System Changes of the Economic Governance: Economic and Debt Crisis in Europe and the Fiscal Pact as the Main Attribute of Economic Integration in the Current EU


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SYSTEM CHANGES OF THE ECONOMIC GOVERNANCE: ECONOMIC AND DEBT CRISIS IN EUROPE AND THE FISCAL PACT AS THE MAIN ATTRIBUTE OF ECONOMIC INTEGRATION IN THE CURRENT EU

Hana Bartušková - Irena Vrňáková*

ABSTRACT
This article deals with the current issues of the European economic integration development and analysis of reforms in economic governance in the context of the debt crisis of the Euro area member states. Sub-themes of the text are the effects of the debt crisis on the European economy and on the member states of the European Union. Specifically, we will also consider the influence of the debt crisis on economic growth, the real and nominal convergence of member countries and, subsequently, perspectives of functioning of the single currency. The first part is devoted to the statistics of real and nominal economic variables in the EU and developments in recent years, with the emphasis on the global economic crisis and subsequent debt crisis in the euro area. In the second part, we deal with analysis of selected reform of the Stability and Growth Pact as an instrument of coordination of economic policy of the euro area’s member states, namely budgetary surveillance contained in the so-called Six-Pack, Two-pack and the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (Fiscal Pact). Each new component of economic governance and its tools are a key factor not only for economic prosperity and development of the EU, but also for preserving and strengthening the EU’s position in the world economy.

Key words: governance, debt crisis, fiscal policy, fiscal pact, economic integration, European Union

Introduction
The economic and debt crisis revealed a number of problems in the

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Ing. Irena Vrňáková, Department of World Economy, Faculty of International Relations, University of Economics, W. Churchill Sq. 4, 130 67 Prague 3, Czech Republic, i.vrnakova@seznam.cz.
European Union and the euro area. Among the most serious issues we can find excessive focus on deficits rather than on government debts, lack of supervision, competitiveness and macroeconomic imbalances (credit growth leads to the accumulation of private sector debt), poor economic performance and lack of sanctions enforcements, the relatively slow decision making process at the higher level of economic governance and absence of emergency financing mechanism for countries in a sudden financial trouble. In addition, there was no financial support which would be able to prevent contagion to other countries at risk. As a result, Greece, and then Ireland and Portugal, have been unable to borrow on financial markets at reasonable interest rates. The EU was forced to intervene, which resulted in the creation of a mechanism for crisis management and the development of various financial policies to be used in case of emergency of financial trouble in the euro area.

This paper will proceed as follows. First, we are going to describe the economic situation in the European Union since 2000. The economic governance of European markets and economies came to main importance, especially during the economic crisis. The European Union was unable to maintain the situation and restore economic growth. Main focus is also going to be on debt situation in member states and the whole EU. The next chapter will describe the development of economic governance in Europe and in the closing part we will evaluate the effectiveness of the measures taken in respect of the debt situation in the EU and the euro area.

1 Economic situation in EU and euro area since 2000

The European Union is not a homogenous area, so the economic crisis in 2008 hit the European economy with different impacts. Poland was even able to maintain the economic growth within the world economic crisis. But other European countries were not able to restore economic growth even during the next 5 years after 2008.

Due to economic integration (especially monetary integration) the economic governance of Europe represents critical importance. In this chapter we are going to focus on an overall picture of economic variables in the European Union and also the euro area during the years of the crisis and afterwards.

1.1 Economic growth and other economic variables

On Figure 1 we can see a development of economic growth before, during
and after 2008 world economic crisis.

Fig. 1
Real GDP Growth in European Union (EU27) and euro area (EA17) in % (2000 – 2014)

Source: Eurostat (2013a)

The European Union was staggeringly hit by the crisis in 2008, the main impact of the crisis could be seen in 2009, when the economic growth in Europe was lower than -4 %. The European economy started to recover in 2010, but due to development in the euro area and problems with debt crisis in Greece and other states with single currency, GDP started to fall again and Europe entered the so-called debt crisis.

