European Stability Mechanism

FISCAL ADJUSTMENTS DURING CRISES

The experience of the sovereign debt crisis and beyond

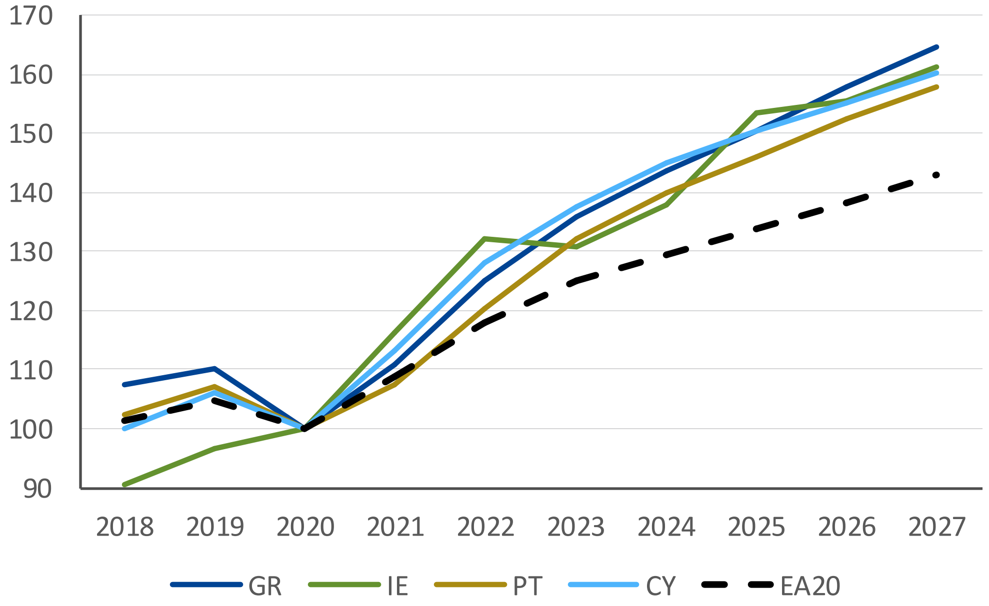
Rolf Strauch, ESM Chief Economist and Management Board Member

Finnish Parliamentary Working Group on Fiscal Policy, 3 December 2025

FROM CRISIS TO RESILIENCE: BENEFICIARY MEMBER STATES TODAY

Real economic output per capita

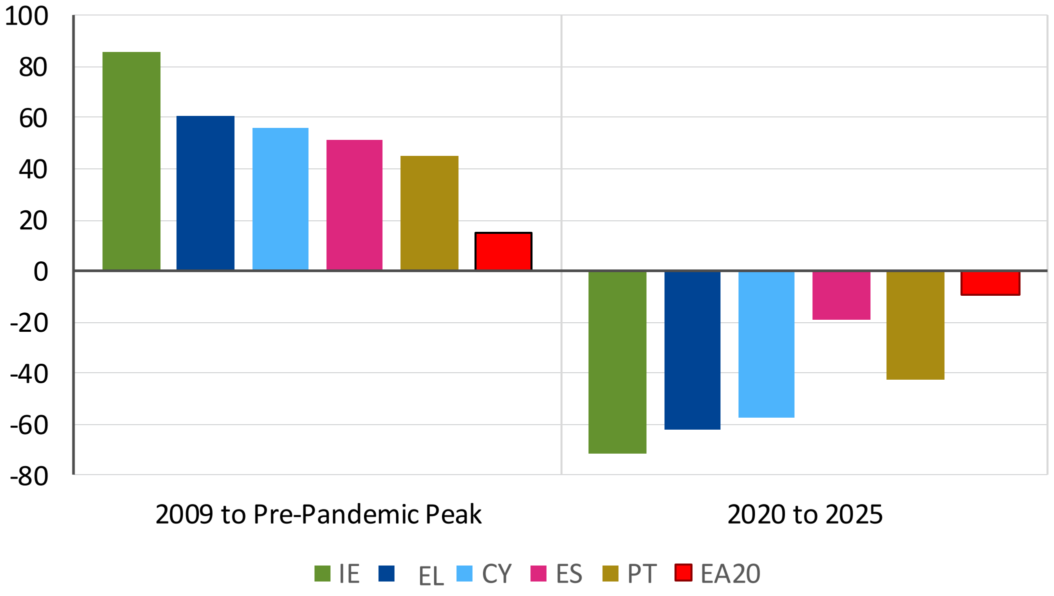
(2020=100)



