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REPORT

on the long-term sustainability of public finances for a recovering economy
(2010/2038(INI))

Committee on Economic and Monetary Affairs

Rapporteur: Liem Hoang Ngoc

Rapporteur for the opinion (*):
Sergio Gaetano Cofferati, Committee on Employment and Social Affairs

(*) Associated committees - Rule 50 of the Rules of Procedure

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MOTION FOR A EUROPEAN PARLIAMENT RESOLUTION

on the long-term sustainability of public finances for a recovering economy (2010/2038(INI))

The European Parliament,

– having regard to the Commission staff working document of 12 August 2009 entitled 'Public Finances in EMU – 2009' (SEC(2009)1120),

– having regard to the Commission communication of 14 October 2009 entitled 'Long-term sustainability of public finances for a recovering economy' (COM(2009)0545),

– having regard to the Commission's recommendation of 28 January 2009 for a Council recommendation on the 2009 update of the broad guidelines for the economic policies of the Member States and the Community and on the implementation of Member States' employment policies (COM(2009)0034),

– having regard to its resolution of 18 November 2008 entitled 'EMU@10: The first 10 years of Economic and Monetary Union and future challenges'[1],

– having regard to its resolution of 11 March 2009 on a European Economic Recovery Plan[2],

– having regard to its resolution of 13 January 2009 on public finances in the EMU 2007-2008[3],

– having regard to its resolution of 9 July 2008 on the ECB annual report for 2007[4],

– having regard to the recommendations issued at the Pittsburgh Summit, calling for efforts to support growth to be sustained until recovery is assured,

– having regard to Rule 48 of its Rules of Procedure,

- having regard to the report of the Committee on Economic and Monetary Affairs and the opinions of the Committee on Employment and Social Affairs and the Committee on Budgets (A7-0147/2010)

A. whereas the Commission communication voices concerns about the long-term sustainability of public finances in the context of high deficit and debt levels, especially in the light of population ageing, and whereas the effect of ageing on the sustainability gap is calculated in most Member States to be five to 20 times higher than the effects of the current economic crisis,

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[1] OJ C 16 E, 22.1.2010, p. 8.
[2] Texts adopted, P6_TA(2009)0123.
[3] Texts adopted, P6_TA(2009)0013.
[4] Texts adopted, P6_TA(2008)0357.

B. whereas the Stability and Growth Pact (SGP), despite its revision in 2005, was not enough to prevent the current crisis,

C. whereas there is an urgent need to look in greater depth at the phenomenon of the falling birth rate in the European Union and its causes and implications, with a view to reversing this worrying trend,

D. whereas fiscal policy is not sustainable if it implies an excessive accumulation of government debt over time,

E. whereas, given the projections underpinning the communication and the fact that the ageing population will have serious impacts on the long-term sustainability of European countries' public finances, a policy horizon through 2060 is an appropriate one,

F. whereas the debt and deficit increases suffered by the Member States during the crisis and projected demographic developments will make fiscal sustainability an acute challenge,

G. whereas long-term demographic changes, in particular an ageing population, across the EU Member States have implications for the funding of national pension schemes,

H. whereas some Member States have not taken enough steps to reduce their administrative expenditure, bring their healthcare spending under control and reform their health and retirement systems, and whereas all the Member States should adopt the best practice in this area,

I. whereas all the Member States saw their deficits and debt ratios increase in 2009 as a result of the fall in tax revenue caused by the crisis and the implementation of special recovery measures,

J. whereas, in response to the first signs of a recovery, the European Council recommended in September 2009 that fiscal policies should be ‘reoriented towards the long-term sustainability of public finances’, and pointed out that ‘exit strategies need to be designed in a coordinated manner as soon as the recovery takes hold, taking into account the specific situation of individual countries’,

K. whereas in recent times it has been possible to see a positive correlation between sound public finances and the resilience of a country's economy,

L. whereas increasing government debt places a severe burden on future generations,

M. whereas government debt in some Member States has increased in a way that undermines stability and results in high government expenditure on interest payments at the expense of the increasingly important spending on health and pension systems,

N. whereas increased public borrowing distorts financial markets by pushing interest rates higher, with negative consequences for households as well as for investments in new jobs,

O. whereas a lack of effective statistical governance or independent statistical institutions in Member States is undermining the integrity and sustainability of public finances,

P. whereas other parts of the world which until recently were competing by producing low-quality goods are now entering the high-quality segments; whereas these competitors use advanced technology, whilst still paying moderate hourly wages and not having to grapple with adverse demographic trends, and against a background of individuals totalling a high number of working hours in their lifetimes; whereas in Europe full employment was last reached before the oil crisis of 1973, whereas full employment nevertheless remains an objective towards which the EU has to strive, in conformity with the spirit of the Treaties, without turning its back on its high level of social protection and human development,

Q. whereas there are various means to reduce the sustainability gap, such as increasing general productivity, and, most importantly increasing the productivity of the welfare services, raising the retirement age, increasing the birth rate or increasing the numbers of immigrants,

R. whereas population trends are shaped by changes in the fertility rate, which are to a large degree dependent on maternity incentives and benefits and migration flows,