This debt crisis showed the heterogeneity of the euro area and the main problems and disparities in economies of the EU. Even though the single monetary policy had maintained a long period of stable economic development in the euro area since 2000, with a low inflation rate and a low interest rate, the development during 2008 crisis showed prominent weaknesses in monetary governance in Europe. Different conditions and, above all, diverging attitudes of the member states of the EU highlighted discrepancies in its budget and fiscal
policies. The highly indebted countries like Greece, Ireland, Portugal, Spain, Italy, that had been able to gain a main advantage of low interest rates since 1999, got in troubles in the moment of raising the interest rates in Europe (Feldstein, 2011) mainly due to their expansive social and fiscal policies. An insolvency of these states to meet their financial commitments was the main reason for the incoming debt crisis in the euro area and the European Union.

Before we examine the situation with debts in the EU (euro) members states let us just take a quick look at the main economic variables in the European Union and the euro area during the crisis.

Table 1
Main economic variables in EU27 2005 – 2012

<table>
<thead>
<tr>
<th></th>
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<tbody>
<tr>
<td>GDP (mil. Euro)</td>
<td>11 072 290,9</td>
<td>11 701 131,1</td>
<td>12 406 299,9</td>
<td>12 473 092,3</td>
</tr>
<tr>
<td>Real GDP (PPS Euro per inhabitant)</td>
<td>22 500</td>
<td>23 700</td>
<td>25 000</td>
<td>25 000</td>
</tr>
<tr>
<td>Real GDP growth (%)</td>
<td>2,1</td>
<td>3,3</td>
<td>3,2</td>
<td>0,3</td>
</tr>
<tr>
<td>Unemployment (%)</td>
<td>9,0</td>
<td>8,3</td>
<td>7,2</td>
<td>7,1</td>
</tr>
<tr>
<td>Inflation (HICP in %)</td>
<td>2,3</td>
<td>2,3</td>
<td>2,4</td>
<td>3,7</td>
</tr>
<tr>
<td>Longterm interest rate (%)</td>
<td>3,7</td>
<td>4,0</td>
<td>4,6</td>
<td>4,5</td>
</tr>
<tr>
<td>Real GDP (PPS Euro per inhabitant)</td>
<td>23 500</td>
<td>24 500</td>
<td>25 100</td>
<td>25 600</td>
</tr>
<tr>
<td>Real GDP growth (%)</td>
<td>-4,3</td>
<td>2,1</td>
<td>1,6</td>
<td>-0,3</td>
</tr>
<tr>
<td>Unemployment (%)</td>
<td>9,0</td>
<td>9,7</td>
<td>9,7</td>
<td>10,5</td>
</tr>
<tr>
<td>Inflation (HICP in %)</td>
<td>1,0</td>
<td>2,1</td>
<td>3,1</td>
<td>2,6</td>
</tr>
<tr>
<td>Longterm interest rate (%)</td>
<td>4,1</td>
<td>3,8</td>
<td>4,3</td>
<td>3,7</td>
</tr>
</tbody>
</table>

Source: Eurostat (2013a,b,c), authors' own calculation
Table 2
Main economic variables EA17 2005 – 2012

