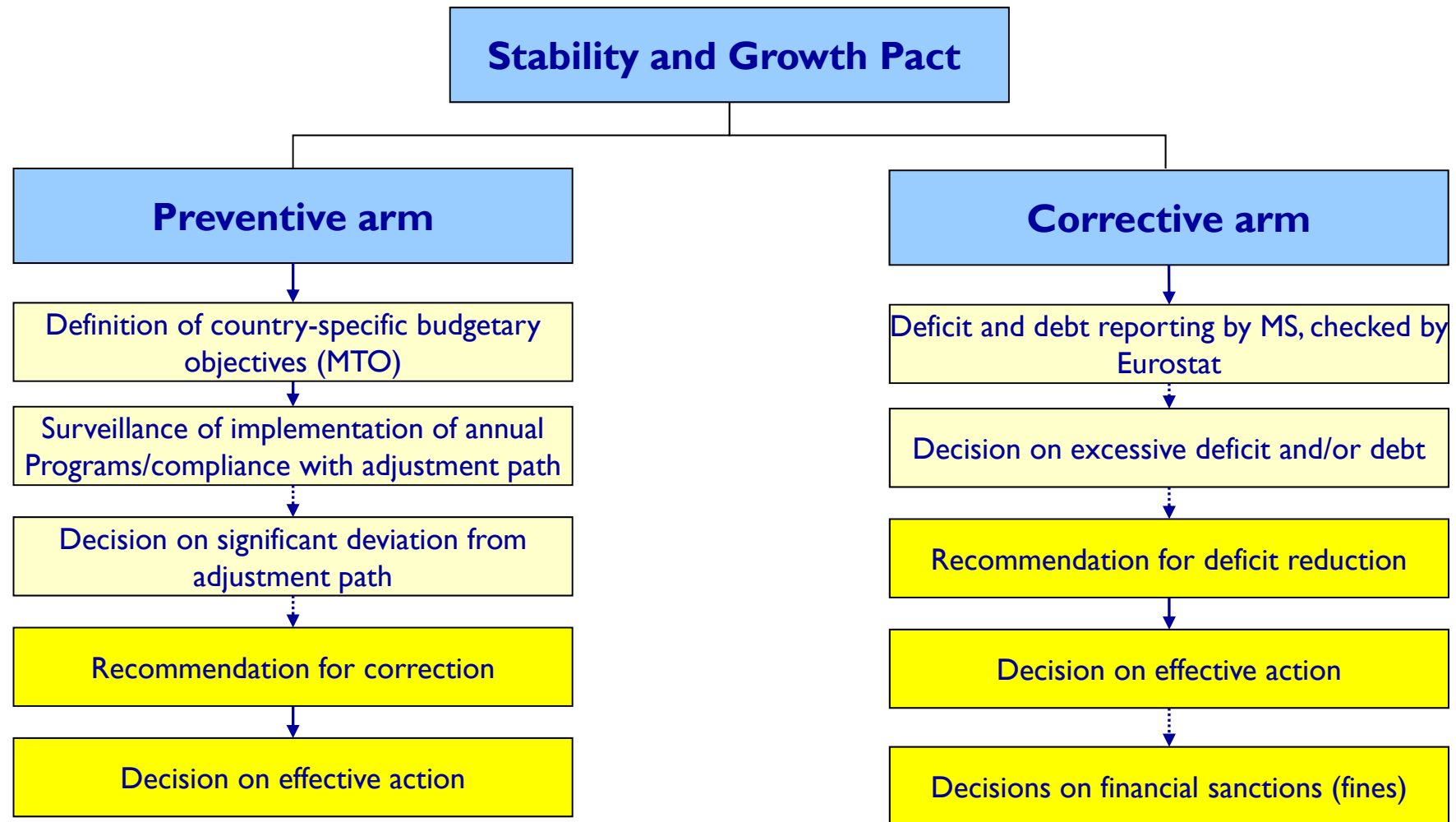
# Outline

- **Motivation**
- Impact of the reinforced EU fiscal governance framework
  - “Six-pack” (fiscal elements)
  - “Fiscal compact”
  - “Two-pack”
- The new fiscal framework: a quantum leap?
- The way ahead – conclusion