S. whereas the current debt and deficit levels threaten the very existence of the welfare state,

T. whereas a failure to implement structural reforms and consolidate public finances will have an adverse effect on expenditure on health care, pensions and employment,

U. whereas many Member States are in breach of the SGP, and whereas proper compliance with it would have mitigated the negative effects of the crisis,

V. whereas the sustainability of public finances is not only crucial for Europe in general, but,also for the budget of the European Union specifically,

W. whereas, although the budget of the European Union is currently limited to approximately 1% of total European GNI, the general principles and underlying assumptions of 'sustainability' should also apply to it,

1. Expresses its deep concern about the long-term sustainability of public finances in the aftermath of the financial and economic crises; recalls that the efforts made in the framework of the SGP prior to the crises were to a very high degree geared towards meeting the growing demographic challenge; acknowledges that much of this effort has been wiped out by the need dramatically to increase government expenditure in order to prevent the worldwide meltdown of the financial system and to alleviate the social consequences of this meltdown;

2. Deplores the fact that, even before the crises started, a number of Member States' performance in consolidating their public finances were not impressive despite the fact that economic conditions were favourable; points out that this was a breach of the preventive arm of the SGP, especially after its redrafting in 2005, and one which seriously diminished Member States' capacity to act in a counter-cyclical way as the crises unfolded, leading to more uncertainty, higher unemployment and increased social problems;

3. Is aware that the current levels of public expenditure cannot be maintained indefinitely;

welcomes the European Council's decision to refrain from deciding on a follow-up package of help measures until the present one's results have been thoroughly analysed and the need for further action has been clearly demonstrated;

4. Acknowledges that the operations designed to prevent a meltdown of the financial sector were successful, although vigilance is still vital; expects the financial burden in relation to the rescue of the banking sector to decrease; lauds the central banks' coordinated approach to achieving this goal; is proud of the ECB's leading role in saving the banking sector; puts its full weight behind the reform of the system of prudential supervision and the redrawing of the framework of the financial architecture;

5. Emphasises that the SGP must aim for balance or surplus over time, requiring surplus in economic good times and pension schemes transparently financed in the framework of public budgets or by funded private schemes;

6. Points out that the long-term sustainability of public finances is essential for stability and growth, and for maintaining appropriate levels of public expenditure; stresses that high debt and deficit levels are a threat to sustainability and will have adverse effects on public health care, pensions and employment;

7. Expresses its deep concern at the high deficit and debt levels in the Member States; warns against using the crisis as a pretext not to consolidate public finances, not to decrease public spending and not to implement structural reforms, all of which are essential for a return to growth and employment;

8. Points out that the consolidation of public finances and the reduction of deficit and debt levels are essential to maintaining a modern welfare state and a system of redistribution which caters for society as a whole, but especially supports the less privileged parts of it;

9. Stresses that, if public debt and interest rates continue to increase, the costs in the form of interest rate payments will no longer be bearable by present and future generations without endangering welfare state models;

10. Is deeply concerned that many Member States are in breach of the SGP; deplores the fact that Member States failed to consolidate their public finances in economically favourable times before the crisis; agrees with the Commission statement that debt sustainability should be given a very prominent and explicit role in surveillance procedures; urges the Commission rigorously to ensure compliance with the SGP;

11. Warns against an abrupt ending of support to the real economy, in order to avoid a double dip; draws attention to the undesirable effects of either prematurely withdrawing support measures or waiting too long before taking corrective measures on the sustainability of public finances; points out that these measures were explicitly meant to be timely, targeted and temporary; welcomes the Commission's work on the exit strategy from the present contingency measures; supports the Commission's approach based on exit strategies that are differentiated between countries in time and scope; understands that the withdrawals from the measures will start in 2011 for the first batch of countries; encourages the Member States to do their utmost to implement the exit strategies as soon and as resolutely as possible;

12. Calls on the Commission to draw up a Green Paper on the birth rate in the European Union in order to identify the causes and implications of the falling birth rate, as well as solutions and alternatives regarding this problem;

13. Considers that the fiscal exit strategy should be launched before the monetary exit strategy in order to allow the latter to be correctly implemented, thus ensuring that the ECB, which successfully avoided a slip into deflation, can equally well ensure that inflation does not ruin the recovery; understands that the ECB has hinted that, in the absence of timely fiscal reining-in, its monetary tightening would regrettably have to be stronger than anticipated;

14. Emphasises that a decrease in financial stimulus must be combined with efforts to make the internal market more dynamic, competitive and attractive to investment;

15. Emphasises that a gradual and controlled exit from the deficits is of crucial importance in order to keep interest rates down and the debt burden limited, thereby safeguarding the ability to maintain welfare spending and standards of living for households;

16. Points out that low interest rates are conducive to investment and the recovery; is aware of the effects of a government's intense borrowing activities on interest levels; deeply deplores the fact that this has led to increased interest-rate spreads within the EU; warns Member States to take into account the effects of their budgetary decisions on market interest rates; is of the opinion that sound public finances are a prerequisite for secure jobs; points out that by driving up the cost of borrowing, governments also increase the burden on their own budgets;

