



Assessing public debt sustainability: challenges ahead

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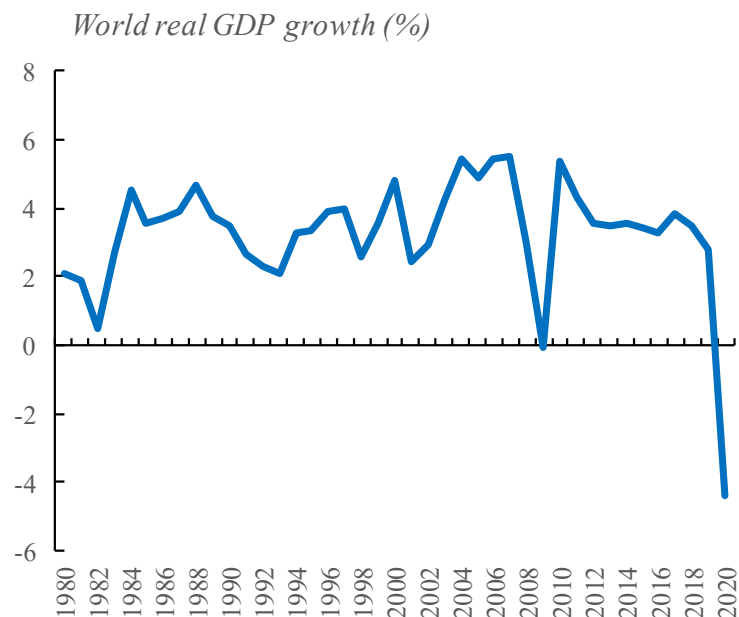
ECFIN.C – Macroeconomic policies

Irish Fiscal Council conference, 8-9 February 2021

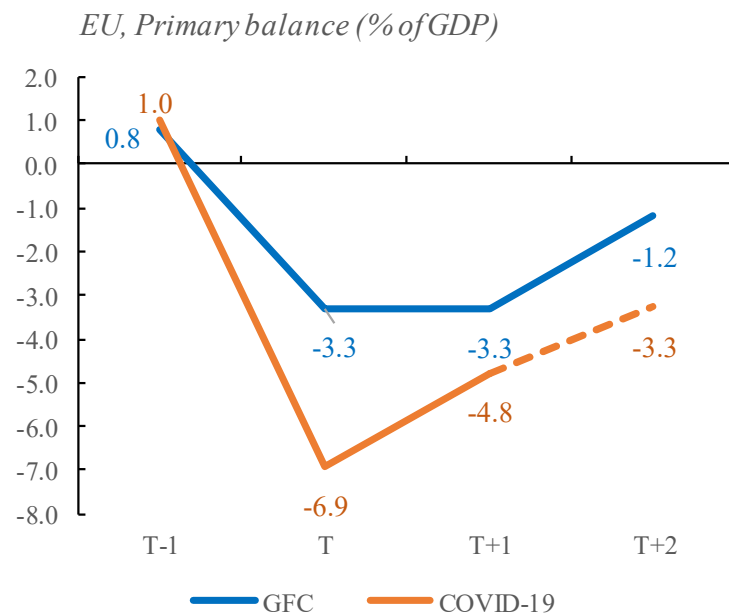
Outline

- An analysis of debt sustainability risks through the lens of the COM regular fiscal sustainability analysis framework (DSM 2020)
- Opportunities/challenges ahead:
 - The potential implications of EU recent initiatives (NGEU/RRF) on debt sustainability
 - Debt sustainability meets new fiscal risks