# Motivation

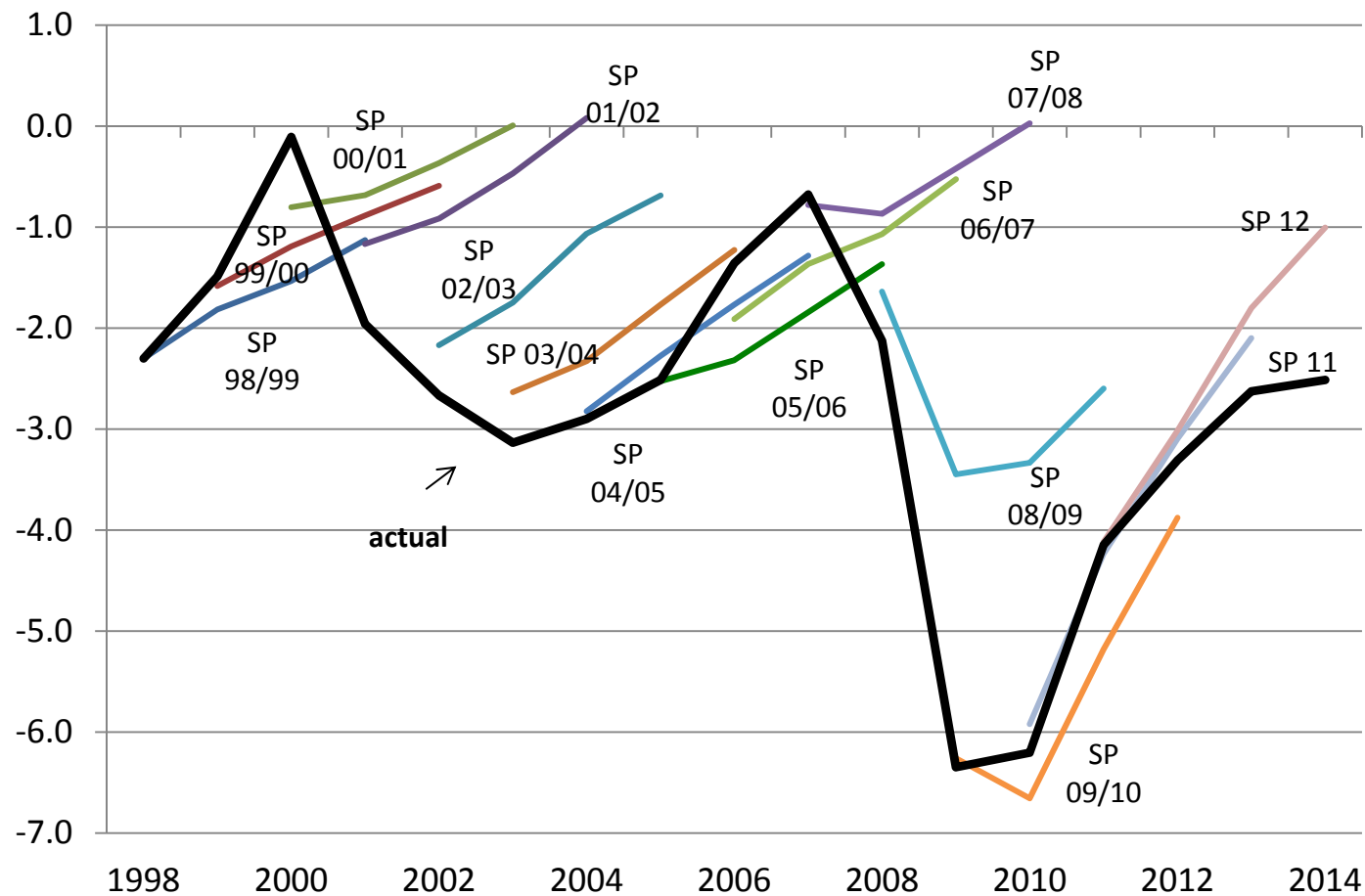
- **Conclusions of Barnes et al. (2013):**
  - “Over the very long term, the new fiscal rules imply very low levels of debt.”
  - “The requirements can thus not be considered to be a permanent approach.”
  - “... discretion will be needed in implementing the rules.”
- **Key questions of our contribution:**
  - Has the EU fiscal framework really been sufficiently reinforced?
  - Do we really need a less binding framework?
  - Is discretion really required and not stronger automaticity?

# The SGP has already been in place since 98/99 ...



# Despite the SGP, fiscal deficits have been moving targets in the euro area

**Fiscal plans vs fiscal outcomes of structural balances in % of GDP**  
(euro area weighted averages)



Notes: MTO in % of GDP based on 2012 data, BB = balanced budget, EMU membership in bold, until 2002 only cyclically-adjusted data.

Source: ex post data from European Commission.

# Non-compliance with the MTOs has been the rule, not the exception

	Structural net lending (+) / borrowing (-) (in % of GDP)															
	<b>MTO</b>															
	<b>2012</b>	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Belgium	<b>0.50</b>	-1.0	-1.0	<b>0.0</b>	-0.1	-1.1	-1.4	-0.9	-1.2	-1.2	-2.0	-3.9	-3.3	-3.4	-2.7	-2.7
Germany	<b>-0.50</b>	-1.6	<b>0.4</b>	-3.8	-3.8	-3.2	-2.9	-2.2	-1.7	-0.9	-0.9	-0.9	-2.3	-0.7	<b>0.2</b>	<b>0.3</b>
Estonia	<b>&gt;0</b>	-2.2	-0.5	-0.7	-0.5	<b>0.4</b>	<b>1.5</b>	<b>0.1</b>	-1.1	-1.5	-4.5	-1.1	-1.2	<b>-0.7</b>	<b>-0.4</b>	<b>-0.4</b>
Ireland	<b>-0.50</b>	<b>1.2</b>	<b>2.8</b>	<b>-0.5</b>	<b>-1.2</b>	<b>0.3</b>	<b>1.6</b>	<b>1.7</b>	<b>2.3</b>	<b>-1.5</b>	<b>-7.5</b>	<b>-10.1</b>	<b>-9.4</b>	<b>-7.9</b>	<b>-7.9</b>	<b>-7.5</b>
Greece	<b>BB</b>	-3.3	-4.0	<b>-4.6</b>	<b>-4.3</b>	<b>-5.6</b>	<b>-7.8</b>	<b>-5.3</b>	<b>-7.2</b>	<b>-7.7</b>	<b>-9.6</b>	<b>-14.7</b>	<b>-8.7</b>	<b>-5.4</b>	<b>-1.5</b>	<b>0.7</b>
Spain	<b>&gt;0</b>	-1.8	-2.0	-1.6	-0.9	-0.8	<b>0.3</b>	<b>0.8</b>	<b>1.6</b>	<b>1.0</b>	-4.4	-8.7	-7.6	-7.5	-6.3	-4.0
France	<b>BB</b>	-2.4	-2.9	-3.1	-4.3	-4.6	-4.6	-4.5	-3.9	-4.4	-4.1	-6.1	-5.7	-4.5	-3.4	-2.0
Italy	<b>BB</b>	-2.1	-1.8	-4.3	-3.8	-5.4	-5.1	-5.4	-4.1	-3.3	-3.7	-4.3	-3.7	-3.7	-1.4	-0.4
Cyprus	<b>BB</b>	-4.4	-3.0	-3.3	-4.9	-8.0	-4.9	-2.9	-1.1	<b>2.6</b>	-0.6	-6.2	-5.3	-5.9	-4.6	-4.8
Luxembourg	<b>0.50</b>	<b>2.3</b>	<b>3.7</b>	<b>4.8</b>	<b>1.0</b>	<b>0.6</b>	<b>-0.9</b>	<b>-0.2</b>	<b>0.6</b>	<b>1.6</b>	<b>2.5</b>	<b>0.9</b>	<b>0.0</b>	<b>0.2</b>	-1.1	-0.9
Malta	<b>BB</b>	-7.9	-7.5	-6.7	-6.6	-6.2	-5.9	-3.8	-2.8	-2.8	-5.4	-3.7	-4.6	-3.5	-3.5	-3.2
Netherlands	<b>-0.50</b>	<b>-0.5</b>	<b>0.7</b>	-1.1	-1.7	-1.8	-0.9	<b>0.5</b>	<b>0.4</b>	-1.1	-0.7	-4.1	-3.9	-3.4	-2.2	-1.1
Austria	<b>-0.45</b>	-2.8	-2.6	<b>-0.3</b>	-0.7	-0.9	-0.7	-1.3	-1.8	-1.9	-1.9	-2.8	-3.4	-2.3	-2.6	-2.1
Portugal	<b>-0.50</b>	<b>-4.3</b>	<b>-4.8</b>	<b>-6.1</b>	<b>-4.1</b>	<b>-5.6</b>	<b>-5.7</b>	<b>-6.0</b>	<b>-4.4</b>	<b>-3.7</b>	<b>-4.4</b>	<b>-8.5</b>	<b>-8.4</b>	<b>-6.2</b>	<b>-4.1</b>	<b>-2.5</b>
Slovenia	<b>BB</b>		-4.3	-4.0	-2.5	-2.6	-2.5	-2.0	-2.8	-2.9	-4.8	-4.3	-4.6	-4.7	-2.8	-2.0
Slovakia	<b>BB</b>	-6.9	-11.4	-5.8	-7.8	-2.1	-2.1	-1.8	-3.3	-3.6	-4.2	-7.5	-7.4	-5.4	-5.1	-3.2
Finland	<b>0.50</b>	<b>0.8</b>	<b>5.5</b>	<b>4.3</b>	<b>4.2</b>	<b>3.3</b>	<b>2.5</b>	<b>2.8</b>	<b>3.0</b>	<b>2.4</b>	<b>2.4</b>	<b>1.0</b>	<b>-0.4</b>	<b>0.3</b>	<b>-0.6</b>	<b>-0.1</b>
Euro area		-1.2	-2.9	-3.1	-3.3	-3.0	-2.6	-2.1	-2.0	-2.9	-4.6	-4.4	-3.5	-2.2	-1.3	-1.5

