



Economic Governance Review

Main finding and state of play

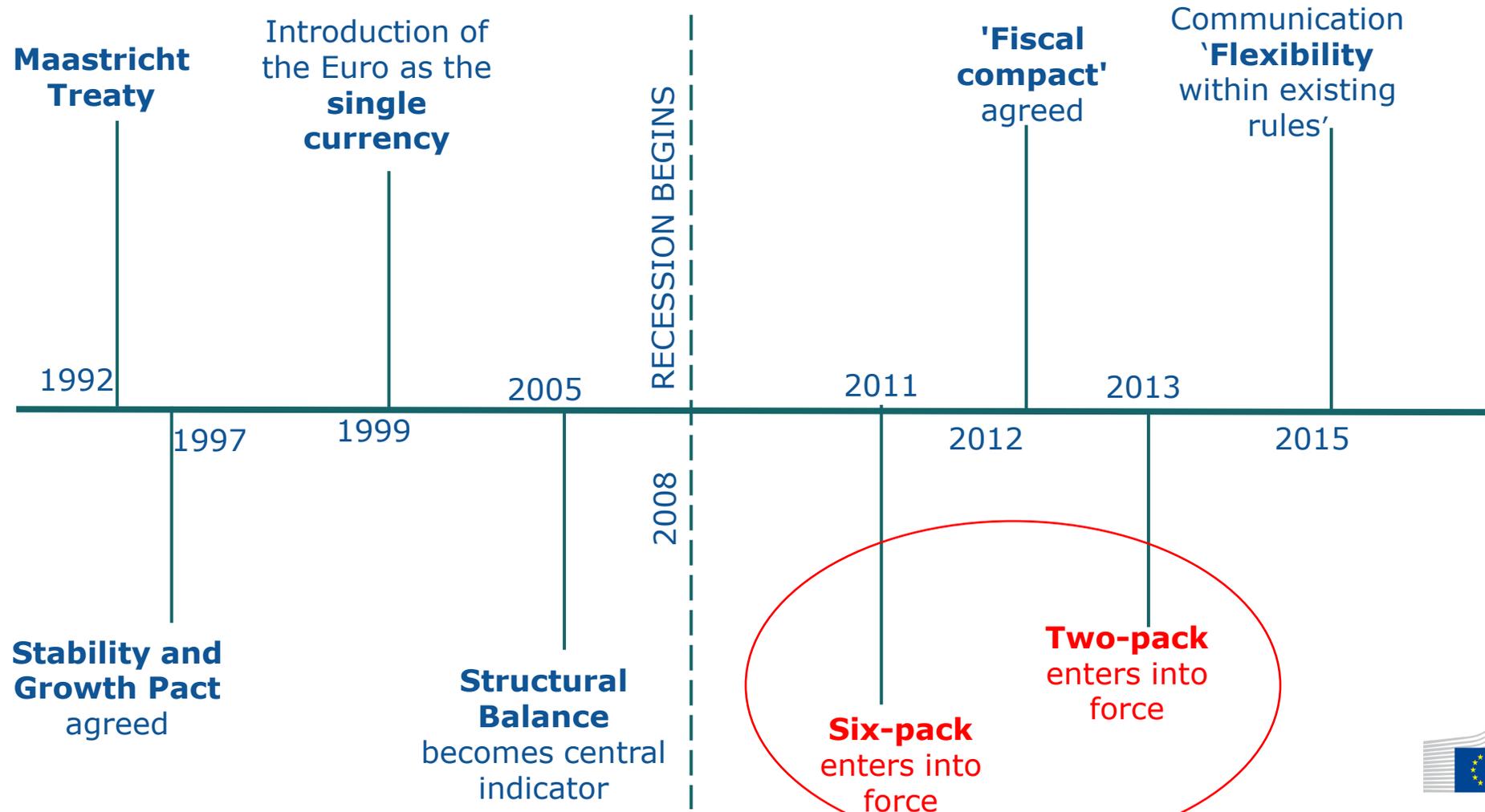
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Outline

- 1. Context and general approach of the review**
2. Assessment of the fiscal surveillance framework
3. Open questions for a public discussion and next steps

The evolution of the framework

Timeline of relevant changes



Six-pack

Regulation No 1176/2011	<i>“on the prevention and correction of macroeconomic imbalances”</i> : Lays out the details of the macroeconomic imbalance surveillance procedure
Regulation No 1174/2011	<i>“on enforcement measures to correct excessive macroeconomic imbalances in the euro area”</i> : Possible sanctions on other corrective procedures under the MIP for EA MS
Regulation No 1175/2011	<i>“amending Council Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies”</i> : Strengthening of the preventive arm through expenditure benchmark and significant deviation procedure
Regulation No 1177/2011	<i>“amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure”</i> : debt reduction benchmark, ‘comply-or-explain’ principle for the Council
Regulation No 1173/2011	<i>“on the effective enforcement of budgetary surveillance in the euro area”</i> : details possible sanctions under the preventive/corrective arm of SGP
Directive 2011/85	<i>“on requirements for budgetary frameworks of the Member States”</i> : specific requirements w.r.t unbiased forecasts and independent fiscal institutions

Two-pack

Regulation No 472/2013	<i>“on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability”</i> : programme support and surveillance for EA MS under financial stress
Regulation No 473/2013	<i>“on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area”</i> : common budgetary timeline for the EA and assessment of draft budgetary plans

Six-pack

Regulation No 1176/2011 “on the prevention and correction of macroeconomic imbalances”: Lays out the details of the **macroeconomic imbalance surveillance procedure**

