A view of fiscal consolidation results in the European Union

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Institute of Public Finance | No. 79 | Zagreb May 12, 2015
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PRESS RELEASES

A view of fiscal consolidation results in the European Union

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The EU28 reduced its governments' deficit by 0.3 percentage points compared with 2013, but its general government debt rose by 1.3 percentage points. Croatia is one of seven Member States contributing to the growth of general government deficit and debt in the EU. The Eurostat's news release, issued on 21 April 2015, contains new data on government finance for the period 2011-2014. The data are based on a new methodology for calculating government deficit and debt (in accordance with ESA 2010), used under the excessive deficit procedure.

The EU28 governments' deficit decreased by 0.3 percentage points, i.e. from 3.2% of GDP in 2013 to 2.9% in 2014. Twelve countries failed to meet the Maastricht criterion of the consolidated general government deficit not exceeding 3% of GDP. The countries with the largest deficits are Cyprus (8.8%), Spain (5.8%) and Croatia and UK (5.7% each). The deficits of other Member States range between 3.2% and 4.9% of GDP. Four Member States recorded budget surpluses: Denmark (1.2%), Germany (0.7%) and Estonia and Luxembourg (0.6% each). Government deficits below 3% were reported in Latvia (0.7%), Lithuania (1.4%) and Romania (1.5%). Twelve countries reduced their government deficits, most of all Slovenia (by 10 percentage points, see Graph 1).

General government debt-to-GDP ratio in the EU28 rose by 1.3 pp, i.e. from 85.5% of GDP in 2013 to 86.8% in 2014. General government debt exceeded 60% in sixteen countries, primarily Greece (177%), Italy (132%), Portugal (130%), Ireland (110%), Cyprus (108%) and Belgium (107%). The lowest debt-to-GDP ratios were seen in Estonia (10.6%), Luxembourg (23.6), Bulgaria (27.6%), Romania (39.8%) and Latvia (40%). The fastest debt growth occurred in Slovenia, Bulgaria, Spain, Cyprus, Sweden and Croatia. As many as nine Member States reduced their general government debts, particularly Ireland (by as much as 13.6 pp, see Graph 2). The Maastricht criterion of the general government debt not exceeding 60% of GDP should be revised. It has not made sense for quite a long time, and it is an illusion to expect that certain countries will manage to meet this target in the foreseeable future (ten years) as well. Instead of gross debt, the European Commission should set a new criterion based on the net debt concept, i.e. the difference between financial liabilities and financial assets.

The share of interest expenses on general government debt in GDP in the EU28 decreased by 0.2 pp, from 2.7% to 2.5% of GDP. In nine Member States, interest expenses exceeded 3% of GDP, most of all in Portugal, Italy and Hungary (by 4% to 5% of GDP), followed by Greece, Croatia, Spain, Slovenia and Belgium (3%-4%). Seventeen countries reported interest expenses ranging from 1% to 3% of GDP, while the lowest interest expenses were seen in Bulgaria, Sweden, Luxembourg and Estonia (see Graph 3).

General governments' expenditure in the EU decreased from48.6% to 48.1% of GDP. Government spending shrank by 0.2 to 10.7 pp in fifteen Member States (by 7 pp in Slovenia and Greece). The decline in government spending was due to reforms and GDP growth, as an indirect award for the implementation of the reforms. Finland had the highest (58% of GDP) and Romania the lowest government spending (34% of GDP). In fourteen Member States, government spending went up from 0.2 pp to a maximum of 7 pp of GDP (Cyprus). Croatia is among countries which saw an increase in government spending of 0.3 pp (see Graph 4).

In 2014, subsidies went up by 0.1 pp in the EU, standing at an average of 1.3% of GDP. Subsidies between 2% and 2.9% of GDP were reported by Belgium, Czech Republic, Denmark, France and Croatia. In all the other Member States, they remained at the previous year's levels. Only in France, subsidies increased by 0.5 pp of GDP. Fifteen Member States reported subsidies from 1% to 1.9%, and in eleven countries they ranged from 0.3% to 0.9% of GDP. In Croatia, subsidies were cut by 0.1 pp, while more significant reductions were seen in Bulgaria, Greece, Slovenia, Poland, Romania and Estonia (see Graph 5).

Stocks of liabilities from trade credits and advances. As a consequence of the financial crisis, Member States prolonged the repayment of their liabilities. Eurostat wished to include these transactions in the statistics because of their potential impact on debt and deficit. Trade credits are unpaid (usually short-term) government liabilities resulting from transactions in goods and services which have not been paid in cash immediately but with a certain delay. Member States are required to report data on their respective trade credits to Eurostat twice a year (at end-March and end-September), together with the reporting of government deficit and debt data[1]. While the expenditure relating to trade credits is included in ESA government expenditure in line with the accrual principle, and thus it impacts the Maastricht deficit, the stock of trade credits is not included in the Maastricht government debt. Italy has the highest level of trade credits (3.1%), followed by Slovenia (2.9%) and Croatia (2% of GDP). In Croatia, trade credits decreased from HRK 7.2bn (2.2% of GDP) in 2013 to HRK 6.6bn (2.0% of GDP) in 2014[2].