Notes: MTO in % of GDP based on 2012 data, BB = balanced budget, EMU membership in bold, until 2002 only cyclically-adjusted data.

Source: ex post data from European Commission.

# Despite repeated non-compliance, sanctions have never been imposed in the corrective arm of the SGP

	Net lending (+) / borrowing (-) (in % of GDP)															
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Belgium	-0.6	0.0	0.4	-0.1	-0.1	-0.1	-2.5	0.4	-0.1	-1.0	-5.5	-3.8	-3.7	-3.0	-3.4	-3.5
Germany	-1.6	1.1	-3.1	-3.8	-4.2	-3.8	-3.3	-1.6	0.2	-0.1	-3.1	-4.1	-0.8	-0.2	-0.2	0.0
Estonia	-3.5	-0.2	-0.1	0.3	1.7	1.6	1.6	2.5	2.4	-2.9	-2.0	0.2	1.1	-1.1	-0.5	0.3
Ireland	2.6	4.7	0.9	-0.4	0.4	1.4	1.7	2.9	0.1	-7.4	-13.9	-30.9	-13.4	-8.4	-7.5	-5.0
Greece	-3.1	-3.7	-4.5	-4.8	-5.7	-7.6	-5.5	-5.7	-6.5	-9.8	-15.6	-10.7	-9.4	-6.8	-5.5	-4.6
Spain	-1.2	-0.9	-0.5	-0.2	-0.3	-0.1	1.3	2.4	1.9	-4.5	-11.2	-9.7	-9.4	-8.0	-6.0	-6.4
France	-1.8	-1.5	-1.6	-3.3	-4.1	-3.6	-2.9	-2.3	-2.7	-3.3	-7.5	-7.1	-5.2	-4.5	-3.5	-3.5
Italy	-1.9	-0.8	-3.1	-3.1	-3.6	-3.5	-4.4	-3.4	-1.6	-2.7	-5.4	-4.5	-3.9	-2.9	-2.1	-2.1
Cyprus	-4.3	-2.3	-2.2	-4.4	-6.6	-4.1	-2.4	-1.2	3.5	0.9	-6.1	-5.3	-6.3	-5.3	-5.7	-6.0
Luxembourg	3.4	6.0	6.1	2.1	0.5	-1.1	0.0	1.4	3.7	3.2	-0.8	-0.8	-0.3	-1.9	-1.7	-1.8
Malta	-7.2	-5.8	-6.4	-5.8	-9.2	-4.7	-2.9	-2.8	-2.3	-4.6	-3.9	-3.6	-2.7	-2.6	-2.9	-2.6
Netherlands	0.4	2.0	-0.2	-2.1	-3.1	-1.7	-0.3	0.5	0.2	0.5	-5.6	-5.1	-4.5	-3.7	-2.9	-3.2
Austria	-2.3	-1.7	0.0	-0.7	-1.5	-4.4	-1.7	-1.5	-0.9	-0.9	-4.1	-4.5	-2.5	-3.2	-2.7	-1.9
Portugal	-3.1	-3.3	-4.8	-3.4	-3.7	-4.0	-6.5	-4.6	-3.1	-3.6	-10.2	-9.8	-4.4	-5.0	-4.5	-2.5
Slovenia	-3.0	-3.7	-4.0	-2.4	-2.7	-2.3	-1.5	-1.4	0.0	-1.9	-6.0	-5.7	-6.4	-4.4	-3.9	-4.1
Slovakia	-7.4	-12.3	-6.5	-8.2	-2.8	-2.4	-2.8	-3.2	-1.8	-2.1	-8.0	-7.7	-4.9	-4.9	-3.2	-3.1
Finland	1.7	7.0	5.1	4.2	2.6	2.5	2.9	4.2	5.3	4.4	-2.5	-2.5	-0.6	-1.8	-1.2	-1.0
Euro area	-1.5	-0.1	-2.0	-2.7	-3.1	-2.9	-2.5	-1.4	-0.7	-2.1	-6.3	-6.2	-4.1	-3.3	-2.6	-2.5

Note: EMU membership in bold.

