Implications of the Statistical Treatment of Investment Platforms for Budgetary Surveillance

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Disclaimer: The views expressed therein are solely mine and do not necessarily reflect an official position of the European Commission

Outline

- "The Pact": A convenient scapegoat but reality is different
- A crash course on the Stability and Growth Pact: main steps
- Treatment of the Investment Platforms highly dependent upon their statistical treatment

Yes, the Pact is not so bad for public invest'

- The Stability and Growth Pact ("the Pact") is *not* responsible for the lack of public investment in Europe
  - ✓ A set of deep structural factors, e.g. dry pipelines, permitting, administrative capacity
  - ✓ Introducing inefficient Pact exemptions, rather than addressing real issues
  - ✓ Countries with fiscal space can use it for investment; the others can freely improve the composition of their spending
- The other way round, the Pact is a public good for Europe and for investment
  - ✓ The guarantee of sustainable public finance and solvent sovereigns
  - ✓ Supported by serious analysis: Missale et al. (2011), The main driver of investment decline is the concern about sustainable public debts, regardless of the existence of fiscal rules.
  - ✓ Huge costs of confidence crisis for public investment (EA in 2011-3 and GR)
- The unpleasant truth: public investment is often low-priority spending for Member States
  - ✓ Paradox: public investment good for growth (when efficient)
  - ✓ But political economy: less electorally profitable, less strong lobbies
  - ✓ Result: (unfortunately) easier to cut investment than other spending

Golden rule for investment? potentially self-defeating

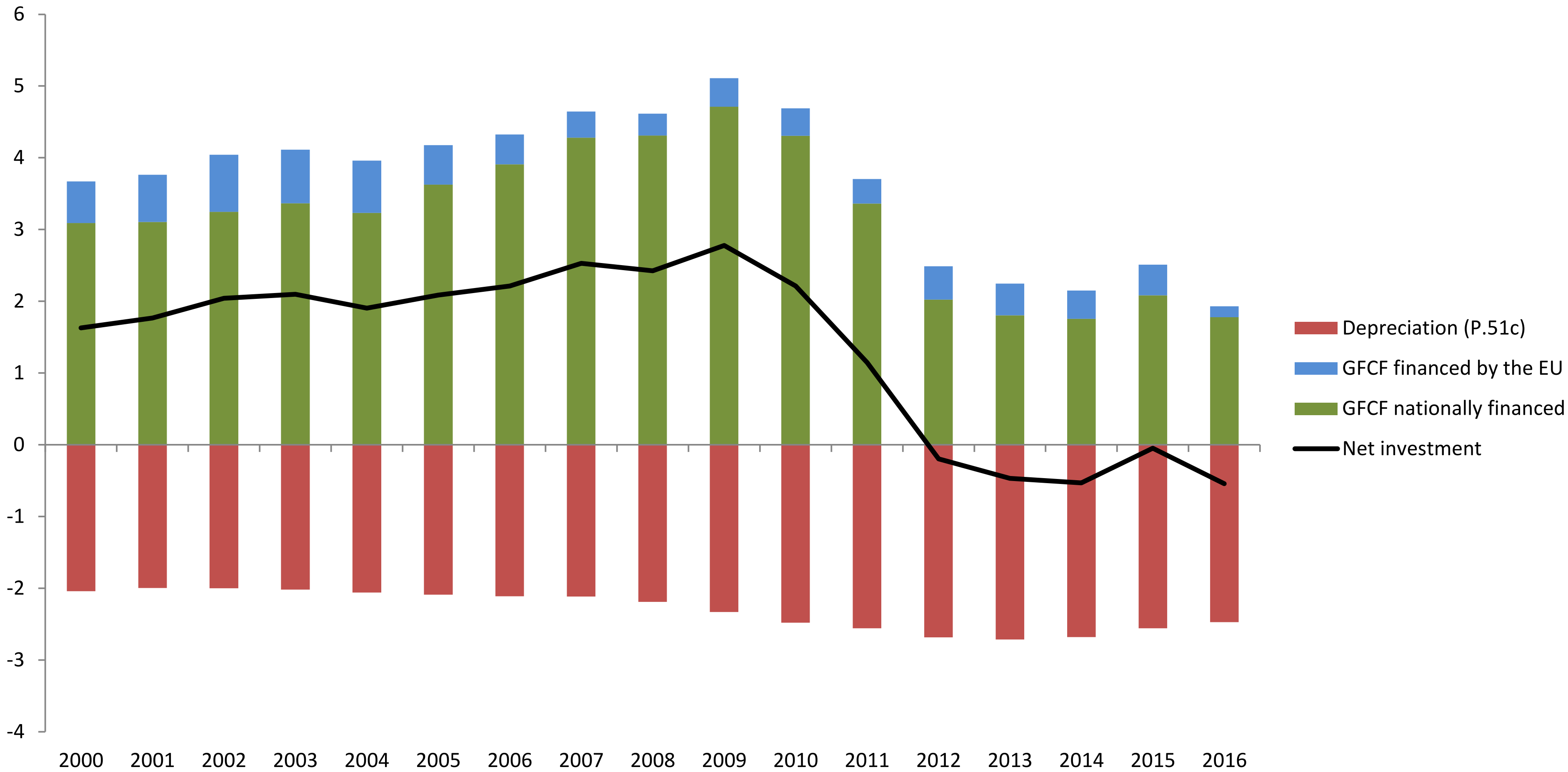
Golden rule = general exemption of net investment from the Pact

