



FISCAL FRAMEWORKS IN EUROPE: BACKGROUND AND PERSPECTIVES

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For registration information please contact Research@nationalbanken.dk

For additional information please contact Ida Willumsen, iw.fi@cbs.dk

MOTIVATION

The financial crisis in the *European Union* (EU) led the way to a new emphasis on stronger fiscal rules and institutions within a framework that defines each participant's responsibility for maintaining sustainable public finances, without imposing adverse effects on the partner economies.

The best known fiscal rules, the EU's *Stability and Growth Pact* (SGP), failed to promote adequately sustainable public finances in the period before the Great Financial Crisis. The *Fiscal Compact*, as contained in the 2012 *Treaty on Stability, Coordination and Governance*, introduced new rules on public finances to be implemented in national legislation.

However, it is not obvious if national rules jointly legislated are actually more likely to impose greater fiscal discipline than the supranational rules of the original SGP. Nonetheless, several countries have found national fiscal rules helpful in achieving greater budgetary discipline, yet allowing counter-cyclical policy actions to be taken.

An important but widely neglected aspect is the impact of fiscal rules on output and investment returns. This is crucial, in addition to the effect on fiscal imbalances, in order to better understand the economy's ability to meet its pension liabilities and social support – either directly in the form of state pensions or indirectly via private pension funds. These issues take on added importance in an era when populations are ageing and increasingly depend on pensions, health care etc.

More generally, the institutional design, political context and operational aspects of European fiscal frameworks, both at the national and supranational level, leave a number of questions unanswered, particularly with respect to output growth, stability, the sustainability of public finances and their relation to capital and external imbalances, the issue of fiscal dominance over monetary policy, different monetary stances, risk sharing, and transfers between economies.

Other work in this area might also include reviews of how well the general principles imbedded in a supranational fiscal framework would fit the conditions of individual countries. There are considerable differences between the European economies in terms of fiscal imbalances, external imbalances, their tolerance for further integration or tendency to federalism, attitudes or susceptibility to risk, access to/depth of capital markets, diversification and so on.

There are also certain generic problems which any general fiscal institutional or rule-based framework would need to overcome: enforcement techniques, common bonds to strengthen monetary federalism, risk management of economic disasters, structural reform, and the role of a fiscal oversight council at the European level. These are bigger issues, with impacts not restricted to the fiscal framework.

CONFERENCE

To study these and related issues, a research conference will be held in Copenhagen on June 1-2, 2017, hosted by Danmarks Nationalbank. The general theme is the political economy and institutional design of fiscal frameworks in Europe. The conference will re-evaluate fiscal frameworks in Europe in light of experience gathered since the formation of the Economic and Monetary Union (EMU). The implications for the design of fiscal policy stemming from demographic changes, and the implications for the design of pension systems, health care etc., will also be addressed.

More specifically, the following issues will be relevant to the conference:

- Enforcement of fiscal frameworks and rules
- Effectiveness and credibility of fiscal rules
- Fiscal space and long term management of public debt
- Should the desirability to accept new entrants to the EA be re-evaluated in light of recent experience?
- Fiscal policy commissions and councils
- How the bond markets have responded to the European debt crisis? Is the pricing of the risk of sovereign default consistent with economic fundamentals? Or is there evidence of overreaction in the markets?
- Refinancing techniques and arrangements, including restructuring of public debt
- GDP bonds and fiscal space
- Bailing-out governments or bailing out financial sectors?

- What are the costs of default, and are they larger or smaller than the costs of staggering on with high debt ratios/costs of borrowing or structural reform?
- Expansionary fiscal consolidation: where do we stand?
- Should rules and institutions be adopted in the EA to allow for an orderly sovereign debt default and restructuring?
- Fiscal implications of demographic change
- Debt consequences of entitlement spending

The conference will be held jointly between Danmarks Nationalbank, the Copenhagen Business School and Bruegel.

The organizing team includes:

- Professor Michael M. Hutchison, Department of Economics, University of California, Santa Cruz, USA; hutch@ucsc.edu
- Professor Svend E. Hougaard Jensen, Department of Economics, Copenhagen Business School, Denmark; shj.eco@cbs.dk
- Head of Research, Federico Ravenna, Danmarks Nationalbank, fera@nationalbanken.dk
- Director, Guntram Wolff, Bruegel, guntram.wolff@bruegel.org

The format is a two-day event, scheduled for June 1-2, 2017.

The location of the conference is Danmarks Nationalbank in Copenhagen.

All papers accepted for the conference would be original research.

After the presentation of each paper, comments will be given by a discussant, followed by a general discussion.

Also, there will be two keynote speeches, where policy perspectives are presented by leading policymakers/advisors.

The conference brings together prominent scholars working in the areas of fiscal institutions, fiscal sustainability, banking regulatory and supervisory issues, banking crises, and so on, and applying their expertise to the context of fiscal policy in Europe.

Authors will primarily be academics, but would also involve researchers from central banks, governmental agencies, and international institutions.