Source: ex post data from European Commission.

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- **Impact of the reinforced EU fiscal governance framework**
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# Main reforms of the EU fiscal framework since 2011

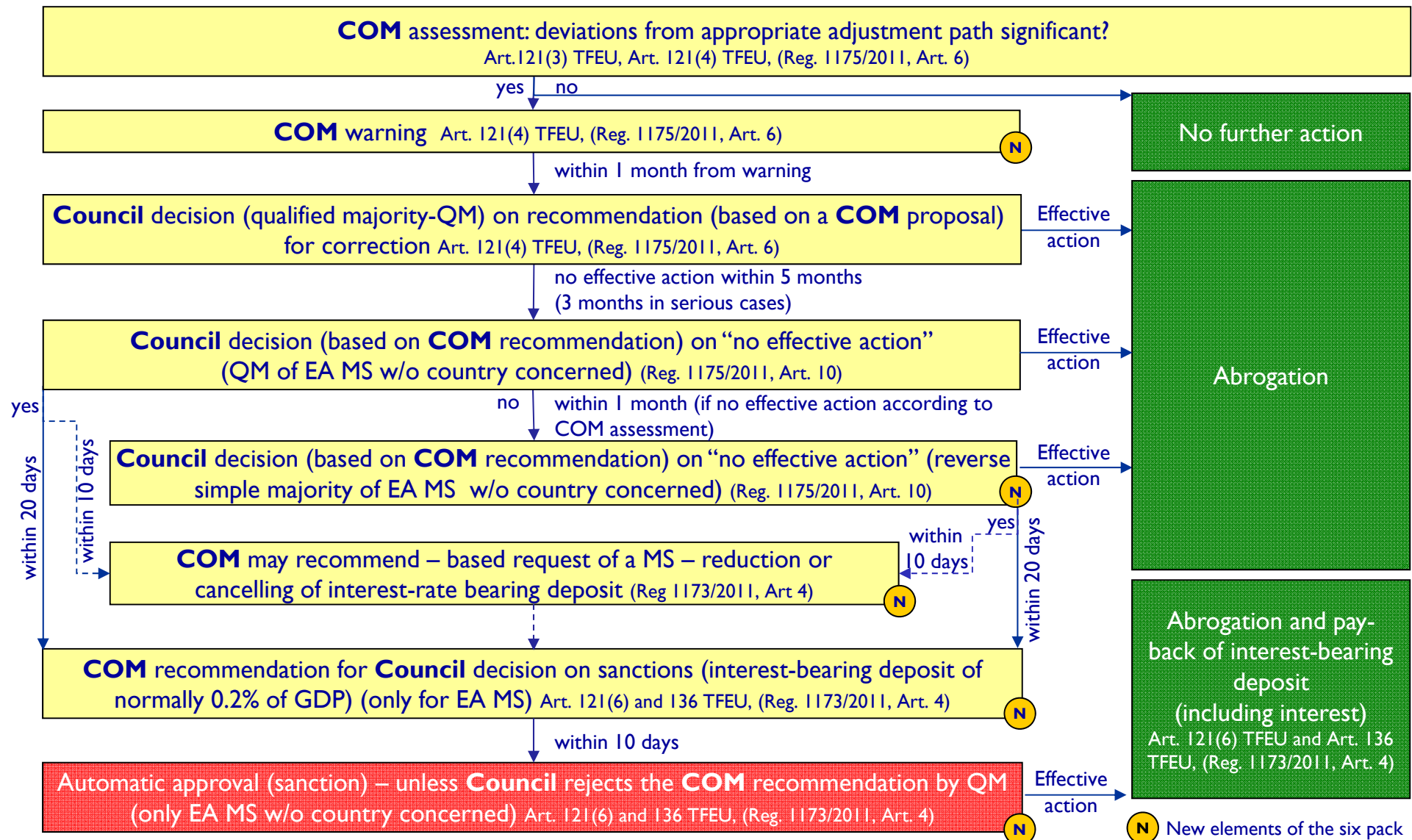
- **Euro+ pact**
- **European Semester**
- **Six-pack**
  - six EU legislative proposals of which four are fiscal – entered into force in December 2011
- **Treaty on Stability, Coordination and governance in the EMU (TSCG), which includes the **fiscal compact****
  - signed by HoSoG with the exception of the UK and the CZ on 2 March 2012
  - entered into force on 1 January 2013
- **Two-pack**
  - two regulations proposed by the EU COM in November 2011
  - still in the triilogue negotiations between the EU Council, the EU COM and the EP; expected to be finalised in early 2013