- Creates an illusion: investment should still be financed!
  - ✓ Threaten the sustainability of public finance…
  - ✓ … which is a condition of financing investment in the longer run!
- Generates calls for exempting other expenditures, thereby weakening the enforcement of the Pact
  - ✓ Make your pick: Investment, Education, Social spending, Active labour Market policy, Energy efficiency, Defence, Development policy ...
  - ✓ … what is left? Interest rate …
  - ✓ … too bad: not in the hand of the government!
- Incentivises creative accounting practices, selling as investment what is not in reality
  - ✓ Risk of limited effect on physical investment and risk of penalising other future-oriented expenditure, e.g. education and R&D, not considered as investment.
- Not least, does *not* help government in practice
  - ✓ Net investment the right concept= change in capital stock (w/o depreciation)
  - ✓ Since net investment is negative in many MS, giving space for other spending
  - ✓ Implementation issues: net investment is a not observable + privatisation
  - ✓ MSs don't like it: They prefer a favourable treatment under very specific conditions (one-off + investment clause), not a blancket exemption

Golden rule for investment? potentially self-defeating

First example: Belgium

Golden rule for investment? potentially self-defeating



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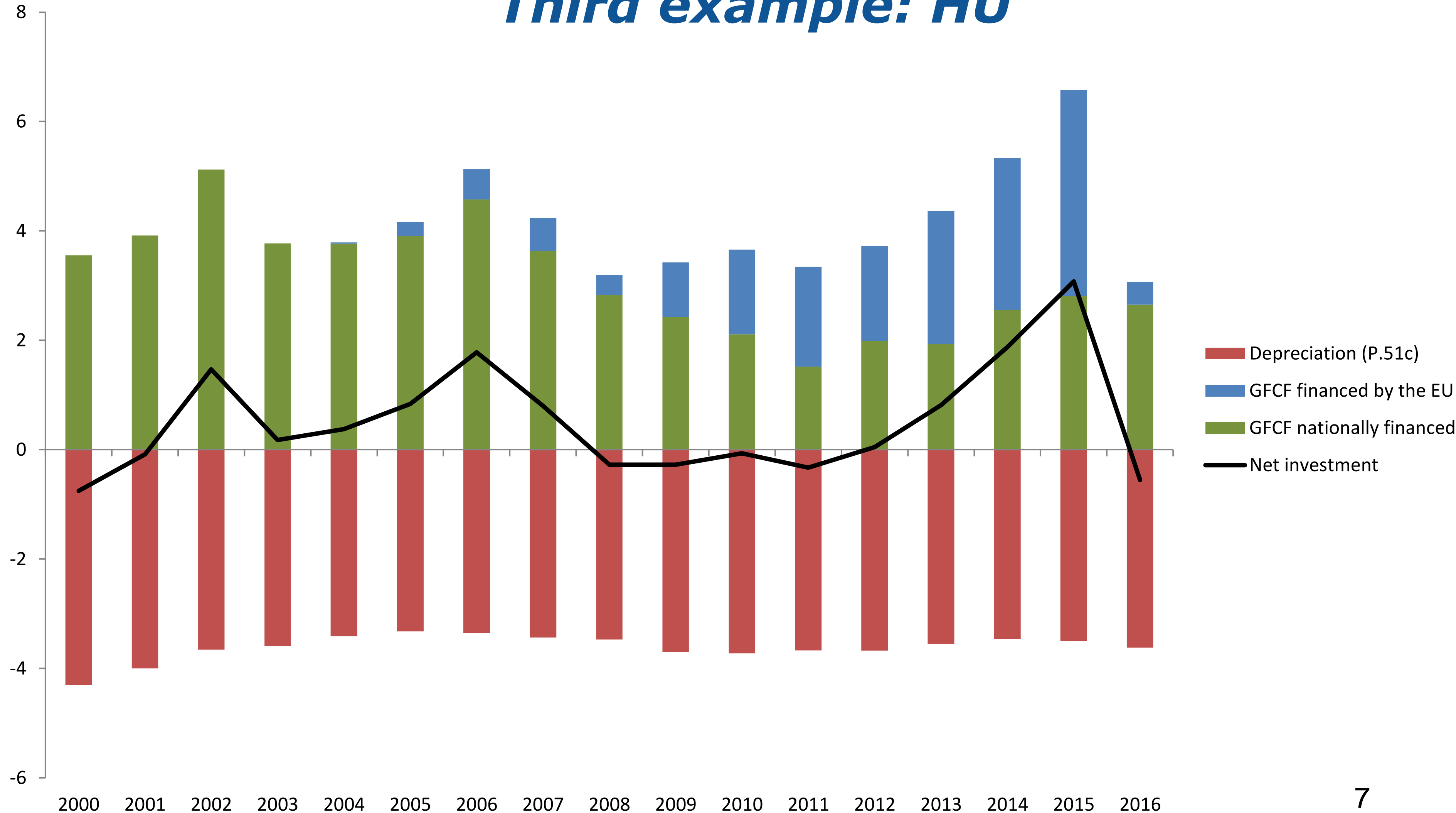

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The two arms of the Pact

	Preventive arm	Corrective arm
When?	Deficit < 3% of GDP *and* Debt < 60% of GDP (or sufficiently diminishing)	Deficit > 3% of GDP *or* Debt > 60% of GDP and not sufficiently diminishing
Objective?	Ensure prudent fiscal policies	Correct gross policy errors
Require-ment?	Structural balance (excl. cyclical budget impact and **one-off** factors) should remain at country-specific Medium-Term Objective (close to balance) or on a path towards it	Headline balance should be brought below 3% of GDP
Procedural steps?	If deviation: Significant Deviation Procedure after an '*overall assessment*'	3 steps: - Opening of an excessive deficit procedure (EDP) - Intermediate annual targets to be respected ("effective action") - Abrogation, if excessive deficit corrected.