Sources: AMECO, Central Statistics Office of Ireland, Debt Sustainability Monitor 2024

Change in Debt-to-GDP: beneficiary member states (BMSs)

Percent of GDP



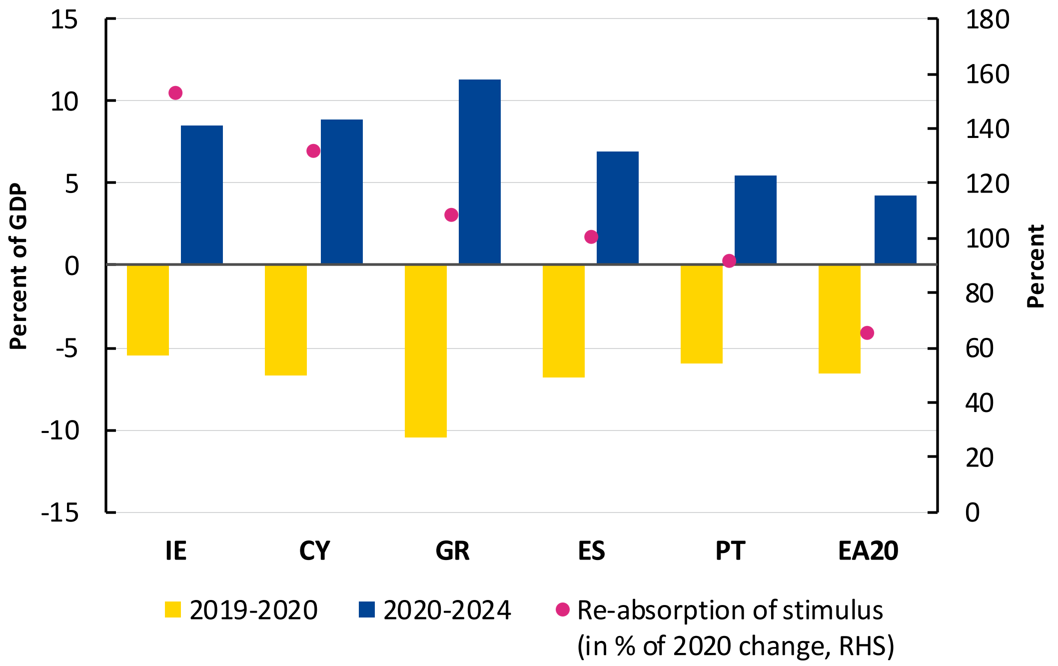
Sources: AMECO; Central Statistics Office of Ireland

Notes: The pre-pandemic peak of Debt-to-GDP was in 2014 for Spain, Portugal, Cyprus and the Euro area; in 2019 for Greece; and in 2012 for Ireland. AMECO data is used to calculate the Debt-to-GDP. In the case of Ireland, Debt-to-Modified GNI is used, which is available till 2024