# The impact of the six pack on the Stability and Growth Pact

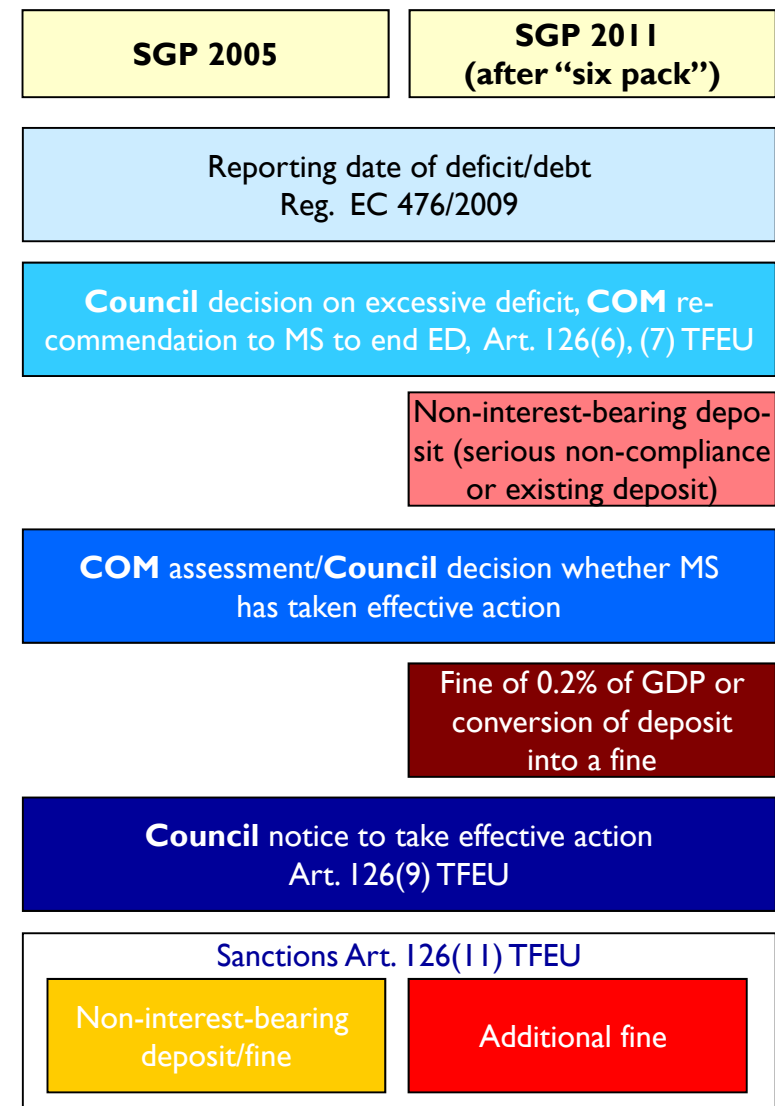
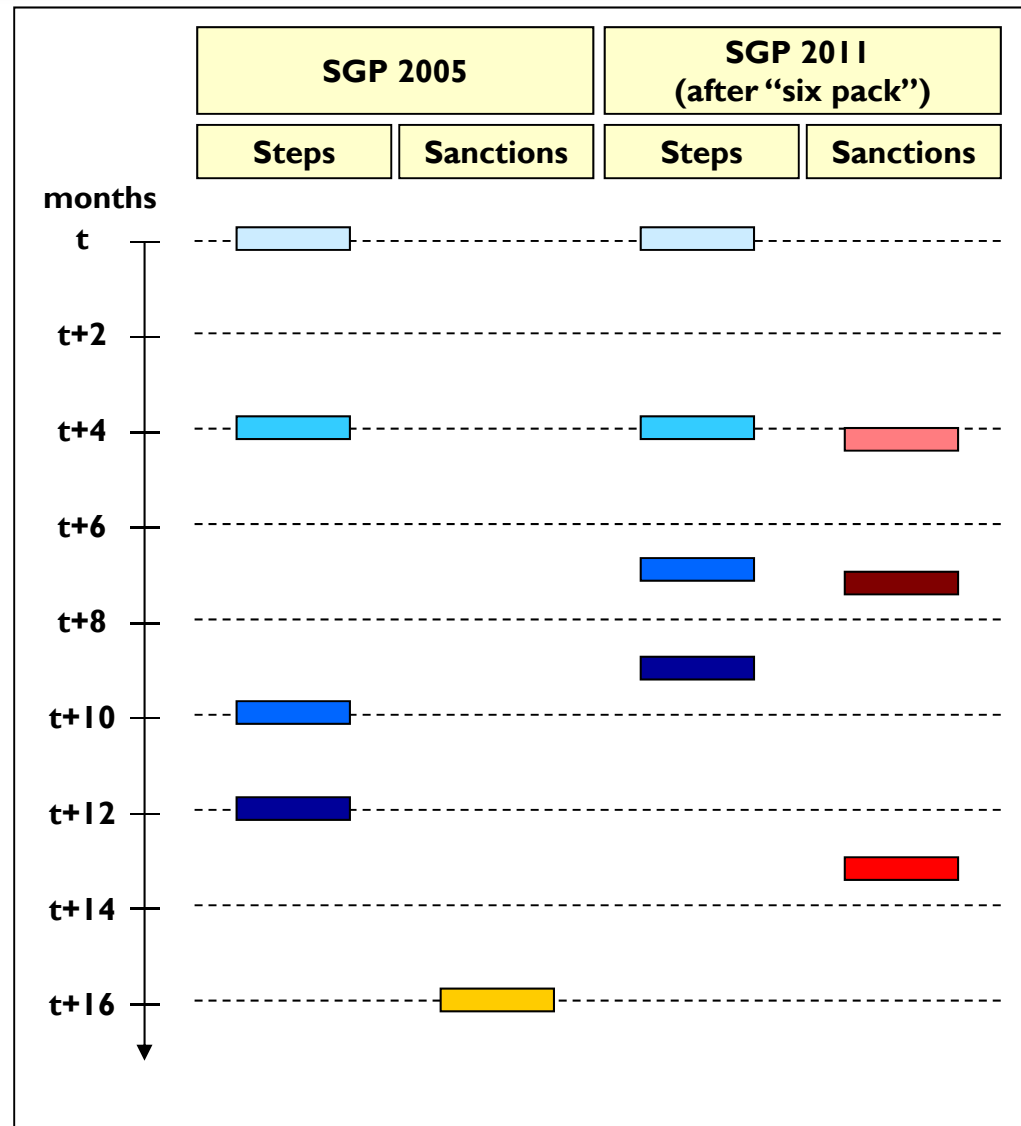
- **Preventive arm**
  - expenditure rule and financial sanction (interest-bearing deposit)
  - more automaticity through reversed qualified majority voting (RQMV)
- **Corrective arm**
  - equal footing of public debt criterion
  - financial and non-financial sanctions (earlier, gradually increasing and more automatic)
- **Criteria relatively soft**
  - large number of exemptions (relevant factors) / loopholes