<table>
<thead>
<tr>
<th>Main economic variables in Euro area 2005 – 2012 (EA17)</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP (mil. Euro)</td>
<td>8 145 194,5</td>
<td>8 564 379,5</td>
<td>9 029 746,9</td>
<td>9 241 644,5</td>
</tr>
<tr>
<td>Real GDP (PPS Euro per inhabitant)</td>
<td>24 500</td>
<td>25 800</td>
<td>27 200</td>
<td>27 200</td>
</tr>
<tr>
<td>Real GDP growth (%)</td>
<td>1,7</td>
<td>3,2</td>
<td>3,0</td>
<td>0,4</td>
</tr>
<tr>
<td>Unemployment (%)</td>
<td>9,2</td>
<td>8,5</td>
<td>7,6</td>
<td>7,6</td>
</tr>
<tr>
<td>Inflation (HICP in %)</td>
<td>2,2</td>
<td>2,2</td>
<td>2,1</td>
<td>3,3</td>
</tr>
<tr>
<td>Longterm interest rate (%)</td>
<td>3,4</td>
<td>3,8</td>
<td>4,3</td>
<td>4,3</td>
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<tr>
<td>2009</td>
<td>2010</td>
<td>2011</td>
<td>2012</td>
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</tr>
<tr>
<td>GDP (mil. Euro)</td>
<td>8 922 237,0</td>
<td>9 174 615,3</td>
<td>9 427 031,5</td>
<td>9 488 923,5</td>
</tr>
<tr>
<td>Real GDP (PPS Euro per inhabitant)</td>
<td>25 500</td>
<td>26 500</td>
<td>27 200</td>
<td>27 500</td>
</tr>
<tr>
<td>Real GDP growth (%)</td>
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<td>2,0</td>
<td>1,5</td>
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</tr>
<tr>
<td>Unemployment (%)</td>
<td>9,6</td>
<td>10,1</td>
<td>10,2</td>
<td>11,4</td>
</tr>
<tr>
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<td>1,6</td>
<td>2,7</td>
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<td>3,6</td>
<td>4,4</td>
<td>4,0</td>
</tr>
</tbody>
</table>

Source: Eurostat (2013a,b,c), authors' own calculation

According to tables 1 and 2 the long-term interest rates and the inflation are lower in the euro area than in the whole European Union, due to the strict monetary policy of European bank. On the other side, the unemployment rate is higher in the euro area probably due to the single monetary policy and insufficient coordination of fiscal policies between the member states. The GDP growth is lower in the euro area. Due to the single currency, the economic crisis in the euro area is a little deeper and will probably last a longer time. This shows us the importance of the EU economic governance that rises even more in case of the single currency in the euro area. Currently, economic governance seems to be failing to prevent economic crisis changes that were necessary to take. Changes of economic governance in the euro area that could get over this effect of insufficient economic integration in Europe is going to be the main focus of second chapter of this paper.

2 The economic governance and its system changes

In this part we will deal with analysis of selected reforms of the Stability and Growth Pact as an instrument of coordinating economic policy in the area of EU member states, namely budgetary surveillance contained in the so-called Six-Pack, Two-pack and the Treaty on Stability, Coordination and Governance in the
Economic and Monetary Union (Fiscal Compact). Subsequently, we will discuss other measures as macroeconomic surveillance, deepening coordination in EMU and the European Stabilisation Mechanism (ESM). The main task of this chapter will be to closely examine the content of a key pillar of the reform EU economic governance, including new tools and outline current and future trends.

2.1 The concept of economic governance

Economic governance is a concept of an effective management of economic and social resources within the Union. It includes standards and principles which are used to ensure greater economic integration and deepen further cooperation. Economic governance falls under the system of regional governance, which is characterised by cooperation between more regions (countries). This cooperation is particularly in areas such as macroeconomic stability, development financing or market liberalisation. For example, the European program of IMF implemented in 2008-2010 in order to offset the crisis, particularly in Ireland, Hungary, and Greece. (Cihelková, 2011, p. 75)

The European Parliament describes the economic governance as "a system of institutions and procedures implemented to achieve the objectives of the European Union in the economic field, namely the coordination of economic policies to promote economic and social progress of nations of the EU" (European Parliament, 2013). The global economic crisis, which started in 2008 and has exposed fundamental issues and unsustainable trends in some states, also showed that the EU needs a model of economic governance to be more effective than the current economic and fiscal coordination. So-called ad hoc responses proved to be insufficient. Recent developments in the area of economic governance includes not only the revision of existing rules and adoption of new rules to strengthen the coordination and surveillance of both policies (fiscal and macroeconomic), but also the procedure to govern the financial crisis. Economic governance is, therefore, a response to the economic challenges of globalisation and the challenges that come with it.