Regulation No 1174/2011 “on enforcement measures to correct excessive macroeconomic imbalances in the euro area”: Possible **sanctions on other corrective procedures under the MIP** for EA MS

Regulation No 1175/2011 “amending Council Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies”: Strengthening of the preventive arm through **expenditure benchmark and significant deviation procedure**

Regulation No 1177/2011 “amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure”: **debt reduction benchmark, ‘comply-or-explain’ principle for the Council**

Regulation No 1173/2011 “on the effective enforcement of budgetary surveillance in the euro area”: details **possible sanctions under the preventive/corrective arm of SGP**

Directive 2011/85 “on requirements for budgetary frameworks of the Member States”: specific requirements w.r.t **unbiased forecasts and independent fiscal institutions**

Two-pack

Regulation No 472/2013 “on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability”: **programme support and surveillance** for EA MS under financial stress

Regulation No 473/2013 “on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area”: **common budgetary timeline** for the EA and assessment of draft budgetary plans

Review of the Six- and Two-Pack: a legal requirement

- First review published on 28 November 2014, but it was based on insufficient experience with the reformed framework.
- Legislation requires a review every five years thereafter.
- Where appropriate, the report shall be accompanied by proposals for amendments.

General approach of the review

Comprises **one Communication** and **two Staff Working Documents**

Assessment of effectiveness of the surveillance framework, with a focus on the six-pack and two-pack

Economic context has materially changed over the last decade

- Challenges posed by low potential growth, low interest rates, low inflation, low reform momentum
- Need to transform our economies: become the first climate-neutral continent, be fit for the digital age, deal with population ageing and ensure that nobody is left behind.

Plans for an inclusive debate with stakeholders following the Communication

- Open but precise questions to guide the debate with stakeholders
- **in light of the COVID-crisis and the need to focus on the RRF and the immediate policy response, the public consultation has been put on hold**

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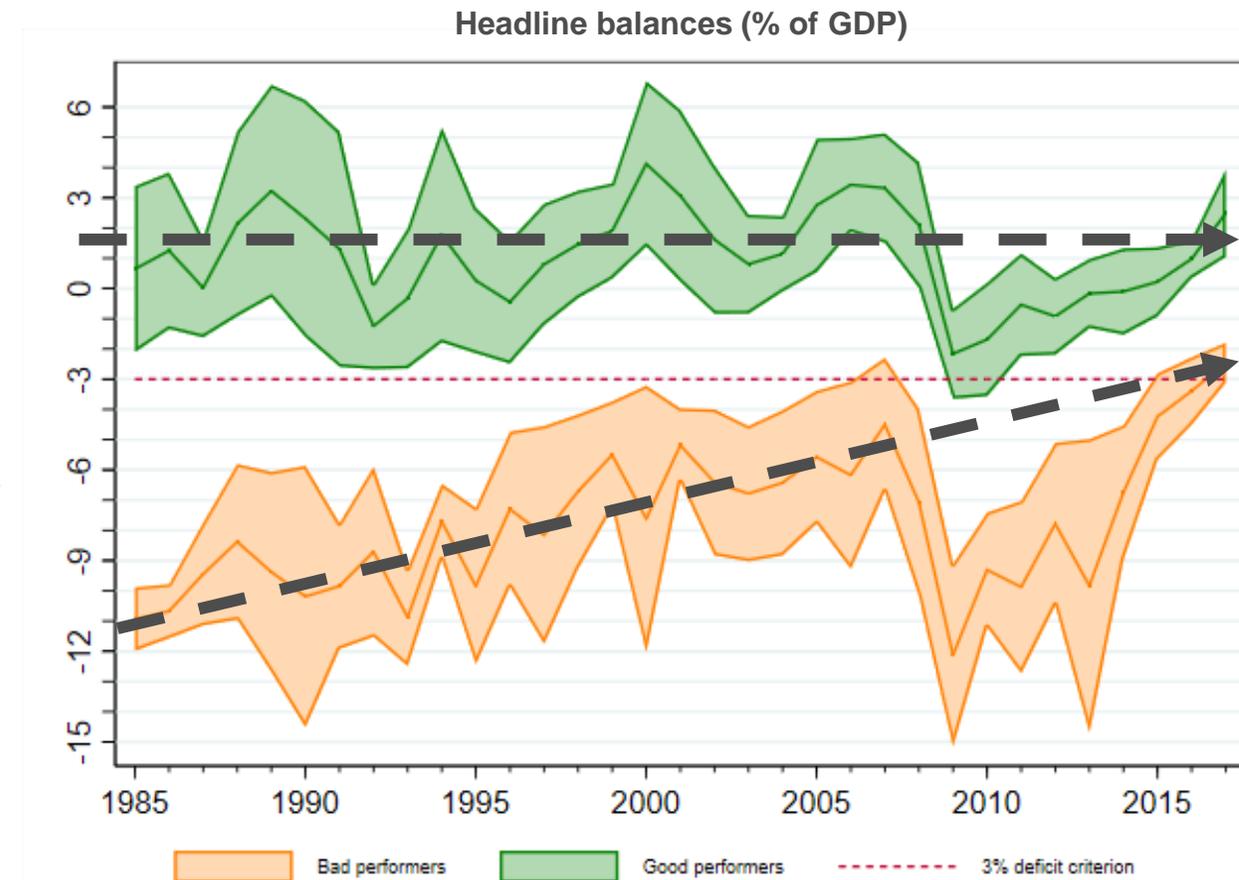
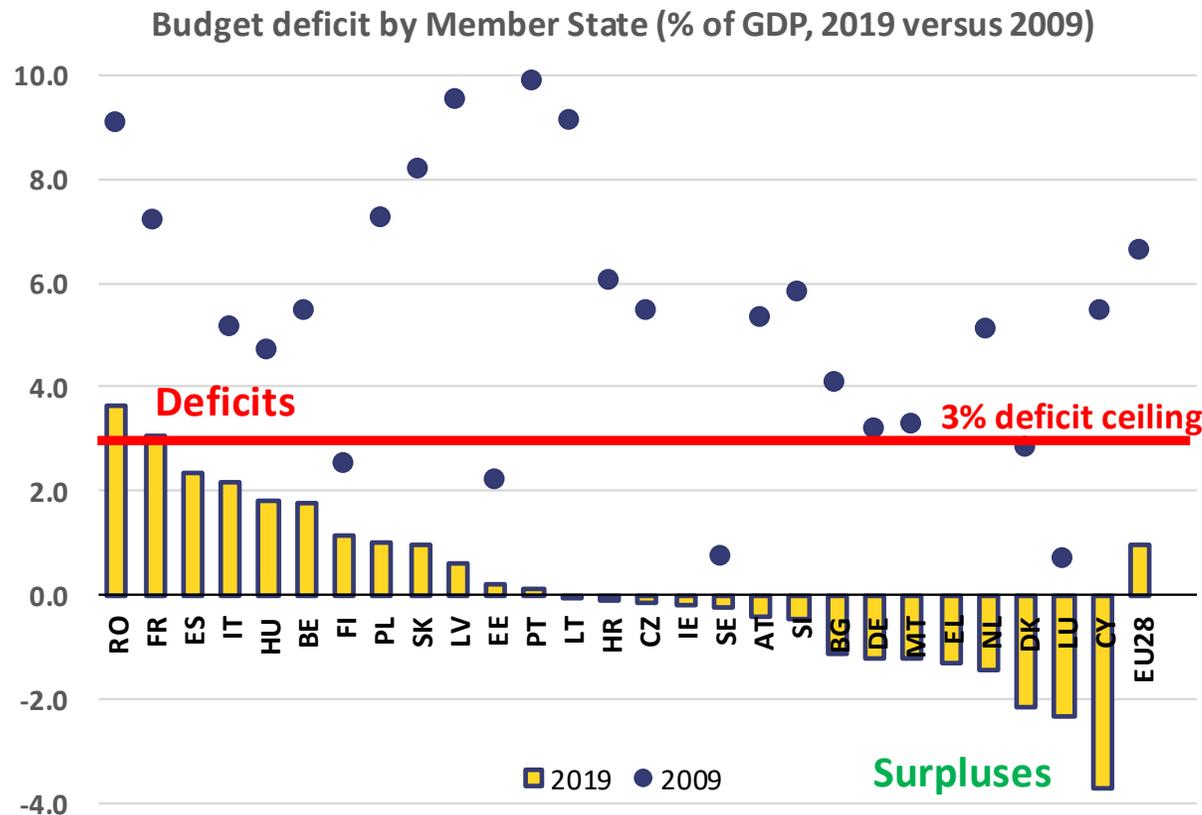
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Assessment of the fiscal surveillance framework