17. Points out that the anti-cyclical effects of the SGP can only work if the Member States effectively achieve a budgetary surplus in good times; calls, in this connection, for the better implementation of the preventive arm or the SGP as well; calls for a shift from the 'spend first, repay later' attitude to a 'save for a possible future emergency' principle; recalls that the SGP requires the Member States to achieve a budget that is balanced or in surplus over the medium term, meaning that a deficit of 3% is not an aim, but the absolute limit allowed for, even under the revised Pact; warns decision-makers as well as businesses to get used to non-conventional fiscal and monetary measures and to expect these to become the norm;

18. Calls for structural reforms to be carried out in parallel to the unwinding of the aid packages in order to prevent future crises, increase the competitiveness of European businesses, achieve more growth and boost employment;

19 Emphasises, in the context of the need to achieve sound public finances, that in 2011 at the latest all Member States should start to reduce their sustainability gap by 1% of GDP yearly;

20. Acknowledges that fiscal stimulus and unfettered automatic stabilisers have proved to be successful and suggests that the Commission ask the Member States to strive towards a balanced budget by allocating primary budget surpluses to debt repayment once the economy is on the way to sustained recovery;

21. Points to the special importance of measures to promote employment and long-term

investments aimed at increasing the potential for economic growth and bolstering the competitiveness of the European economy;

22. Emphasises that, in view of the current demographic challenges the EU is facing, anti-crisis measures should not have long-term effects on public finances, the cost of which would have to be met by present and future generations;

23. Supports the idea that greater coordination of economic policies within the European Union is a must and brings additional synergies;

24. Acknowledges that the SGP is not a sufficient tool for harmonising the fiscal and economic policies of the Member States;

25. Supports, therefore, a review of the mechanisms needed to bring the national economies within the EU back on a convergence track;

26. Suggests that the Commission should draw up an appropriate mechanism for cooperation with the IMF in special cases where Member States receive balance-of-payments support from the latter;

27. Points out that high inflation is not an answer to the need for fiscal adjustment, because it would impose substantial economic costs and pose a threat to sustainable and inclusive growth;

28. Agrees with the Commission that 'successful fiscal expansion to counter recession and longer-term fiscal sustainability are not incompatible', but warns against the risks of excessive and artificial expansion based on higher public expenditure, which are liable to undermine the policy;

29. Takes the view that managing public finances on the basis of a series of specific short-term decisions will establish the long-term sustainability of public finances, and that it is within the scope of this series of short-term decisions, through the provision of a structure for the short term, that the issue of the sustainability of public debt must be addressed;

30. Takes the view that budgetary policy must, predominantly by means of reallocation, convert available savings into growth-boosting investment, such as investment in research and development, modernising the industrial base, developing a greener, smarter, innovative and more competitive EU economy and in rising to the challenge of education;

31. Emphasises that a substantial proportion of public-sector and welfare spending can be productive expenditure if it is directed towards projects that have a beneficial impact on the accumulation of physical and human capital and on the promotion of innovation; underlines the need to control the increase in the debt burden in order to ensure that rising interest-rate costs do not squeeze out crucial welfare spending; stresses that ever more scarce resources make it essential to improve the quality of public-sector spending;

32. Emphasises that the role of social protection systems as 'social safety nets' has proven particularly effective in times of crisis; underlines that stable public finances are a precondition for ensuring that this is also the case in the future;

33. Points out that the long-term sustainability of statutory pension schemes depends not only on population trends, but also on the productivity of the active population (which affects the potential growth rate), the effective retirement age and the proportion of GDP allocated to the financing of such schemes; stresses, further, that consolidating public finances and reducing of debt and deficit levels are important factors for sustainability;

34. Notes that changing demographics, especially an ageing population, mean that state pension schemes in many Member States have to be reformed from time to time, especially as regards the contributive base, so as to keep them financially sustainable;

35. Points out that the debt burden increases when real interest rates are higher than the GDP growth rate, and that markets assess risks as more serious when the debt burden increases;

36. Takes the view that interest rates for government borrowing reflect how markets value the debt sustainability of a Member State;

37. Points out that rising deficits make borrowing more expensive, partly due to the fact that markets assess risks as more serious when the debt burden is increasing faster than economic growth and the ability to pay back loans;

38. Stresses that the current financial crisis has emphasised in the clearest possible way the direct link between financial market stability and the sustainability of public finances; emphasises, in that context, the need for strengthened and integrated supervisory legislation on financial markets that include strong mechanisms for consumer and investor protection;

39. Asks the Commission to carry out studies to assess the quality of the Member States' debts;

40. Notes that if Member State public finances are to be credible, effective and genuinely independent statistical governance and proper Commission oversight are required;

41. Suggests, in particular, that the Commission assess the effects of the fiscal spending deployed by the Member States in order to kick-start their economies, in terms of its impact on production, on government accounts and in stimulating and protecting employment, both in the short and long term;

42. Notes that the SGP still forms the backbone of discipline required to achieve the long-term sustainability of public finances and that the Member States should run surpluses on their public finances in 'good times' and deficits only in 'bad times';