One-offs

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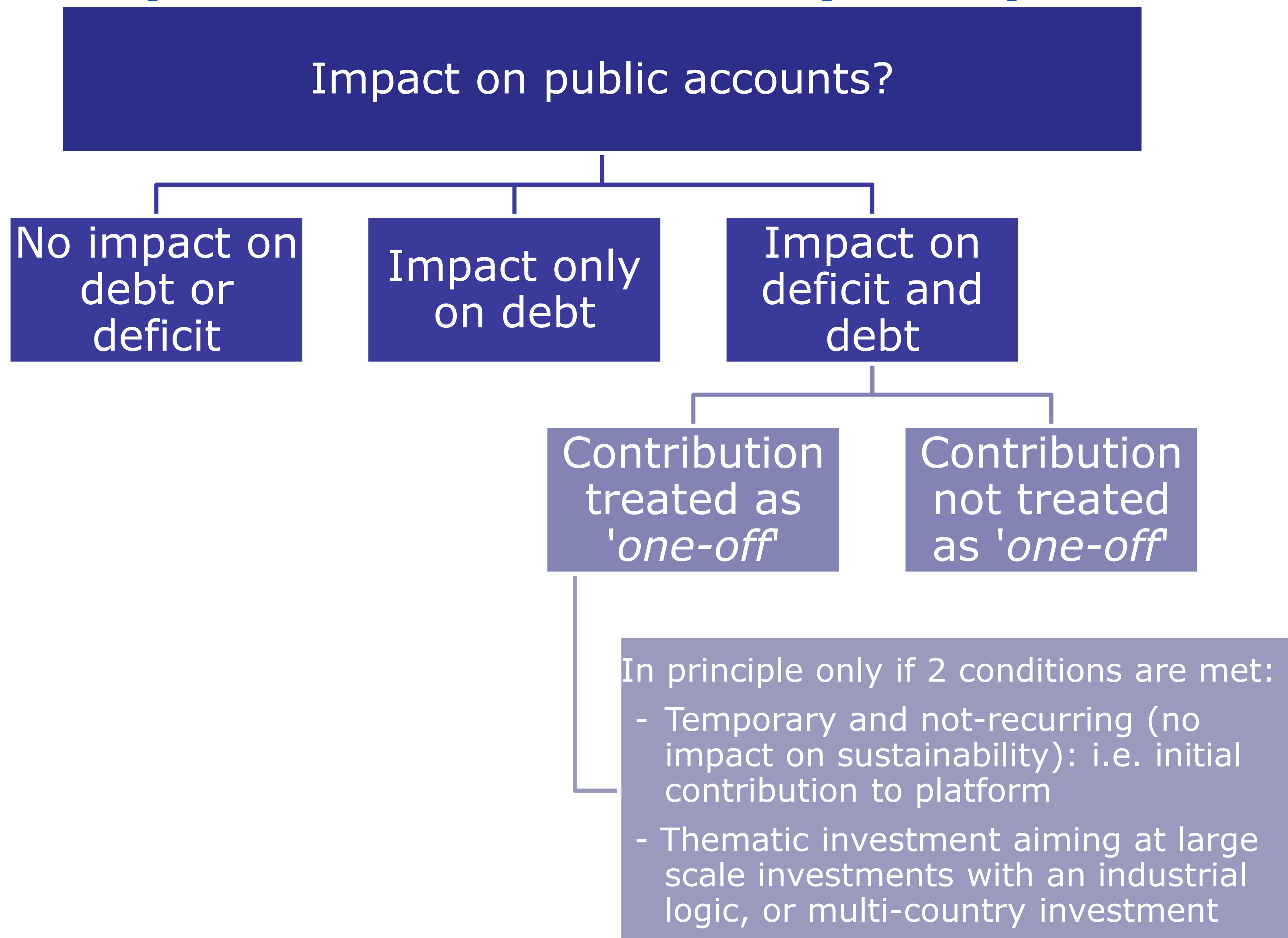
Implications depend on statistical treatment (ESTAT) and one-off treatment (ECFIN)



Implications for fiscal surveillance if debt or deficit impact

	Affected requirement of the Pact	How Commission can cater for contribution to investment platform
Member State in the corrective arm ('Excessive Deficit Procedure')		
Impact on deficit	Correction of excessive deficit	Abrogation of the EDP could be delayed (no flexibility)
Member State at risk of an Excessive Deficit Procedure		
Impact on debt	60% ceiling or debt reduction requirement	Temporary increase in investment could be a *'relevant factor'* for not opening an EDP
Impact on deficit	3% ceiling	Increase in investment could be a *'relevant factor'* for not opening an EDP (if breach is small and temporary)
Member State in the preventive arm		
Impact on deficit	Structural balance requirement	• *If contribution is considered as one-off:* no impact on structural balance because excluded from calculation • *If contribution is not considered as one-off:* could lead to significant deviation. However: possibility to use *investment clause* allowing deviation in bad economic times

Conclusions

- Avoiding two misconceptions distracting from seeking real solutions: “Obstacles to public investment come from the Pact, ... itself a bureaucratic artefact”

- In many cases, contributions to the platforms have potentially large effects under the Pact if recorded as *debt* & *deficit increasing* by Eurostat according to the rigorous classification of National Accounts ESA2010.

- The Pact treats public investment favourably, but not with unreasonable blanket exemptions
  - ✓ When justified, (deficit-increasing) initial contributions to platforms can be discounted from the preventive arm of the Pact (one-off). Should be non-recurrent & temporary and be aimed at large scale investment.
  - ✓ Relevant factors (not to open an Excessive Deviation Procedure)
  - ✓ Investment clauses could also be activated in bad times
  - ✓ Anyway, in the Pact, there is no hindrances to using fiscal space or to making space by reshuffling fiscal spending, with a view to boosting public investm’

Thank you!

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