- Sustainability of public finances
- Economic stabilisation at the level of individual Member States and euro area
- Quality of public finances, including the development of public investment
- Ownership and governance of EU fiscal rules
- National fiscal frameworks

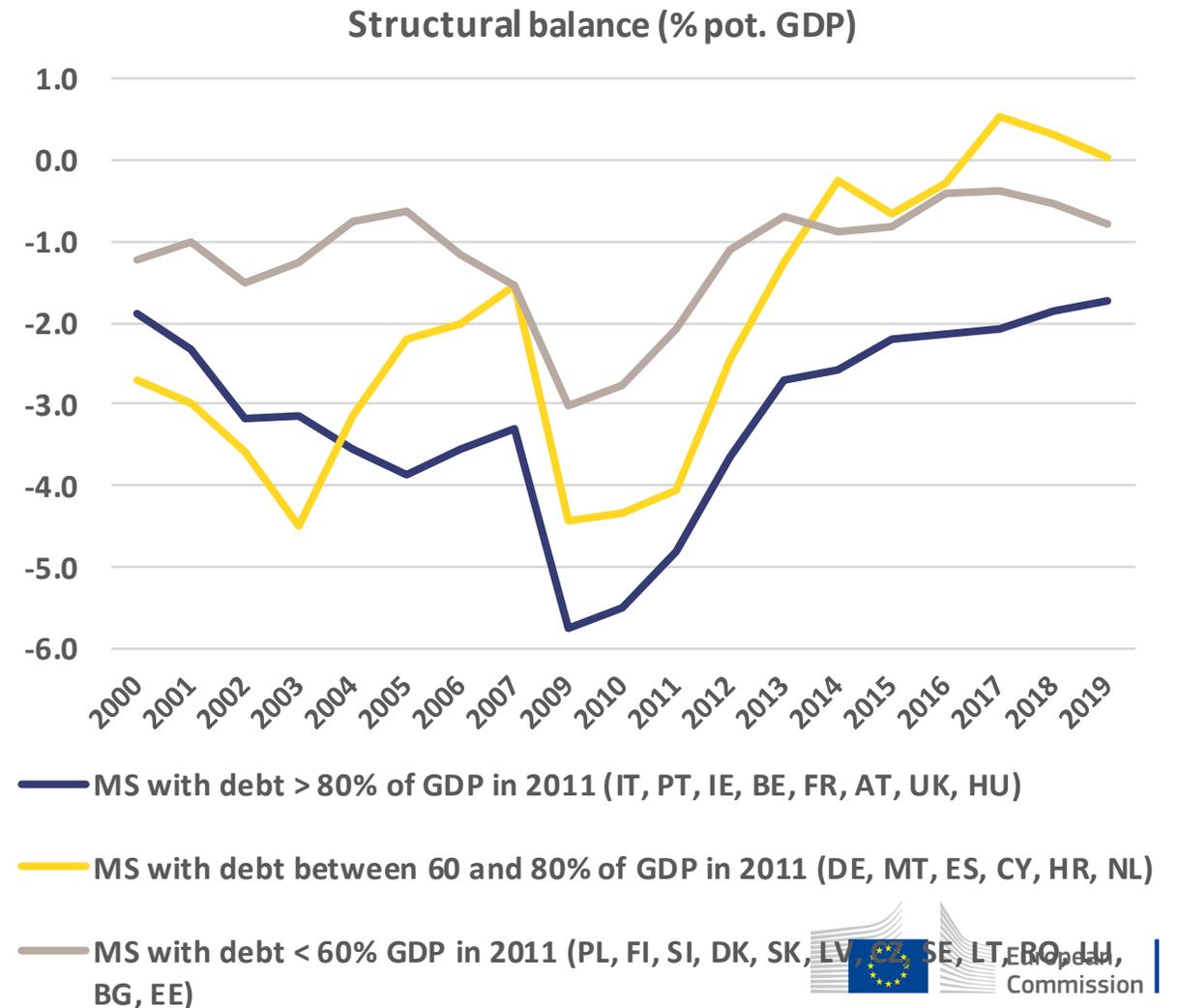
Sustainability: excessive deficit procedure effective in bringing deficits below 3%