FISCAL POLICY IN THE 2020S: MORE TEMPORARY AND TARGETED

Primary balance 2020-2024

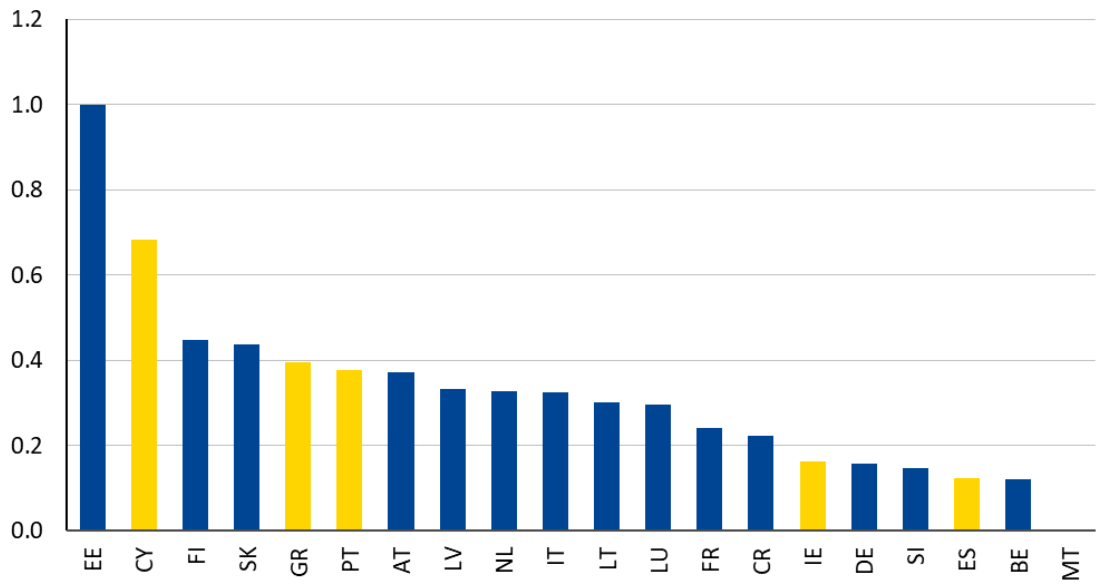
(percent of GDP)



Source: Eurostat and ESM staff calculations

Household support measures 2022-2023

(share of targeted measures over total)



Source: IMF (2022), "Targeted, Implementable, and Practical Energy Relief Measures for Households in Europe", WP/22/262 and ESM staff calculations

FOCUS ON HOW TO ADJUST, NOT JUST HOW MUCH

Awareness → Efficiency → Agility → Prioritisation → Tax-base

1. **Recognise new environment**
2. **Raise efficiency with Public Financial Management (PFM) and digitalisation**
3. **Make budgets more agile**
4. **Prioritise growth-enhancing spending**
5. **Broaden tax bases, reduce distortions**

FOCUS ON HOW TO ADJUST, NOT JUST HOW MUCH

Awareness | Efficiency | Agility | Prioritisation | Tax-base

Broad awareness of a new economic environment

BMSs:

- Recognition that the post-global financial crisis world required a different fiscal and tax framework
- Early re-assessment of fiscal risks and spending rigidities

Parallel today:

- Europe must adapt to a new security, trade, and industrial landscape (Ukraine, US policy shifts)

FOCUS ON HOW TO ADJUST, NOT JUST HOW MUCH

Awareness → **Efficiency** → Agility → Prioritisation → Tax-base

Broad awareness of a new economic environment

Public-service reforms and better PFM systems *(Portugal, Greece)*

Spending reviews and digitalisation of procedures *(Ireland, Cyprus)*

Reduced administrative and compliance costs → stronger growth with limited fiscal drag

FOCUS ON HOW TO ADJUST, NOT JUST HOW MUCH

Awareness | Efficiency | **Agility** | Prioritisation | Tax-base

More agile budgets through reduced rigidities

Rebalancing towards flexible spending, limiting entitlement-driven or automatic items

Strengthening medium-term frameworks and fiscal councils to create space for reprioritisation

Spending composition and agility enhance resilience to shocks *(European Stability Mechanism 2024)*

FOCUS ON HOW TO ADJUST, NOT JUST HOW MUCH

Awareness | Efficiency | Agility | **Prioritisation** | Tax-base

Effective spending prioritisation

Protect high-return investment (education, R&D, digital, infrastructure)

Target low-efficiency subsidies and recurrent spending instead of blanket cuts

Better procurement and debt-management reforms to free fiscal space

Result: debt falls **without** undermining long-run growth

EFFICIENCY AND AGILITY: PENSION SPENDING

Portugal – raising retirement age and automatic life-expectancy link

Programme: EU/IMF Economic Adjustment Programme (2011–14)

