

PUBLIC DEBT. HOW IT WORKS, HOW TO REDUCE IT.



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Allow me to put public debt in a broader perspective

2 preliminary remarks:

- the euro is a voluntary commitment, as well as the rules framing public deficit and debt
- The EU is not a state

4 points:

- Lack of coherence
- Diversity of situations within the Euro Area
- Quality of growth
- « Indebted to nature » - DNB, 2020



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First preliminary remark: the euro is a voluntary commitment, in our own interest

- Belonging to the euro was **voluntary**.
- The objectives was **to put an end to competitive devaluations** within the single market; **to safeguard price stability and financial stability**
- **It was not conceived by Germany to « dominate » Europe, or impose « austerity »**, as often (and wrongly) said in the public debate
- The German people was against the creation of a single currency. Germany (and others, in particular the NL) asked for **guarantees**.
- All governments **accepted freely** (Maastricht treaty) to limit public deficit and public debt / to accept an independent Central Bank that could not finance national spendings.
- These principles were supposed to make the euro viable as it is « a currency without a state »



Second preliminary remark: the EU is not a state

We permanently compare the Euro Area with States, in particular the US. It is a huge mistake:

- the Euro area has **no central government enjoying discretionary powers**
- **It has no budget as such** (the EU has one that represents around 1 % of the GDP / in the US the federal budget represents around 25 %),
- the EU single market is **less integrated** (in particular it lacks a cross border capital markets and a genuine banking union)
- **labour mobility** is less developed than in the US

Governments made **huge convergence efforts before** joining the euro, but stopped afterward.

Art 121 of the treaty (to look at economy as a matter of common interest) was never taken seriously



Lack of coherence...

If we are convinced that excessive debt:

- Creates **vulnerabilities**:
 - costs, above all if interest rates increase;
 - Dependence (if detained by foreigners);
 - « doom-loop », if detained by national banks);
- **Has a crowding-out effect** (savings not used for more productive spendings);
- **Does not bring growth automatically**, as we observe that the most indebted countries in the EA are not the most dynamic (Eurofi - Macro economic scoreboard, Sept 2024)

Why did governments make so many efforts to escape the EU rules ?

See the demands of « more flexibility » in implementing the rules, or to deduct some expenditures from the 3 % expenditure limit (defence or investment or greening or social etc) and to avoid sanctions.



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There are diverse situations within the Euro Area

- Who buys the debt ? More foreigners for France, less for Italy
- Does the state have a primary surplus? (Italy, yes; France no)
- What about structural reforms? (stronger efforts in Italy for pensions, in 2011; Fr 2022 / gender unbalanced labour market in Italy more than in France)
- Which level of taxes? Much higher in France (one the highest in the OECD) than in Italy – the Italian government could reduce dramatically the level of debt by introducing a wealth tax for example; less margin of manoeuvre in FR
- Demography: for long France had an advantage, less true now



Quality of growth ?

- Which denominator (GDP) ? the quality of public spending / the nature of growth matter a lot to determine the capacity to reimburse
- Are debts made to finance decarbonation and the transition to become nature positive ?
- Or are they partly harmful subsidies, including at EU level ? Such as part of the CAP
- NGEU: joint indebment without knowing how to repay / with which tax equity



We are « indebted to nature »

- Financial debt is only one aspect of our indebtedness
- Report drafted by the Dutch Central bank, 2020
- Time to take into account the use of natural capital / to price negative externalities and the value of ecosystem services



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THANKS.



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