In the euro area, there are more organs that are responsible for economic policy. The main actors are (European Commission, 2012b):

- The European Council is to determine policy guidelines.
- The Council coordinates economic policy and takes decisions which may be binding on individual EU countries. The Council also meets "Eurogroup" (the finance ministers of the euro area), which coordinates
common interests for the euro area and controls the euro. It only deals with aspects related to the euro area.

- EU member states set their national budgets within agreed limits on deficits and debt, and determine their own structural policies involving labour, pensions and capital markets.
- European Commission proposes to the Council guidelines for the implementation of economic and fiscal policy, monitors performance and ensures compliance with the decisions of the Council.
- The European Central Bank (ECB) sets monetary policy in the euro area and seeks the price stability as the main objective.
- The European Parliament is to participate in the legislative process and matters relating to economic governance together with the Council.

2.2 System changes to economic governance on the fiscal side

The global economic crisis has shown that fiscal and macroeconomic imbalances are closely linked, not only within national borders, but also at the EU level, and even more for the euro area. Therefore, the enhanced economic governance as a system that was established in 2011 is still in the further development and refers to several economic areas, including fiscal policy, macroeconomic issues, crisis management, etc. In this part we will deal with specific selected measures.

There has been economic coordination before 2011, but it functioned only on the basis of consensus without legally enforceable rules, except in the area of fiscal policy framework established by the Stability and Growth Pact. It turned out that this coordination had been not strong enough to prevent the growing macroeconomic and fiscal imbalances in the euro area.

Greater coordination of economic policies within the EU was deemed necessary and would be addressed by stimulating growth and job creation in the future: this target was revised and institutional system and procedures of coordination were strengthened with the adoption of the so-called Six-pack in 2011 followed by proposals for a banking union and setting the ESM (European Stability Mechanism). In 2013, the Commission proposed further legislative changes (including the so-called Two-pack), which entered into force on 30 May 2013.

The central pillar of stability and fiscal discipline in the euro area is the
Stability and Growth Pact (SGP). The Pact, which was established in 1997, is committed to maintain the euro area states government deficit below 3 % of GDP and public debt below 60 % of GDP or prove its reduction. The Pact should ensure that national budgets in the medium term will be sustainable, balanced or in surplus.

This system has a preventive and a warning component. Prevention is based on a regular monitoring and early warning system, allowing making some necessary corrections. Member states submit their Stability Programmes (the euro area countries) or Convergence Programmes (countries outside the euro area) in which they set medium-term goals and ways to achieve them. The programs are continually evaluated by the European Commission. This assessment is the basis for the opinion of the Council, which monitors the implementation of programs. In case of significant deviation, the Council submits recommendations to the member state, to maintain the budget deficit over a period of time. The main goal of SGP was to maintain sustainable budget deficits in the member states and to ensure fiscal stability in the euro area.

Figure 2 below illustrates the situation of government deficits since 2000. Last time when the sum of European budgets was in surplus was in 2000. Since then the expansive fiscal policies are a reality in Europe. The average budget deficit in Europe was around 6 % of GDP during the crisis in 2009 and 2010. You can see that the whole EU and the euro area were unable to meet the 3 % criterion of SGP.
But it is different in case of every single member state. On Figure 3 and 4 we will be able to see situation in the member states of EU. Only little more than half of the member states were able to manage their gross debt ratio to GDP in 2010 below 60% level. Only 5 states (Denmark, Sweden, Finland, Luxembourg and Estonia) were able to manage deficits of fiscal budget as low as 3 % to GDP or less. On the other side, there are a lot of states which have been achieving quite high deficits during last few years. For Ireland, Greece and United Kingdom the ratio goes even above 10 %.