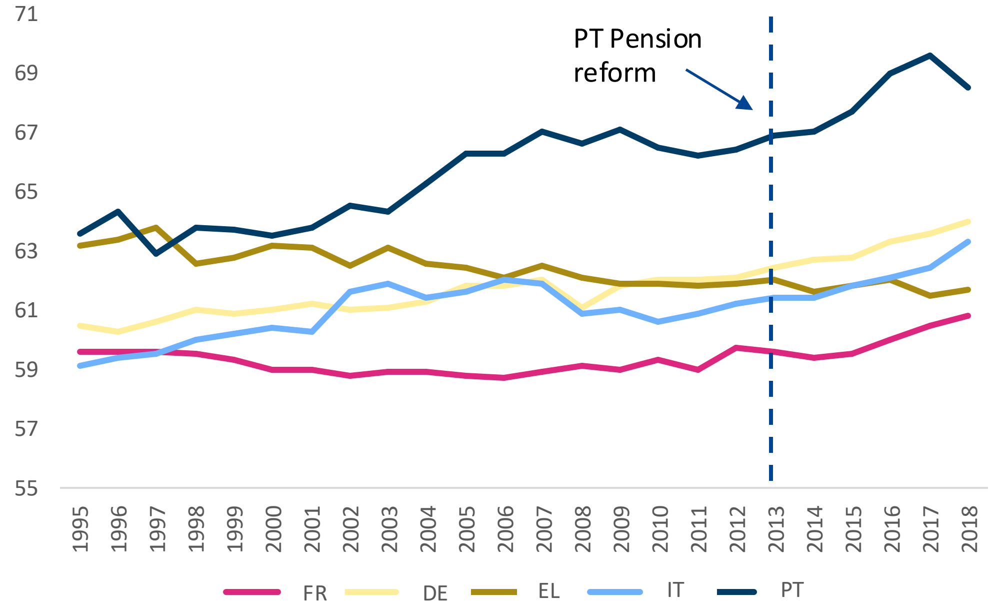
Key measures:

- **Increase statutory retirement age to 66**
- **Introduce an automatic link to life expectancy** for the statutory retirement age
- Tighten access to early retirement and adjust benefit formulas to improve sustainability

Classic example of parametric pension reform with very large long-term savings and limited immediate hit to demand.

The Memorandum of Understanding (MoU) explicitly frames this as a measure to ensure long-term sustainability of the pension system.

Average effective retirement age
(in years, men)



Source: OECD (2018) - Database on Average Effective Retirement Age

EFFICIENCY AND AGILITY: PENSION SPENDING

Greece – comprehensive parametric pension reforms

Programme: First and Second EU/IMF Economic Adjustment Programmes, later ESM programme

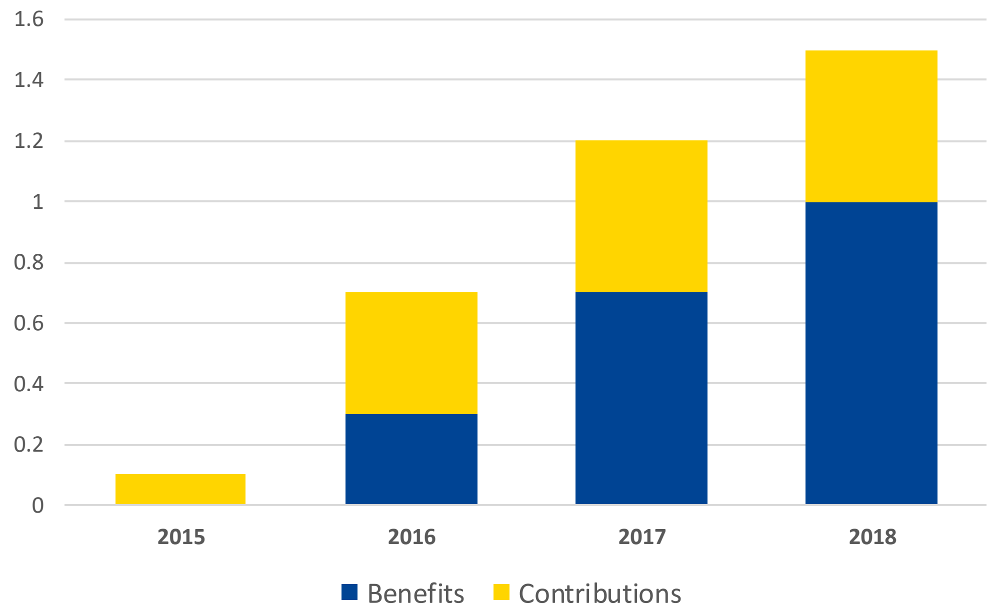
Key measures:

- **Raise normal retirement age to 65, later to 67,** with
  - equalisation of men's and women's retirement ages
  - indexation of the retirement age to life expectancy
- **Merge fragmented pension funds** into a smaller number of funds and shift to a **notional defined-contribution logic with a sustainability factor adjusting benefits to contributions**
- **Tighten early-retirement pathways** and increase required contributory years for a full pension

Greece illustrates how a very fragmented, generous system can be put on a rule-based, life-expectancy-linked path
Low-growth-cost measure needed where ageing pressures are high.