43. Stresses that recent speculative attacks against several European economies had as their primary target the euro itself and European economic convergence; in that sense, is convinced that European problems need European solutions, which should offer internal means of avoiding any risk of defaults by combining national fiscal discipline with last-resort mechanisms of financial support;

44. Calls for the structural deficit to be one of the indicators used in determining the long-term sustainability of public finances;

45. Regards a renewed growth and jobs strategy as a key contributor to sustainable public finances in the European Union; believes that the European Union needs to modernise its economy and particularly its industrial base; calls for a reallocation of funding in the EU and the Member States' budgets towards greater investment in research and innovation; points out that the new Europe 2020 strategy needs binding instruments to succeed;

46. Highlights the need for the sustainability of public finances in EU Member States to be constantly monitored in order to assess the extent of long-term challenges; also highlights the need for the regular publication of information on open public-sector liabilities and the liabilities of social systems, e.g. pension schemes;

47. Calls on the Commission to consider the reduction of long-term sustainability gaps in public finances as an essential part of the EU 2020 strategy;

48. Calls on the Member States, after plugging their sustainability gaps, to reduce their public debt-to-GDP ratio to a maximum of 60%;

49. Points out that the interest rate spreads on the capital markets are the main indicators of the solvency of individual Member States;

50. Is extremely worried about the disparities in the quality of statistics that can be observed in the EU in general and in the eurozone in particular;

51. Points out that the long-term sustainability of public finances is also fundamentally linked to the EU budget and its financing;

52. Highlights the very positive role of the EU budget, albeit much limited by the MFF, in mitigating the effects of the crisis through the financing of the European Recovery Plan and the redeployment of funds towards priority areas in that regard; deplores, however, the lack of adequate coordination between Member States' economic and fiscal policies to combat the economic and financial crisis as well as to ensure the long-term sustainability of public finances;

The social and employment dimension of the crisis exit strategy

53. Notes that the increase in unemployment and government debt and the reduction in growth caused by the economic crisis are at odds with the sustainable public finance objective; notes the need for the Member States to consolidate their accounts and improve the liquidity of public finance in order to lower the cost of debt, but also the need for this to be done in a balanced way and within a reasonable time frame, taking into account the particular circumstances in the Member States; stresses, however, that indiscriminate cuts in public investment, research, education and development will have a negative impact on prospects for growth, employment and social inclusion, and considers, therefore, that long-term investment in these areas must continue to be promoted, and where necessary expanded;

54. Emphasises that the current recovery is still fragile and that unemployment is continuing to rise in most Member States, with young people especially hard hit; firmly believes that no end can be announced to the economic crisis until unemployment falls substantially

and sustainably and highlights the fact that the European welfare states have demonstrated their value in providing stability and contributing to the recovery;

55. Regards it as essential to assess properly the social and employment-related effects of the crisis and to formulate at EU level a recovery strategy based on support for employment, training, investments that lead to high economic activity, the boosting of business competitiveness and productivity, especially for SMEs, and the revitalisation of industry, whilst ensuring its transition towards a competitive sustainable economy; believes that these objectives should be at the heart of the Europe 2020 strategy;

56. Takes the view that the economic recovery strategy should under no circumstances give rise to fresh structural imbalances and major income disparities, which are holding back productivity and competitiveness in the economy, but should rather introduce the reforms needed to tackle such imbalances; considers that the financial and fiscal measures taken by the Member States should protect salaries, pensions, unemployment benefits and households' purchasing power without jeopardising the long-term sustainability of public finances or Member States' capacity to provide essential public services in the future;

57. Notes that the population ageing forecast in the coming decades poses an unprecedented challenge for the EU countries; takes the view, therefore, that the anti-crisis measures should not, in principle, have long-term consequences for public finances and overburden future generations with the repayment of current debts;

58. Stresses the importance of linking economic recovery with targeted policies to address structural unemployment, in particular unemployment among young people, older people, disabled people and women, with a view to increasing quality employment, thereby enhancing the productivity of both labour and investment; in this respect, considers policies to improve the quality of human capital, such as education, or healthcare policies aimed at developing a more productive and longer-working workforce and policies aimed at lengthening the duration of professional activity, to be important; calls on the Member States and the Commission to strengthen their employment and labour-market policies and measures, placing them at the heart of the Europe 2020 strategy;

The impact of demographic change and the employment strategy

59. Considers that the sustainability of public finances depends largely on the ability to raise employment levels to meet demographic and budget-related challenges, with particular reference to the sustainability of pension schemes; takes the view that the existing European human capital can be supported in the medium term by appropriate migration policies leading to the integration of migrants into the labour market and the award of citizenship;

60. Stresses that increased levels of employment are essential if the EU is to cope with an ageing population, and emphasises that high labour market participation is a precondition for economic growth, social integration and a sustainable and competitive social market economy;

61. Takes the view that the Europe 2020 strategy should take the form of a 'pact on economic, employment and social policy' aimed at sustaining the competitiveness of the

