# Public Deficits in Europe

During the run-up for euro membership the prospective partner countries managed to reduce their public deficits (Table 1). In 1998, the year preceding the introduction of the euro (1 January 1999; euro banknotes and coins were introduced at the beginning of 2002) only two countries had deficits *not* less than 3 percent, while in 1999 each of the 12 euro countries met this upper limit value, some countries even showing surpluses. (The 3 percent and 60 percent upper limit reference rules were introduced with the Maastricht Treaty of 1992, formally launching the European Monetary Union project. The Stability and Growth Pact of 1997 added to the rules that budgetary positions should normally be "close to balance or in surplus" and provided mechanisms for multilateral surveillance and enforcement.) In 2000, the average public budget balance of the 12 euro countries was even slightly positive. In meeting the other reference value, the debt to GDP ratio of 60 percent at maximum, countries were less successful when forming the euro area (Table 2). In 1999 it was only 5 out of 12 countries that met the debt standard.

The development of deficits from 2001 until 2005 took another direction than before 1999 (Table 1). The *average* public deficit of the euro countries increased continuously and became not much less than the upper limit value in 2004 and 2005 (forecast). The debt level, however, has continued to improve slightly (Table 2), being influenced not only by the budget balance but also by sales of public assets (e.g. UMTS).

**Table 1**

**Nominal budget balance in EU–12 countries (as % of GDP), 1993–2005**

| | Average 1993–98 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|---|---|---|---|
| Austria | –3.8 | –2.5 | –2.4 | –1.6 | 0.1 | –0.4 | –1.3 | –1.3 | –2.1 |
| Belgium | –3.8 | –0.7 | –0.4 | 0.1 | 0.5 | 0.0 | 0.2 | –0.5 | –0.8 |
| Finland | –3.4 | 1.6 | 2.2 | 7.1 | 5.2 | 4.3 | 2.1 | 1.8 | 2.0 |
| France | –4.4 | –2.7 | –1.8 | –1.4 | –1.5 | –3.1 | –4.1 | –3.7 | –3.6 |
| Germany | –3.0 | –2.2 | –1.5 | 1.3 | –2.8 | –3.5 | –3.9 | –3.6 | –2.8 |
| Greece | –7.9 | –2.5 | –1.8 | –2.0 | –1.4 | –1.5 | –3.0 | –3.2 | –2.8 |
| Ireland | –0.4 | 2.3 | 2.3 | 4.4 | 1.1 | –0.1 | 0.2 | –0.8 | –1.0 |
| Italy | –6.5 | –3.1 | –1.8 | –0.7 | –2.7 | –2.4 | –2.5 | –3.2 | –4.0 |
| Luxembourg | 2.4 | 3.2 | 3.7 | 6.3 | 6.3 | 2.7 | –0.1 | –2.0 | –2.3 |
| Netherlands | –2.4 | –0.8 | 0.7 | 2.2 | 0.0 | –1.6 | –3.2 | –3.6 | –3.3 |
| Portugal | –4.8 | –3.2 | –2.9 | –2.9 | –4.4 | –2.7 | –2.9 | –3.5 | –3.9 |
| Spain | –5.1 | –3.0 | –1.2 | –0.9 | –0.4 | –0.1 | 0.3 | 0.5 | 0.6 |
| EU–12 | –4.2 | –2.3 | –1.3 | 0.1 | –1.6 | –2.3 | –2.7 | –2.8 | –2.6 |

Source: Flores, E. et al. (2005) and sources given there.

For 2005, only Finland's and Spain's budgets are projected to be clearly "in surplus", while the Belgian budget, with a deficit of 0.8 percent, can be regarded as "close to balance". All other countries will most probably miss the standards of the Stability and Growth Pact by far, and some will not even meet the laxer provisions of the Maastricht Treaty.

The usual explanation put forward by the national governments focuses on the argument that there is a current but temporary deficiency of economic growth. Budg-

**Table 2**

**General government gross debt in EU–12 countries (as % of GDP), 1993–2005**

| | Average 1993–98 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|---|---|---|---|
| Austria | 65.5 | 63.7 | 67.5 | 67.0 | 67.1 | 66.6 | 65.0 | 65.5 | 65.3 |
| Belgium | 130.4 | 119.6 | 114.8 | 109.1 | 108.1 | 105.8 | 100.5 | 97.4 | 94.3 |
| Finland | 55.1 | 48.6 | 47.0 | 44.6 | 43.9 | 42.6 | 45.3 | 44.5 | 44.3 |
| France | 54.0 | 59.5 | 58.5 | 57.2 | 56.8 | 58.6 | 63.0 | 64.6 | 65.6 |
| Germany | 55.8 | 60.9 | 61.2 | 60.2 | 59.4 | 60.8 | 64.2 | 65.6 | 66.1 |
| Greece | 108.7 | 105.8 | 105.2 | 106.2 | 106.9 | 104.7 | 103.0 | 102.8 | 101.7 |
| Ireland | 76.3 | 53.8 | 48.6 | 38.4 | 36.1 | 32.3 | 32.0 | 32.4 | 32.6 |
| Italy | 121.4 | 116.7 | 115.5 | 111.2 | 110.6 | 108.0 | 106.2 | 106.0 | 106.0 |
| Luxembourg | 6.7 | 6.3 | 6.0 | 5.5 | 5.5 | 5.7 | 4.9 | 4.5 | 3.8 |
| Netherlands | 74.1 | 66.8 | 63.1 | 55.9 | 52.9 | 52.6 | 54.8 | 56.3 | 58.6 |
| Portugal | 60.4 | 55.0 | 54.3 | 53.3 | 55.6 | 58.1 | 59.4 | 60.7 | 62.0 |
| Spain | 63.8 | 64.6 | 63.1 | 61.2 | 57.5 | 54.6 | 50.8 | 48.0 | 45.1 |
| EU–12 | 72.2 | 74.1 | 72.8 | 70.4 | 69.4 | 69.2 | 70.4 | 70.9 | 70.9 |