Benefits from the 2015-2017 pension reforms

(in percent of GDP)



Source: Kangur, Kalavrezou and Kim (2021), "*Reforming the Greek Pension System*", WP/21/188
Note: *Benefits* include tightening early retirement rules; harmonizing the main pension benefit rules, phasing out the solidarity grant, and consolidating the main pension funds. *Contributions* include putting auxiliary, dividend, and lump-sum funds on more sustainable footing and harmonising contribution rules.

AWARENESS AND EFFICIENCY: INDEPENDENT FISCAL COUNCIL

Portugal and Greece – establishment of an independent fiscal council as a programme condition

Programme: EU/IMF and ESM Economic Adjustment programmes

Key measures:

- **Fiscal surveillance** and **monitoring**
- **Macroeconomic** and **budgetary forecasting**
- Monitoring **compliance with national fiscal rules**
- MoU requirements on **transparency** and **communication**

Strong and encompassing fiscal council brings awareness and underpin credibility, without needing large immediate cuts. *However*, political traction builds over time.

EGR gives space for a broader scope of fiscal councils (comply-or-explain),
Independent Fiscal Institutions in the Revised Legal Framework State of Play, European Commission, 2025

International Financial Institutions – Changes of roles after the Economic Governance Review (EGR)

Area	Pre-Reform Role	Post-Reform (EGR 2024) Novelties
Macro forecast endorsement	Widespread but inconsistent	Reinforced; tied to MTFSP credibility
Monitoring fiscal rules	Mainly national rules	Explicit monitoring of EU net expenditure path
Assessing plans	Annual budgets	Central role in multi-year fiscal-structural plans
Escape clauses	Optional or limited	Expected to assess NEC justification and implications
Independence standards	Variable	Minimum EU-wide safeguards
Role in EU cycle	Informal	Systematically integrated into Commission assessments

PRIORITISATION: MEDIUM-TERM EXPENDITURE FRAMEWORK

Ireland – Medium-Term Expenditure Framework (MTEF) with binding ceilings

Programme: EU/IMF Economic Adjustment programme (2010–13)

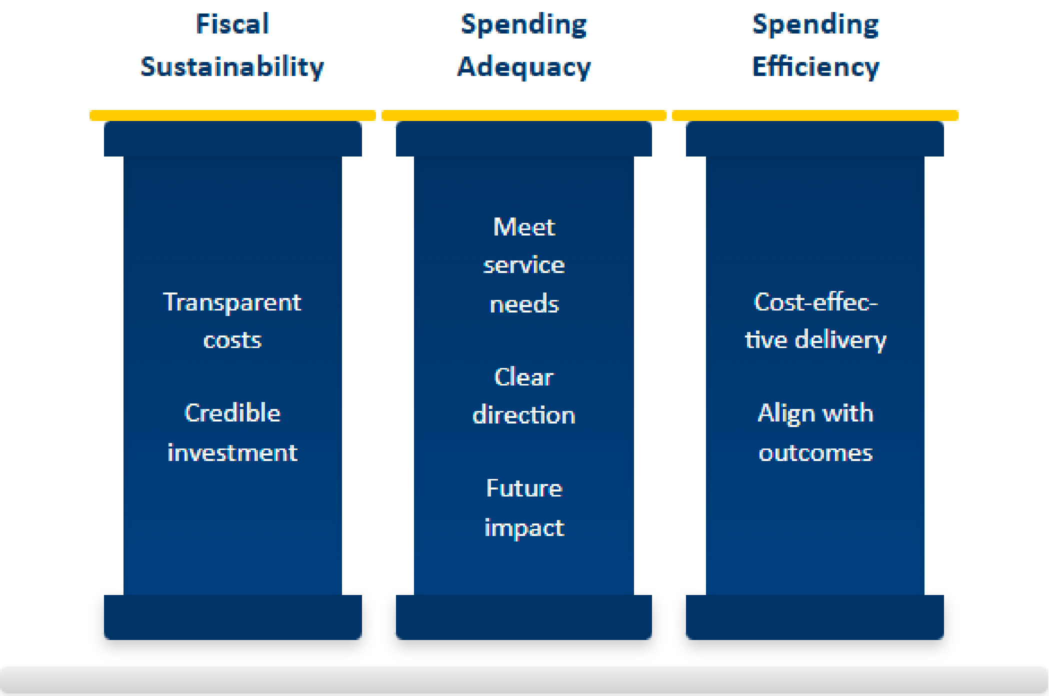
Key measures:

- **Introduce a MTEF with binding multi-annual expenditure ceilings** consistent with fiscal targets – a specific structural benchmark under the programme
- Move budgetary procedures towards **performance budgeting**, focusing on outputs/outcomes.

During the programme fiscal adjustment was mainly expenditure-based, through public-service efficiency reforms & better targeting of welfare spending.

Today, that revenues are strong, the MTEF creates a transparent anchor for the fiscal council and other institutions to assess policies and hold the government to its commitments.

The Irish Framework: three core pillars



Source: ESM, based on Department of Finance, ‘Medium-term Expenditure Framework’, Sept. 2025

BROADENING THE TAX BASE – PROPERTY TAX

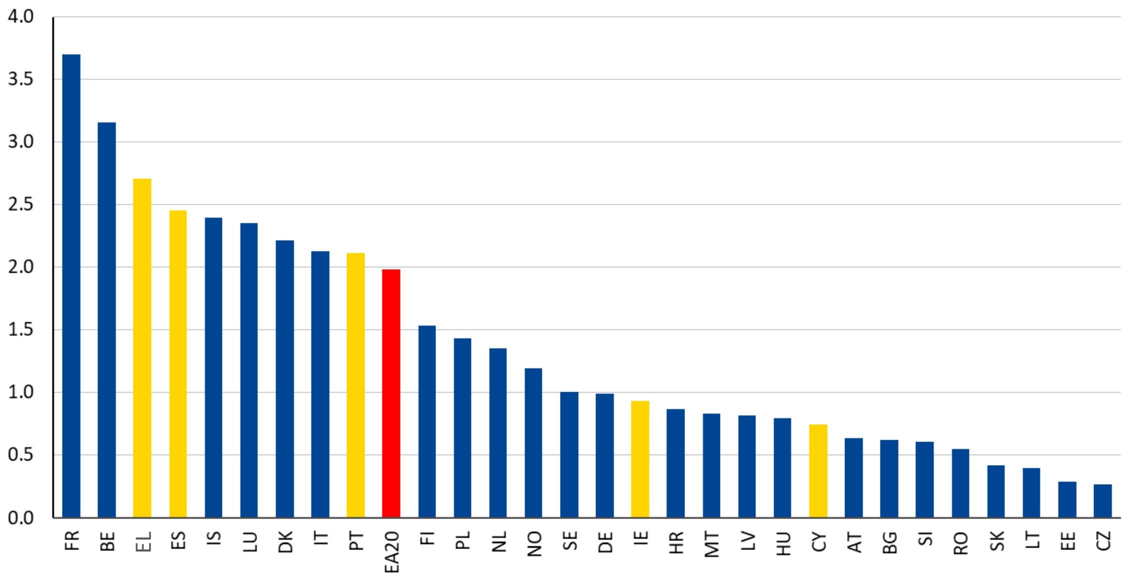
All countries, different fiscal outcomes

Key measures:

- **Greece –** creation of a unified, broad-based property tax (ENFIA) covering almost the entire property stock; high-yield and stable.
- **Portugal –** broadening of municipal property tax (IMI) via valuation updates and elimination of exemptions**.**
- **Spain –** wider VAT and property-tax bases via reduced exemptions and updated cadastral values**.**
- **Ireland –** Local Property Tax (LPT); self-assessed and used to finance local authorities. *But with relative low rates and narrow definition (residential only) revenues remain constrained.*
- **Cyprus –** modernised Immovable Property Tax and broader coverage**.** *But without regular revaluation revenues remain weak*

Property taxes, 2023

(percent of GDP)



Source: European Commission, DG Taxation and Customs Union, based on Eurostat data – Extracted in February 2025

Rebalancing and broadening (e.g. property/environmental bases, rationalising tax expenditures) is growth-friendly.

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