Jean Monnet Module

“Economic Policy in the European Union”

Session 5.4. European economic governance: the future of the EU

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INDEX

EVENTS HIGHLIGHTING ECONOMIC UNION

Economic and Monetary Union, 1999

Internal Market, 1993

Customs Union, 1968

Free Trade Area, 1958

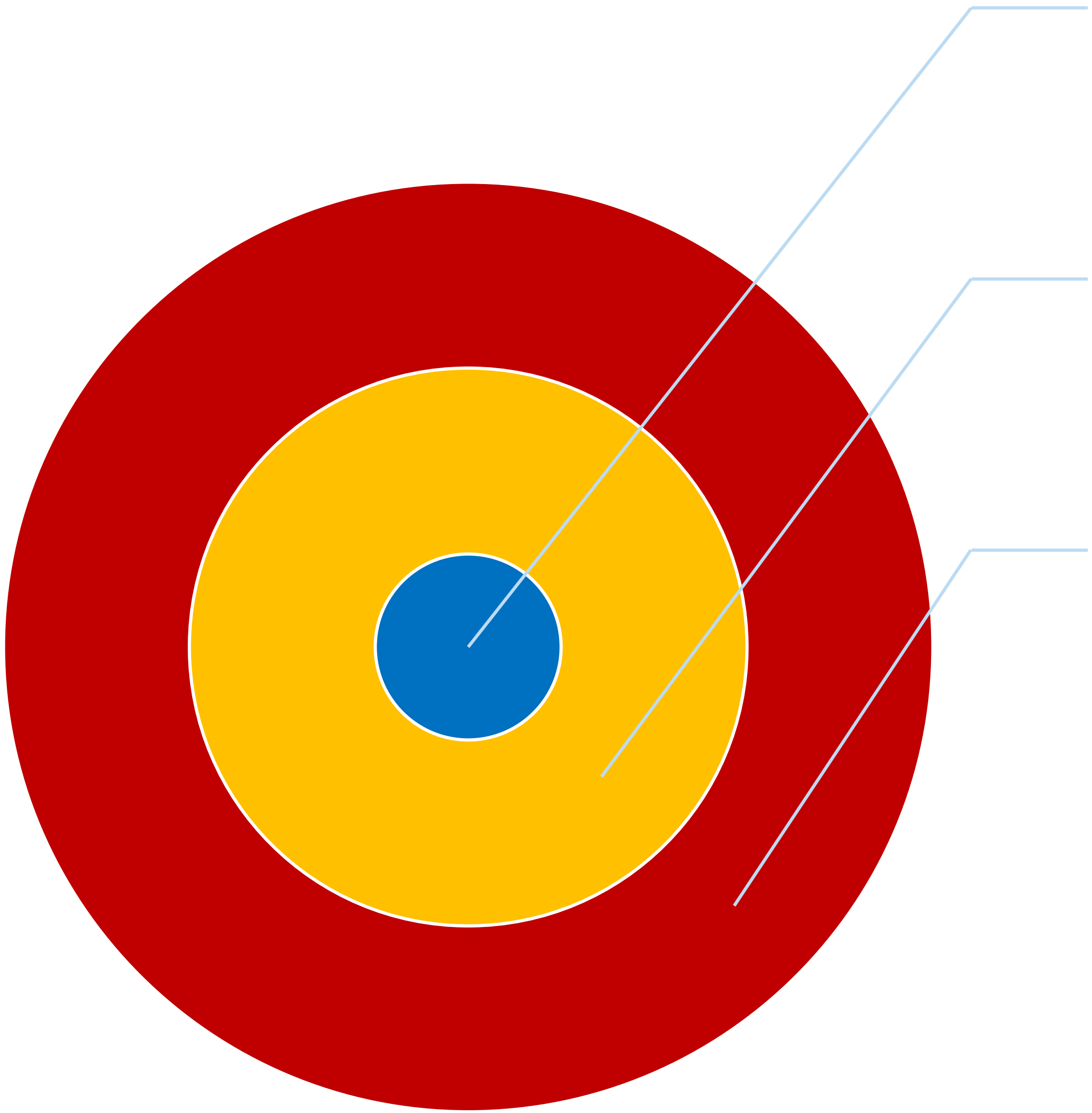
Monetary Union Necessary conditions	**Economic union** Necessary conditions
- Total and irreversible convertibility of currencies - Liberalization of capital movements and integration of financial markets - Irrevocable fixing of exchange rates	- Single market - Macroeconomic policy coordination - Common policies for structural change and regional development

SOVEREIGN DEBT CRISIS IN THE EURO AREA

- International financial crisis, summer 2007 → Eurozone liquidity crisis → sovereign debt crisis
  - Risk premia skyrocket in peripheral countries
- False data for Greece → distrust
  - Withdrawal of deposits
  - Exponential increase in debt
  - Bankruptcy or bailout?
  - Contagion effect

RESCUES. FINANCIAL INSTRUMENTS IN THE FACE OF THE CRISIS

- 2010. **European Financial Stability Mechanism**
- 2010. **European Financial Stability Facility**
- 2012. **European Stability Mechanism (ESM)**
  - Reformed in 2021 (signed in January, still under ratification)
  - Support to the RUF
  - Simplified access to credit lines to prevent minor crises from escalating



Single monetary policy
National budgetary independent policies (fiscal discipline and excessive deficit procedure)
Tradition of the **Public deficit** and **unemployment**

EVIDENCE AND POTENTIAL SOLUTIONS

Insufficient coordination of national economic policies

Avoid accumulation of imbalances.

Ensuring convergence and stability

Strengthening economic governance

ECONOMIC GOVERNANCE

System of institutions and procedures established to achieve the EU's objectives in the economic field, i.e. the coordination of economic policies to promote economic and social progress for the EU and its citizens.

HOW IS ECONOMIC GOVERNANCE STRENGTHENED?

Economic union

- Completing the Single Market
- Macroeconomic policy coordination
- Common policies for structural change and regional development

COMPLETING THE SINGLE MARKET

COMPLETING THE SINGLE MARKET

- European Economic Recovery Plan (2008)
- End of Lisbon Strategy → 2010: Europe 2020
- Strategic Agenda 2019-2024
- European System of Financial Supervision (2010)
  - European Banking Authority
  - European Securities and Markets Authority
  - European Insurance and Occupational Pensions Authority

COMPLETING THE SINGLE MARKET

- Single Capital Market

  - Banking Union:
    - MUS, 2011
    - MUR, 2013
    - EDIS (European Deposit Insurance Scheme), ongoing

- Digital Single Market (under conditions of competitiveness, protection of personal data, independence of place of residence,...)