PROGRAMME

Thursday, June 1, 2017:

8:30-9:00am Registration, Coffee

9:00-9:15am Welcoming remarks

Session 1: Fiscal Institutions

9:15-10:00am Roel Beetsma, University of Amsterdam, the Netherlands; Xavier Debrun, IMF; Victor Lledo, IMF; and Xiaoxiao Zhang, IMF: *"The rise of independent fiscal institutions: Recent trends and perspectives"*
Discussant: Charles Wyplosz, Graduate Institute of International and Development Studies, Switzerland

10:00-10:45am Zareh Asatryan, ZEW, Mannheim, Germany; Xavier Debrun, IMF; Friedrich Heinemann, ZEW, Mannheim, Germany; Michal Horvath, York University, UK; L'udovít Ódor, and Mustafa Yeter, ZEW, Mannheim, Germany:
"Making the most of the European Fiscal Board"
Discussant: Roel Beetsma, University of Amsterdam, the Netherlands

10:45-11:15am Coffee break

11:15-11:40am Árpád Ábrahám, European University Institute, Italy; Eva Carceles-Poveda, Stony Brook University, USA; Yan Liu, Wuhan University, China; and Ramon Marimon, European University Institute, Italy: *"On the optimal design of a Financial Stability Fund"*

11:40-12:05pm Gregory Claeys, Bruegel; Zsolt Darvas, Bruegel; and Álvaro Leandro, Bruegel, Belgium: *"A proposal to revive the European Fiscal Framework"*

12:05-12:30pm David Vines, Oxford, UK: "The Macroeconomic Imbalances Procedure: Are the purposes being achieved?"

12:30-1:00pm Roundtable on Fiscal Institutional Design: Ramon Marimon, Gregory Claeys and David Vines

1:00-2:00pm Lunch

Session 2: Fiscal Rules, the welfare state and inequality

- 2:00-2:45pm Torben M. Andersen, University of Aarhus, Denmark: "*Budget rules and public sector size and structure*"
Discussant: Michael Burda, Humboldt-Universität zu Berlin, Germany
- 2:45-3:30pm Mathias Klein, DIW Berlin, Germany, and Roland Winkler, TU Dortmund University, Germany: "*Austerity, inequality, and private debt overhang*"
Discussant: Gregory Claeys, Bruegel, Belgium
- 3:30–3:45pm Coffee break
- 3:45-4:30pm Xavier Debrun, IMF, and Lars Jonung, Lund University, Sweden: "*Rule-based fiscal policy: How sustainable is it?*"
Discussant: Carolin Nerlich, Fiscal Policies Division, ECB
- 4:30-5:15pm Andrew Hughes Hallett, George Mason University, USA, Svend E. Hougaard Jensen, Copenhagen Business School, Denmark, Thorsteinn S. Sveinsson, Central Bank of Iceland, and Filipe Vieira, Copenhagen Business School, Denmark: "*From here to there: The transition path of sustainable fiscal strategies under adverse demographics*"
- 7:00-9:30pm Dinner at the Royal Danish Opera
- Dinner speech: Niels Thygesen, University of Copenhagen, and chairman of the European Fiscal Board

Friday, June 2, 2017:

- 8:30-9:15am Breakfast

Session 3: Fiscal Dimensions of Monetary Policy

- 9:15-9:40am Marco Del Negro, Federal Reserve Bank of New York, USA: "*On the fiscal implications of central banks' balance sheets*"
- 9:40-10:05am Henrique Basso, Banco de Espana, Spain and James Costain, Banco de Espana, Spain: "*Fiscal delegation in a monetary union: Instrument assignment and stabilization properties*"

- 10:05-10:30am Giancarlo Corsetti, University of Cambridge, UK; Luca Dedola, ECB; Marek Jarociński, ECB; Bartosz Maćkowiak, ECB; and Sebastian Schmidt, ECB:
"Macroeconomic stabilization, monetary-fiscal interactions, and Europe's monetary union"
- 10:30-11:00am Roundtable on Monetary-Fiscal Interactions: Marek Jarociński, Henrique Basso and Marco Del Negro
- 11:00-11:30am Coffee break
- 11:30-12:15pm Keynote address: Marco Buti, Director-General for Economic and Financial Affairs at the European Commission
- 12:15-1:15pm Lunch

Session 4: Public Debt, Rules and Financial Markets

- 1:15-2:00pm Guntram Wolff, Bruegel, Belgium: *"On the no-bail-out clause and sovereign debt restructuring mechanism: How does it relate to Europe's fiscal framework?"*
 Discussant: Ramon Xifré, ESCI-Universitat Pompeu Fabra and IESE Business School, Spain
- 2:00-2:45pm U. Michael Bergman, University of Copenhagen, Denmark, Michael M. Hutchison, University of California, Santa Cruz, USA, and Svend E. Hougaard Jensen, CBS, Denmark: *"European policy and markets: Did policy initiatives stem the sovereign debt crisis in the Euro Area?"*
 Discussant: Massimo Giuliodori, University of Amsterdam, the Netherlands
- 2:45–3:00pm Coffee break
- 3:00-3:45pm Wolf Heinrich Reuter, Staff of the German Council of Economic Experts, Germany: *"When and why do countries break their national fiscal rules?"*
 Discussant: Victor Lledo, IMF
- 3:45-4:00pm Closing remarks