Source: Flores, E. et al. (2005) and sources given there.

et deficits are, thus, necessary in order to strengthen – instead of undermine – growth forces. Indeed, economic growth in Europe was much more favourable in 1999 and 2000 than in later years. But it was only in 2000 that on average governments of euro countries did *not* produce a *budget deficit*. And that surplus was minimal. (Cyclically-adjusted figures (not shown) give, basically, a similar picture.) Part of the current budget difficulties seems to stem from not having adhered to the rules in the better years of 1999 and 2000. Moreover, countries should accept some theoretical as well as some new empirical evidence which strengthens the (old) scepticism towards an active use of fiscal policy in stabilising the economy, let alone in the attempt to increase economic growth. One piece of evidence which specifically supports this scepticism relates to the fact that the net effect of fiscal policy in Europe between 1992 and 2003 was *pro-cyclical* (Flores et al. 2005; Buti and van den Noord 2004).

**Table 3**

**Long–term debt to GDP ratio in EU–15 countries, 2005**

| | 2003 | Programme scenario | | | 2003 budget scenario | | |
|---|---|---|---|---|---|---|---|
| | | 2010 | 2030 | 2050 | 2010 | 2030 | 2050 |
| Austria | 66.4 | 53.9 | 24.4 | 15.9 | 55.1 | 26.1 | 18.4 |
| Belgium | 102.3 | 74.8 | 11.5 | –5.0 | 67.2 | –35.7 | –114.0 |
| Denmark | 42.7 | 24.6 | –19.5 | –34.8 | 6.9 | –65.5 | –131.9 |
| Finland* | –14.6 | –33.4 | –30.1 | 6.0 | –52.8 | –79.5 | –88.6 |
| France | 61.4 | 56.0 | 52.2 | 72.0 | 71.8 | 142.1 | 288.0 |
| Germany | 64.0 | 62.2 | 86.5 | 175.7 | 74.3 | 156.5 | 336.6 |
| Greece | 101.7 | 75.1 | 42.2 | 151.0 | 72.2 | 52.4 | 181.0 |
| Ireland | 33.1 | 26.7 | 36.4 | 105.0 | 27.0 | 50.1 | 138.4 |
| Italy | 106.0 | 86.6 | 28.9 | –27.8 | 92.0 | 82.7 | 107.8 |
| Luxembourg | 4.9 | –0.9 | –9.4 | 1.2 | –3.9 | –35.7 | –47.8 |
| Netherlands | 54.0 | 49.1 | 67.6 | 140.0 | 53.8 | 88.7 | 185.9 |
| Portugal | 59.5 | 48.0 | 5.3 | –42.4 | 60.9 | 72.1 | 127.6 |
| Spain | 51.8 | 36.3 | –1.6 | 36.6 | 31.6 | –21.4 | –12.4 |
| Sweden* | 33.0 | 16.4 | –0.4 | 46.7 | 15.2 | 19.8 | 97.6 |
| United Kingdom | 39.3 | 42.5 | 71.6 | 138.7 | 45.3 | 89.5 | 177.5 |

Notes: *Adjusted gross debt, netting off the accumulated liquid financial assets. Due to differing measurement concepts, debt figures for 2003 in Tables 2 and 3 differ somewhat.

Source: Flores, E. et al. (2005) and sources given there.

Why is the question of budget discipline so important? Because the budget positions of some countries pose a risk for the sustainability of the public finances of these countries and of the European Monetary Union as a whole. Table 3 reproduces a projection of long-term debt for the EU-15 countries, as calculated by the European Commission. Figures of such a long-term projection exercise are necessarily rather questionable. But they show what might happen if policy is not changed. The projection is made under two assumptions for the cyclically-adjusted primary balance (CAPB). In the (more favourable) "programme scenario" it is assumed that the CAPB can be held at the level of the "programme", i.e. of the latest updated stability or convergence projection (over 5 years) of a country, while the (less favourable) "2003 budget scenario" assumes that CAPB remains at the level of the latest fiscal year.

In nearly all countries, the debt-to-GDP ratio (for both scenarios) is projected to improve, in some cases considerably, between 2003 and 2010. This might be mainly due to the assumption of budget discipline and of higher growth rates (higher than current ones, even if on a lower level than in the 1990s). The turn-around into a negative direction will occur around 2030 when the impact of ageing populations is severely felt. For some countries this turn-around is expected to occur later. In 2050, within the programme scenario, 8 countries out of 15 will have worse debt figures – sometimes much worse – than they had in 2003.

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## References


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