

AT A GLANCE

Policy Recommendations for the Euro Area and its Member States under the 2014 European Semester

On 4 September 2014, the Committee for Economic and Monetary Affairs (ECON) held an Economic Dialogue with the Eurogroup President. Three in-depth analyses were provided to Members in advance of this dialogue on **Fiscal and macro-structural challenges and policy recommendations for the Euro Area and its Member States under the 2014 Semester Cycle**. These papers were prepared by renowned experts, namely 1) [P. Bofinger](#); 2) [J.F. Kirkegaard](#) and 3) [D. Gross and C. Alcidi](#). This note summarises their main policy recommendations¹.

In the area of European Semester Cycle 2014

P. Bofinger:

- Country Specific Recommendations (CSRs) are not transparent as they are presented in a very vague form without numerical targets and often in a coded language.
- The CSRs lack a systematic framework for policy coordination. First, there is no comprehensive assessment of the challenges for macroeconomic targets. Second, the decisive issue of the aggregate fiscal policy stance is not addressed explicitly. Third, there is no discussion of whether individual countries could adjust their fiscal policies in order to generate a better, i.e. more symmetric, outcome for the whole system. Fourth, there is no awareness of potential negative spill-over effects from wage-related national structural reforms. The need of a symmetric adjustment process in the euro area is not reflected in the CSRs.
- The establishment of an Independent Council of Economic Experts (appointed by the European Parliament for a five year term) would improve the democratic accountability of the European Semester. It should have the task to present an annual report by the end of May which would analyse the main challenges to the euro area and identify the required policy response.

J.F. Kirkegaard:

- There is a need for euro area policy makers to sustain their recent crisis-induced reform eagerness to pull the region away from the threat of economic stagnation. The important policy challenge is to ensure that fiscal consolidation protects public investment spending.

D. Gross and C. Alcidi

- CSRs contain many generally accepted policy goals, but provide few indications, if any, on how to achieve these goals. Trade-offs are generally ignored or papered over by vague formulations that are difficult to operationalize such as ‘growth-friendly fiscal consolidation’.
- Too much emphasis is placed on investment as a pre-condition for sustainable growth. CEPS calculations suggest that as the growth rates of the working-age population decline, the required rate of investment in the euro area will fall by about 2.5 to 3.5 p.p. of GDP. This implies that part of the observed fall in investment since 2008 is likely to be permanent.
- Creating fast insolvency procedures to deal with excessive private sector debt is one overlooked priority for structural reforms. Excessive debt constitutes a millstone for households and small

¹ The full set of documents is available on EP homepage:

<http://www.europarl.europa.eu/committees/en/econ/publications.html?id=ECON00011#menuzone>.

enterprises as it remains legally in existence even if the banks had written it down on their balance sheets.

In the area of Banking Union

D. Gross and C. Alcidi:

- Completion of the banking union should remain a priority as many important details still need to be hammered out and in particular two specific issues related to financial stability: 1) How to deal with banks that according to the Asset Quality Review of the ECB fail to meet capital requirements – and cannot find needed capital on the market. In these cases delicate problems of state aid and systemic financial stability will arise and in extreme cases an intervention of the ESM might be required and 2) How to link the riskiness of individual banks to the contributions they have to make (indirectly) to the Single Resolution Fund.

J.F. Kirkegaard:

- There is a need to overhaul national bankruptcy procedures to facilitate private debt deleveraging and ensure the reduction of financial fragmentation in the euro area. While the Banking Union puts in place several important new institutions to integrate the euro area banking system, it will need to be complemented with national bankruptcy reforms to achieve its goal of comparable lending rates throughout the euro area and help the euro area private sector reduce its debt load to restore economic growth.

In the area of the role of the President of the Eurogroup

P. Bofinger:

- In order to avoid deflation, the President of the Eurogroup (PEG) should prepare the outline of a coordinated programme for public investments in the Member States as soon as possible.

J.F. Kirkegaard:

- The PEG should be made a full-time position, and the post could have its democratic legitimacy enhanced through an expansion of the Spitzenkandidat-framework to also include it. This proposal would require that the variable institutional geometry of the EU be extended to also the European Parliament. It would have to create a new euro area-only institutional setting, including a new euro area-only committee in front of which the PEG could regularly appear.
- The PEG should if Member State achievement of SGP fiscal consolidation goals and implementation of CSRs is in doubt publicly present a detailed list of required CSRs to be implemented in return for additional flexibility to be granted towards achieving SGP fiscal goals. Failure by a Member State government to achieve either CSR or fiscal target goals would with the public support of the PEG and the European Commission result in the immediate activation of the corrective elements of the SGP's excessive deficit procedure.
- The PEG should seek to promote such national ownership by involving as many national stakeholders as possible in the process, preferably through direct meetings held in the respective Member States.

D. Gross and C. Alcidi:

- On the macroeconomic side, the asymmetric adjustment within the euro area and the lack of sufficiently strong domestic demand growth in the core countries will of course remain a central policy challenge for the euro area, but there is little the PEG can do within the current institutional set up that would have any measurable impact on this problem.

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