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"Fiscal Compact", Sovereignty and Austerity

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While it accounts for only six of the sixteen articles in the "Treaty on Stability, Coordination and Governance"[1] which is due to come into force in the autumn, the European "Fiscal Compact" is arousing contradictory expectations and attracting conflicting criticism which it is worthwhile exploring in greater depth with regard to the concepts of stability, sovereignty and austerity.

1 – A compact symbolising the Europeans' economic and financial interdependence

The current crisis reminds us Europeans that sharing a single currency implies compliance with certain common disciplines, because excessive imbalances in a country's public and private accounts have a negative impact both on neighbouring countries and on the euro zone as a whole.

The reform of the Stability and Growth Pact ratified by the Council and Parliament in late 2011 has led to a strenghtening of those disciplines' scope and application. It allows member states to more easily preempt and sanction breaches committed by one or other country as identified by the Commission. A new "highway code" is thus already in force in the budgetary area and it has been accompanied by the creation of more sophisticated and more automatic detector radars than in the past – a crucial safeguard to ensure that there are no more accidents or chances of "careering off the road".

In this context, the "Fiscal Compact" is basically designed to proclaim in an even more symbolic manner the member states' earnest in the handling of their accounts, in return for acts of European solidarity[2] which have become necessary on account of the crisis. Its technical added value is basically the building of a "golden rule" limiting member states' "structural deficit" to 0.5% of their GDP into their national constitutions or equivalent (Article 3), as well as a commitment to cut public debts by an average of one-twentieth per year when those debts top 60% of GDP (Article 4). Less revolutionary than they may sound, these two measures are also designed to highlight the pledge by all of the euro-zone member states to adopt a more stringent line than they have in the past (to the point where some of them found themselves on very shaky ground when the crisis hit...).

2 – A safeguard controlling the abuse of public accounts, not their substance

Like the Stability and Growth Pact, the "Fiscal Compact" simply provides a framework for breaches in the field of public debts and deficits. Naturally, it does not prevent its 25 signatory states from maintaining full sovereignty over the determination of the level and shareout of their public spending or the manner in which they fund that spending. On the path to monetary union, each country then remains free to choose the size, power, configuration and colour of its vehicle.

Thus, public spending in 2011 accounted for 38% of GDP in Estonia and Slovakia, almost 46% of GDP in Germany and 56% of GDP in France. This variety evinces national choices which are different by their very nature, and the "Fiscal Compact" does not provide for any kind of convergence in this field. The same is true regarding the breakdown of public spending: spending on social welfare in 2010 accounted for less than 12% of GDP in Cyprus, approximately 18% of GDP in Luxembourg and Slovenia and approximately 24% of GDP in Finland and France; spending on education stood at less than 4% of GDP in Greece but rose above 6.5% of GDP in Estonia and Cyprus; while spending on defense accounted for 0.5% of GDP in Ireland and Luxembourg as opposed to four times that figure in France and Greece[3].

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[1] *Words underlined refer to online documents which can be consulted on Notre Europe's website (www.notre-europe.eu).*
[2] See António Vitorino, "The European "Fiscal Compact": a goal or a starting point?", *Tribune, Notre Europe*, June 2012.
[3] See http://epp.eurostat.ec.europa.eu/statistics_explained/index.php/General_government_expenditure_statistics

In the event of a breach in national public accounts, the European authorities (the Commission and the member states) will still be able to accompany their recommendations and their sanctions with specific demands concerning the financial redeployment and structural reforms that the countries involved need to implement. However, those countries will still have a "performance obligation" (to correct the breaches identified) rather than a "best efforts obligation", given that they will be free to achieve the desired result by whatever decisions seem to them the most effective and fair. Only "countries under programmes" like Greece are and will continue to be forced to allow more intrusive interference on the part of the EU (and of the IMF) in return for the aid programmes that they have asked to be allowed to tap into. This exceptional situation follows from the fact that those countries have *de facto* lost their sovereignty, by putting themselves in a position of excessive dependence on their private creditors that grant them loans with unbearable interest rates.

3 – European disciplines that are not necessarily a synonym for austerity

Do the painful budgetary, economic and social adjustments which a number of "countries under programmes" are being forced to implement, herald the new political and legal framework set up under the "Fiscal Compact"? Or is this compact's task not, rather, to prevent the appearance of breaches so huge that they make such tough austerity measures inevitable?

The second of these alternatives is the one we would be wise to choose as regards public spending: European countries will be able to continue substantially increasing these spending in order to provide a little more "fuel" in the event of an economic slowdown or recession, such as during the current crisis (3 additional GDP points on average for European countries from 2007 to 2011). In fact, it is precisely in order to carve out these margins for manoeuvre in the event of a poor economic climate that countries will have to contain their structural deficit to 0.5% of their GDP (not to do away with it). The same will apply to the efforts allowed in the field of public debt reduction – efforts which will be judged in the long term on the basis of the path pursued by the national authorities involved. The aim of these gradual adjustments is to boost investor confidence and thus to bring down the rates at which governments borrow, thereby increasing their margins for manoeuvre in this area too.

The "Fiscal Compact" also reaffirms the need to take into consideration the economic context and any exceptional circumstances which countries in the euro zone may be facing, by promoting the need for budget stability in the medium term. This reflects the way in which the Stability and Growth Pact has been implemented, including in the course of the recent crisis. Thus the crisis has prompted the European authorities to display flexibility over the deadlines within which the countries in the euro zone have been urged to bring their deficits back down to 3% of GDP (a threshold which France, for instance, has crossed on fully six separate occasions in the past ten years).

Quite apart from the success of the bail-out plans devised at the European level, the recent adoption of a "growth pact" reminds us that austerity or recovery are not going to depend primarily on the scope or rhythm of national budget adjustments. They are going to rest also, and indeed above all, on the entire range of actions national reforms designed to boost euro-zone member countries' competitiveness and thus their growth and employment performances. But they will also rest on a deepening of the internal market, and the mobilisation of European funds[4] that has to be massively increased (be they EIB loans, Community budget and structural funds, project bonds, etc.).

It is because they failed to manage their public or private accounts and their competitiveness strategies properly that Spain, Greece, Ireland and Portugal today are having to conjugate restricted sovereignty with enforced austerity. In adopting and implementing the "Fiscal Compact", the Europeans are then being urged once again to illustrate the virtues of the old proverb "prevention is better than cure".

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[4] "Austerity but also growth", Declaration by Notre Europe's European Steering Committee, 19 November 2011.