The most sustainable budgets can be found traditionally in Scandinavia, where the government budgets were even able to stay balanced during crisis. Among new member states the situation is best in Estonia, which has been achieving a really strict budgetary discipline. Not even mentioning that the gross debt in Estonia is as low as 10 % of GDP.
Fig. 3
Gross debt in member states of EU in 2000, 2005, 2010 (% to GDP)

Source: Eurostat (2013d)

Fig. 4
Budget deficit/surplus in member states of EU in 2000, 2005, 2010 (% to GDP)

Source: Eurostat (2013d)
It became soon clear that major economies such as France or Germany, which forced the Pact from the very beginning, failed to comply with the limits and did not pay any penalty. For example, the deficit of Germany exceeded the 3% limits in a period of 2001 – 2005 (Germany budget deficits to GDP in %: -3,1 % in 2001, -3,8 % in 2002, -4,2 % in 2003, -3,8 % in 2004 and -3,3 % in 2005) (Eurostat, 2013d). France exceeded the 3% in a period of 2002 – 2004 (France state deficits to GDP in %: -3,1 % in 2002, -4,1 % in 2003, -3,6 % in 2004) (Eurostat, 2013d). All this just showed the weak points of economic governance in form of SGP. Consequently, there was a revision in 2005 to the Stability and Growth Pact and its output was the amendment to the regulation of the Council. The result was to strengthen preventive means (to differentiate medium-term budgetary objective by country, minimise annual adjustment in the cyclically-adjusted budget position) and weakening of the repressive part of SGP (for example certain dates or account of unforeseen economic circumstances and other factors). It was established that member states must better utilise the possibilities of the economic cycle.

The main goal was to monitor the long-term aspects of the sustainability of public finances. The revised Pact made possible exceeding 3% deficit limit of public finances, "if they were exceeded only slightly, exceptional and temporary." Deficiency can be considered as exceptional if there is a significant economic downturn and even in case of a fall over a longer period. The deadline for correcting the excessive deficit was prolonged when the deficit was due to extraordinary circumstances. Like in the original SGP, it was not sanctioned when a total debt of member state exceeded the limit of 60% of GDP. (MFCR, 2010)

The impact on the German and France deficits was positive. Both of the countries managed to meet the 3% limit in 2006 and 2007. On the other side, deficit in other countries started to grow. Greece, Italy, Hungary, Poland, and Portugal were unable to meet the limit during the next years. And when the 2008 economic crisis hit the European markets only 13 EU member states were able to maintain their budget discipline within the limit.

2.3 Six-pack

In 2009, with the Lisbon Treaty, came the strengthening of power of the European Commission to implement the SGP (CNB, 2013). In response to the crisis it became apparent that the current form of the Pact is still inadequate and
needs further revision. With this objective a new rule (the Six-pack) was implemented. This package has a greater emphasis on reducing high levels of government debt. A new feature is that the launch of the excessive deficit procedure can take place not only because of excessive government deficit, but also because of unfavourable government debt. We can say that the EU adopted a "six-pack" to promote fiscal discipline and economic coordination in an effort to restore confidence in the euro area. During the economic crisis it became evident that fiscal discipline is a big problem in the euro area as you can see from Figure 5.

Fig. 5
Budget deficit/surplus in the EU member states in 2008 and 2009 (% to GDP)

The six-pack entered into force on 13 December 2011 and is divided into three parts. It consists of strengthening and modification of existing budgetary surveillance, it added a new macroeconomic surveillance, established a mechanism for crisis management in the euro area, and the European Stability Mechanism (ESM). Due to the urgency of the situation and economic crisis in Europe all the changes, except for crisis management mechanism, have been incorporated into EU law through secondary legislation, thus avoiding the necessity to make a time-consuming revision of the Treaties.
The six-pack consists of six sub-legislative acts and imposes financial sanctions for the euro area members in a gradual way; sanctions may even reach 0.5% of GDP. The six-pack introduces reverse qualified majority voting for most sanctions, thus increasing their likelihood for euro area, and implies that a recommendation or a proposal of the Commission is considered adopted in the Council unless a qualified majority of member states votes against it. (European Commission, 2012d)

