economia e politica
Rivista online di critica della politica economica

Economia e Politica
Rivista online ISSN: 2281-5260
http://www.economiaepolitica.it

The appeal: Overcoming the Fiscal Compact for a new European development

We live in a period where Europe is faced with a real emergency, even if very few seem to have noticed it. A deadline is imminent, to which the press and politicians have paid very little attention, but which, in fact, has huge economic and social importance. Article 16 of the Fiscal Compact (or Intergovernmental European Budget Pact) declares that, within five years of its entry into force (i.e. by 1st January 2018), based on an evaluation of its implementation, the 25 signing European countries are required to take the necessary steps to incorporate the rules into the legal framework of the European Treaties.

On several occasions politicians from various backgrounds have expressed their impatience with the Pact; and legal experts attentive to community legislation have denounced the Pact as contrary to the principles enshrined in the European Treaties, and should therefore, in no way be incorporated into them or into European law. Moreover, already in 2013, on the basis of an Italian initiative, the Financial Times published the "The economists' warning", signed by some of the best known living economists, who described monetary unification as an experiment destined to implode without a profound revision of the whole set of rules, including those provided for by the Pact.

The debate on the integration of the Fiscal Compact into the EU Treaties or EU laws has been, therefore relatively sporadic with given the urgency of the impending deadlines, but at the same time has periodically become both inflammatory and quite intense. An in-depth analysis of its effective functioning and of the results produced does not seem have been seriously undertaken. Yet it is surely necessary to carry out a thorough assessment of the consequences of its implementation, and this should constitute a necessary precondition for any modification aiming at a possible integration of the pact into the European Treaties or Law. This is important since any hasty integration may well turn out to be inopportune.

We have no intention of replacing the political bodies that have the mandate to carry out such an evaluation, but we want to emphasize some aspects on which the Pact is simply wrong and counterproductive, and would mean that any institutional reinforcement of the whole Pact would be undesirable.

The first point is the need, which has been emphasized several times and by different participants in the political debate in the past, and already referred to by the Maastricht Treaty, to separate public investments from the calculation of deficits: a correction that, with respect to the purpose of ensuring economic stability and the growth of the Union, is much more relevant than those stemming from the possible widening of the deficit margin, foreseen by the Stability and Growth Pact (SGP). Just to mention a few data which reinforce this point: the ratio of investment to GDP contracted between 2007 and June 2017 by about 2 percentage points on average in the EU , by more than 3 points in the Eurozone, almost 5 points in Italy, 10 in Spain, and 17 in Greece. Even disregarding the debate on the size of the fiscal multipliers, it is clear to everyone that, in a crisis phase, national States have a duty to support, with the backing of the European Union, the economic activity and employment with robust structural measures, and not just anti-cyclical ones. This type of intervention, moreover, should be extended to cover public investment in human capital: if not all the public expenditure on education and research, which is possibly too encompassing, at least that for facilitating the use of basic research in productive activity and boosting the employment of research and technology workers.

A second critical aspect and that which is the subject of most discussion, is the obligation to balance structural public accounts. The principle presupposes first the regularity and equivalence in terms of positive and negative phases in the evolution of the economy, or at least the non-prevalence of the recessionary phases, which given the current state of the global economy is far from obvious. Second this would require indisputable methods of calculating the state of the economy with respect to its "potential" condition. The current procedure used by the European Commission does not satisfy either requirement; witness the fact that the OECD itself uses a very different calculation for estimating "potential GDP". For example, in the case of Italy the OECD procedure leads to much more favorable results, which the Italian Government has so far failed to explain to the Commission. In short, although it is not granted that it exists, a more reasonable and generally acceptable procedure of calculation of any overruns is necessary. In the absence of this the suspicion of being faced with unjustified burdens derived from an inconsistent economic "theory", and therefore wrong not only on their merits but also in the method of deriving them , will only be reinforced.

Even the obligation for countries with a debt above 60% of GDP to reduce the surplus by one twentieth each year is questionable. When it was established under the Maastricht Treaty, the 60% parameter was nothing more than the average value of the Union member States. Today, against the less than brilliant results of a quarter century of European economic policies, this average value has increased to 90%. Under these conditions, and in the face of even greater sovereign debt in Japan and the United States, more realistic objectives would be reasonable.

Moreover, this obligation – which has to be met irrespective of possible recessionary conditions – risks accentuating the debt problem.

Finally, in the current phase of significant reduction of the Quantitative Easing, the desirable openness at national and European level of a serious and in-depth discussion on the Fiscal Compact must also propose a reconsideration of the institutional mission of the ECB, which should be expanded to include, in addition to the stability of the euro, also the objective of minimizing unemployment. Just consider how much faster and stronger the recovery of employment would be, and how soon the same banking system could be strengthened, with the support of the market rather than the central bank, had an investment instrument like the slim Juncker Plan been financed by monthly figures amounting to only a tenth of the expenditure incurred for QE.

The prospect of embodying fiscal compact rules into the European Treaties seems to have disappeared since in early December 2017 the EU Commission has proposed simply to include them into the EU law – rather than into the Treaties - in a milder form that allows for some flexibility according to the rules of the SGP. Its directive will be submitted to the EU Parliament for approval. However, its incorporation into the EU law should also be resisted, as it entails some ambiguity (will the fiscal compact remain in force?) and can continue to reinforce the usual deflationary environment. It is our conviction that the necessary guarantee of flexibility – which under the SGP is decided by the EU Commission – could simply be ensured by the golden rule of public budgets, requiring the budget to be balanced only in its current account, but with no limit to public investment.

The double dip that has swept through the European economy in the last decade has shown – beyond any reasonable doubt – that it is precisely the whole European machine that needs deep structural reforms. As shown by recent studies carried out in the context of the International Labor Organization, these reforms must aim at a clear orientation of European and national economic policies towards a development model led by wages, domestic consumption and new investments, rather than insisting on a mercantilist model, problematic in terms of global equilibrium as well as incapable of ensuring progress, convergence and economic and social cohesion within the Union.

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