Professional reservations about the data. In its news release, Eurostat expressed reservations about the quality of data for Bulgaria and Portugal. In Bulgaria, there was a problem with the Deposit Insurance Fund data, due the payment of deposits worth BGN 3.7bn (about EUR 1.89bn) to the depositors of the bankrupt *Corporate Commercial Bank*. This transaction is likely to increase government deficit. Similarly, Eurostat had reservations about data reported by Portugal, namely the statistical treatment of data on the recapitalisation of the *Novo Banco* in the amount of EUR 4.9bn (2.8% of GDP)[3].

The Portuguese statistical office has recorded the entire amount as a financial transaction with no impact on the government deficit. Eurostat will, in co-operation with the Portuguese statistical office, assess the final impact of this transaction based on the data on the amount of receipts from the privatisation of *Novo Banco*. This recapitalisation transaction will probably be recorded as an increase in government deficit.

Political reservations about the data - Croatia. In Croatia, political reservations about the Croatian Bureau of Statistics (CBS) data were expressed by the Ministry of Maritime Affairs, Transport and Infrastructure, with respect to the way of recording the Zagreb Airport concession. The CBS has, in line with ESA 2010 and Manual of General Government Deficit and Debt, recorded the said concession as an item increasing the general government debt, because, in case of an early termination of the concession agreement, the government would be forced to assume more than half of the debt on account of an issued guarantee. According to Eurostat rules, such transactions are recorded as contributions to debt growth. Hence, the CBS has recorded the concession transaction correctly.

Compared to other EU Member States, Croatia is a country with average government spending, an average size of public debt (growing at extremely high rates), a huge government deficit and heavy interest expenses on debt. Croatia has higher subsidies on average and a higher default risk than other Member States. The default risk exists in state owned companies (primarily the national railway and motorway companies). In contrast to other Member States which are faced with banking system problems and growing costs of bank recapitalisation, potential fiscal risks in Croatia are mainly related to the operations and high liabilities of state owned companies.

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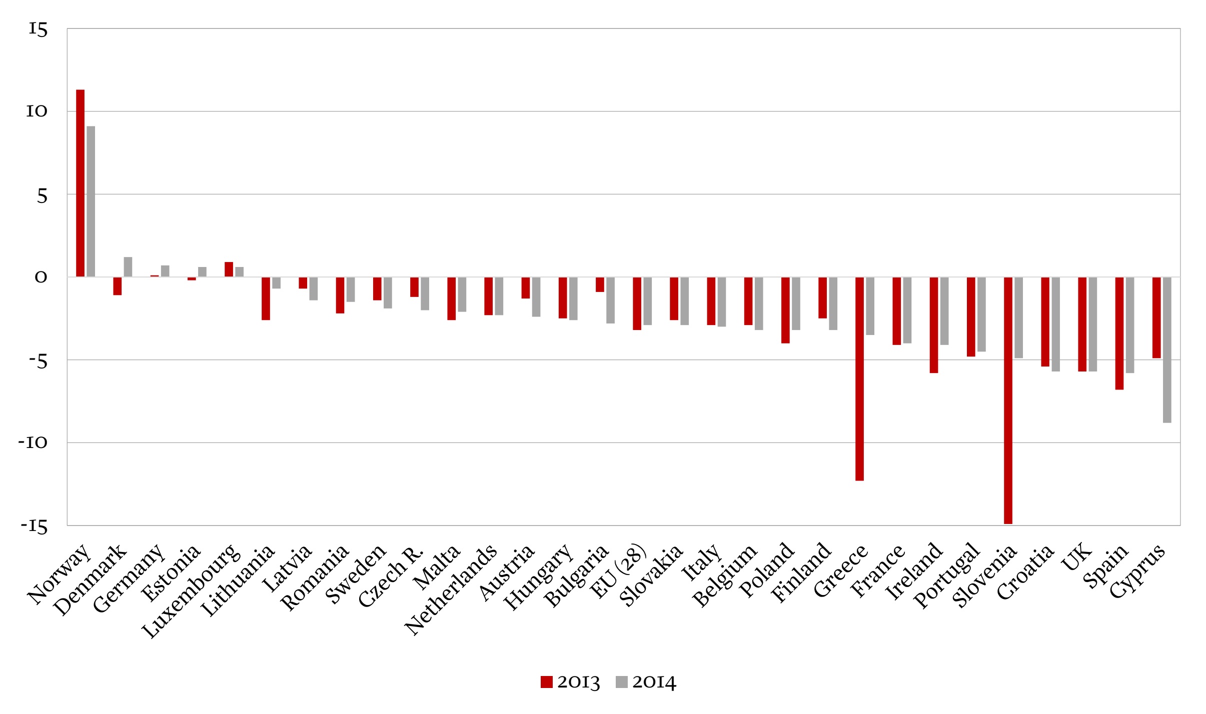
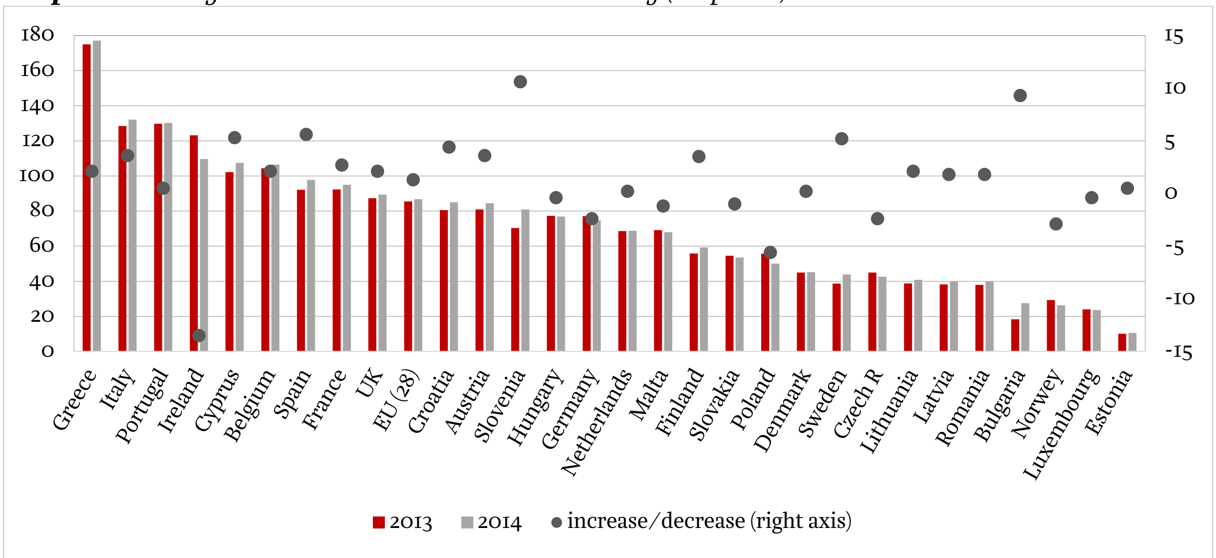
[1] See Table 4 under the note on deficit and debt: *Provision of other data in accordance with the statements contained in the Council minutes 22/11/1993*.
[2] These are estimated data on trade credits taken out by public companies (HRT, Croatian Railways Infrastructure Ltd, Rijeka-Zagreb Motorway Ltd and Croatian Motorways, Ltd), classified as 'general government sector' units.
[3] For more details, see Banco de Portugal web site.

