CONFERENCE UNDER ARTICLE 13 OF THE FISCAL COMPACT

SESSION 2 - EU ECONOMIC AND FINANCIAL GOVERNANCE TOOLS

Background Note

The new and stricter EU fiscal rules demand the consolidation and gradual reduction of debt.

European national governments, unable to resort to taxation, given that the average tax burden is already high (38.8% in the EU and 39.5% in the Eurozone) and any additional increase might harm the competitiveness of their economies, are making efforts to enforce tough programmes for curbing public spending, which, at a time of weak private demand, heighten the risk of precipitating a recession.

In the wake of the economic and financial crisis of 2008, many Eurozone Member States have had to cope with a substantial increase in their debt.

The public debt/GDP ratio in the EU and the Eurozone has increased by more than 15 percentage points, from 74.3% to 89.5% and from 79.9% to 96% respectively.

This has given rise to a wide-ranging debate in Europe concerning possible tools that, coupled with a recovery in growth rates, might reduce the impact of debt on European economies, especially those most exposed to international speculation, which are forced to set aside a very large part of their budget to service government bond interest payments.

Various proposals have been put forward, including the establishment of a European Redemption Fund (ERF), into which the portion of Eurozone states' public debt in excess of 60% of GDP would be transferred. The ERF would issue securities with a redemption period of up to 20-25 years that would be backed by the proceeds of the taxes collected nationally and by public assets including, in particular, gold and foreign exchange reserves.

On the other hand, the purpose of Eurobills - debt securities with a maturity of less than one year- would be to ease tensions in the market for government bonds.

The promoters of both solutions aim not only to stabilise markets but also to reduce the risk of recourse to the European Stability Mechanism (ESM).

As recommended in the final report of the group of experts appointed by the European Commission to investigate the implications of joint debt management mechanisms, any system for the joint issuance of bonds has to include robust safeguards against moral hazard. Some possible safeguards might include a

requirement that certain preconditions be met (involving a trial period and restrictions on participation), enhanced coordination of the fiscal and economic policies of Member States, and the use of incentives and sanctions.

Another proposal is the so called P.A.D.R.E. - "Politically Acceptable Debt Restructuring in the Eurozone" - whereby the European Central Bank, borrowing on the market at low interest rates through the issuance of bonds, would acquire the government debt of Eurozone countries which would, in turn, gradually reduce their debt with the ECB by waiving their seigniorage rights.

Meanwhile, we have already seen the successful launch in 2012 of the so-called "project bonds". Designed to finance specific projects, these constitute a risk mutualisation mechanism set up by the European Commission and the European Investment Bank than enables companies intending to carry out projects in the fields of trans-European transport and energy, telecommunication networks and broadband to issue bonds to attract capital market investors.

Finally, the Euro Union Bond project, articulated in 2011 and often endorsed in the subsequent debate. Under the project each Member State, in proportion to its share capital in the European Central Bank, would contribute stocks of publicly-owned corporations, portions of real estate assets and some of its central bank's gold reserves to a mutual fund. The original idea was for a fund with a paid-up capital of one thousand billion Euros that could guarantee the issuance of three thousand billion in bonds with a maturity of 10 years and an average yield of 3%.

In order to prepare our debate, we would like to raise the following questions:

a) Would it be useful to modify the current arrangements with a view to deepening economic and monetary union on the basis of the roadmap agreed by the European Council in December 2013?

b) Which of the instruments referred to above are to be considered preferable or practicable?

c) What other initiatives might be envisaged to reduce the debt burden without precluding the implementation of pro-growth policies, with particular regard to investment expenditure?