COMPLETING THE SINGLE MARKET

2011. **Single Market Act. Stimulating growth and regaining confidence**

- Access to finance for SMEs. Avoid fragmentation
- Citizens' mobility: Recognition of qualifications
- Intellectual Property Rights. European patent and licensing market
- Consumers. Dispute resolution legislation
- Srvices. Legislation on the European standardisation system
- Networks. Energy and transport infrastructure
- Digital Single Market. Mutual recognition of identification and electronic authentication.
- Social enterprises. Solidarity Investment Funds.
- Taxation
- Social cohesion
- Regulatory environment of Companies. Simplification of accounting rules
- Public contracts. Review and modernisation of the regulatory framework

COMPLETING THE SINGLE MARKET

2012. **Single Market Act II**

- Transport infrastructure
- Cross-border mobility of citizens and businesses
- Digital Single Market
- Social entrepreneurship, cohesion and consumer trust

COMPLETE THE SINGLE MARKET. STRATEGY (2015)

- **Modern and innovative** (helping companies, micro-enterprises and start-ups by facilitating innovation and job creation)

- **Deeper** (coordination and cooperation)

- **Fairer** (protection and benefits for citizens, consumers and businesses)

MACROECONOMIC POLICY COORDINATION

Until 2011

Since 2011

BROAD ECONOMIC POLICY GUIDELINES

Stability Programs/ Convergence

+

National Reform Programmes

- Coordinate national economic policies and meet EU objectives
- European Commission and Council of the EU: assess whether budgetary targets (SGPs) are being achieved

Improving Economic Governance

Legislative Package of six, 2011

(Six-Pack)

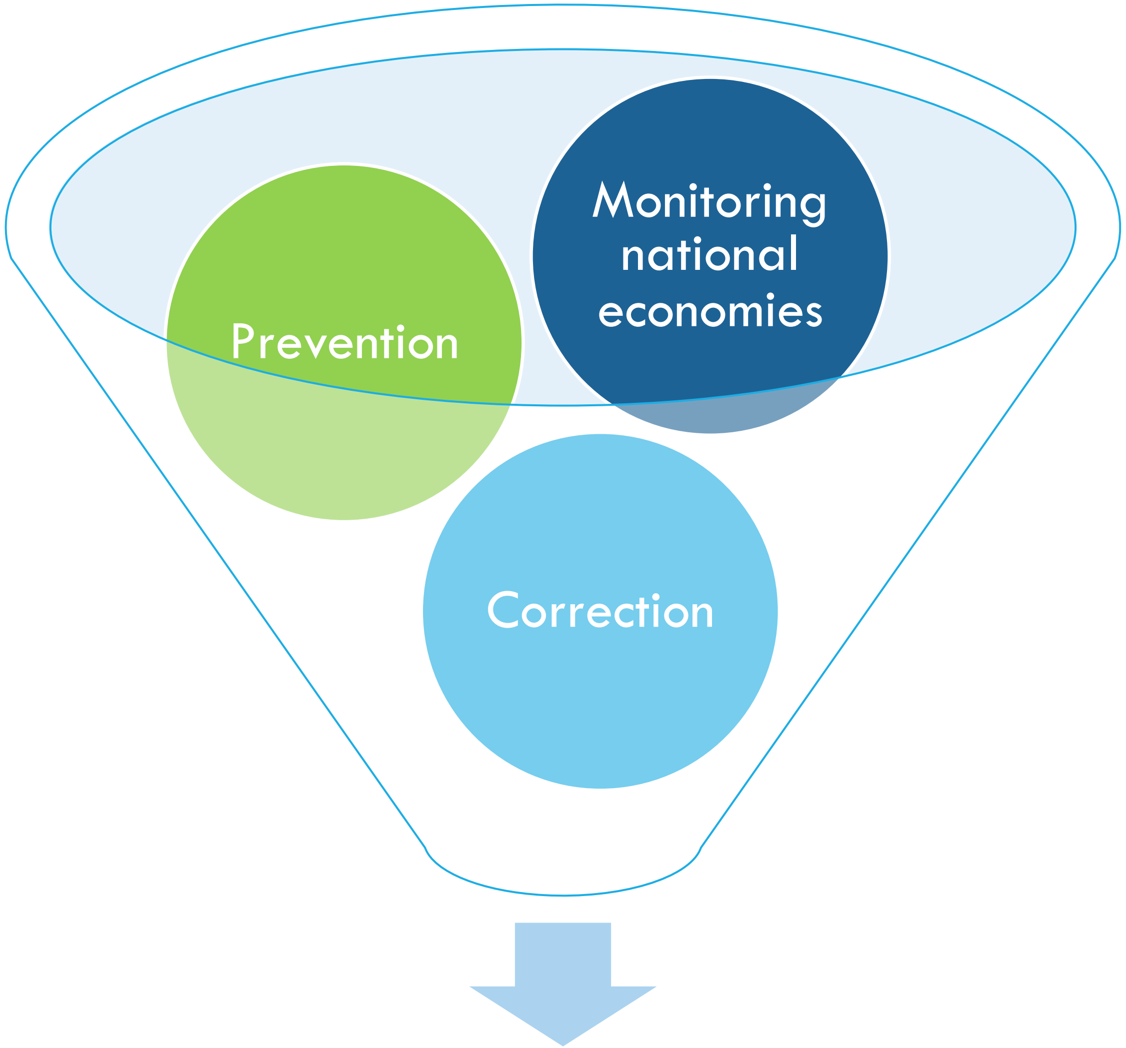
Legislative package on budgetary surveillance, 2013

(Two-pack)

