THE "STUPIDITY PACT" IS NOT STABLE

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The positions recently adopted by the French and Italian authorities concerning the 3% of public deficit threshold have imparted a fresh boost to the recurring debate on the Stability and Growth Pact, which former Commission President Romano Prodi once called a "stupid" pact. It is more important than ever to clarify the terms of this debate. As the member states present their stability or convergence programmes to the European authorities and with the up-coming European elections of May 2014, it is more important than ever to clarify the terms of this debate.

1. The Stability and Growth Pact is not a dogma carved in stone

The 3% of public deficit threshold was built into the Maastricht Treaty as one of the "convergence criteria" to be met in order for a member state to join the single currency, and it was then revived in the Stability Pact adopted in 1997. This threshold, which is designed to prevent "excessive" deficits (but not deficits in and of themselves), was established taking into account some basic assumptions: in the context of a 5% nominal GDP growth rate (3% of real growth and 2% of inflation), the member states that have a public debt of 60% of GDP can stabilise the level of their debt only if the public deficit does not exceed 3%. The aim was thus to avoid budgetary slippages which may fuel excessive indebtment and threaten the stability of the common currency area.

This standard fiscal threshold has not been held up as a dogma since the Stability Pact was adopted. In seventeen years only four countries out of twenty-eight have never seen their deficit exceed 3% of their national wealth (Estonia, Finland, Luxembourg and Sweden). For some countries, compliance with the threshold has been the exception rather than the rule (France, for example, has met the criterion only seven times, while Portugal has never met it at all). But despite this, no financial penalty has ever been levied, the Commission's only proposal in that respect (against France and Germany in 2003) having been thrown out by the member states. In view of this, it is therefore paradoxical to see the Stability Pact as a kind of "straitjacket" when it bears a far greater resemblance to a broad "cloak" which can be adjusted in times of economic difficulty.

Before its recent reform, the stability pact was in part "stupid" inasmuch as it focused excessively on the 3% of public deficit threshold, with which Spain and Ireland were complying perfectly, yet that did not stop them from experiencing a major crisis. The pact was thus complemented by a new procedure designed to monitor imbalances in competitiveness as well as private debts.

The pact can perfectly well be reformed further even if it has only just been reformed. Yet what is certain is that those countries that do not comply with the letter or the spirit of the pact are not best placed to persuade the other member states. It would be rather like Hell's Angels trying to propose a reform of the Highway Code...

2. The Stability Pact is a pact resting on political trust among the member states

While the 3% of public deficit threshold is not a "dogma", it is nevertheless the symbolic element of a pact established on the basis of mutual trust and confidence when the transition to the euro took place, and it is applied in respect of an economic but also political context.

What is certain in this connection is that countries which have regularly exceeded the 3% threshold, whether in times of crisis or when the economic situation was more favourable, are less likely to benefit from an understanding and indulgent attitude on their partners' part. This is especially true when they have enjoyed extra time to meet their commitments, which it would be sensitive to renegotiate before they have shown that they really are seeking to honour those commitments. Conversely, those countries making real efforts to improve their economic and social results, through important structural reforms, can expect a more accommodating stance on the European authorities' part.

At this juncture, the Commission is called on to play a more decisive role in this field. While it still falls to the Commission to propose potential penalties against a country, the Council will now definitely adopt them unless a qualified majority of member states mobilises to block them (whereas previously a qualified majority was required to adopt them). In view of this, the composition of the Commission appears to be more crucial than ever, as indeed is the election of the MEPs tasked with approving its investiture. The party balances in the next College of Commissioners will, of course, affect the degree of accountant's zeal with which the Stability Pact is applied, as well as the kind of priority accorded to European measures in support of growth and employment.

In any event, it is not merely the adoption of penalties against them that countries regularly exceeding the 3% threshold need to fear – indeed those penalties would also be "stupid" because they would have a financial impact on countries already in deep financial water... Far worse is the loss of credibility and influence caused by their ongoing failure to meet their commitments, which also undermines their ability to properly defend their interests and their priorities in every other sphere of European life – Italy, for instance, is most definitely handicapped in this way.

3. The debate on the Stability Pact is also economic in nature

The debate on the application of the Stability Pact also has an economic dimension, an aspect which must be explored in greater depth at both the national and the European levels.

The economic debate in question primarily concerns the member states, which would be well advised to ask themselves whether the succession of excessive public deficits has been beneficial for them in terms of employment, growth, reducing inequality and boosting collective well-being; and to ask themselves also whether a reduction of these excessive deficits, as a result of decisions made by them rather than by Brussels, might not be useful to reduce their dependence on the financial markets and to rediscover increased room for manoeuvre while at the same time putting paid to the wretched state of being constantly upbraided and reminded to obey the European rule. Those are key questions for such countries as France and Italy, and it would be a good idea to address them without giving in to the superficial temptation to denounce alleged "dogmas from Brussels".

This economic debate on the application of the Stability Pact also needs to be pursued at the European level, in consideration of the current state of the EU's economies and the fear of a possible deflation. From a strictly economic standpoint, is it really urgent to bring national deficits back down to below the 3% mark in a Europe where they can barely maintain inflation (which is very weak) and where they do not necessarily arouse the financial market's mistrust (France, for instance, has been borrowing at all-time low rates)? If all of the member states "put their houses in order" at the same time and at the same pace, even at the cost of drastic budget cuts, will the European village benefit from that? Shouldn't the European strategy aiming at reducing public deficits be in line with the progress accomplished concerning the coordination of economic policies in the euro area, in order to stimulate growth and create jobs? Does too much stringency not kill stringency itself (and growth with it) in the same way as "too much taxation kills taxation"? All of these questions undoubtedly lie at the heart of the campaign leading up to the European elections on 22-25 May 2014, the outcome of which is likely to open up a new political cycle in the life of the EU.

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If the Stability Pact is not completely stable, it is not completely stupid either. Let those countries in difficulty set their economies back on track, let them make choices designed to bring down unemployment and to boost growth – the rest "will be added to them".

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