

Comments on the paper  
“The SGP from the Perspective  
of the New Member States” by  
Messrs. Orban and Szapary

By Neven Mates

# Not a radical paper—No major SGP reform is recommended

- As long as their deficits are significantly below 3 percent, the NMS should be given more time to reach the CBS criterion;
- This applies only to the pace of achieving the CBS, not to its level;
- The longer adjustment period would allow the NMS to finance the transition costs and investment in highly needed infrastructure;
- The proposal is not inconsistent with the existing SGP. In fact, the EU Commission indicated recently that the medium-term objectives (MTOs) of member countries could reflect considerations of public investment needs.

# Arguments for a more lenient implementation of SAP rules for NMS:

- Generally, the NMS have lower levels of debt (with the exception of Cyprus, Malta and Hungary, with debt-to-gdp ratios above or close to the 60 percent ceiling);
- The NMS are likely to have higher nominal GDP growth, owing to the Balassa-Samuelson and the catching up effects. Higher deficits are therefore consistent with a given target for the debt-to-GDP ratio.

- The accession-related spending and the need to improve infrastructure are transitory costs, which supports the case for financing by borrowing;
- Transition countries among the NMS have achieved more progress in introducing fully-funded pension schemes than the EU-15 countries on average.

- The NMS will need to make larger efforts to reach the CBS targets as they will benefit less from the yield convergence.

# Arguments against a more lenient rules the NMS

- Large current account deficits, caused by credit booms, remain a source of vulnerability. (However, so far the transition countries have been resilient to the current account crises.)
- Deterioration in the population structure is likely to be more pronounced in the NMS than in E-15;
- The sensitivity of the budget deficit to the output variation is only marginally smaller in the NMS than in the EU-15;
- Government is oversized in the NMS, compared to their per capita income;

Should the NMS care about adjusting the SGP rules to suit them better, or about the general picture?

- “Perfect rules”, like permanent balance rule, would probably benefit the NMS, particularly the transition countries (On balance, the higher nominal GDP growth and the transitory nature of accession related spending seem to have more weight than the prospects of something larger deterioration in the population structure and the current account considerations);
- However, should the NMS try to improve the rules to suit them better, or to insist on the implementation of the existing rules?

- The implementation of the SGP is facing many challenges;
- Two core members are increasing their debt to GDP ratios and persistently breaching the 3 percent deficit limit;
- Two other highly-indebted members are not achieving substantial progress in reducing their debt indicators;
- Several other members are not in observance of deficit criteria;
- The 3 percent deficit limit does not guarantee fiscal sustainability for many EU members, particularly in the context of much lower potential growth rates than assumed at the time when the ceiling for the headline deficit was set;
- Concerns about fiscal sustainability of many EU countries are growing, and in the absence of serious adjustment efforts, all members will pay the price;
- Chances to improve the rules change the rules so as to acknowledge the transitory. It makes more sense for the NMS to accept the current fiscal rules and insist on their implementation, then to look for a perfect rule.

- If undertaken, the revisions in SGP targets are unlikely to result in an improved pact;
- The NMS should therefore insist on the implementation of the current pact as a first step toward ensuring fiscal solvency of all member states;
- Interest in ensuring fiscal solvency in the union is much stronger than the relatively minor improvements that a perfect pact could provide.