Fiscal pact (2012). Balanced budget rule

- Deficit/GDP of 0.5% without taking action

European Semester, 2011



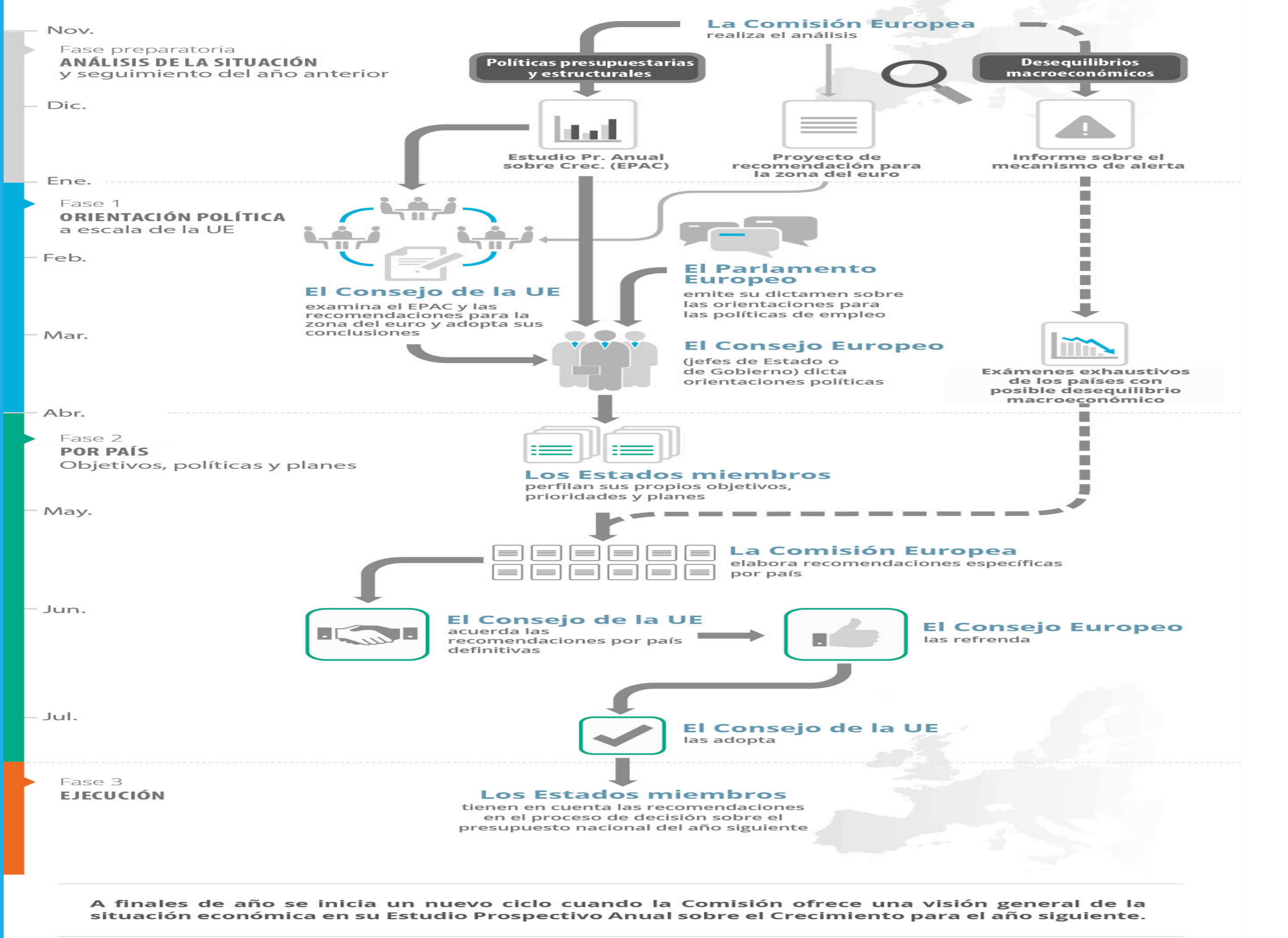
EU Economic Governance

MONITORING NATIONAL ECONOMIES

EUROPEAN SEMESTER, 2011

- Stability and convergence in the EU
- Sound public finances
- Fostering economic growth
- Preventing excessive macroeconomic imbalances
- Implementing EU strategies (Europe 2020, Strategic Agenda 2019-2024)

EUROPEAN SEMESTER



EUROPEAN SEMESTER BY COUNTRY

LEGISLATIVE PACKAGE OF SIX, 2011

Directive 2011/85/EU on requirements for budgetary frameworks of the Member States. **Fiscal policy is decentralised: SGP reflected in national budgets.**

Regulation (EU) No 1173/2011 on the effective budgetary application in the euro area. Sanctions Regulation.

Regulation (EU) n°1174/2011 of 16 November 2011 on observation measures to correct excessive macroeconomic imbalances in the euro area.

Regulation (UE) n°1175/2011 of 16 November 2011 that modifies the Regulation (CE) n° 1466/97 relative to the reinforcement of the surveillance of the budgetary positions and to the surveillance and coordination of the economic policies.

Regulation (EU) n°1176/2011 of 16 November 2011on prevention and correction of macroeconomic imbalances.

Council Regulation (EU) No 1177/2011 of 8 November 2011 amending Regulation (EC) No 1467/97 on speeding up and clarifying the excessive deficit procedure.

LEGISLATIVE PACKAGE ON BUDGETARY SURVEILLANCE, 2013

Regulation (EU) No 473/2013 of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and correcting the excessive deficit of the euro area Member States

Regulation (EU) No 472/2013 of the European Parliament and of the Council of 21 May 2013 on the strengthening of economic and budgetary surveillance of Member States of the euro area experiencing or threatening serious difficulties with regard to their financial stability.

PREVENTION

PREVENTION. SIX-PACK

- SGP. Reformed in 2005 and 2011. Prudent fiscal policies (public deficit and public debt).
- Medium-Term Budgetary Objectives (MTO)
  - The countries of the Eurozone reflect their Medium-Term Objectives (MTO) in the Stability Programmes (Convergence). It evaluates whether the objective is feasible in itself or in its way of achieving it.
  - Updated every three years (or sooner if necessary)
  - Business cycles are taken into account.
  - If deviation from the MTO, the Commission recommends the Council to open:
    - Significant deviation procedure (countries): possibility of correcting MTO deviations by returning to prudent fiscal policy and avoiding opening of excessive deficit procedures
- Spending benchmark. Complements MTOs. It puts net spending growth at a sustainable point by helping to comply with MTOs.

