



Economic Governance Review

State of play and outlook

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Outline

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2. Findings of the review on the SGP and national fiscal frameworks published in March 2020
3. Looking ahead
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 - 4.2 The Commission's updated approach to fiscal policy response

The 6/2 Pack Review: motivation

Putting the review into context

- Assessment of the effectiveness of the 6/2 Pack is backward looking and was published on 5 February 2020, before the outbreak of the pandemic.
- One month later, the debate launched by the review was put on hold due to the pandemic and the need to respond to the crisis.
- Commission Communication on an updated approach to fiscal policy of 5 March emphasises that the debate on the economic surveillance framework will resume “once the recovery takes hold”.

The 6/2 Pack Review: motivation

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.”

Political occasion:

- The start of a new political cycle in the Union as an appropriate moment to take stock and adapt the framework to new challenges and priorities.

Legal basis of the governance framework

Secondary legislation

- Regulation (EC) 1466/97('preventive arm'): aims to ensure sound budgetary positions
- Regulation (EC) 1467/97('corrective arm'): aims to correct gross policy errors
- Six-pack legislation:
 - **Five Regulations:** strengthen SGP and establish surveillance of macroeconomic imbalances
 - **One Directive:** set requirements regarding national fiscal frameworks
- Two-pack legislation: two Regulations for euro area countries given risk of spillovers

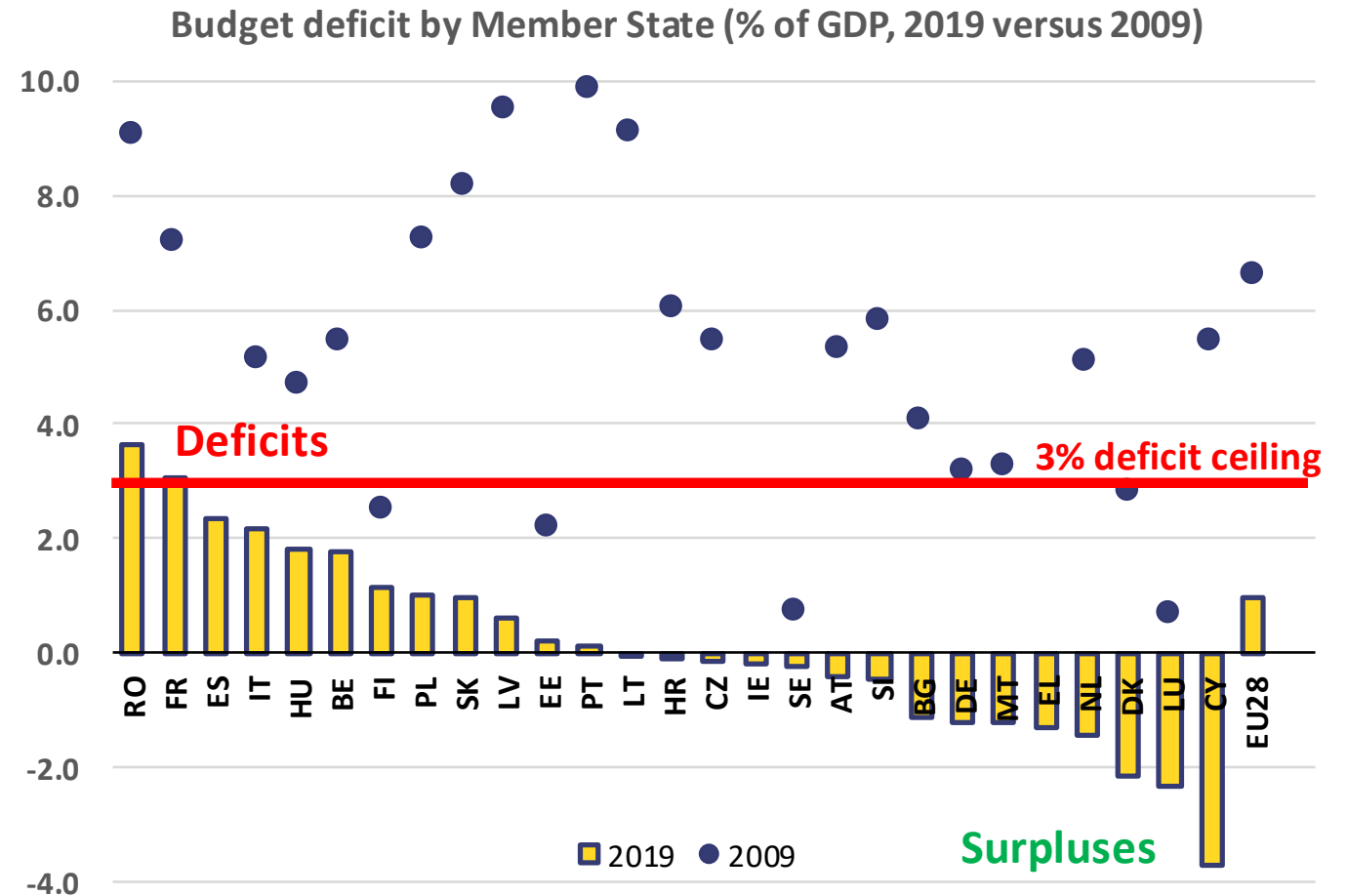
Other documents that specify the implementation of surveillance

- Code of Conduct of the SGP / Code of Conduct on the two-pack
- Vade Mecum on the SGP / Compendium on the MIP
- Commission Communication and commonly-agreed position on flexibility in the SGP, etc.

Findings on the SGP and national fiscal frameworks published in March 2020

Sustainability of public finances

- The corrective arm has proven effective in reducing and maintaining government deficits below 3%.
- Effectiveness of simple numerical rule: easy to grasp
- But: problem of nominal strategy under EDP.

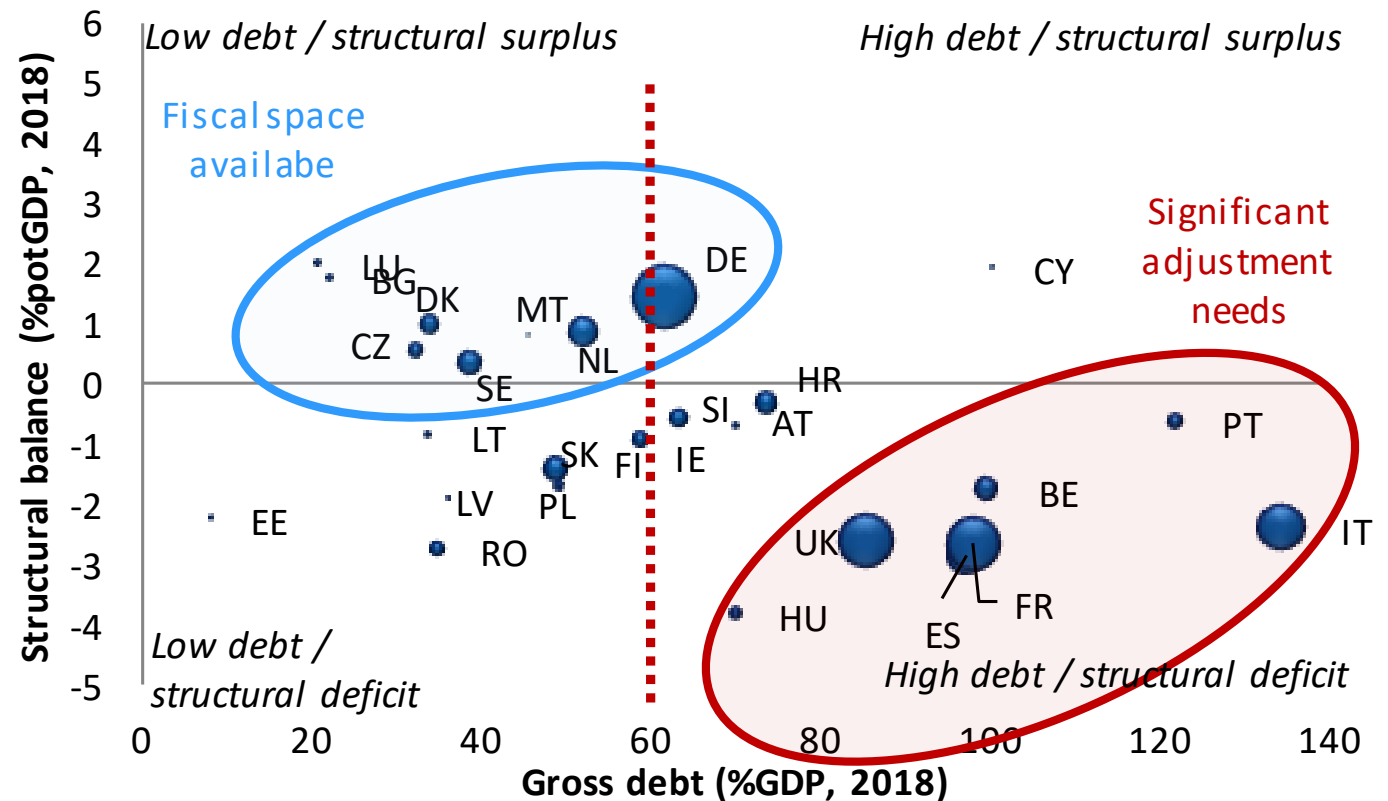


Sustainability of public finances

- 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.

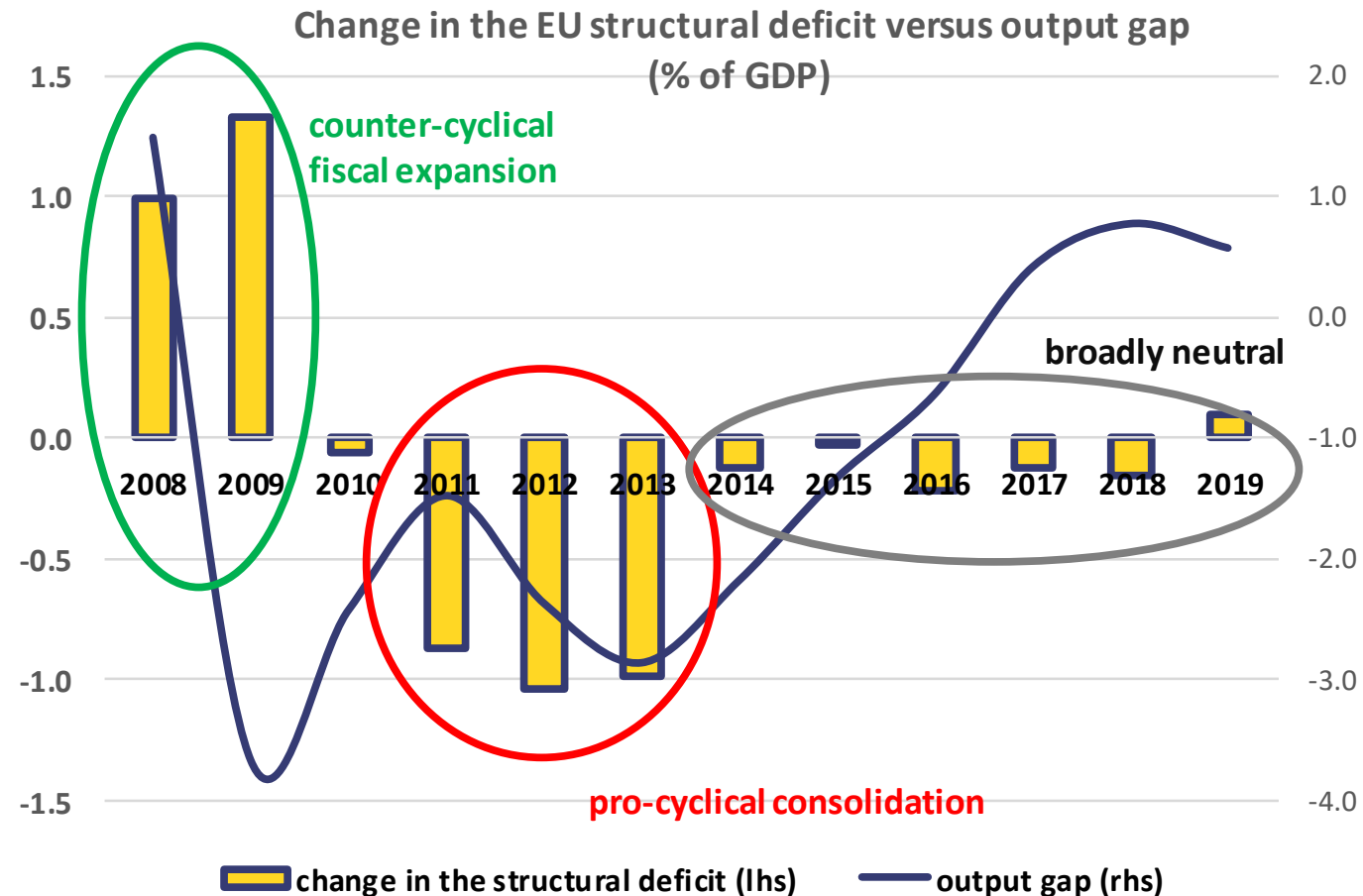
→ *Did 3% act as a target rather than a ceiling?*

→ *Is there too much focus on Member States with minor fiscal imbalances?*

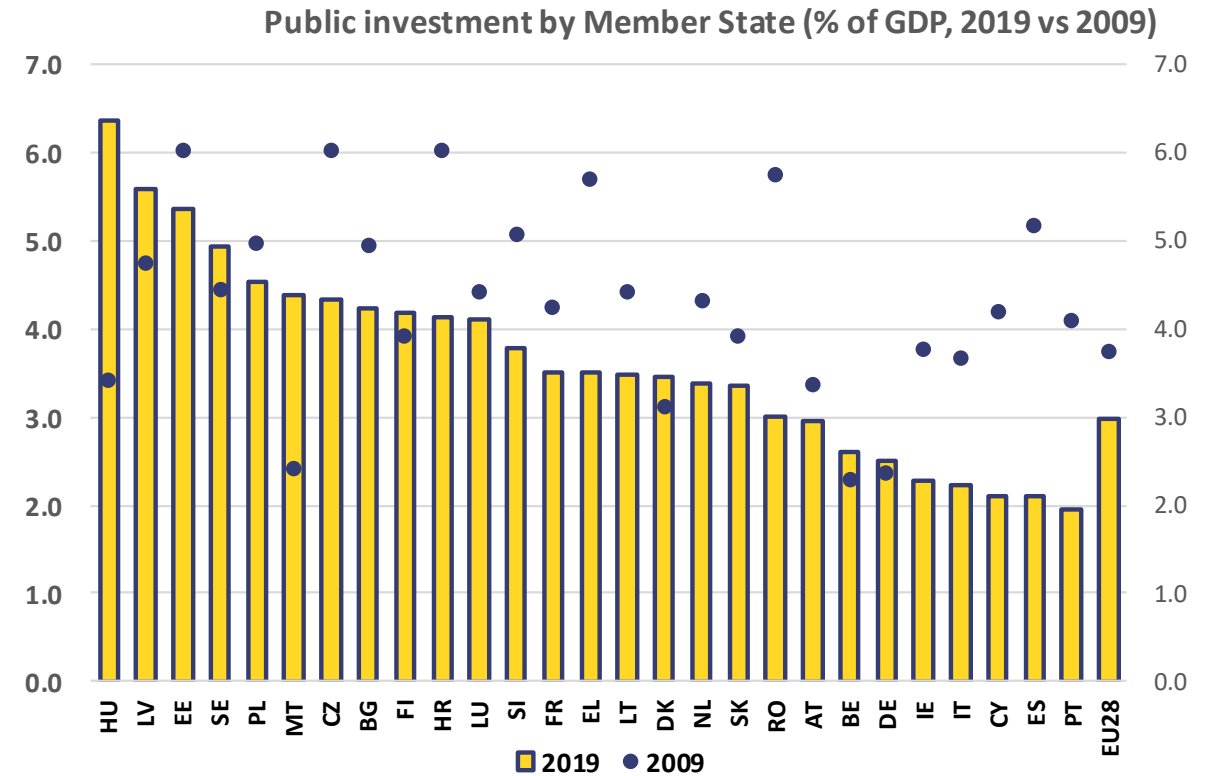
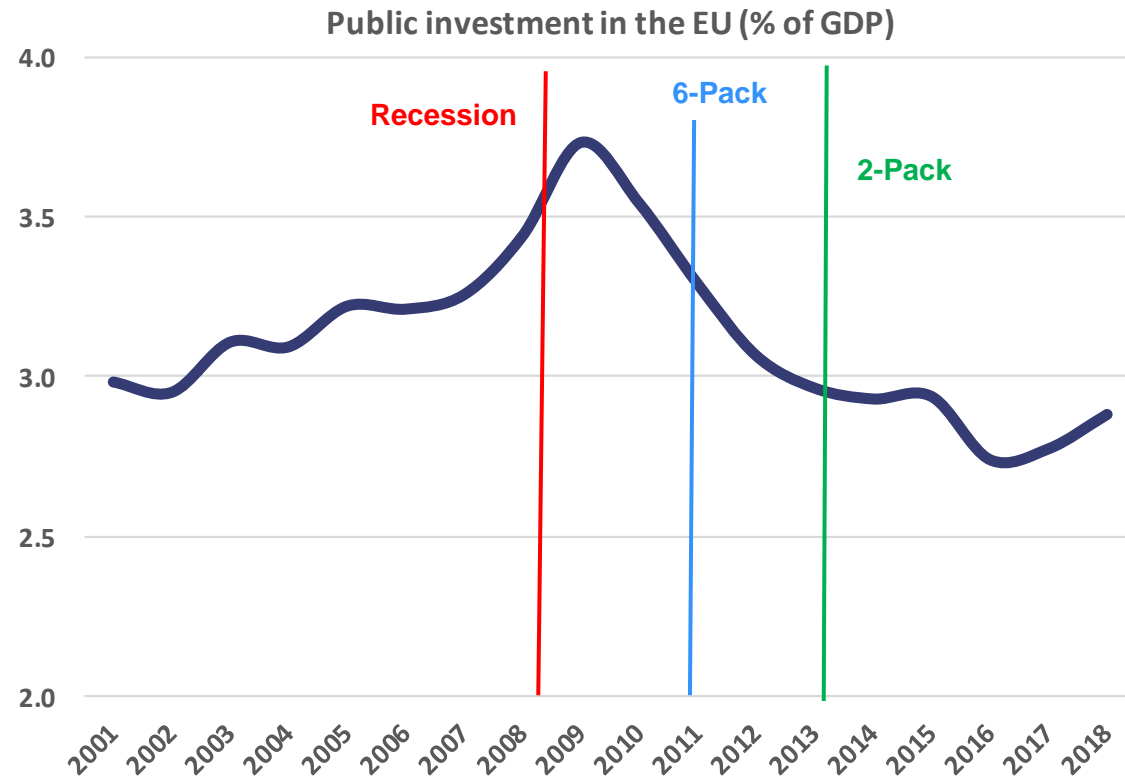