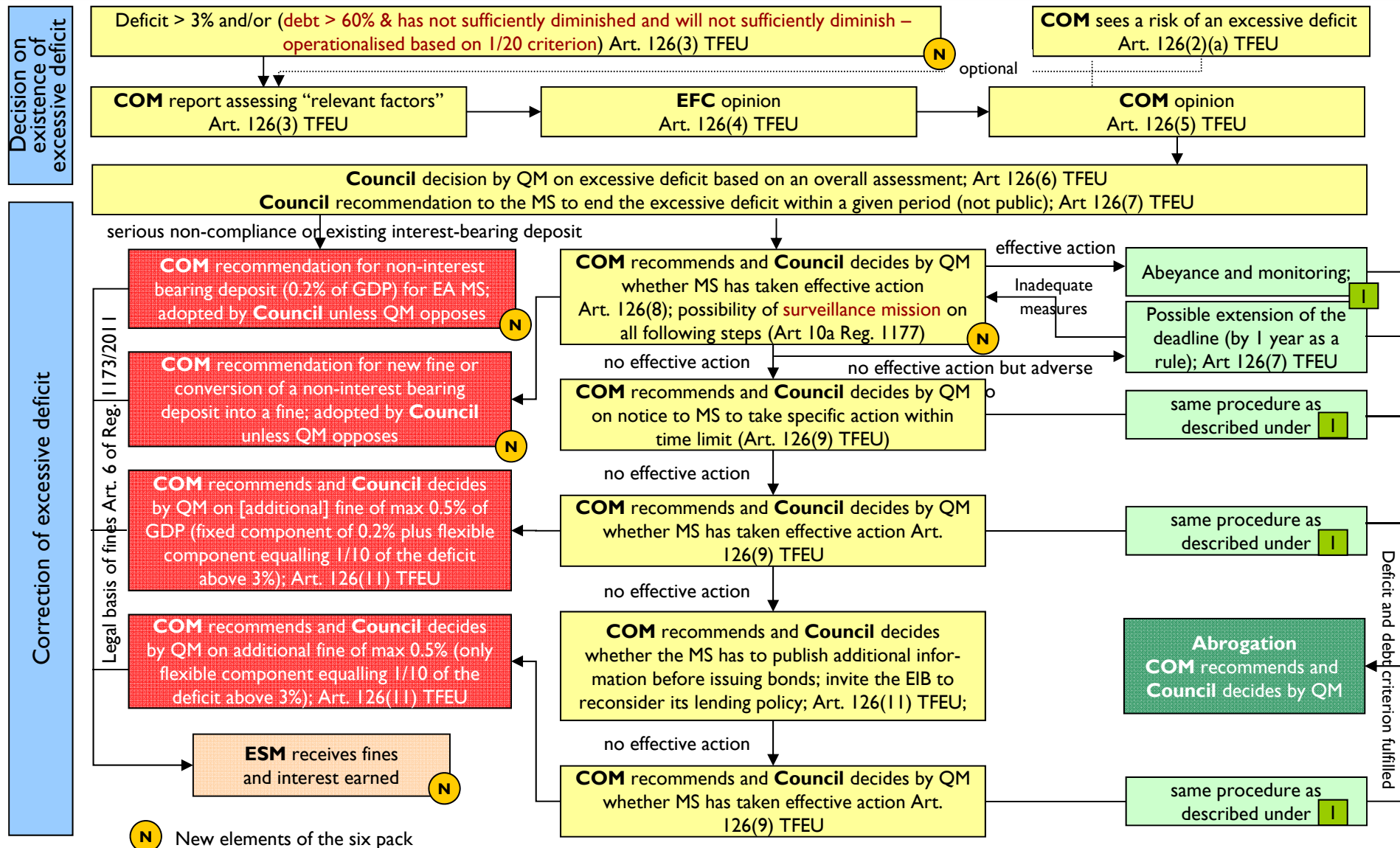
# ... an additional warning, reversed simple majority voting and a new financial sanction are introduced



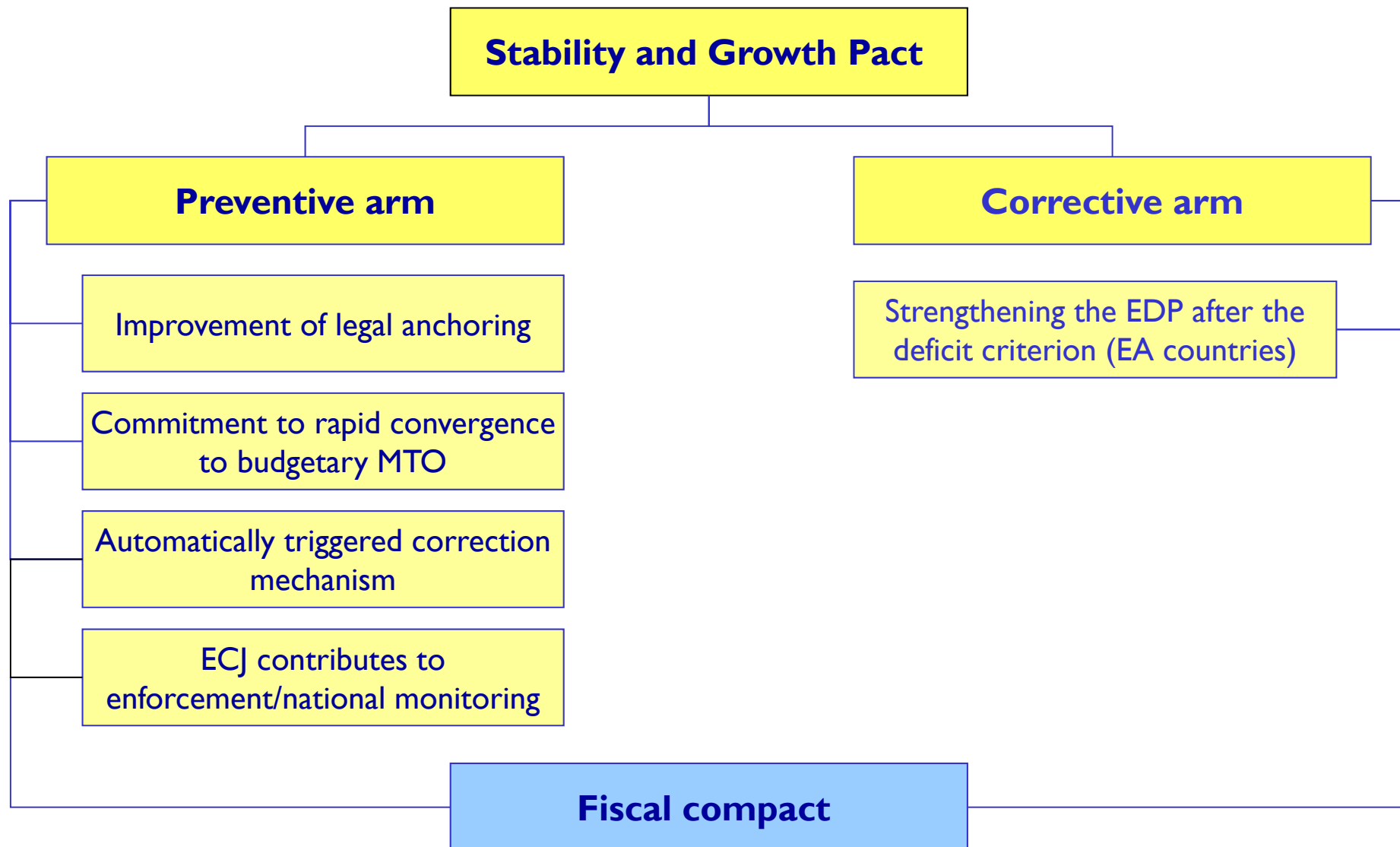
# Sanctions can now be implemented earlier in case of persistent non-compliance