PREVENCIÓN. TWO-PACK

- Budgetary calendar and common fiscal rules: Identify, prevent and address macroeconomic imbalances. Indicators
    - Applicable in the euro area. Special rules for States included in the excessive deficit procedure.
- The Commission publishes an overall assessment of the budgetary outlook in the Eurozone.
- The Commission examines and delivers an opinion on each draft national budget.
    - If the project does not comply with the SGP, the affected State must submit a revised project: Economic Partnership Programme.
- This surveillance takes place in the autumn, between two European semesters: it completes economic governance and ensures coherence between budgetary policy and other economic policy decisions.
- Incorporates elements of the Stability Treaty or Fiscal Compact.

TREATY ON STABILITY, COORDINATION AND GOVERNANCE OF EMU. FISCAL COMPACT

- In force since 2013
- Stricter tax provisions than the Stability and Growth Pact

Structural Deficit: component related to structural situations and not subject to cyclical factors or extraordinary expenses

- Balanced budget rule: annual structural deficit limited to 0.5%
- A maximum structural deficit of 1% is allowed as long as the Public Debt to GDP ratio is below 60%.

CORRECTION

CORRECTION. EXCESSIVE DEFICIT PROCEDURE

- When does it start?
  - Public deficit above 3% of GDP.
  - The gap between the country's debt level and the 60% benchmark is breached. It should be reduced by 0.05% per year on average over three years.

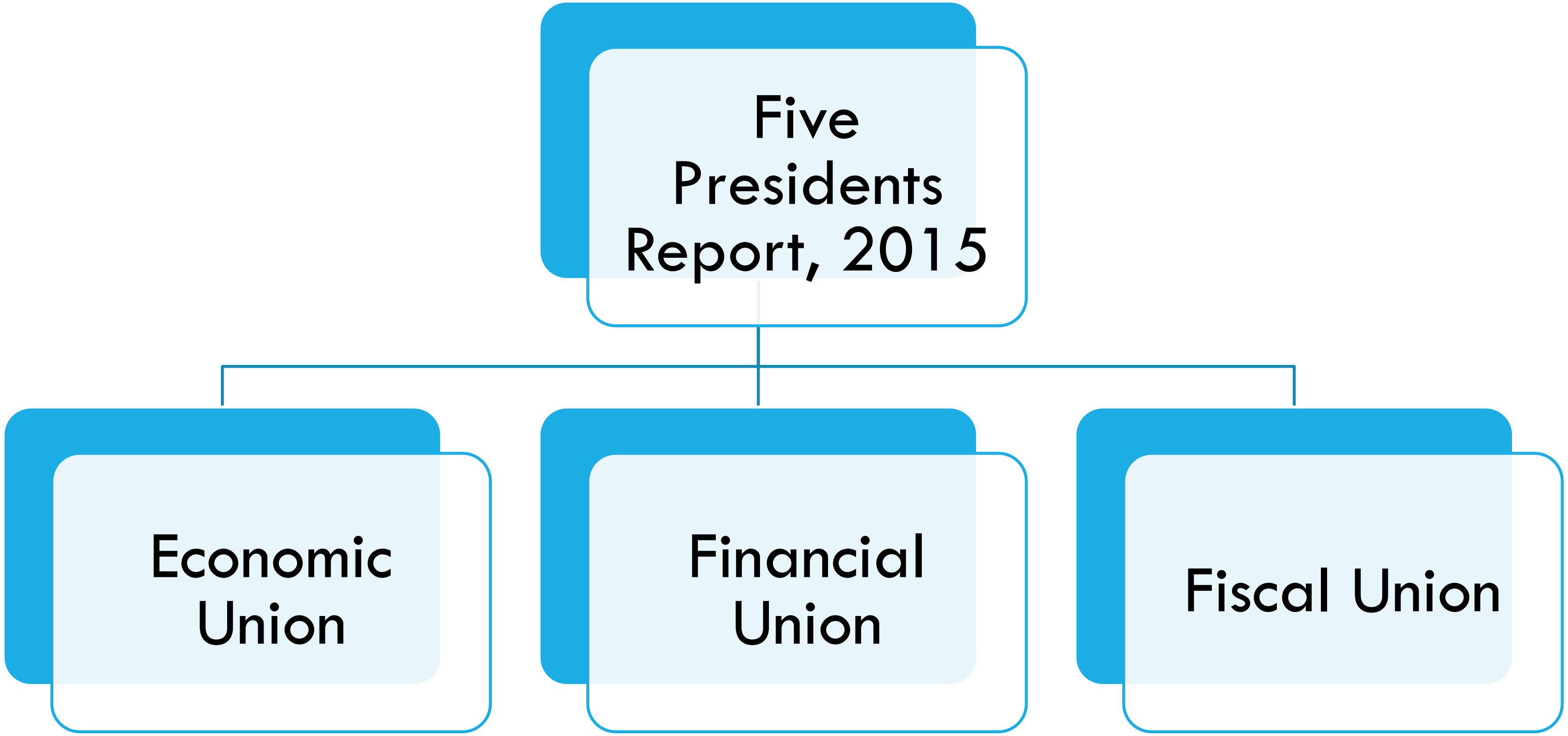
- State of play of excessive deficit procedures

  - If preventive and corrective measures are not complied with: sanctions
    - Deviations from a prudent fiscal policy: Interest-bearing deposit
    - Deviations from the corrective arm (recommendations): Non-interest-bearing deposit equivalent to 0.2% of GDP
    - The proposal for sanctions is submitted by the Commission. It is adopted unless the Council rejects it by qualified majority (reverse qualified majority).
    - If exceptional events occur and beyond your control: extension of the deadline for correction and review of recommendations.

CORRECTION. EXCESSIVE IMBALANCE PROCEDURE

- Macroeconomic imbalance.
- Under this procedure, the Commission may ask the Council to submit a corrective action plan to the country concerned. It is approved by the Council.

  - Monitoring that could terminate the procedure.
  - Insufficient corrective plans → sanctions: fine equivalent to 0.1% of its GDP (the fine can be suspended by qualified majority voting the members of the eurozone).