- The corrective arm has been an effective tool for reducing and maintaining government deficits below the 3% threshold.
- Effectiveness of simple numerical rule: easy to grasp
- But: problem of nominal strategy under EDP.



Sustainability of public finances: lack of traction of preventive arm in some Member States

- Compliance with the preventive arm has clearly improved since SGP reform, incl. for high-debt MS
 - Partly thanks to interest and revenue windfalls.
- BUT:
- Despite improvement, still insufficient use of favourable conditions to build buffers in some high-debt Member States.
Insufficient traction of the preventive arm

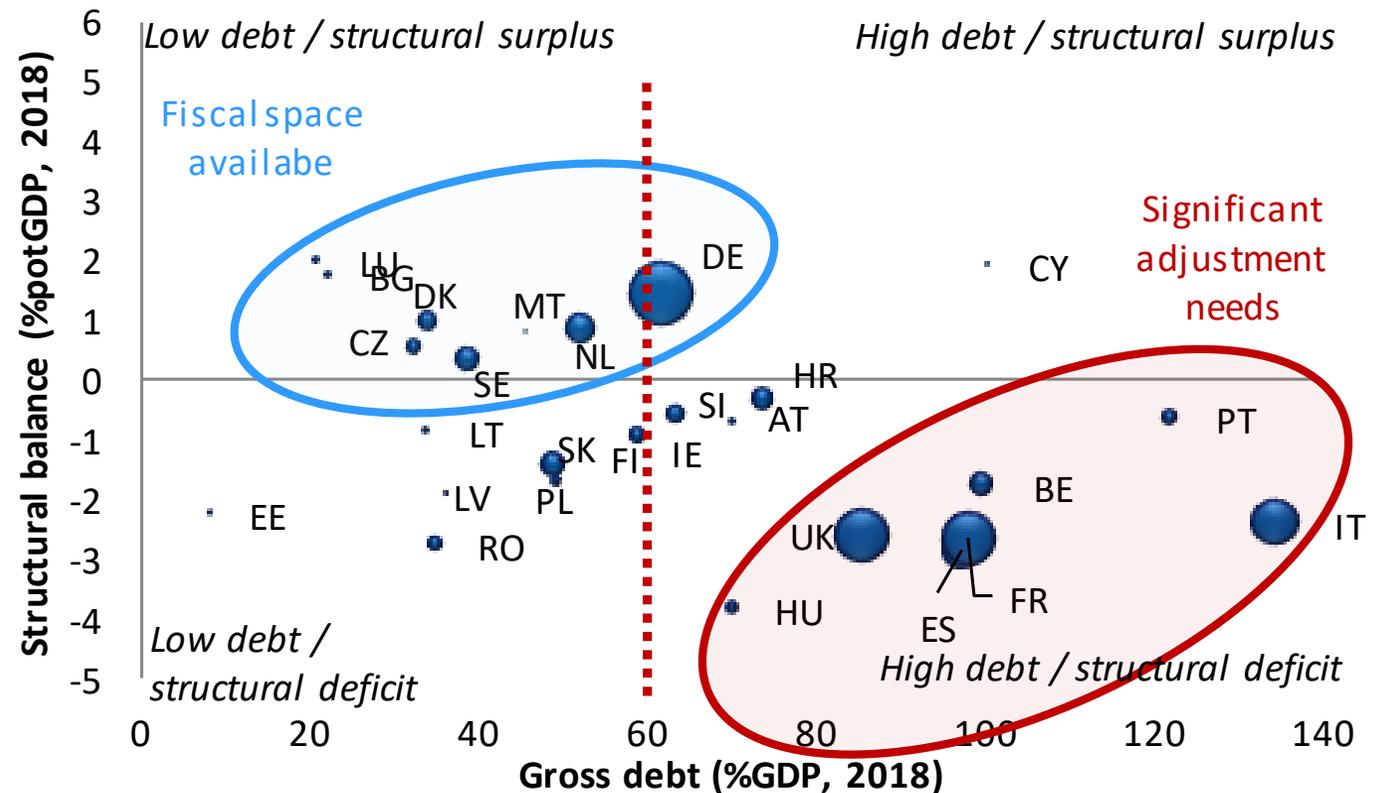


Sustainability: aggregate debt has fallen, but remains very high in some Member States

- Most high-debt Member States still far away from their MTO, despite interest windfalls.
- Insufficient traction of preventive arm in those Member States: Failure to use favourable conditions to reduce debt and build buffers.