An unprecedented crisis and fiscal policy response



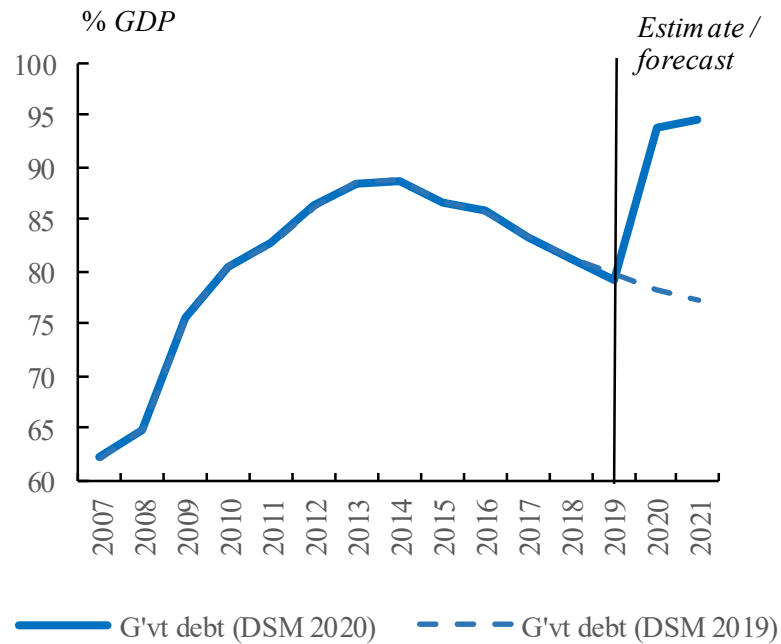
Source: WEO (Oct. 2020)



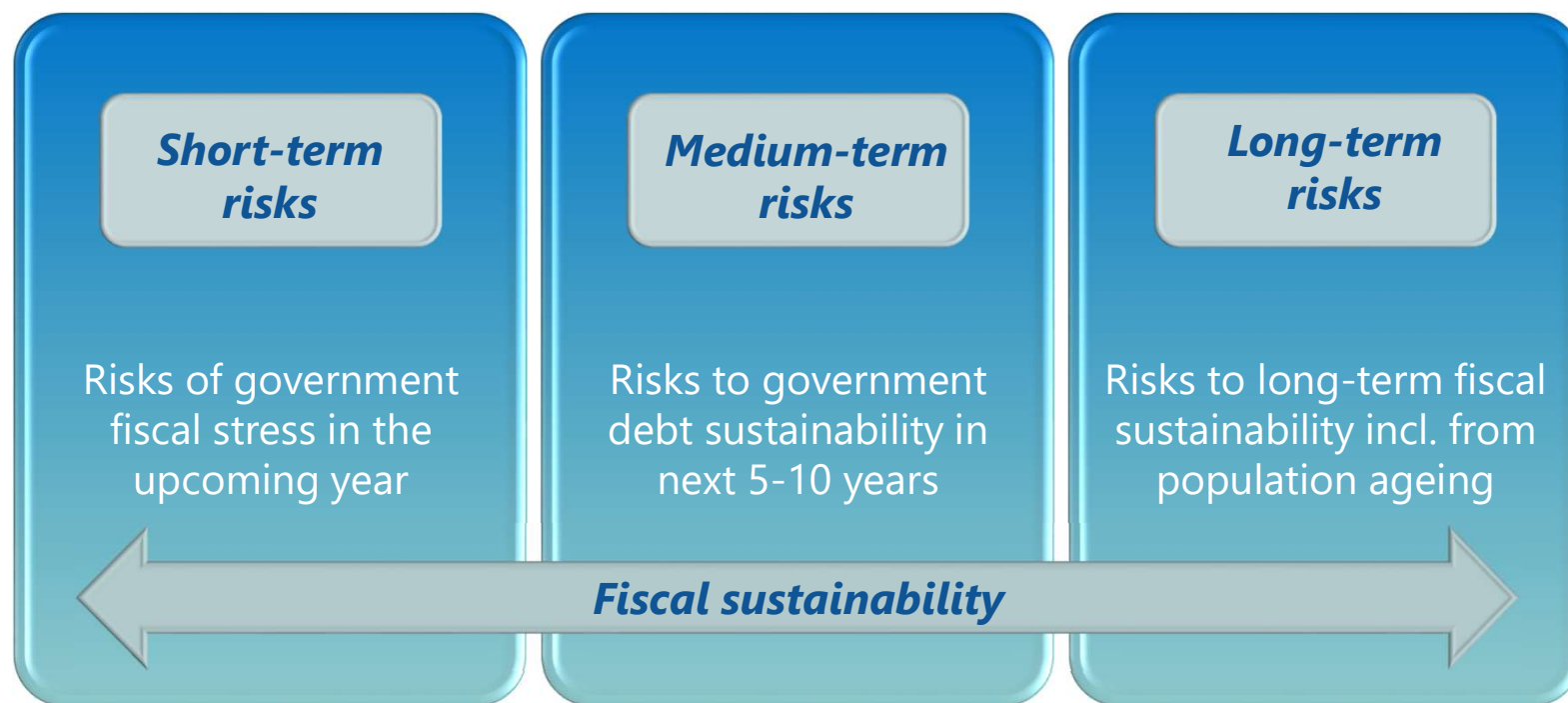
Source: AMECO (Nov. 2020)