POLITICAL UNION
(Democratic legitimacy)
Integration of social, financial and economic aspects

FIVE SCENARIOS FOR THE FUTURE (WHITE PAPER ON THE FUTURE OF EUROPE, MARCH 2017)

- Stay the same
- Single market only
- Those who want to do more, do more
- Do less but efficiently
- Doing much more together

STRENGTHENING EMU. THREE STAGES (2015-2025)

Stage 1. Deepening (07/15- 06/17)

- Promote competitiveness and structural convergence. System of competitiveness authorities in the euro area.
- Complete the financial union. **Banking Union**
- Improving democratic accountability: greater parliamentary participation and scrutiny (country recommendations, PNR, Annual Growth Survey), strengthening the Eurogroup
- Responsible fiscal policies at national and eurozone level. Fiscal Union (**European Fiscal Board**, consultative capacity)

Stage 2. Completing EMU

- More far-reaching actions to make convergence effective (binding: establishment of common high-level standards defined in EU legislation). **European Fund for Strategic Investments**
- Possibility of creating a treasury in the eurozone

Final phase (until 2025, at the latest)

- Deep and genuine EMU

EUROPEAN FISCAL COUNCIL, 2015

- Evaluate the implementation of the budgetary framework (national-eurozone)
- Assess and suggest the future budgetary policy for the euro area
- Cooperating with independent national tax councils

- **Origin:** Five Presidents Report "Completing European EMU"
- **Objective:** to strengthen economic governance
- Independent body advising the European Commission

EU STRATEGIC AGENDA 2019-2024

- European Green Deal
- Digital Europe
- Economy at the service of people
- Strongest Europe in the world
- Promotion of the European way of life
- Boosting European democracy

ROLE OF THE INSTITUTIONS

European Council

- Coordinated national policy priorities. Guidelines.
- It adopts the recommendations and decisions proposed by the Commission.

European Commission

- Prepares draft recommendations and decisions. Evaluate the application.

Member States

- They implement the recommendations and decisions adopted by the Council.

Eurogroup

- Debate on EMU issues. It manages the ESM.

ECB

- It participates in Eurogroup discussions on monetary policy issues.

European Parliament

- Delivers opinion on the Annual Sustainable Growth Strategy and the European Semester cycle

GOVERNANCE REVIEW

- February 2020. European Commission launches governance review: public debate to assess whether tools introduced in 2011 and 2013 have been effective in terms of:

  - Sustainability of public finances and growth
  - No macroeconomic imbalances
  - Closer coordination of national economic policies
  - Convergence of Member States' economies

BUDGET SHORTFALL

RECOVERY PLAN FOR EUROPE

Multiannual Financial Framework 2021-2027

+

Temporary Recovery Instrument (Next Generation EU)

Recovery and Resilience Plans (access to Funds)

→

Genuine stimulus package

MFF, 2021-2027
(ALLOCATIONS BY HEADING)

	MFP	*NextGenerationEU*	*TOTAL*
1. Mercado único, innovación y economía digital	132 800 millones de euros	10 600 millones de euros	143 400 millones de euros
2. Cohesión, resiliencia y valores	377 800 millones de euros	721 900 millones de euros	1 099 700 millones de euros
3. Recursos naturales y medio ambiente	356 400 millones de euros	17 500 millones de euros	373 900 millones de euros
4. Migración y gestión de las fronteras	22 700 millones de euros	-	22 700 millones de euros
5. Seguridad y defensa	13 200 millones de euros	-	13 200 millones de euros
6. Vecindad y el mundo	98 400 millones de euros	-	98 400 millones de euros
7. Administración pública europea	73 100 millones de euros	-	73 100 millones de euros
TOTAL MFP	1 074 300 millones de euros	750 000 millones de euros	1 824 300 millones de euros

Todos los importes en miles de millones de euros a precios constantes de 2018. Fuente: Comisión Europea

** Los importes incluyen el refuerzo selectivo de diez programas por un total de 15 000 millones de euros, en comparación con el acuerdo de 21 de julio de 2020. Los programas son Horizonte Europa, Erasmus+, EU4Health, Fondo para la Gestión Integrada de las Fronteras, Derechos y Valores, Europa Creativa, InvestEU, Agencia Europea de la Guardia de Fronteras y Costas y Ayuda Humanitaria.*

NEW REVENUE STREAMS

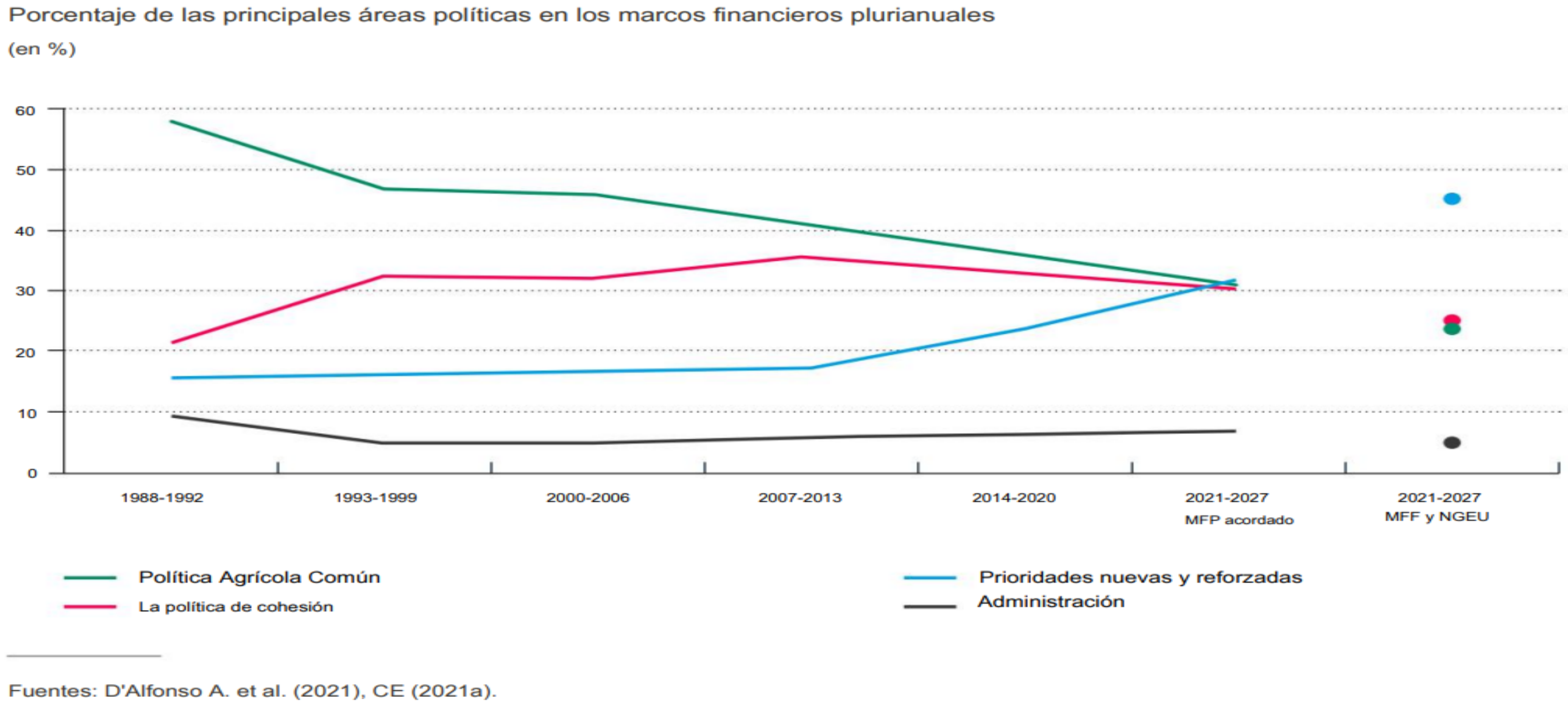
The European Commission shall present, by June 2021, proposals for revenue sources linked to:

- A carbon border adjustment mechanism
- A digital tax
- An emissions trading system

By June 2024 at the latest:

- A tax on financial transactions
- A contribution linked to the business sector
- A new common corporate tax base

BREAKDOWN, BY AREA, IN THE MFFS (SOURCE: EUROPEAN COMMISSION)

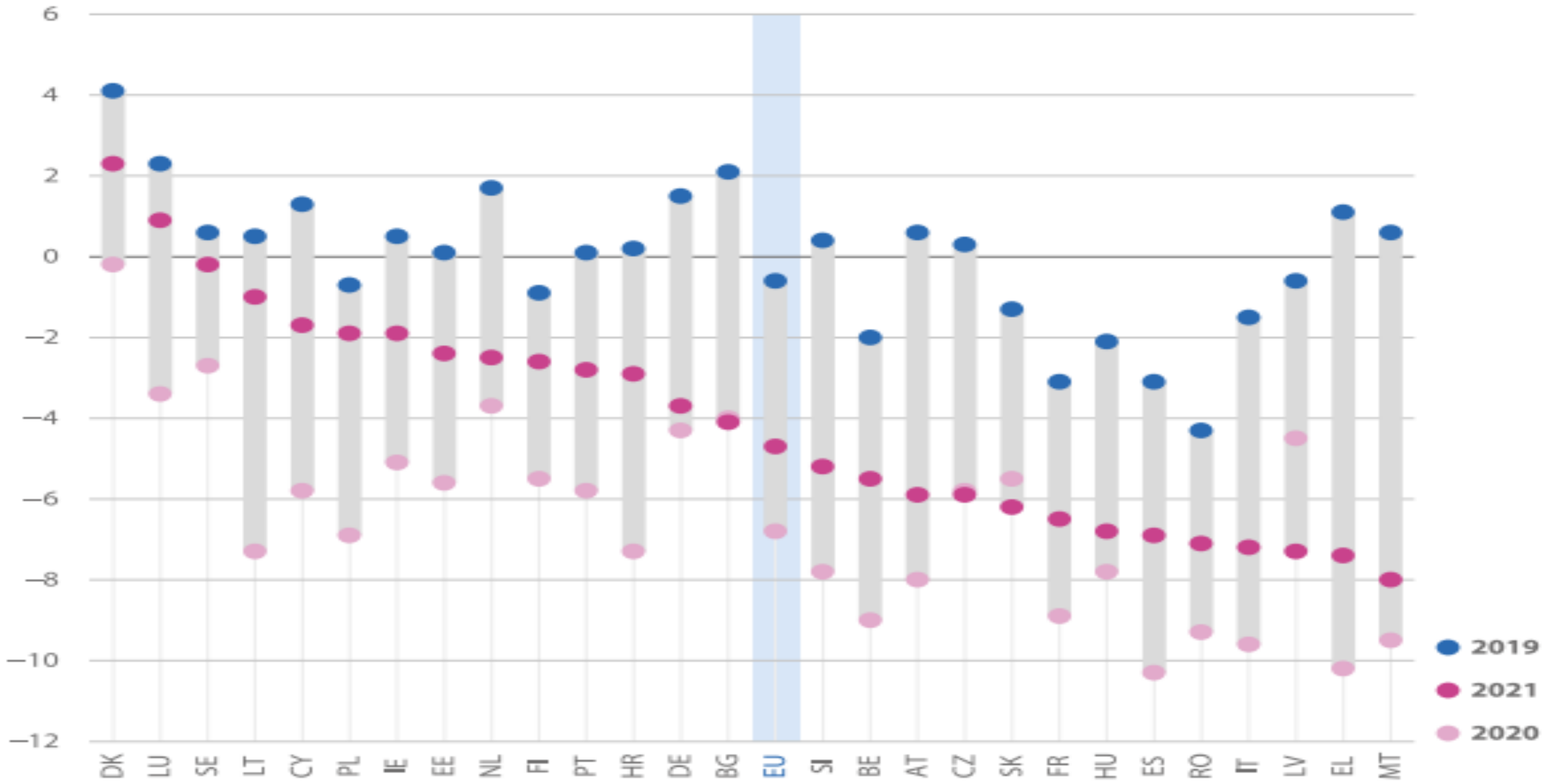


- NextGenerationEU (€750 billions)
  - European Resilience and Recovery Facility (€672.5 billions)
    - Loans (€360 billions)
    - Grants (€312.5 billions)
  - Recovery Support for Europe's Cohesion and Territories, REACT-EU (€47.5 billions)
  - Additional funds to European programmes or funds
    - Horizon Europe (€5 billions)
    - InvestEU (€5.6 billions)
    - Rural Development (€7.5 billions)
    - Just Transition Funds (€10 billions)
    - Resc EU (€1.9 billions)