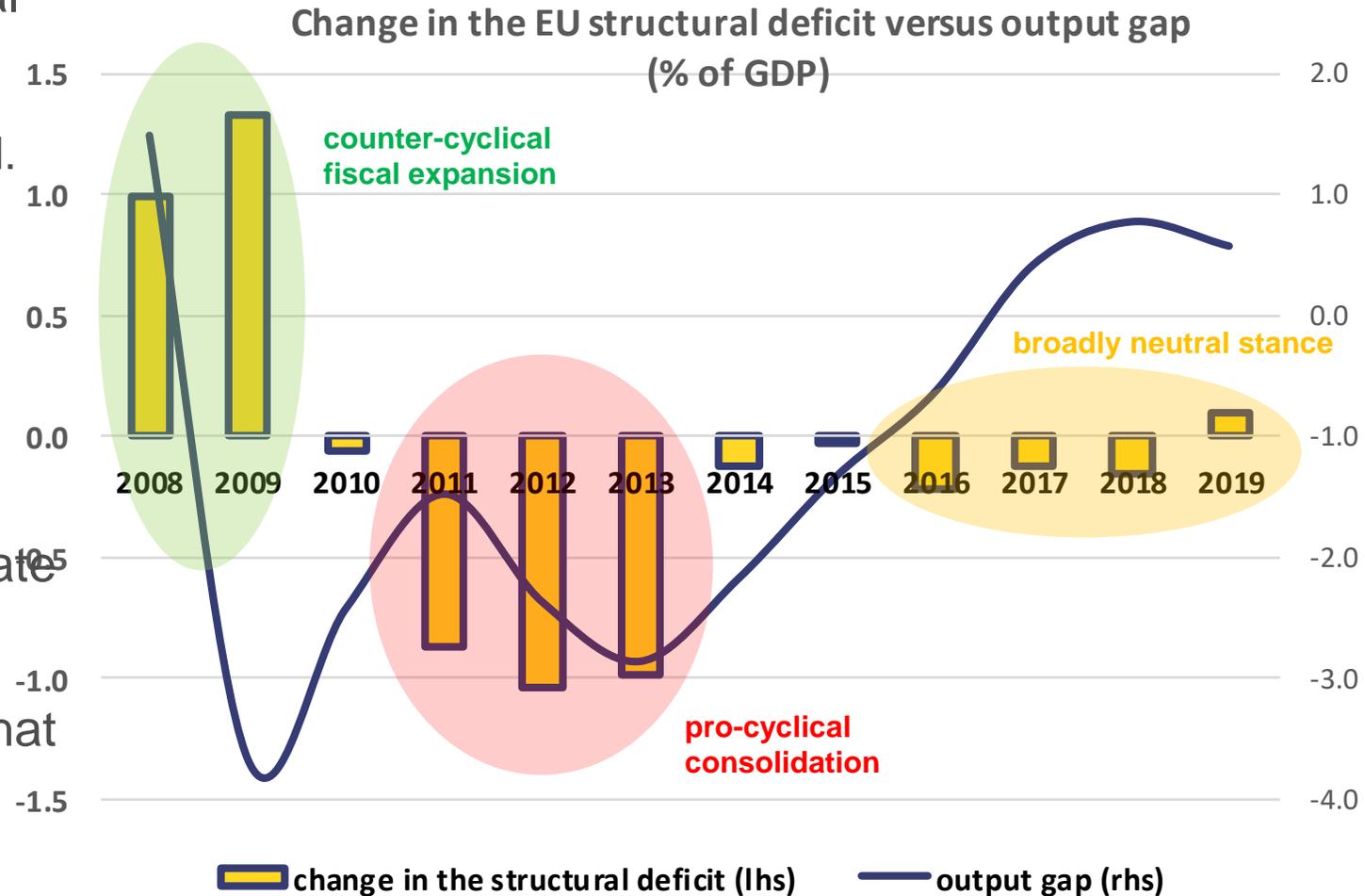
→ *Did 3% act as a target rather than a ceiling?*

- Too much focus on Member States with minor fiscal imbalances?

