



*European Fiscal Rules*  
*Comment by*

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## Reason for Rules

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- **Agree:** Avoid national/euro area externalities
- Maintain room for stabilisation
- **Plus:** maintain quality of public finances
- Prevent repeat of bailouts and their financial and political costs



## Problems with fiscal rules in EU

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- Reliance on output gap, structural balance and change in structural balance **all problematic** (unobservable, unstable)
- Ex-ante and ex-post problems due to measurement, shocks and policy errors hard to separate, **who bears risk?**
- Measurable targets (-3, 60) and process not time consistent
- Growing complexity, exception seeking, policy opportunism, precedents, and intransparency stoke rule erosion

**YES**



## EU Rules blamed for the right and wrong things

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- Pro-cyclical tightening and loosening due to non-compliance in boom, in bust only in crisis countries: **YES**, but **NOT** rules
  - Have not succeeded in ensuring sustainability and quality everywhere
- Lack of enforcement mechanism/time consistency due to governance

**YES**



## Nominal expenditure rules

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**Pro:** expenditure measurable

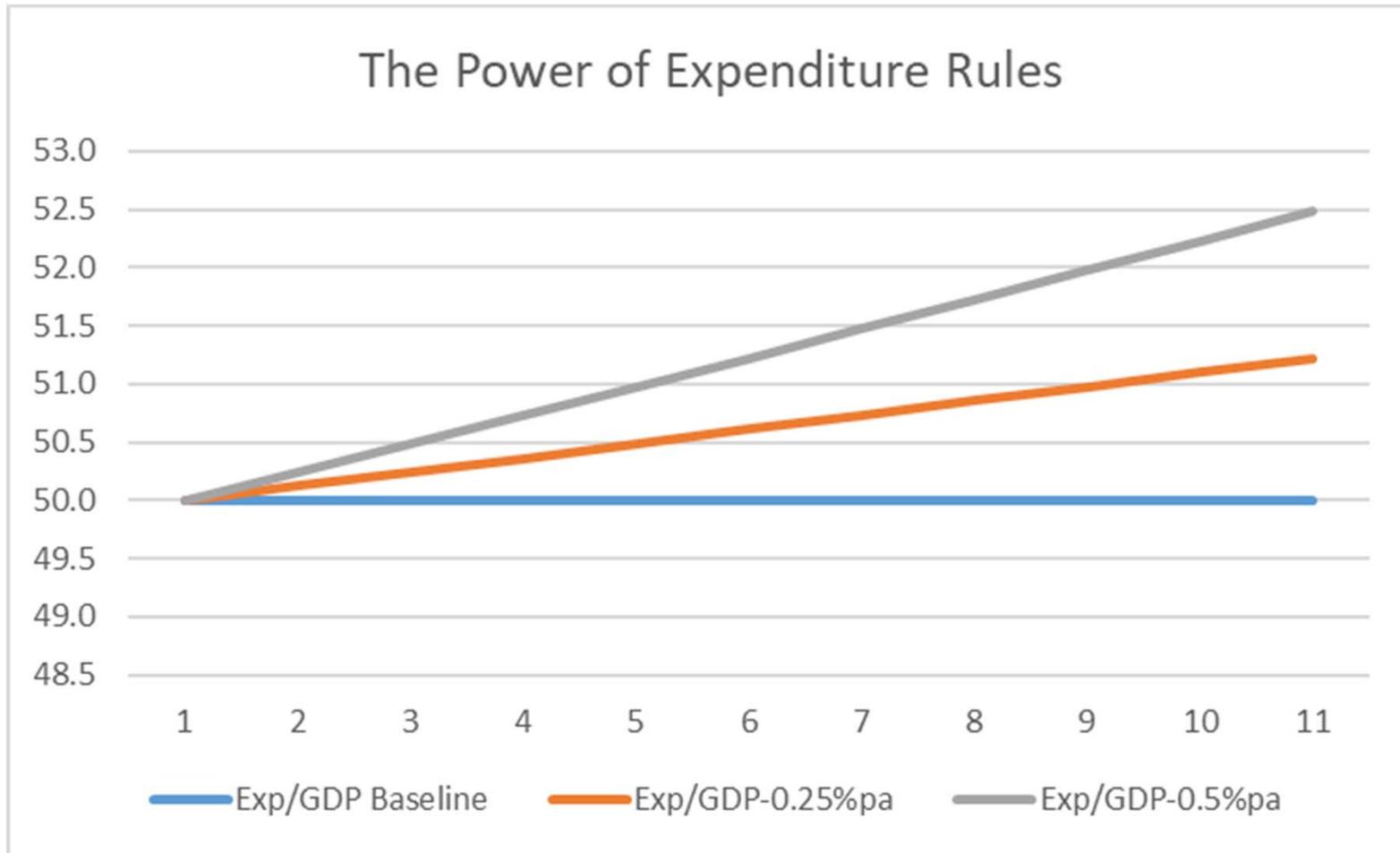
- Debt as sustainability anchor

**Con:** relies on trend/potential output estimates which are not measurable, plus uncertain inflation outlook

- Proposed mechanism includes same complications (exclusions, exceptions)
- Risk of circumvention via revenue side and off budget expenditure
- Possibly conflict with national budget anchors (deficit/credit)?
- Needs agreement by 27



# The power of expenditure rules





## Governance: Paper has great ideas

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- Strengthen national fiscal responsibility/reduce Brussels bashing
- Strengthen role of national fiscal councils
- Analysis and monitoring, opinions (change mandate)
- Comply and explain procedures
- ALL **YES**—**But** how to strengthen national implementation of fiscal compacts? Why failed?



## Governance and enforcement at European level

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- Current enforcement with potential fines and reliance on peer-judgements not effective: **YES**
- **Multi-pronged** approach needed (EU rules, markets, national): **YES**
- EU budget payments conditional on SGP compliance: **YES**  
**but** did not work in past?
- Compliance as pre-condition for stabilisation facility and ESM: **YES**, **but** what if always compliance (Italy!)?
- Collective action clauses on all government bonds (ESM Treaty): **YES** **but** what about sub-national? Bank credit lines/loans?
- Issuance of junior bonds for spending excess: **YES** **but** why the caveat of not destabilising, that is the threat!





## Strengthen governance of SGP

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- Change Regulations and Fiscal Compact to introduce expenditure rule: **NOT SURE**, high costs of reaching agreement, might lead to further loosening
- Simplification: **YES but** what (?), regulations DIFFICULT
- Other: Change Commission internal working procedures/make ECFIN independent?





# Conclusion

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- **Expenditure rule has strong logic**
  - But proposed framework not easy, not simplification
  - Excellent proposals for non-SGP based enforcement
- **Governance**
  - Simplification/change of Code of Conduct useful (stronger expenditure base)
  - Not sure it is worthwhile to change SGP regulations and fiscal compact
  - Commission should strengthen enforcement through internal channels
- **Patience**; more urgency when debt/interest rates/risk premia rise