European economy and focused on labour market integration for all, i.e. one that best protects citizens from social exclusion; stresses that all policies should be mutually reinforcing so as to achieve positive synergies; takes the view that the strategy should be based on guidelines, and where possible indicators and benchmarks that are measurable and comparable both nationally and at EU level, backed up by bonus mechanisms for those who meet the targets and corrective mechanisms for those who do not, respecting flexicurity principles and the social dialogue method;

The sustainability of social protection systems

62. Considers that a public-finance policy coordinated at EU level and geared to sustainable growth, quality employment and the adoption of the reforms needed to ensure the viability of social-welfare systems is one of the necessary responses to the consequences of the financial, economic and social crisis and the challenges posed by demographic changes and globalisation;

63. Points out that the long-term equilibrium of statutory pension schemes depends not only on population developments, but also on the productivity of those in work, which influences the potential growth rate, as well as on the proportion of GDP reserved for financing those schemes;

64. Stresses the importance of the imminent Green Paper on pension reform, and considers that the development of sustainable, secure, well-diversified pension systems with different sources of financing which are linked to labour-market performance or the financial markets and could take the form of company schemes, and which involve public, supplementary employer-based and individual schemes, is vital and should be encouraged contractually and fiscally; recognises, therefore, the importance of pension literacy among EU citizens;

65. Emphasises that, in the long term, implicit pension liabilities make up one of the largest parts of the total public debt, and that the Member States should regularly publish information on their implicit pension liabilities, following the commonly agreed methodology;

66. Takes the view that the need for both sustainable public finances and adequate social welfare and inclusion schemes means that the quality and efficiency of administration and of public expenditure needs to be raised, and that Member States should be encouraged to consider measures which ensure that the tax burden is shared more equally by means of a gradual, incisive reduction of the tax burden on employment and on SMEs; takes the view that this could help to reduce poverty, guarantee social cohesion and boost economic growth and productivity, which are key factors in the competitiveness and sustainability of the European economic and social model;

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67. Instructs its President to forward this resolution to the Council, the Commission, the ECB and the governments of the Member States.

EXPLANATORY STATEMENT

1. Coordinating counter-cyclical policies and structural reforms

The implementation of budgetary policy is a key component of the Member States' economic policies. The Stability and Growth Pact limits their freedom to pursue discretionary policies. The 2005 revised pact sets out exceptional circumstances in which those limits may temporarily be overstepped in order to allow automatic stabilisers to function. Indicators of a 'recovering economy' must now be identified in order to determine the exact point at which exit measures should be deployed. Economists agree that an economy with full employment is one in which production capacity is saturated. In practice, this situation arises when the rate of utilisation of capital resources exceeds 85%. Budgetary and monetary stimulus measures may therefore be deemed necessary below a certain growth rate.

As far as the economic situation in the European Union is concerned, 2009 saw a drop in production and very low production capacity utilisation rates (71% on average). The recovery is particularly fragile in that it is based on firms' rebuilding of stocks and a slight upturn in exports. In most of the Member States, consumption is stagnating and investment remains low as a result of the drop in orders. This is reducing European economies' growth potential.

The Commission could consequently apply a simple rule in order to determine the point at which exit strategies should be stepped up. As long as production capacity utilisation rates are lower than normal, non-conventional measures should be maintained. As soon as the economy reaches this point, measures aimed at ensuring a return to budgetary balance (such as using primary budget surpluses for debt repayment) may be recommended.

2. Towards a sustainability criterion for public finances

The Commission communication acknowledges the need to maintain non-conventional measures until the economy has recovered, and raises the issue of the long-term sustainability of public finances.

Even so, as the communication and its companion report emphasise, 'there is no one clear-cut definition of a sustainable fiscal position'[1] and 'there is no defined upper limit to sustainable debt levels. Limits to sustainability differ across countries and time.'[2] The Commission nevertheless attempts to suggest a sustainability criterion such that debt does not sap 'the government's capacity to deliver the necessary public services (...) and ability to adjust policy in response to new challenges'. It is concerned about the adverse impact on growth potential and government deficits of population ageing and the rise in welfare spending.

The Commission communication attempts to establish the likely trajectory between now and 2060 in terms of the proportion of expenditure and taxes that the EU Member States will have

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[1] Companion report to the Communication from the Commission to the European Parliament and the Council on the Long-term Sustainability of Public Finances for a Recovering Economy, 14 October 2009.
[2] Communication from the Commission to the European Parliament and the Council on the Long-term Sustainability of Public Finances for a Recovering Economy, 14 October 2009.

to commit in order to keep government debt below the acceptable limit of 60% of GDP throughout that period.

The projections underpinning the Commission communication are based on assumptions that will inevitably change over a lengthy period of time. The long-term growth rate is affected by a succession of short-term business investment decisions, which themselves depend on the economic situation and the discretionary policies pursued by the authorities. Good macroeconomic policies are likely to increase the potential growth rate and relax constraints on financing social protection systems. In addition, population trends depend on fluctuations in fertility rates and migration flows. Lastly, the constraints on financing welfare spending depend on society's demand for public goods and the degree to which compulsory contributions are acceptable. Such demand is considerable in some Member States, and has not necessarily sapped their economic dynamism in the past. The effectiveness of the 'social safety nets' associated with the European social model is now acknowledged, and they are particularly useful in times of crisis. For that matter, they could be extended and updated by redefining their scope and financing base.