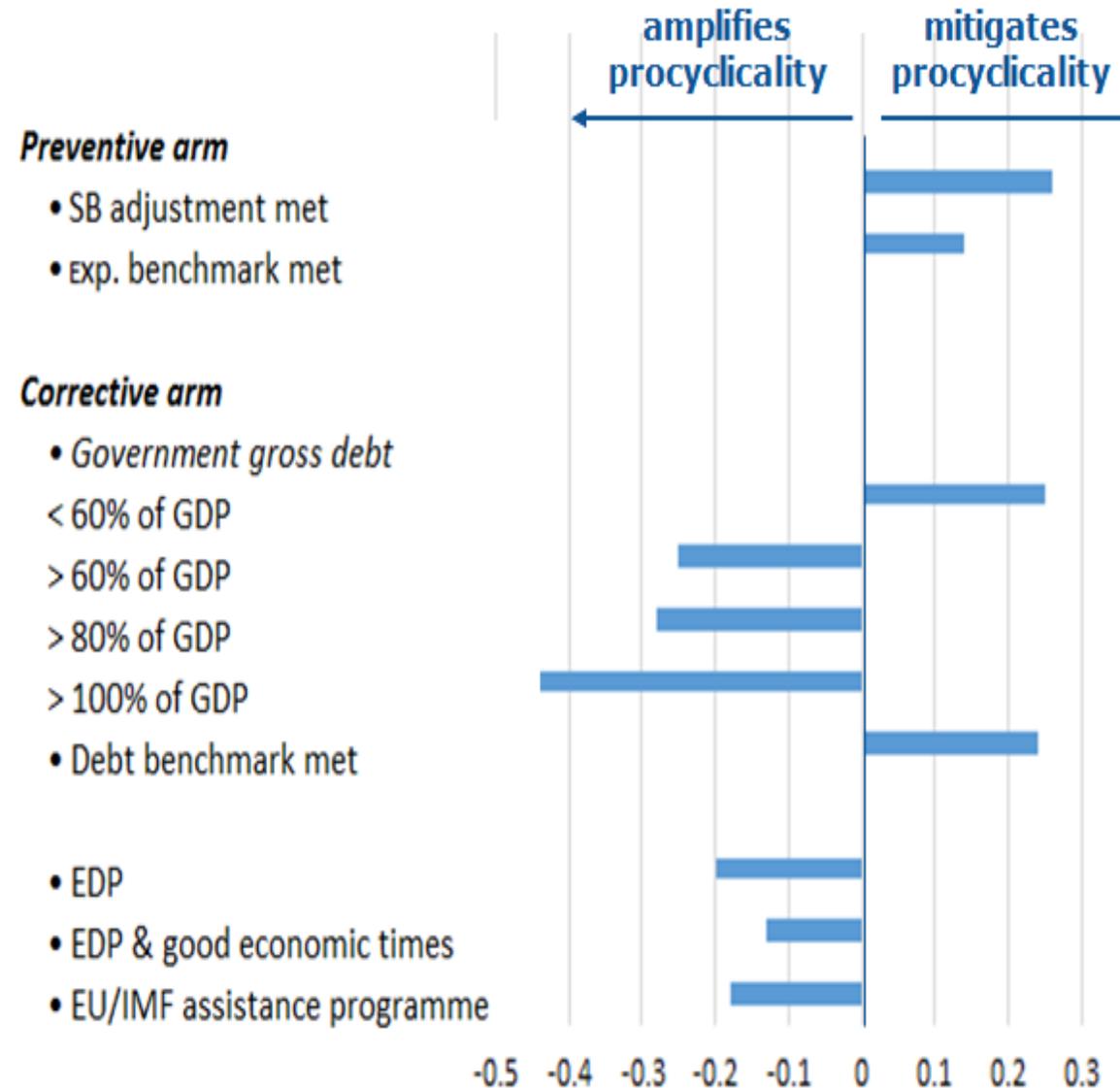


Fiscal stabilisation: Problem of pro-cyclicality

- Fiscal policies remained pro-cyclical in many Member States:
 - fiscal consolidation in 2011-13 (incl. market pressure)
 - lack of adjustment when economic conditions improved
 - better compliance with fiscal rules would reduce pro-cyclicality
- The EU cannot enforce the aggregate EA fiscal stance.
- Monetary policy at lower bound: What role for fiscal policy in policy mix?