2.4 Treaty on Stability, Coordination and Governance in Economic and Monetary Union

After the crisis, the EU emphasised the need to pursue further economic and financial integration. The crisis brought the idea to EU officials to create a fiscal union to create a greater economic integration. If the fiscal policies were adhered to by all member states, the European Central Bank believed that this would also settle the crisis and increase their competitiveness. With this object the system was reinforced by Germany (supported by France) in 2012 by additional rules for all countries, and new control measures for countries receiving financial aid or whose financial stability is threatened. In March 2012, all EU countries except the UK and the Czech Republic, signed the Treaty on Stability, Coordination and Governance in Economic and Monetary Union (TSCG, Fiscal Compact). The treaty entered into force on 1 January 2013. This treaty strengthens the economic surveillance of the euro area and adopts a set of rules for stricter budget discipline through budget pact and is binding on the euro area members. The agreement is accompanied by structural reforms to fortify economic policy coordination and improved governance of the euro. The goals have been set as sustainable growth, employment, competitiveness and social cohesion.

The 2008 economic crisis showed a weak point of the economic governance in the EU. Growing member states' debt was getting harder and harder to manage. Some European countries were in difficulty to find sustainable financial resource. Interest rates were rising and also paid interest started to be a great problem for some countries (PIIGS) because of high interest rates.

In Figure 6 and 7 we can see a debt situation in the European Union and also in the euro area. You can see that the gross debt is steadily rising during the whole period of 2000 – 2012. The increase of gross debt since 2008 was 50% compared to 2012.
As you can see the total amount of debt had been increasing slowly but steadily until 2008 when the debt increased rapidly. Until 2008 the ratio of gross debt to GDP was around 60% in EU and less than 70% in the euro area. Rapid development during the crisis in 2008 and the expansive fiscal policy in member states led to almost 90% ratio gross debt to GDP in both the European Union and the euro area. The ratio of total indebtedness is higher in the euro area than in the European Union. This is a consequence of characteristics of member states of the euro area, as these economically developed states have a long history of central government deficits and expansive fiscal policy. Due to strict requirements for macroeconomic coordination and a budgetary discipline in the euro area member states, this situation is changing, and the main progress in this direction could be seen especially during economic crisis in 2008.

Source: Eurostat (2013d)
You can see from the Figure 6 that the difference between indebtedness of EU and the euro area has been diminishing since 2008. You can see this change more obvious on the Figure 7 that illustrates growth of gross state debt in percent. The growth rate of debt is steady and low around 4% and it was even decreasing during the period of 2004 – 2007. When the economic crisis hit the European markets in 2008 and the expansive fiscal policies started, the indebtedness also started to growth rapidly. The 10% growth in indebtedness in the euro area and almost 13% growth in the European Union was the main reason for increasing ratio of state debts in Europe.
We can see that the growth of gross debt has been quite alarming since 2007. To put the debt situation in the European Union to wider perspectives, we are going to examine the amount of interest paid for the European debts. Total amount of interests that have been paid since 2000 can be found in Figure 9. Compared against the GDP, EU member states pay on average approximately 3% of GDP for interests of their debt. This number is little higher in the euro area (3.1 % in 2012, Eurostat 2013d) compared to 2.9 % in the European Union (Eurostat, 2013d).
The gross debt in EU and the euro area has been steadily rising mainly due to economic crisis in 2008, but also due to a mostly loose budgetary discipline in member states. Expansive macroeconomic policies and excessive deficits are the reason for this steady growth in indebtedness in Europe. Moreover, the interest paid for the EU debt is steadily rising as the debts are bigger and also interest rates growth due to the debt crisis in Europe.