It is in the context of this succession of short-term decisions that the issue of government debt must be raised. Deficits are desirable where there is an imbalance between savings and investment. In such cases, public policy must tap available savings by means of borrowing, in order to finance investment expenditure. Such an imbalance was already present in embryonic form well before the onset of the October 2008 cash crisis; the EU experienced negative growth from the second quarter of 2008, and growth in the euro area has remained below its potential rate since the start of the decade.

In order to kick-start investment, budgetary policy is desirable in those Member States beset by excess saving. Deficits are sustainable as long as financing them does not put pressure on interest rates on government borrowing or entail the transfer to taxpayers of an intolerably large debt burden. The debt burden rises when real interest rates exceed the economic growth rate. Accordingly, when interest rates are low, they are the main criterion for measuring the sustainability of short-term debt.

The Member States' borrowing capacity also depends on the attitude of credit-ratings agencies. Recent experience shows that such agencies may under- or over-estimate risks. They will grant an AAA rating only if the state contracting the debt is solvent. A state will receive a higher rating if its debt is used to finance deficits that stimulate growth and future tax revenue. Accordingly, it is important for the Commission to carry out studies that will afford a basis for assessing the quality of the Member States' debts, and to sanction any Member State that may be tempted to overestimate its growth in order to build up a recessionary deficit on the sly.

3. Identifying good and bad debt

Following the Commission's recommendations, when the euro was introduced the Member States undertook to reduce their administrative expenditure and reform their pension systems. The crisis has meant that all the Member States saw their deficits and indebtedness increase significantly in 2009.

The deployment of recovery measures is not the sole reason for their increased deficits. One cause is the automatic downturn in tax revenue, and another is the effectiveness of budgetary policies, as measured on the basis of whether they have achieved the objectives set. A large deficit can finance economic expansion, generating tax revenue and promoting a return to budgetary equilibrium. This is the rationale for the ‘non-conventional’ stimuli recommended by the Commission.

On the other hand, poorly calibrated tax incentives may have a minimal effect on growth. At the same time, such tax expenditure further increases public debt, leading to *recessionary deficits*. The burden of bad debt weighs on households with no propensity to save, which service the debt without any return. Given that deficits weigh most heavily on those households worst hit by the crisis, recessionary deficits must be identified and neutralised as a matter of urgency.

4. What about the Stability Pact?

When the Maastricht Treaty was drafted, the permissible deficit and debt levels were determined by calculating the average deficit and indebtedness of the countries in the European Monetary System. The 2005 revised Stability Pact amounts to the implicit adoption of the principles underpinning a counter-cyclical macroeconomic policy. Such principles seem particularly appropriate when it comes to ensuring the long-term sustainability of public finances. The Commission could explicitly enshrine the rule of counter-cyclical management. It should then make sure its recommendations are compatible with that principle, by avoiding setting overly short deadlines for a return to budgetary equilibrium.

As regards criteria for measuring the long-term sustainability of public finances, the structural deficit indicator is particularly suitable for a long-term assessment in that it measures the state of public finances irrespective of cyclical effects. Lastly, an indicator of structural debt – the ‘government debt-to-assets’ ratio or the ‘net debt-to-GDP’ ratio – could be used to measure the Member States’ solvency.

22.3.2010

OPINION OF THE COMMITTEE ON EMPLOYMENT AND SOCIAL AFFAIRS

for the Committee on Economic and Monetary Affairs

on the long-term sustainability of public finances for a recovering economy
(2010/2038(INI))

Rapporteur (*): Sergio Gaetano Cofferati

(*) Associated committee – Rule 50 of the Rules of Procedure

SUGGESTIONS

The Committee on Employment and Social Affairs calls on the Committee on Economic and Monetary Affairs, as the committee responsible, to incorporate the following suggestions in its motion for a resolution:

1. Notes that the increase in unemployment and government debt and the reduction in growth caused by the economic crisis are at odds with the sustainable public finance objective; notes the need for the Member States to consolidate their accounts and improve liquidity of public finance to lower the cost of debt but also the need for this to be done in a balanced way and within a reasonable time frame, taking into account the particular circumstances in the Member States; stresses, however, that indiscriminate cuts in public investments, research, education and development have a negative impact on prospects for growth, employment and social inclusion, and consequently considers that long-term investments in these areas must continue to be promoted, and where necessary expanded;

2. Underlines that the current recovery is still fragile and that unemployment is continuing to rise in most Member States, with young people especially hard hit; firmly believes that no end can be announced to the economic crisis until unemployment falls substantially and sustainably and highlights the fact that the European welfare states have demonstrated their value in providing stability and contributing to the recovery;

The social and employment dimension of the crisis exit strategy

3. Considers it necessary to asses appropriately the social and employment-related effects of the crisis and to formulate at EU level a recovery strategy based on support for employment, training, investments that lead to high economic activity, the boosting of business competitiveness and productivity, especially for SMEs, and the revitalisation of industry while ensuring its transition towards a competitive sustainable economy; believes that these objectives should be at the heart of the Europe 2020 strategy;