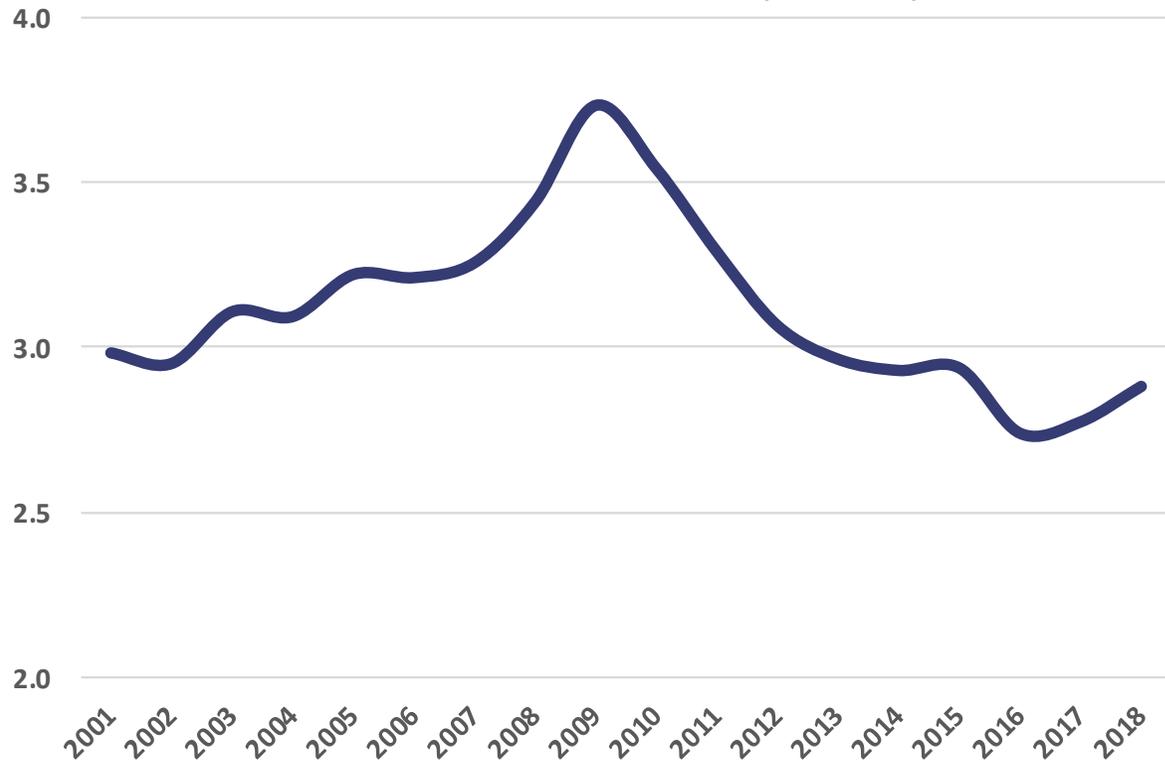


Fiscal stabilisation: compliance with fiscal rules reduces pro-cyclicality.

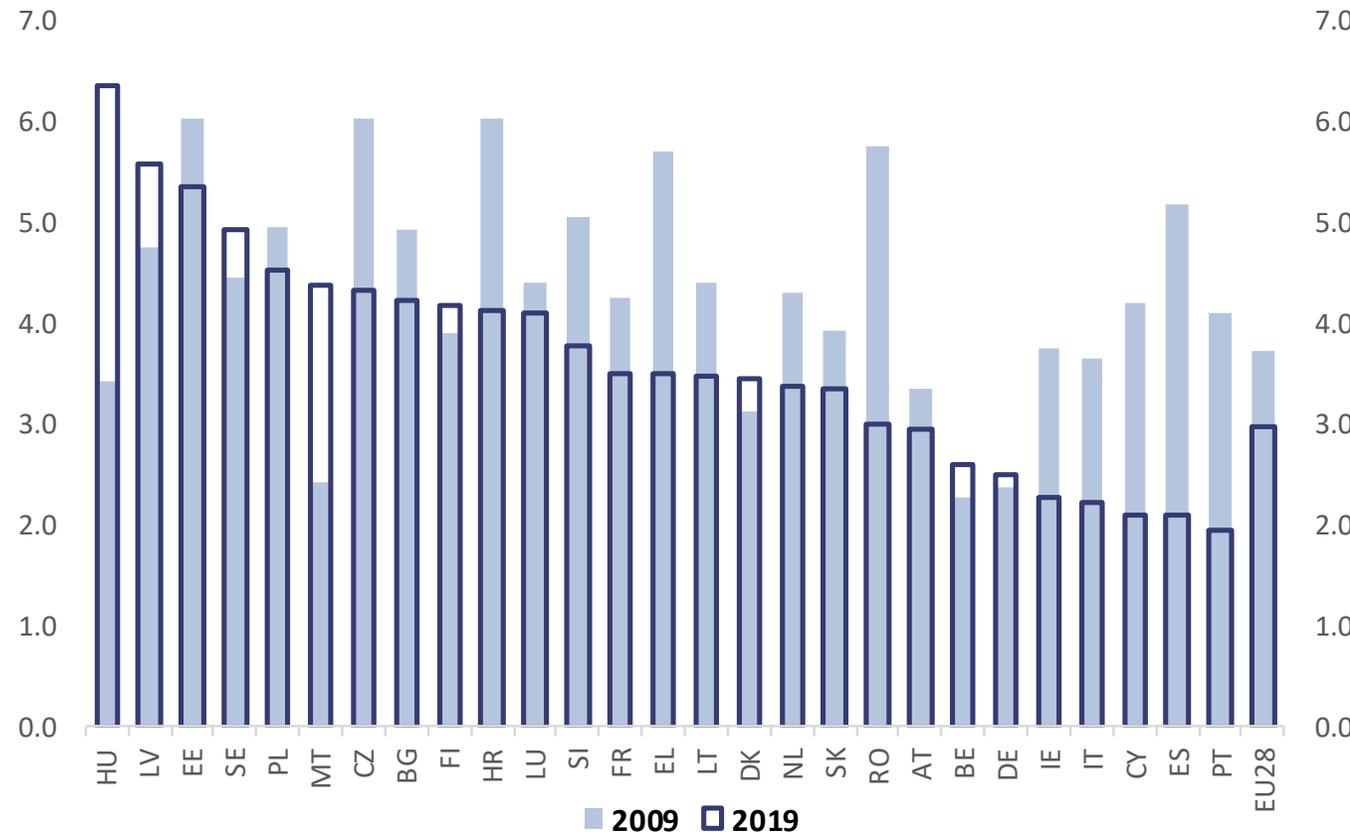


Growth-friendliness: public investment declined during consolidation

Public investment in the EU (% of GDP)



Public investment by Member State (% of GDP, 2019 vs 2009)



Quality of public finances: what is the role of the Pact?