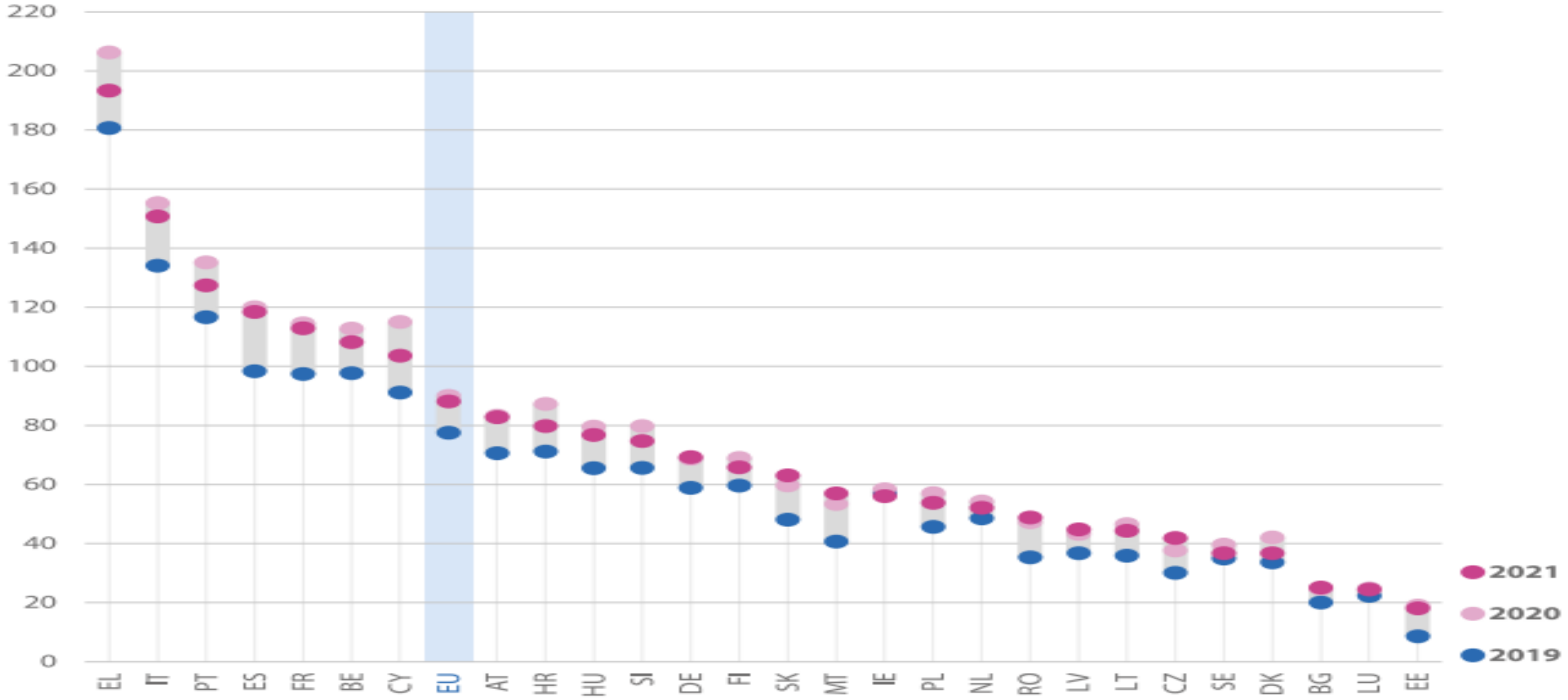
SGP SAFEGUARD CLAUSE (MARCH 2020-2023)

- Economic governance review was suspended in 2020 due to the pandemic.
- Objective: to enable national governments to implement stimulus measures for economic recovery due to the pandemic.
- European Commission (March 2021): "The decision to deactivate or maintain the general safeguard clause for 2022 should be taken as an overall assessment of the situation of the economy based on quantitative criteria. The main quantitative criterion would be the level of output in the EU or euro area compared to pre-crisis levels. The current preliminary indications suggest continuing to apply the general safeguard clause in 2022 and deactivating it from 2023."

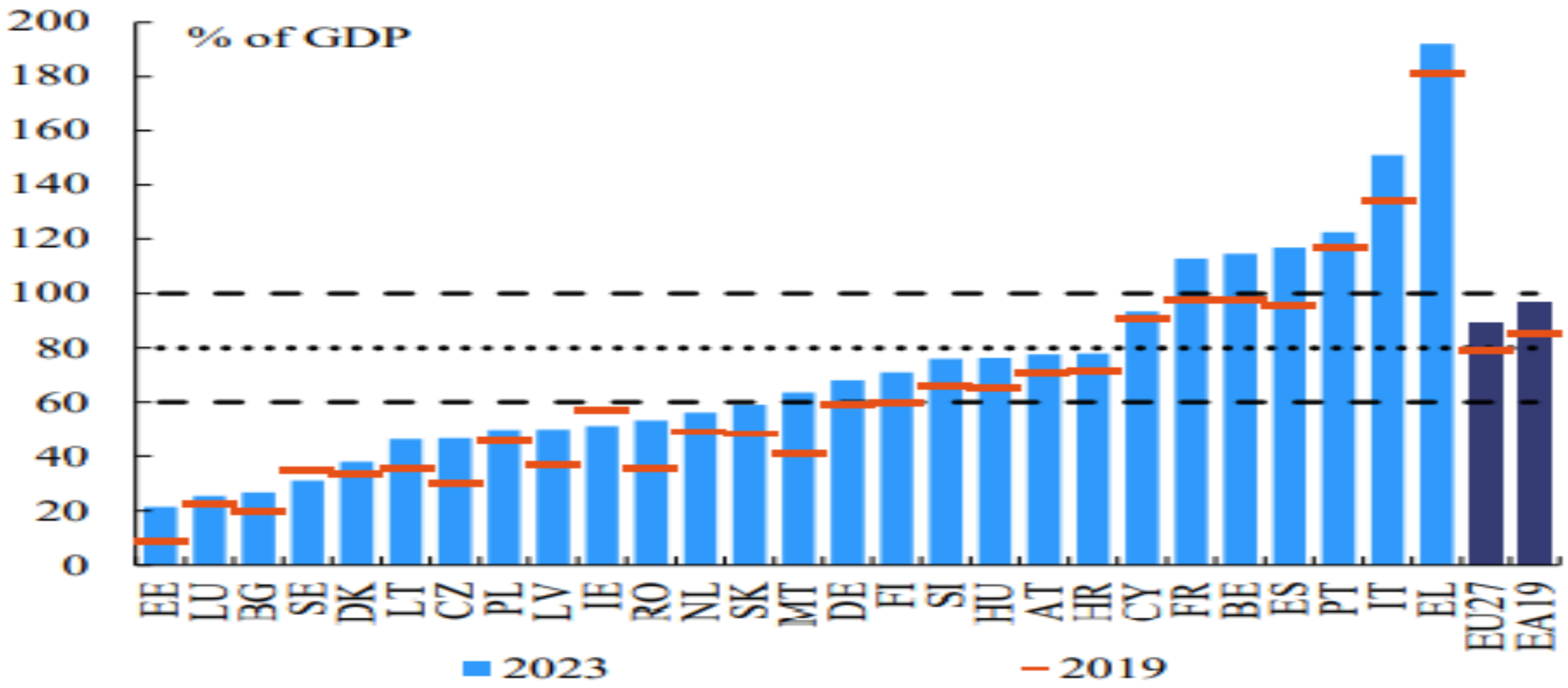
GOVERNMENT DEFICIT (%GDP)
SOURCE: EUROSTAT (2022)