4. Takes the view that the economic recovery strategy should under no circumstances give rise to fresh structural imbalances and major income disparities, which are holding back productivity and competitiveness in the economy, but should rather introduce the reforms needed to tackle such imbalances; considers that the financial and fiscal measures taken by the Member States should protect salaries, pensions, unemployment benefits and households' purchasing power without jeopardising the long-term sustainability of public finances or Member States' capacity to provide essential public services in the future;

5. Notes that the population ageing foreseen in the coming decades poses an unprecedented challenge for the EU countries; therefore the anti-crisis measures should not, in principle, cause long-term consequences for public finances and overburden future generations with repayment of the current debts;

6. Stresses the importance of linking economic recovery with targeted policies to address structural unemployment, in particular unemployment among young people, older people, disabled people and women, with a view to increasing quality employment, thereby increasing the productivity of both labour and investment; in this respect, considers policies improving the quality of human capital, such as education, or health care policies aimed at developing a more productive and longer-working workforce and policies aimed at lengthening the duration of professional activity, to be important; calls on the Member States and the Commission to reinforce their policies and measures for employment and the labour market, placing them at the heart of the Europe 2020 strategy;

The impact of demographic change and the employment strategy

7. Considers that the sustainability of public finance depends largely on the ability to raise employment levels to meet demographic and budget-related challenges, with particular reference to the sustainability of pension schemes; the existing European human capital can be supported in the medium term by appropriate migration policies leading to integration of migrants into the labour market and citizenship;

8. Stresses that increased levels of employment are essential for the EU to cope with an ageing population and emphasises that high labour market participation is a precondition for economic growth, social integration and a sustainable and competitive social market economy;

9. Takes the view that the 2020 strategy should take the form of a 'pact on economic, employment and social policy' aimed at sustaining the competitiveness of the European economy and focused on labour market integration for all, that best protects citizens from social exclusion; stresses that all policies should support each other to achieve positive synergies; the strategy should be based on guidelines, and where possible indicators and benchmarks that are measurable and comparable both nationally and at EU level, backed

up by bonus mechanisms for those who meet the targets and corrective mechanisms for those who do not, respecting flexicurity principles and the social dialogue method;

The sustainability of social protection systems

10. Considers that a public finance policy that is coordinated at EU level and geared to sustainable growth, quality employment and the adoption of the reforms needed to ensure the viability of social welfare systems is one of the necessary responses to the consequences of the financial, economic and social crisis and the challenges posed by demographic changes and globalisation;

11. Recalls that the long-term equilibrium of compulsory pension schemes depends not only on population developments but also on the productivity of those in work, who influence the potential growth rate, as well as on the proportion of GDP reserved for financing those schemes;

12. Stresses the importance of the imminent Green Paper on pension reform and considers that the development of sustainable, secure, well-diversified pension systems with different sources of financing which are linked to labour market performance or financial markets and could take the form of company schemes, and involving public, supplementary employer-based and individual schemes, is vital and should be encouraged contractually and fiscally; therefore, recognises the importance of pension literacy among EU citizens;

13. Underlines that, in the long term, implicit pension liabilities are one of the largest parts of the total public debt, and that the Member States should regularly publish information on their implicit pension liabilities, following the commonly agreed methodology;

14. Takes the view that the need for both sustainable public finances and adequate social welfare and inclusion schemes means that the quality and efficiency of administration and of public expenditure needs to be raised, and Member States should be encouraged to consider measures to ensure the tax burden is shared more equally by means of a gradual, incisive reduction of the tax burden on employment and on SMEs; this could help to reduce poverty, guarantee social cohesion and boost economic growth and productivity, which is a key factor in the competitiveness and sustainability of the European economic and social model.

RESULT OF FINAL VOTE IN COMMITTEE

Date adopted	17.3.2010
Result of final vote	+: 34 –: 5 0: 2
Members present for the final vote	Regina Bastos, Edit Bauer, Pervenche Berès, Milan Cabrnoch, David Casa, Alejandro Cercas, Ole Christensen, Derek Roland Clark, Sergio Gaetano Cofferati, Marije Cornelissen, Karima Delli, Proinsias De Rossa, Frank Engel, Sari Essayah, Ilda Figueiredo, Pascale Gruny, Thomas Händel, Marian Harkin, Roger Helmer, Nadja Hirsch, Stephen Hughes, Danuta Jazłowiecka, Martin Kastler, Patrick Le Hyaric, Veronica Lope Fontagné, Olle Ludvigsson, Elizabeth Lynne, Thomas Mann, Elisabeth Morin-Chartier, Siiri Oviir, Rovana Plumb, Joanna Katarzyna Skrzydlewska, Jutta Steinruck, Traian Ungureanu
Substitute(s) present for the final vote	Jürgen Creutzmann, Julie Girling, Richard Howitt, Dieter-Lebrecht Koch, Ria Oomen-Ruijten, Evelyn Regner, Csaba Sógor, Emilie Turunen

9.4.2010

OPINION OF THE COMMITTEE ON BUDGETS

for the Committee on Economic and Monetary Affairs

on long-term sustainability of public finances for a recovering economy
(2010/2038(INI))