A large increase of public debt ratios in the EU

EU general government debt ratio



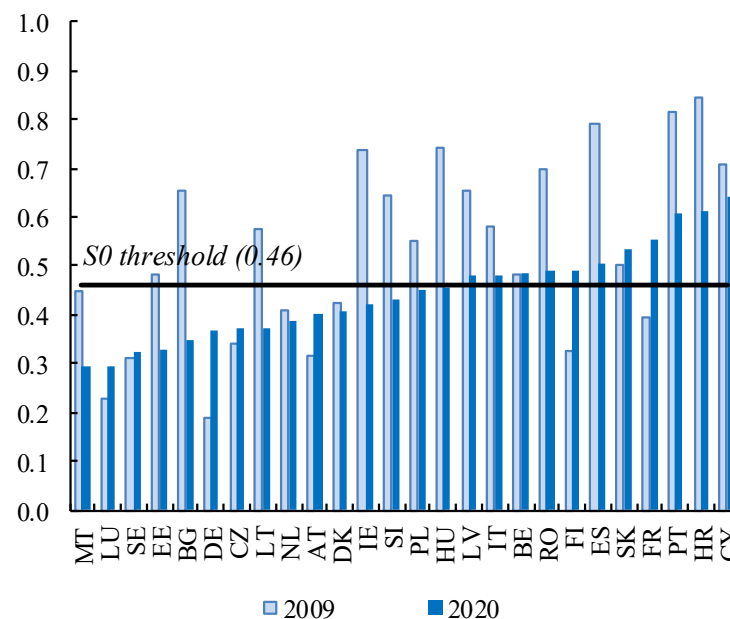
The Commission fiscal sustainability analysis framework



Short-term vulnerabilities have increased

- Eleven countries present short-term vulnerabilities
 - Less than during the GFC – due to sounder macro-financial positions
- ✓ *S0 is an early-warning indicator that measures risks of fiscal stress in the upcoming year (based on 25 variables)*

S0 indicator, 2009 versus 2020



Source: DSM 2020

Sovereign financing conditions supported by rapid and adequate set of policy responses

- EU fiscal rules GEC => fiscal policy to support the economy
- Eurosystem's interventions
- Rapid set-up of new crisis instruments (SURE, ESM PCS, EIB, etc.)
- Agreement on large EU recovery plan (NGEU/RRF)

Government financing needs and (possible) total acquisitions of sovereign bonds by the Eurosystem

	2020			2021		
	GFNs, EUR bn	Public sector asset purchases under APP and PEPP, EUR bn	Public sector asset purchases under APP and PEPP, % GFNs 2020	GFNs, EUR bn	Ranges of possible public sector asset purchases under APP and PEPP, EUR bn	Ranges of possible public sector asset purchases under APP and PEPP, % GFNs 2021
BE	115.1	35.7	31.0	99.0	(16.8 - 32.1)	(16.9 - 32.4)
DE	734.5	226.1	30.8	558.2	(121.2 - 232.2)	(21.7 - 41.6)
EE	2.3	0.6	26.9	1.8	(1.3 - 2.5)	(72.4 - 138.7)
IE	43.4	16.0	36.8	37.0	(7.8 - 14.9)	(21.0 - 40.3)
ES	305.6	116.9	38.3	299.8	(54.8 - 105.1)	(18.3 - 35.0)
FR	598.2	185.4	31.0	606.5	(93.9 - 179.9)	(15.5 - 29.7)
IT	534.6	174.0	32.6	497.0	(78.1 - 149.7)	(15.7 - 30.1)
CY	5.0	2.9	58.9	2.1	(1.0 - 1.9)	(47.4 - 90.9)
LV	3.8	1.5	40.7	1.9	(1.8 - 3.4)	(95.9 - 183.8)
LT	7.5	3.3	43.5	5.7	(2.7 - 5.1)	(46.3 - 88.7)
LU	4.4	1.7	38.5	2.4	(1.5 - 2.9)	(64.1 - 122.7)
MT	1.9	0.4	19.4	1.8	(0.5 - 0.9)	(26.5 - 50.7)
NL	143.7	42.5	29.6	126.1	(26.9 - 51.6)	(21.4 - 41.0)
AT	69.4	27.6	39.8	59.6	(13.5 - 25.8)	(22.6 - 43.3)
PT	39.6	20.7	52.2	31.9	(10.8 - 20.6)	(33.7 - 64.6)
SI	10.0	4.2	42.5	6.3	(2.2 - 4.2)	(35.1 - 67.3)
SK	15.1	7.4	48.8	9.7	(5.3 - 10.1)	(54.3 - 104.1)
FI	42.2	14.1	33.4	36.6	(8.4 - 16.2)	(23.1 - 44.2)

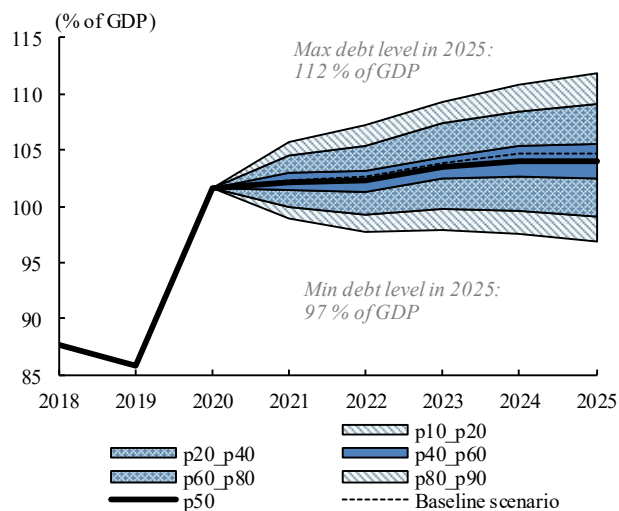
Source: DSM 2020

Assessing medium-term risks in times of uncertainties

- Exceptional high level of uncertainty due to on-going pandemic crisis developments
- Baseline rests on technical assumptions and first estimations of the impact of the crisis on medium-term growth:
 - Gradual fiscal correction assumed, meaning a reversal of temporary measures and 'financing' of permanent ones
 - Some scarring on the economy
 - The effects of NGEU/RRF is not included, given on-going implementation

