Welcome address

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Bank of Italy workshop "The EU Fiscal Governance Framework – headed for the future"

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It is a great pleasure to open the Bank of Italy workshop on "*The EU Fiscal Governance Framework – Headed for the future*". The webinar brings together representatives of institutions, experts and academic scholars, to share views on how to reform this aspect of the EU architecture.

This issue is currently more topical than ever. A series of unprecedented shocks, most importantly the COVID pandemic and the energy crisis, have demonstrated that no European country, in isolation, can effectively shield its citizens from the fallout of global events whose consequences can be only dealt with at a supranational level. Coordinated action and common resources are also warranted to meet the challenges of the green and digital transitions.

In order to provide crucial European public goods we do need to update our governance. Our decision process should be based on a wise mix of rules and discretion, and shored up by new common instruments. How to combine these elements is the core question today.

In my view, this webinar takes a very interesting approach, since it not only focuses on fiscal rules but holds several dimensions of the institutional architecture together.

In the Economic and Monetary Union (EMU), in which budgetary policies remain the responsibility of individual member countries but their consequences affect the euro area as a whole (also via their interaction with the single monetary policy), constraints on the discretion of national policies are necessary. Well-designed fiscal rules are useful to counteract several policy biases (e.g. the deficit bias) which tend to distort policy decisions both outside and – even more so – inside a monetary union. Our distinguished keynote speaker will surely elaborate on that.

On the other side, a truly integrated union also needs a central fiscal capacity – and I believe that all the events since the Global Financial Crisis have made the case very clear. Having a fiscal capacity in place would be important, first of all, for macroeconomic stabilization, complementing and facilitating the task of the single monetary policy. It could also reduce the safe asset shortage that currently characterizes European markets. It would make it easier for European intermediaries to diversify their portfolios and strengthen the role of the euro as an international currency. It would be important for financial stability in the event of market tensions.

The two pillars of fiscal governance – supranational constraints on individual countries' policies and a common fiscal capacity – are strictly interconnected and should be designed jointly in a consistent way. If the former are very rigid and do not provide enough room for action when needed, the latter will have to step-in more frequently (the US are a case in point). If instead the rules leave countries with more room for manoeuvre, the common capacity may only have to intervene in the event of a large-scale shock. Designing the two elements in an integrated way would be important to overcome the political obstacles to a change of the status quo: Member States would accept more easily to lose some fiscal discretion at the national level if it is recreated at the European level via a common capacity.

With regard to the current European fiscal rules, I would dare say that nobody is satisfied with them. Even before the pandemic, the Stability and Growth Pact was considered unsatisfactory in many respects: complexity, procyclicality and weak enforcement were among the shortcomings most often underlined. The sharp increase in debt-to-GDP ratios caused by the pandemic and the need to protect households and firms from the effect of the energy crisis put in serious doubt the viability of a simple return to the Stability and Growth Pact's rules as we have known them so far. Their application would require in some cases unrealistic fiscal adjustments, with a serious risk to be self-defeating or circumvented.

Most of the recent and influential reform proposals, some of which will be presented today, go in the direction of simplifying the overall picture. As pointed out recently by our Governor, "there seems to be a consensus not only on the need to renew the Pact, but also on some of the desirable characteristics of the new system of rules".[1] As it will be argued during the webinar, this consensus could form the basis of a simpler, more countercyclical and enforceable set of rules.

Another important issue that will be addressed today is how to best manage the debt accumulated by euro-area countries due to the pandemic. The joint management of a part of these liabilities, for example through a redemption fund, could strengthen the financial stability of the area, reducing the risk of self-fulfilling crises. It would also immediately add depth and liquidity to the European safe asset market. Clearly, the political and legal obstacles to be overcome to move in this direction are huge. However, from a technical point

[1] *The Governor's Concluding Remarks*, Annual Report, Rome, 31 May 2022.

of view, there are solutions that minimize the possibility of a systematic redistribution between countries and preserve the incentive for fiscal discipline.

This afternoon, we will learn a lot about how the appropriate arrangement for the EU architecture should look like. However, this is not enough. We need to clarify how to get there, and to get there quickly, also acknowledging that sometimes the best is the enemy of the good. The panel that concludes our gathering will offer us a thorough discussion in this perspective.

I think today it will emerge clearly that progress on the institutional reform front, in the current economic and geopolitical juncture, is crucial for the future of the European project. It would be instrumental to preserve the integrity of the internal market. It would support the action of the ECB. Last but not least, it would be a powerful demonstration that Europeans can stay the course in dark times and act together in a far-sighted and bold way, driven by a strong sense of solidarity.

I thank you all again for having joined us and wish you all a rich and fruitful discussion.