The importance of economic governance is obvious. The single currency and monetary integration is based on an economic foundation that can be achieved only through the economic cooperation and fiscal integration in the euro area. The loose discipline in budgets deficits and fiscal policies in member states put an obstacle to any economic development. Since the crisis in 2008, the concept of economic governance in EU has been changing rapidly and it was the main reason for implementing the Fiscal Compact.

Basic objective of the Fiscal Compact was to strengthen fiscal economic pillar of the euro area. Every member state should ensure convergence towards the country-specific medium-term objective (MTO), as defined in the SGP, and the limit of a structural deficit (cyclical effects and one-off measures are not taken into account)
must not exceed 0.5 % of GDP. Countries must implement a correction mechanism which should ensure automatic action to be undertaken in a case of deviation from rules or the adjustment of path towards it. It should additionally include escape clauses for exceptional circumstances. These are measures to reduce the budget deficit and ensure long-term sustainability. In the case of euro area member states, sanctions would be channelled to the ESM; in the case of "non-euro-area member states", the money would be attributed to the EU budget. (TSCG, 2011)

The Fiscal Compact, which is the fiscal part of the TSCG, and the Six-pack run in parallel. On the one hand, a couple of provisions included in the TSCG are mirroring concepts existing in the SGP as reformed by the six-pack: medium-term objectives (MTOs), significant deviation, exceptional circumstances. On the other hand, some provisions of the TSCG are more stringent than the Six-pack. For example, at each stage of the Excessive Deficit Procedure (EDP) euro area member states will support the Commission's proposals or recommendations in the Council if any of euro area member state is in breach of the deficit criterion, unless a qualified majority of them is against it. In practice, this means that if a state breaks the deficit criterion a kind of reverse qualified majority voting applies to all stages of the EDP, even if not foreseen in the Six-pack. Generally, the Commission supports the objective to incorporate key provisions of the TSCG in EU law as soon as possible, it should be a 5-year horizon, but some provisions may be enshrined in secondary legislation without delay. (European Commission, 2012d)

It is probably too soon to evaluate the influence of the Fiscal Compact. But it is true to say that the impact on fiscal deficits of member states was not visible in 2012 and indebtedness in European countries has been still growing since 2012.

2.5 Two-pack

The Six-pack and Fiscal Compact are related also with the „Two-pack“, that includes two regulations applicable to the euro area member states only (Art 136 TFEU). By the first regulation, the common budgetary policy at the national level shall be monitored by independent institutions.

The euro-area member states shall submit their draft budgetary plan for the following year to the Commission and the Eurogroup, along with the independent macro-economic forecast on which they are based. The Commission analyses if the draft budget is in line with the SGP and the recommendations from the European Semester. If the Commission assesses that the draft budgetary plan shows big non-compliance with the SGP, the
Commission can require a revised plan. This regulation complements the preventive part of the SGP, in particular by ensuring appropriate integration of EU policy recommendations in the national budgetary preparations and increasing peer pressure in the Eurogroup. This also implement National Parliaments to the budgetary plans and allow an early detection of risks that a member state does not correct its excessive deficit by the deadline and permit to take action accordingly. (Council of the EU, 2013)

The second regulation relates to the measure on enhanced surveillance of the euro area when a member state experiences or is threatened by financial difficulties. The automatic surveillance of countries applies for all member states that have received any financial or technical assistance in order to maintain EFSF and ESM stability. If a member state does not comply with policy requirements contained in the adjustment programme the country is to face financial consequences. There is also post-programme surveillance which means that according to the draft regulation, a country shall be subject to post-programme surveillance as long as it has not repaid 75% of its debt. (European Commission, 2012d)

EU financial assistance is provided by the following programmes:

- European Financial Stability Facility (EFSF) provides financial assistance to the euro area countries in difficulty raising funds on the financial markets up to EUR 440 billion. As for issuing funds (bonds), they are guaranteed to all euro area countries in proportion to their capital contribution to the ECB. EFSF was created as a temporary rescue mechanism. (EFSF, 2013).