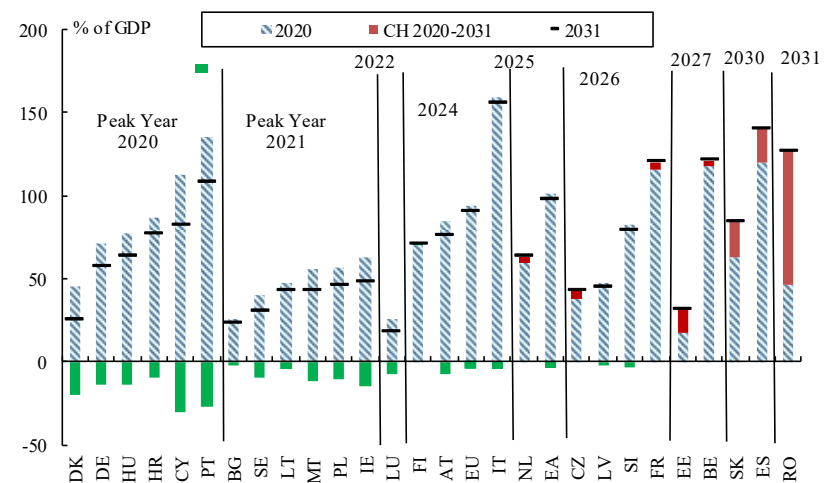
Medium-term risks on the rise

EA stochastic debt projections, 2021-25



Source: DSM 2020

Projected debt ratios by EU country, T+10



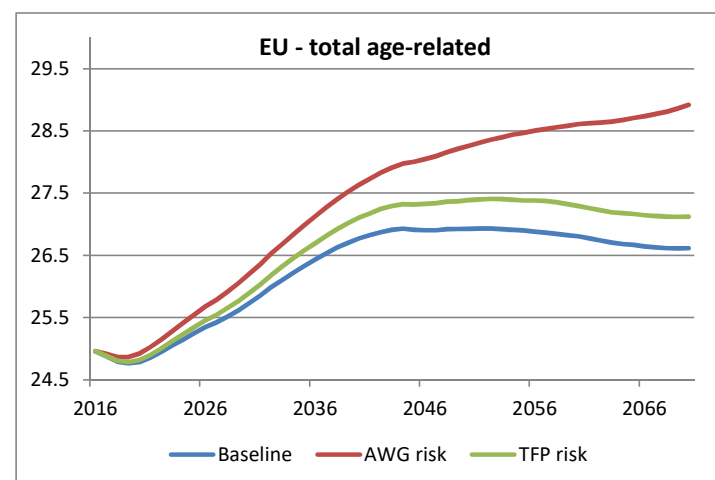
Source: DSM 2020

- A high probability that debt will not decrease in the next 5 years (*not taking into account potential RRF impact*)
- In some highly indebted countries, risks of a late decrease of the debt ratio under the baseline

In the longer term, challenges made acute by population ageing

- Projected long term budgetary costs show a substantial increase until the mid-2040s
- Implementation challenges of pension reforms (with many pension reform reversals observed over the past years)
- Risks higher in case of slow(er) productivity gains and fast(er) increase of health-care costs (due to non-demographic drivers)

Projected long-term budgetary spending (incl. pension, health-care, long-term care and education)



Source: Ageing Report 2018

Potential implications of NGEU/RRF

- Significant potential macroeconomic impact
- Demand (short-term) and supply effects (medium/long term)
- Effects will depend on several factors (additionality/absorption capacity, quality/long lasting impact of measures, etc.)
- Significant impact on debt estimated based on Quest

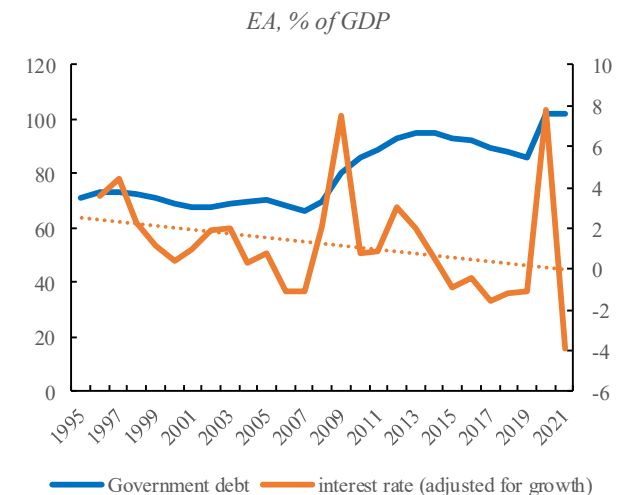
RRF grants: allocation by country

	Maximum RRF Grant available per country		
	Amount (EUR Bls)	Share of GDP (%)	Share of EU (%)
BE	5.9	1.3	1.8
BG	6.3	10.6	1.9
CZ	7.1	3.4	2.1
DK	1.6	0.5	0.5
DE	25.6	0.8	7.6
EE	1.0	3.6	0.3
IE	1.0	0.3	0.3
EL	17.8	10.8	5.3
ES	69.5	6.3	20.6
FR	39.4	1.7	11.7
HR	6.3	13.0	1.9
IT	68.9	4.2	20.4
CY	1.0	4.8	0.3
LV	2.0	6.8	0.6
LT	2.2	4.6	0.7
LU	0.1	0.2	0.0
HU	7.2	5.4	2.1
MT	0.3	2.5	0.1
NL	6.0	0.8	1.8
AT	3.5	0.9	1.0
PL	23.9	4.6	7.1
PT	13.9	7.0	4.1
RO	14.2	6.7	4.2
SI	1.8	3.9	0.5
SK	6.3	7.1	1.9
FI	2.1	0.9	0.6
SE	3.3	0.7	1.0
EU	338.0	2.6	100

Debt sustainability meets new fiscal risks

- Health hazard
 - Climate change phenomenon
 - Digitalisation of the economy (tax bases)
 - Etc.
- ✓ *Key will remain the interest – growth rate differential => ability to sustain (and progressively reduce) high debt levels*

EA government debt and $r-g$



Source: AMECO (Nov. 2020)

Thank you



https://ec.europa.eu/info/sites/info/files/economy-finance/ip143_en.pdf