- Pact in principle neutral regarding the composition of revenues and expenditures, but may affect public investment in specific cases: easier to cut public investment.
- On the other hand: debt sustainability and macroeconomic stability and debt sustainability necessary conditions for public and private investments.
- Pact recognises role of investment:
 - when assessing existence of excessive deficit;
 - flexibility for investment.
- However: 2015 flexibility had limited impact (restrictive eligibility conditions)
- Challenges ahead: green transition, digitalization, demographic ageing

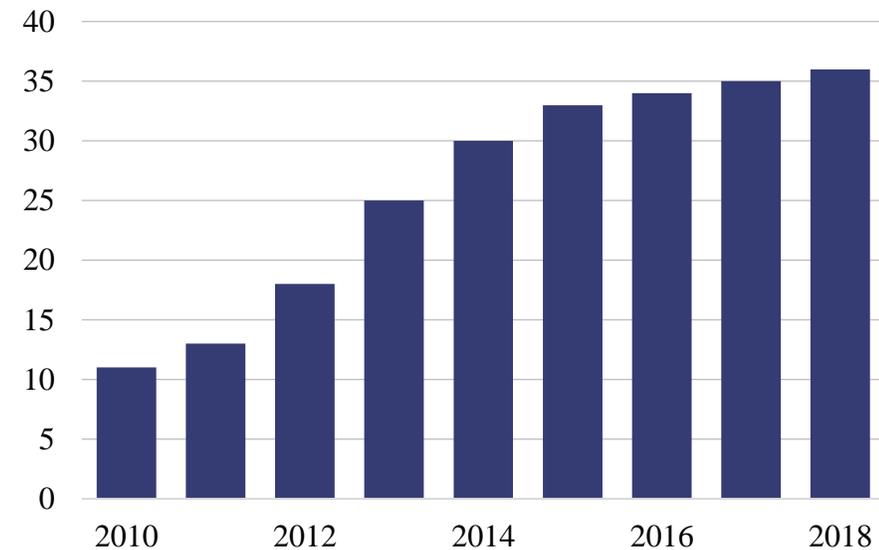
National fiscal frameworks

- Institutional strengthening
 - National rules
 - Independent fiscal institutions
 - Medium-term planning
 - Independent forecasting
- Supports compliance with EU fiscal rules + increases ownership

But:

- Differences in design and implementation practices
- Sometimes not fully aligned with EU rules (Fiscal Compact)

Number of independent fiscal institutions in the EU



Ownership and governance of EU fiscal rules (1)

- Complexity and lack of predictability
 - Accumulation of multiple rules
 - Different indicators of compliance
 - Reliance on unobservable and frequently revised variables
 - Various clauses allowing for deviations
 - Discrepancies between EU and national fiscal rules (based on Fiscal Compact)
- Lack of ownership (but also lack of trust which drives complexity !)
- Draft Budgetary Plans process: useful for ex ante coordination
 - EU rules better taken into account in budget process;
 - but difficulty of influencing national fiscal policy in practice.

Ownership and governance of EU fiscal rules (2)

- Reluctance to launch enforcement procedures and to impose financial sanctions.
 - SDP only in very clear-cut cases (and only non-EA MS)
 - No debt-based EDPs (despite breaches of debt reduction benchmark)
 - No financial sanctions applied under EDP
- Which alternatives for enforcement?
 - Lack of peer pressure (six- and two-pack shifted responsibility on COM)
 - Under-developed political incentives
 - Lack of financial market discipline
- Too detailed focus on compliance with annual requirements?
 - The medium-term orientation of fiscal policy is insufficiently taken into account.
 - Therefore insufficient differentiation between Member States that have markedly different positions and risks.

Fiscal surveillance: Key findings

- All **excessive deficits** have been **corrected** and **half of the Member States reached their medium-term budgetary objective**.
- Aggregate **public debt declined but remains high in some Member States** that did not build buffers during favorable economic times.
- Rules **did not prevent pro-cyclical policies** in some Member States, and the ability to coordinate the aggregate fiscal stance for the euro area remains constrained.
- The framework **did not prevent a decline in public investment** during fiscal consolidation; flexibility (2015) had limited impact.
- Rules have become **increasingly complex** and not always transparent, hampering communication and ownership in the rules.
- **National frameworks have been strengthened**, but the interplay with EU rules is not always optimal.

Overall assessment of the fiscal framework

- Number of shortcomings related to design, implementation and enforcement.
- Need to simplify the rules in order to increase ownership, improve communication, and reduce the political costs for enforcement and compliance.
- An effective framework needs to ensure sustainability where it is most necessary, while allowing for macro-economic stabilisation in both good and bad times. What role for fiscal policy in policy mix in a changed economic context?
- What should be the role of the EU surveillance framework in helping to protect investment, promoting a growth-friendly composition of public finances and sustaining adequate levels of investment, in particular in the context of the European Green Deal?

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Building a renewed consensus

- **When the recovery takes hold, the Commission will relaunch the review of the economic governance framework**
- Consultation / Dialogue phase
 - **Inclusive public discussion with all stakeholders:** European Parliament, Council, ECB, the European Economic and Social Committee, the Committee of the Regions, national governments and parliaments, national central banks, independent fiscal institutions, national productivity boards, social partners, civil society organizations as well as academic institutions.
 - **Events:** Council and Committee discussions, dedicated (bilateral) meetings, workshops, stakeholder seminars, and an online consultation platform
 - **Opportunity for stakeholders to provide their views** on functioning of surveillance and possible ways to enhance effectiveness
- Commission to finalize stance on possible future steps

Questions for public discussion

Rebuilding trust and consensus on **the policy goals**:

- How to better ensure sustainable public finances and tackle macroeconomic imbalances?
- How to avoid pro-cyclicality?
- How to support growth-friendly public finances and incentivise reforms and investment to tackle **economic**, **social** and **environmental** challenges?
- How to take into account euro area dimension and EMU deepening?

Questions for public discussion

How to achieve the policy goals:

- How to make the framework simpler and more transparent?
- How to make the framework more focused on “gross errors”?
- How to ensure effective enforcement?
- What role for national frameworks and how to improve interaction with EU rules?
- How can the SGP and MIP work better together?

Thank you

https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/economic-governance-review_en