- European Financial and Stability Mechanism (EFSM) provides financial assistance to countries in need. Commission is permitted to borrow up to EUR 60 billion on financial markets on behalf of the EU under implicit guarantees from the EU budget. EFSM is an emergency program and in the past has been used by Ireland and Portugal. EFSM is part of a wider safety net. (European Commission, 2012c).

- The European Stability Mechanism (ESM) is a permanent financial assistance. Permanent crisis mechanism, which entered into force in 2012, will eventually replace the EFSF and EFSM. ESM issues debt instruments to finance loans and other forms of financial assistance to euro area up to EUR 500 billion. Since 2012, the ESM is main instrument for funding
new programs. In parallel with the EFSF, the ESM programme will continue with on-going programs for Greece, Portugal and Ireland. Together with the temporary EFSF fund, or the so-called European bailout, they amount to a total of EUR 940 billion. (CT24, 2013)

2.6 Strengthened Economic governance of the EU and the euro area nowadays

The key elements of the new governance system include:

- European Semester,
- Study on economic growth (Annual Growth Survey - AGS),
- Monitoring of public debt - debt reduction below 60% of GDP,
- The macroeconomic surveillance - an early warning of problems and assistance in monitoring and correction of macroeconomic imbalances
- Stricter enforcement of rules, tougher financial sanctions, ranging from interest-bearing deposits to fines.

Strengthened economic governance also includes the new synchronised working model - European Semester, which is used for discussion and coordination of economic and budgetary priorities, closer EU surveillance of fiscal policies, as part of the Stability and Growth Pact and new tools for addressing macroeconomic imbalances, including a tool to help member states to deal with financial problems. The European Semester is the six-month period for each year during which the member states coordinate budgets, macroeconomic and structural policies and reflects the objectives of their national budget processes and other economic policies. Commission annually performs a detailed analysis of plans of economic and structural reforms of member states and subsequently makes recommendations for the next 12-18 months. (European Commission, 2012a)

The aim is to ensure that all policies were analysed and assessed together, and that policy areas that have not yet been systematically included in the economic surveillance - such as macroeconomic imbalances and financial issues - were also included. (European Parliament, 2013)

Conclusion

The single currency should contribute to economic growth not only for member states but also their subjects. However, the common currency must be backed by a proper management of the euro area economies and the common
rules of governance that are respected across all states. New reform measures and rules of EU economic governance consist of a wide range of elements and actors and form relatively complex structure. However, the fact of these reforms is that steps have been taken to strengthen the economic union, especially among the euro area countries to prevent a crisis like the one that began in 2008 in the future. That means new features, such as ex-ante coordination of the national budgets to peer review or shared agreement on economic goals. The new economic architecture also ensures that commitments made by the institutions in Brussels will be enough to establish and adapt to the national level. This should contribute to the strengthening and stability of the euro area, which can lead ultimately to increased integration within the EU, faster economic growth and more jobs for EU citizens.

It is too soon to evaluate a new economic governance system and its influence on debt situation in EU member states but we can see that some countries are reducing their debt and also deficit. The new obligation of the fiscal pact is met so far only by six European countries: Germany, Denmark, Estonia, Bulgaria, Latvia and Greece. Luxembourg and Finland, while the Pact crossed, but because of their public debt below 60% of GDP, subject to a less stringent limit deficit of 1 % of GDP. Rest of the states which agreed with the Pact, the structural deficit, a deficit adjusted for the economic cycle, decrease. According to the European Commission forecasts, in 2014 the agreed limits should be met also by the other states. Hopefully, strict fiscal discipline and economic surveillance will be able to maintain the situation of the European economy and start economic growth once again.

References:


