

Should EMU's fiscal framework be reformed and if so, how?

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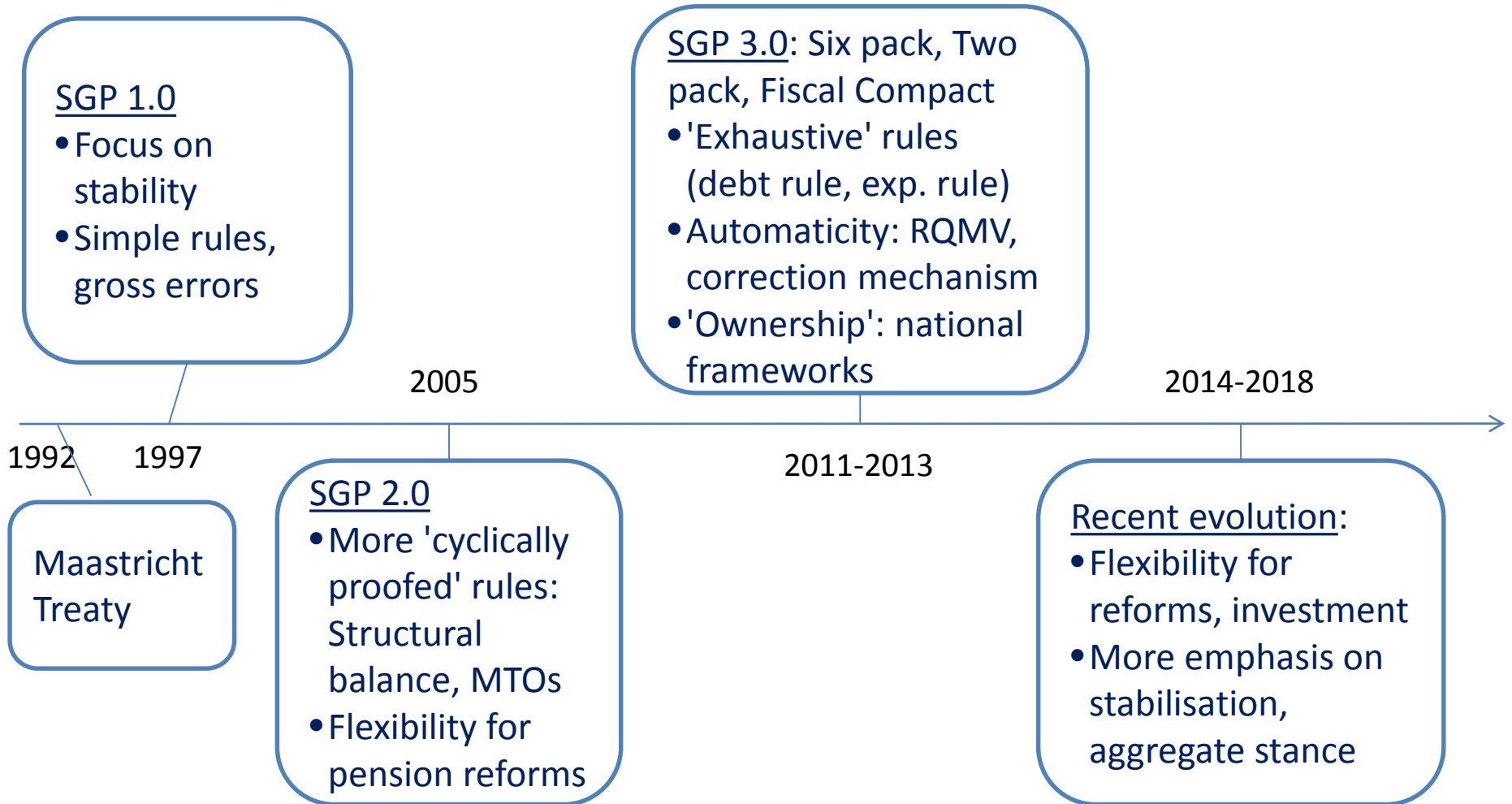
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The Maastricht fiscal framework

- EU fiscal rules: de facto “constrained discretion”
- Focus on sustainability/stability:
 - Avoidance of excessive deficits, focus on gross errors
 - No initial concern for cyclicity
 - Sanctions, but political process
≠ classical infringement procedures
- No bail out rule: hope in market discipline and TINA

The SGP history: searching for the right mix



SGP reforms reflecting an evolving view of fiscal policy in EMU

Conventional view
on fiscal policies in
EMU – pre crisis



**"Put own house
in order..."**

- Rules to tame deficit bias in absence of national exchange rate policy
- Automatic stabilisers: let them play
- Risk of debt monetisation dominates monetary-fiscal relations
- Low spillovers because of offsetting monetary policy reaction
- Threat of financial sanctions helps discipline governments
- Negative coordination suffices

Revising the role of
fiscal policy in EMU
– post crisis



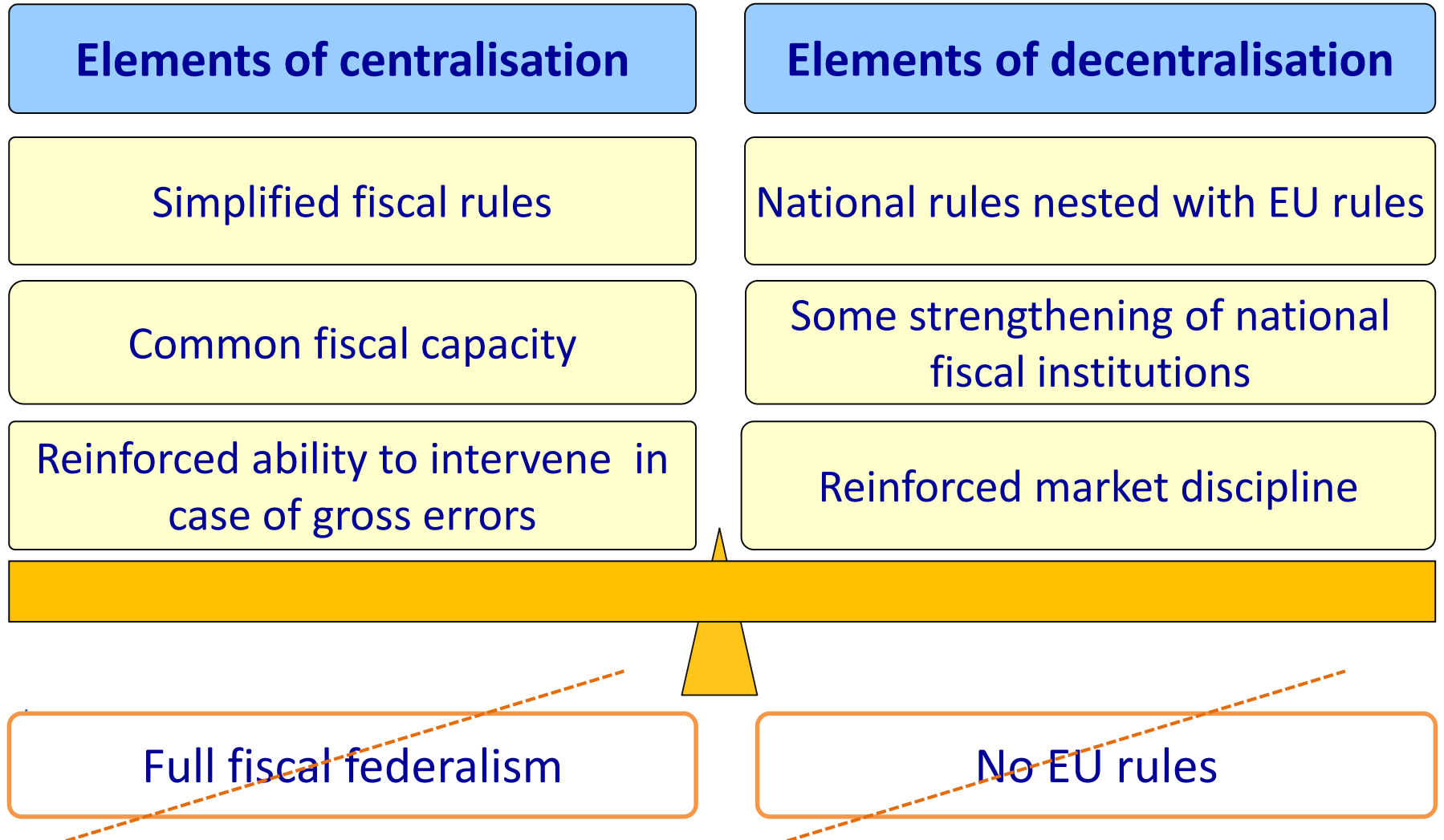
**"...and strengthen
the joint
foundation"**

- Discretionary fiscal policy needed in case of large shocks
- High multipliers and spillovers when monetary policy is constrained
- Aggregate fiscal stance and differentiated fiscal space matter
- Sovereign-banks nexus
- Institutions / rules / markets
- Links fiscal policies/ structural reforms
- Difficult to sanction sovereign states

Overall assessment of the SGP experience

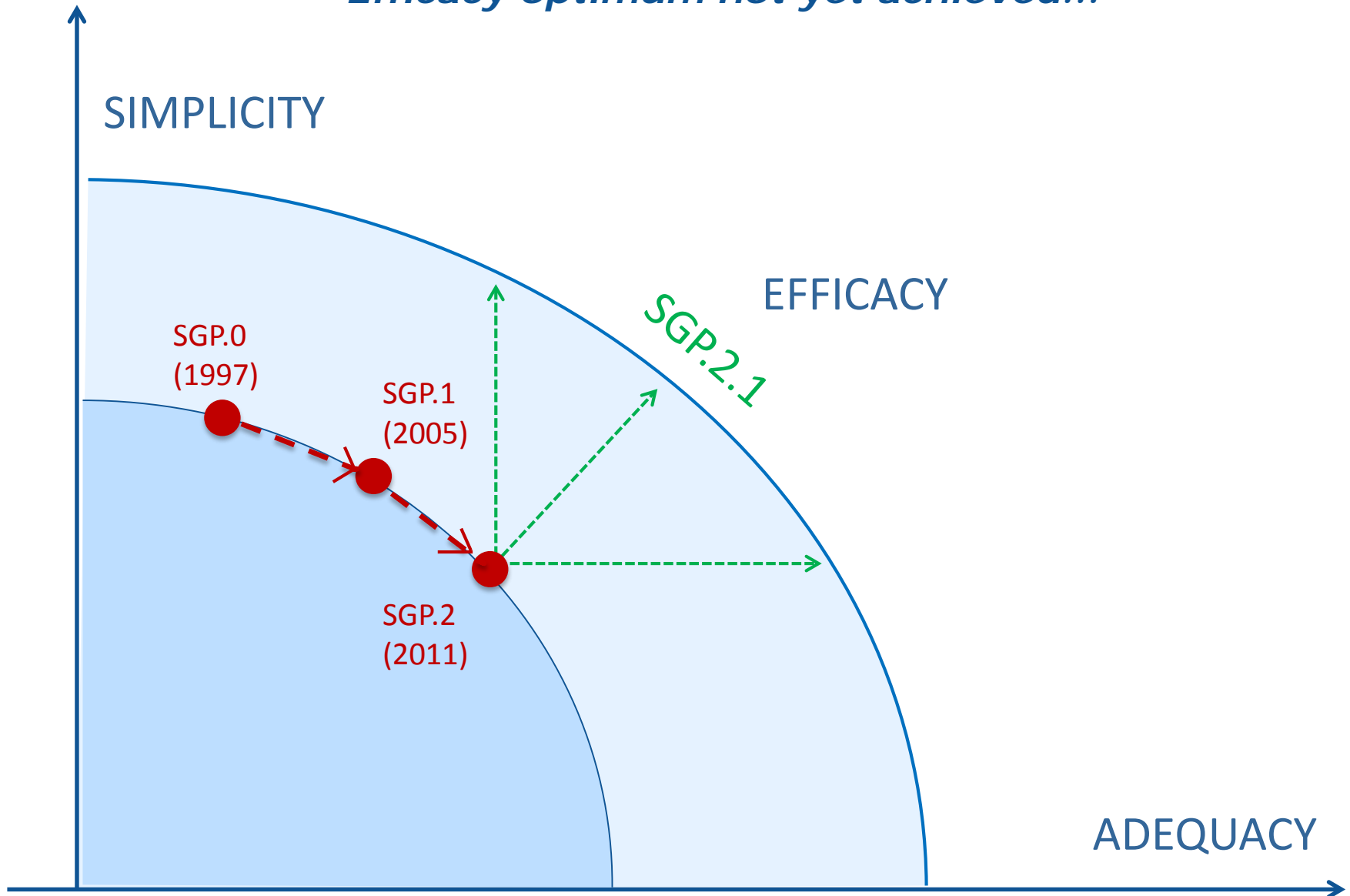
- **A glass half-filled?**
 - SGP partially disciplined policies
 - EA position sound overall but fragilities in some MS
 - Some pro-cyclical tendencies
 - From multilateral to bilateral surveillance mode
- **Unsolved issues**
 - Limited enforcement mechanisms
 - No tool for influencing aggregate stance
 - QPF underrated
- **Political economy not evolving favourably**
 - Erosion of consensus, polarisation of views

Components of a minimum fiscal union balanced with elements of decentralisation



The SGP trilemma

Efficacy optimum not yet achieved...



Some conclusions

- The latest incarnation of fiscal framework has given considerably more weight to growth concerns
- For the medium-term, there are three conceivable avenues:
 - (1) Make the best use of the present framework
 - (2) Improve the fiscal rules
 - (3) Take steps towards fiscal union
- The steps are non-exclusive, even complementary:
 - In the short term a credible implementation of current framework is critical to rebuild trust
 - Combining simplified rules with common stabilisation capacity would be a promising arrangement

Thank you