Fiscal stabilisation: problem of pro-cyclicality

- 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 ELB: What role for fiscal policy in policy mix?



Growth-friendliness of public finances



National fiscal frameworks

Institutional strengthening

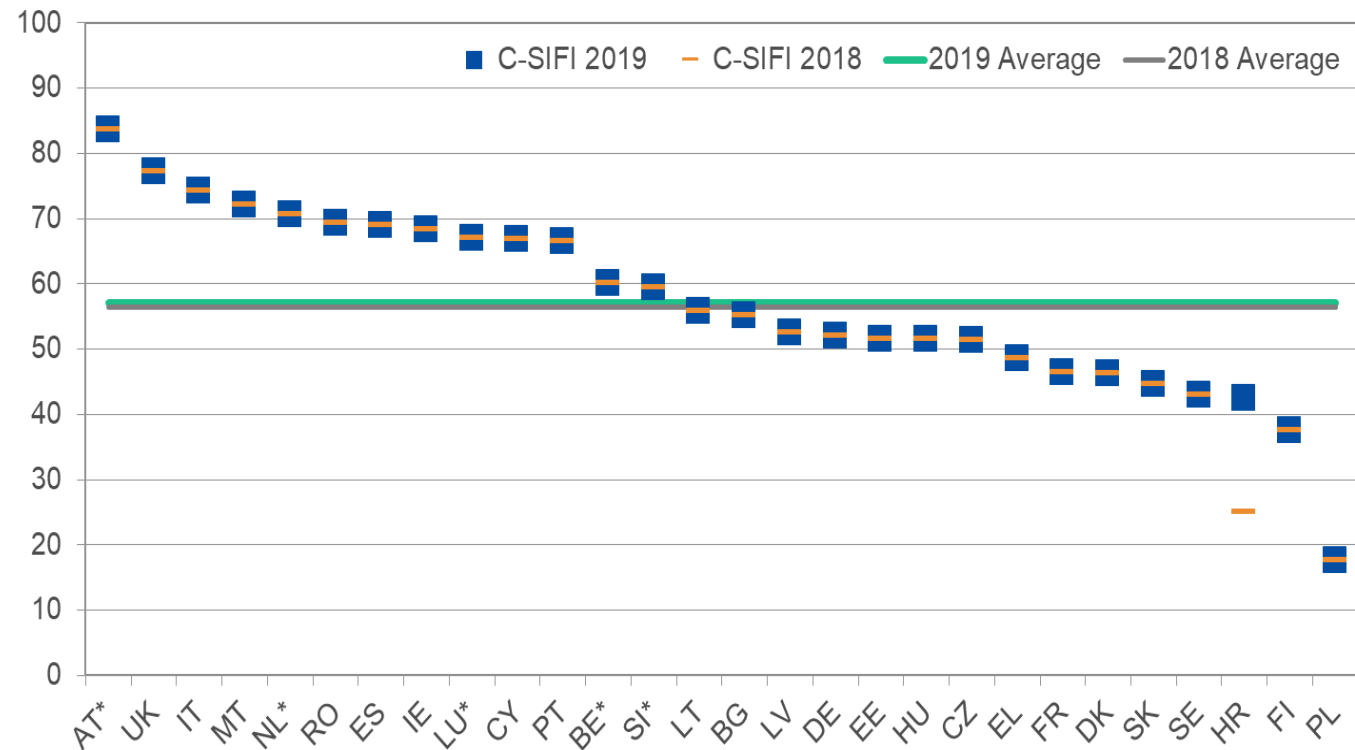
- National rules
- Independent fiscal institutions
- Medium-term planning
- Strengthened forecasting

Supports compliance with EU fiscal rules + increases ownership

But:

- Differences in design and implementation practices

Independent fiscal institutions
Scope Index of Fiscal Institutions by country (C-SIFI)



Governance and ownership

- **Complexity and lack of predictability** harm communication and ownership: multiplicity of rules, divergent compliance indicators, reliance on unobservable and unstable variables, numerous clauses allowing for deviations
- **DBP process**: useful for ex ante coordination
 - EU rules better taken into account in budget process;
 - difficulty of influencing national fiscal policy in practice.
- Reluctance to launch **enforcement procedures** and impose financial sanctions.
 - SDP only in very clear-cut cases (and only non-EA MS so far)
 - no debt-based EDPs (despite breaches of debt reduction benchmark)
 - no financial sanctions under EDP (six- and two-pack shifted responsibility on COM)
- Emphasis on **compliance with annual requirements**.
 - the medium-term orientation of fiscal policy is insufficiently taken into account.
 - focus on adjustment to MTO distracts from differentiating overall fiscal risks between countries.