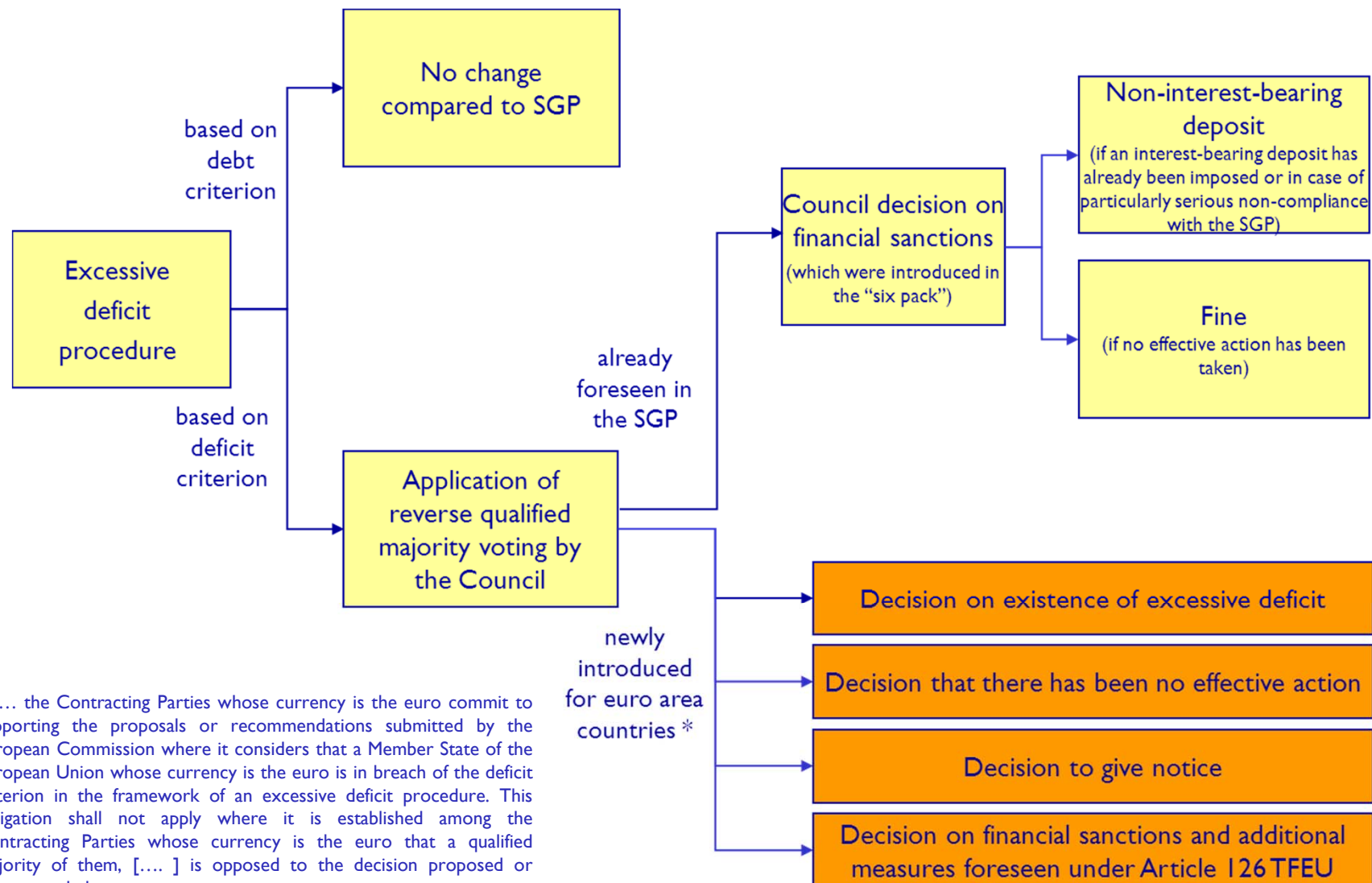
# In the corrective arm, the debt reduction benchmark, new sanctions and RQMV are introduced



# Fiscal compact strengthens the rule-based fiscal governance framework ...



# ... and further increases the automaticity of the EDP under the deficit (but not the debt) criterion



\* ... the Contracting Parties whose currency is the euro commit to supporting the proposals or recommendations submitted by the European Commission where it considers that a Member State of the European Union whose currency is the euro is in breach of the deficit criterion in the framework of an excessive deficit procedure. This obligation shall not apply where it is established among the Contracting Parties whose currency is the euro that a qualified majority of them, [...] is opposed to the decision proposed or recommended.