Rapporteur: Ivailo Kalfin

SUGGESTIONS

The Committee on Budgets calls on the Committee on Economic and Monetary Affairs, as the committee responsible, to incorporate the following suggestions in its motion for a resolution:

A. whereas the Stability and Growth Pact (SGP), despite its revision in 2005, did not suffice to prevent the current crisis,

B. whereas sustainability of public finances is not only crucial for Europe as a whole but, also, for the budget of the European Union specifically,

C. whereas, although the budget of the European Union is currently limited to approximately 1% of total European GNI, the general principles and underlying assumptions of 'sustainability' should also apply to it,

1. Supports the idea that greater coordination of economic policies within the European Union is a must and brings additional synergies;

2. Admits that the SGP is not a sufficient tool for harmonising the fiscal and economic policies of the Member States;

3. Supports therefore a review of the mechanisms to bring the national economies within the EU back on a convergence track;

4. Considers that the review of the targets and mechanisms for convergence of the national economies should be carried out as soon as possible, including by considering the creation of a European monetary fund, in order to define, inter alia, the possible effects of increasing the European added value of the EU budget;

5. Points out that long-term sustainability of public finances is also fundamentally linked to the EU budget and its financing;

6. Recalls that, in its present unsatisfactory form, as much as 70% of the Union's financing comes not from own resources but directly from the national budgets as 'contributions' through the GNI resource; reiterates its worry that crises, that may or may not have arisen due to unsustainable policies, are easily blamed on the Union with budget contributions being seen as an 'additional burden' for national budgets rather than appreciating the joint benefits and the European value added;

7. Highlights the very positive role of the EU budget, although much limited by the MFF, in mitigating the effects of the crisis through financing the European Recovery Plan and the redeployment of funds towards priority areas in that regard; regrets however the lack of sufficient coordination between Member States' economic and fiscal policies to combat the economic and financial crisis as well as to ensure the long-term sustainability of public finances;

8. Takes the view that credit-rating agencies alone should not be responsible for rating sovereign debt, a task which would be more effectively achieved through creating a mechanism for an additional assessment of the fair value of such debts and through increasing the role of Eurostat in providing reliable data;

9. In this respect, encourages efforts to stimulate the channelling of savings available into coordinated investment expenditure through fiscal policies;

10. Suggests that the Commission should set an appropriate cooperation mechanism with the IMF in special cases where Members States receive balance-of-payments support from the latter;

11. Recalls that high inflation is not an answer to the need for fiscal adjustment, because it would impose substantial economic costs and pose a threat to sustainable and inclusive growth.

RESULT OF FINAL VOTE IN COMMITTEE

Date adopted	8.4.2010
Result of final vote	+: 34 –: 1 0: 1
Members present for the final vote	Damien Abad, Alexander Alvaro, Marta Andreasen, Francesca Balzani, Reimer Böge, Andrea Cozzolino, Jean-Luc Dehaene, Isabelle Durant, James Elles, Göran Färm, José Manuel Fernandes, Eider Gardiazábal Rubial, Jens Geier, Estelle Grelier, Jiří Havel, Monika Hohlmeier, Anne E. Jensen, Ivailo Kalfin, Jan Kozłowski, Alain Lamassoure, Vladimír Maňka, Barbara Matera, Claudio Morganti, Dominique Riquet, Sergio Paolo Francesco Silvestris, László Surján, Helga Trüpel, Daniël van der Stoep, Derek Vaughan, Angelika Werthmann
Substitute(s) present for the final vote	François Alfonsi, Frédéric Daerden, Gerben-Jan Gerbrandy, Riikka Manner, Paul Rübig, Georgios Stavrakakis, Theodor Dumitru Stolojan

RESULT OF FINAL VOTE IN COMMITTEE

Date adopted	4.5.2010
Result of final vote	+: 25 –: 6 0: 15
Members present for the final vote	Udo Bullmann, Pascal Canfin, Nikolaos Chountis, George Sabin Cutaş, Leonardo Domenici, Derk Jan Eppink, Diogo Feio, Elisa Ferreira, Vicky Ford, José Manuel García-Margallo y Marfil, Jean-Paul Gauzès, Sven Giegold, Sylvie Goulard, Enikő Győri, Liem Hoang Ngoc, Gunnar Hökmark, Wolf Klinz, Jürgen Klute, Astrid Lulling, Hans-Peter Martin, Arlene McCarthy, Ivari Padar, Alfredo Pallone, Anni Podimata, Antolín Sánchez Presedo, Olle Schmidt, Edward Scicluna, Peter Simon, Peter Skinner, Theodor Dumitru Stolojan, Ivo Strejček, Ramon Tremosa i Balcells, Corien Wortmann-Kool
Substitute(s) present for the final vote	Marta Andreasen, Sophie Auconie, Lajos Bokros, David Casa, Sari Essayah, Carl Haglund, Iliana Ivanova, Thomas Mann, Gay Mitchell, Sirpa Pietikäinen, Andreas Schwab
Substitute(s) under Rule 187(2) present for the final vote	Trevor Colman, Monika Hohlmeier