PUBLIC DEBT (% GDP)
SOURCE: EUROSTAT (2022)



PUBLIC DEBT (% GDP)
SOURCE: EUROSTAT (2022)
NOTE: 2023 FORECASTS



ECONOMIC GOVERNANCE REFORM (SGP)

- Debate on the reform of fiscal rules (SGP)
- Different positions of Member States: frugal (Netherlands, Austria, Sweden, Denmark and Finland)/rest.

  - Germany: Dp is a problem in itself.

  - Italy:.

    - M. Draghi presented budgets with a deficit above 3% but with forecasts of high growth. **Economic growth is the most effective way to reduce debt.**

    - A highly indebted country, such as Italy, would have to reduce DP/GDP levels by 5% per year, negatively affecting economic growth.

ECONOMIC GOVERNANCE REFORM (SGP)

- The debate mainly revolves around the maximum levels of Dp/GDP allowed by the SGP.

Which measures promote growth, and are feasible, and which jeopardize debt sustainability?

AVOID WASTEFUL SPENDING

ECONOMIC GOVERNANCE REFORM (SGP)

- ESM economists: the level of Dp/GDP should go from 60% to 100% while maintaining a deficit at 3%.
- More investments in green economy.
- Replacement of the Golden Rule (unobservable variables and complex systems) by an expenditure rule (would limit spending in Member States).

The Golden Rule

Limit a government's ability to spend more than it collects. The growth of public debt is limited.

The EU sets a structural deficit limit of 0.5% of potential GDP.

If Dp/GDP is below 60%, the structural deficit is set at 1%.

ECONOMIC GOVERNANCE REFORM (SGP)

- The Commission has relaunched the debate when the economic recovery has taken hold

- A priori three scenarios were proposed:
  - Maintaining the JEP
  - Adaptation within the current framework
  - Full Review

ECONOMIC GOVERNANCE REFORM (SGP)

- November 2022. Communication from the European Commission on Economic Governance reform:
  - Strengthening debt sustainability
  - Sustainable and inclusive growth (investment and reforms)
  - Proposal: transparent and risk-based surveillance framework distinguishing between countries and taking into account their public debt challenges
    - Importance of Medium-Term Budgetary Objectives
    - Greater room for manoeuvre for the Member States

ECONOMIC GOVERNANCE REFORM (SGP)

Proposal for reform of Economic Governance (European Commission, Nov 2022)

The Commission presents a baseline budgetary adjustment path (four years). This path should ensure that the debt of Member States with significant or medium debt challenges is on a plausible downward trajectory, and that the deficit is credibly kept below the 3 % of GDP Treaty reference value.

The Member States present plans setting out their medium-term budgetary path, as well as priority commitments for reform and public investment. The Member States could propose a longer adjustment period, extending the fiscal adjustment path to three years when the path is underpinned by a set of reform and investment commitments that support debt sustainability and respond to the EU's common priorities and objectives.

The Commission assesses the plans, making a positive assessment whether debt is on a downward path or remains at prudent levels, and the budget deficit remains credibly below the medium-term 3% of GDP reference value. The Council approves the plans following a positive assessment by the Commission.

Member States submit annual reports on the implementation of the plans to facilitate effective monitoring and ensure transparency.

ECONOMIC GOVERNANCE REFORM (SGP)

- March 2023. The European Commission presents guidelines for the Member States on the implementation and coordination of tax policy for 2024 (in line with the guidelines it presented in November 2022). Adjusted to the current JEP.
  - Because uncertainty persists, no EDP decisions will be made this spring.

- End 2023. The safeguard clause of the SGP is deactivated.

- By 2024. The country-specific recommendations quantified and differentiated according to the public debt problems of each State are resumed.
  - EDPs would be activated in spring 2024, according to current legislation.

- The debate continues.

ECONOMIC GOVERNANCE REFORM (SGP)

- Status of the debate as of March 2023:
  - Convergence on several key issues:
    - The reference values of 3 % and 60 % of GDP in Protocol No 12 annexed to the Treaties should remain unchanged.
    - The medium-term structural budgetary plans prepared by Member States should be the cornerstone of the revised economic governance framework to ensure a sustained reduction of high debt ratios.
    - More effective enforcement of the rules, maintaining financial penalties but reducing their amount while strengthening their reputational impact.
    - Strengthen the debt-based Macroeconomic Imbalances Procedure. It is necessary to respect the principles to ensure national ownership and equal treatment and appropriate differentiation of budgetary efforts.
  - Further discussion is needed on the implementation of these principles.

CONCLUSIONS

- Incomplete Economic Union.
- Budgetary reinforcement in emergency situations. Insufficient MFP.
- Economic governance under review.
- Towards a greater democratic content.

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