# The reform elements of the “two-pack”

## Proposed regulation on monitoring draft budgetary plans

Reg. COM(2011) 821 final

### Budgetary regulation

- Enhance the budgetary surveillance of draft budgetary plans by the European Commission
- Closer monitoring procedures to ensure the correction of excessive deficits

## Proposed regulation on strengthening surveillance procedures

Reg. COM(2011) 819 final

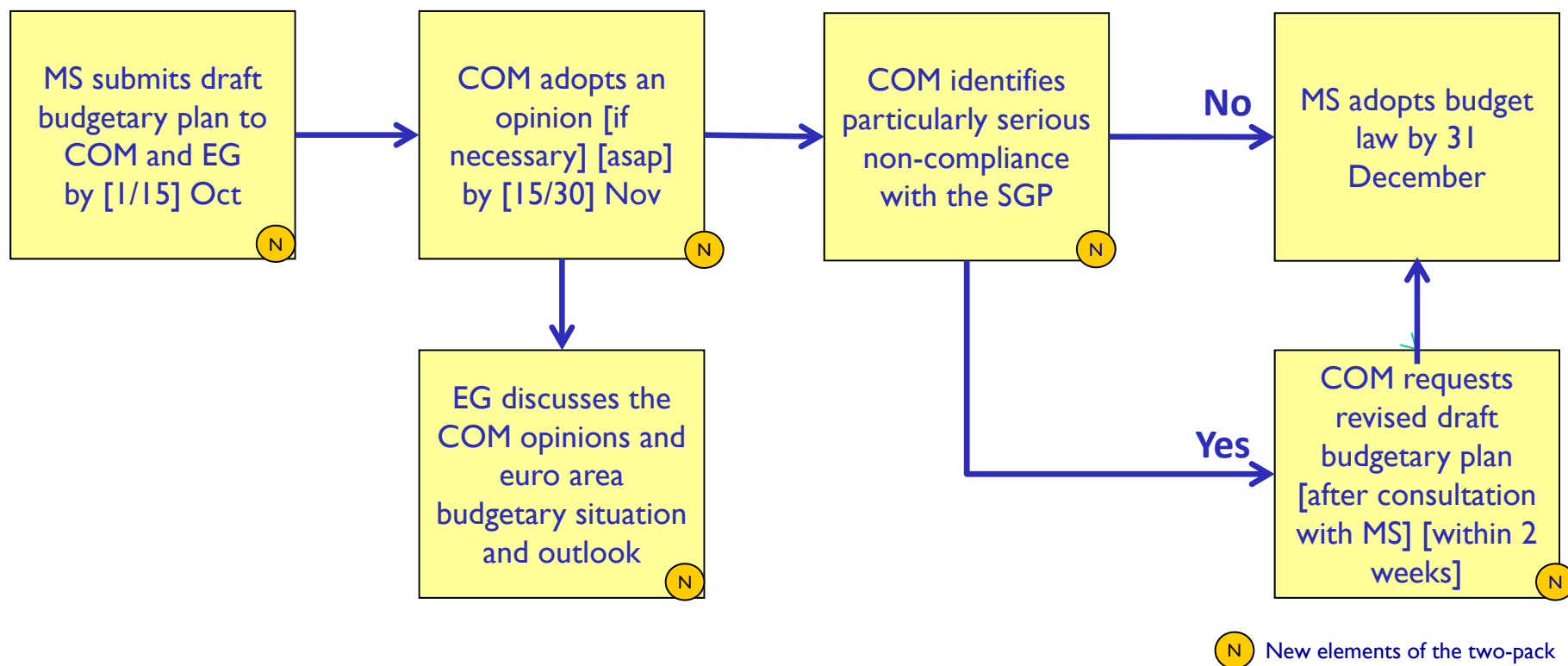
### Stability regulation

- Lays down a surveillance mechanism applicable to euro area Member States experiencing or threatened with financial market tensions and/or receiving financial assistance
- Involvement of the ECB and European Supervisory Authorities

→ Negotiations on-going; but compromise in sight

# The two-pack allows COM to issue an opinion and request a revision of draft budgetary plans ...

## Assessment of draft budgetary plans according to the budgetary regulation (parts in brackets refer to open positions at time of writing)



... and COM can address a recommendation if it sees risks that deadline for correction of excessive deficit will not be met.

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# Requirements for a quantum leap of EU governance in the (Maastricht) world

- **Well-defined numerical fiscal rules:**
  - with strict and ambitious deadlines
  - without escape clauses
- Instruments for **early intervention in draft budget plans**
- Ensure an **automatic correction of past cumulated slippages** (avoid ‘moving deficit targets’)
- Transformation to a **fairly automatic system**
- **Timely, credible and ‘biting’ sanctions**
- **Strong national anchoring**

## The recent reforms have strengthened the framework, but central weaknesses remain

- **Lack of sufficient automaticity** in the procedures of the SGP
- **Effectiveness depends heavily on** a strict and rigorous application of the rules by the **COM**
- No effective prevention of **upward debt trajectories**
- **Debt benchmark unlikely to be strictly applied**
- **Early scrutiny** of draft budget plans and consolidation **may not be effective** in preventing deviations from SGP obligations
- **No ultimate sanction** to enforce necessary adjustments of national policies **in case of repeated non-compliance**

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# The way ahead – a further sharing of fiscal sovereignty is needed

- **Fiscal rules are broadly sound, but implementation is key**
- **Lack of instruments** for situations in which a country's fiscal policy continues to go harmfully astray
- A **qualitative move towards a fiscal union is necessary** to make the fiscal framework fully commensurate to the requirements of the single currency
- **At the core is the further sharing of fiscal sovereignty:** the ultimate authority to decide on fiscal policy needs to be moved to the EA level – subject to democratic accountability (ex ante power to effectively enforce compliance with the existing numerical benchmarks)
- Two concrete options:
  - **prior approval of debt issuance and ex ante intervention rights into national budgets** (not substitutes but rather complements; could be gradually faded-in)
- **Automaticity needs to be further strengthened:** avoiding the possibility of lax implementation or political discretion