In summary

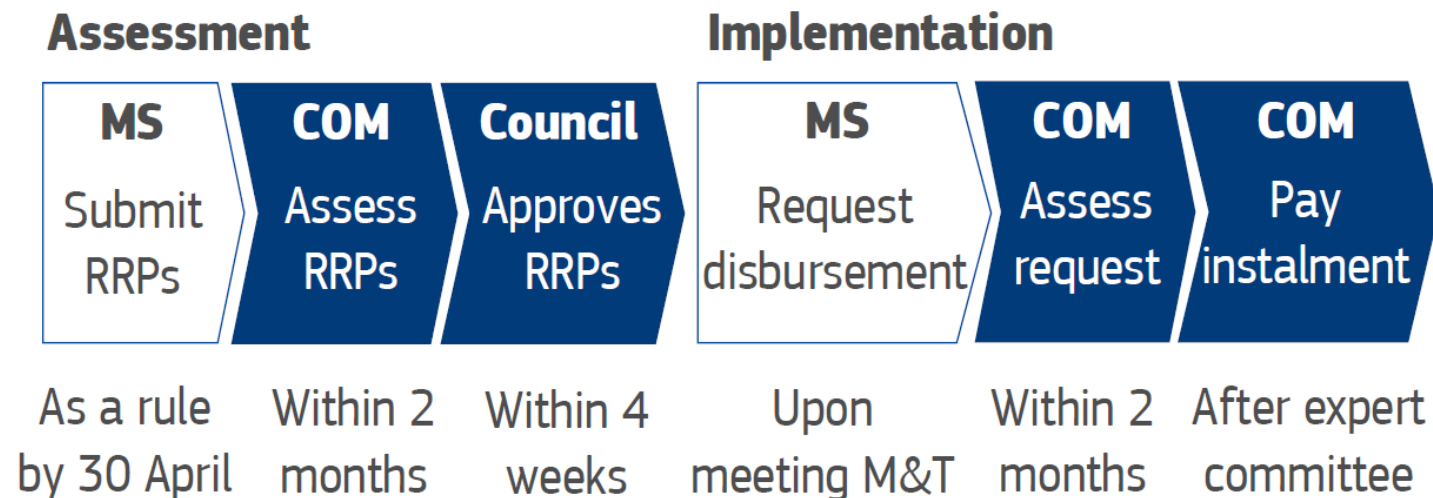
The 2020 review of the effectiveness of economic governance framework revealed a number of shortcomings related to rule design, implementation and enforcement.

- Need to ensure sustainability where it is most necessary, while allowing for macro-economic stabilization in both good and bad times.
- Need to simplify the rules in order to increase ownership, improve communication, and reduce the political costs for enforcement and for compliance.
- Re-define the role of the EU economic governance framework in view of current challenges
- Relaunching the public consultation on the economic governance framework will allow the Commission to reflect on the challenges identified in February 2020 and draw lessons from the current crisis.

Looking ahead

Recovery and Resilience Facility

- The **Recovery and Resilience Facility (RRF)** is the centrepiece of **NextGenerationEU**, the **EUR 750 billion temporary recovery instrument** to help repair the immediate economic and social damage brought about by the coronavirus pandemic.
- Member States will prepare **Recovery and Resilience Plans** that set out a coherent package of reforms and public investment projects.
- Roll-out in 2 phases:



Recovery and Resilience Facility

EUR 672.5 bn

13% pre-financing in 2021

Up to

EUR 312.5 bn grants

- Based on allocation key
- 70% committed until 2022, 30% in 2023
- Measures until 2026

Up to

EUR 360 bn loans

- Capped at 6.8% GNI
- Justified by higher financial needs
- Commitments by 2023

Recovery and Resilience Plans

All Member States must ensure that the investments and reforms included in their plans

- ✓ represent a **balanced response** to the economic and social situation of the Member State
- ✓ effectively address challenges identified in the relevant **country-specific recommendations**;
- ✓ strengthen the **growth potential, job creation** and economic, social and institutional **resilience** of the Member State;
- ✓ respect the **37%** target for **climate objectives** & **20%** target for **digital objectives**;
- ✓ do **no significant harm** to any of the environmental objectives
- ✓ RRP's need to provide **detailed cost estimates**

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Recital 59 of the Regulation: “Member States should be encouraged to seek the opinion of their national productivity boards and independent fiscal institutions on their recovery and resilience plans, including possible validation of elements of their recovery and resilience plan.”

The Commission's updated approach to fiscal policy response

On 3rd March 2021, the Commission published a Communication with **broad orientations for the conduct of fiscal policies** for the period ahead.

- Based on the Commission 2021 winter interim forecast and **to be updated and further detailed** on the basis of the **Commission 2021 spring forecast** as part of the **spring European Semester package**
- Makes considerations for how a future decision on the **deactivation of the general escape clause of the SGP** should be taken
- Outlines **key considerations** to facilitate the coordination of fiscal policies and the preparation of Member States' Stability and Convergence Programmes.

Updated approach to fiscal policy response

In terms of **next steps**, the **European Semester spring package** will entail:

- A largely qualitative assessment of the **Stability and Convergence Programmes**
- Proposals for **country-specific fiscal policy guidance**
- **Reports under Art. 126(3)**
- An **assessment of the application of the general escape clause** of the Stability and Growth Pact

When the recovery takes hold, the Commission will **relaunch the review** of the economic governance framework

Thank you



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