Graph 1 *Governments' deficit/surplus as % of GDP in EU28 and Norway*



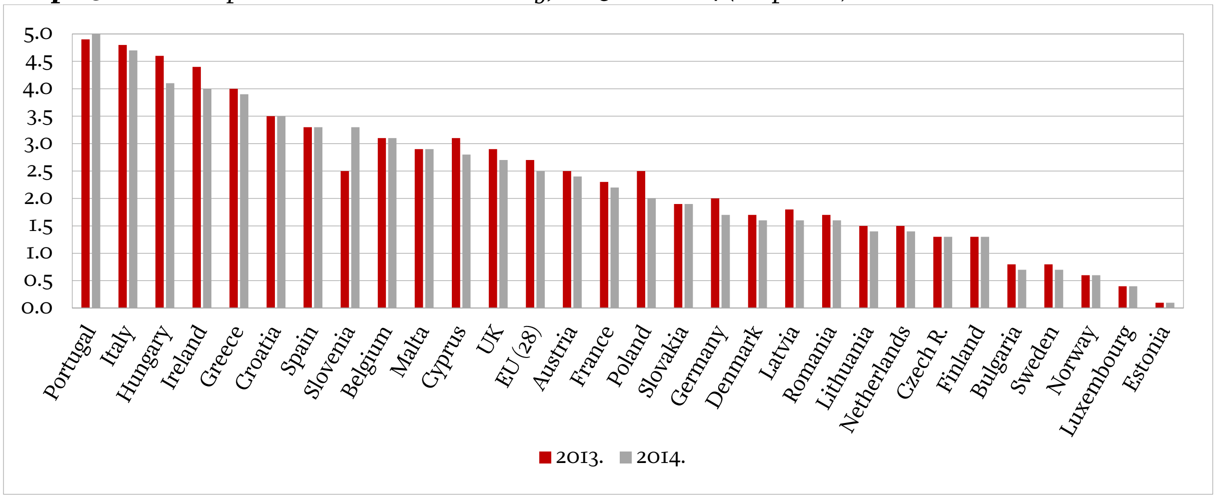
Source: Eurostat, 2015

Graph 2 *General governments' debt in EU28 and Norway (% of GDP)*



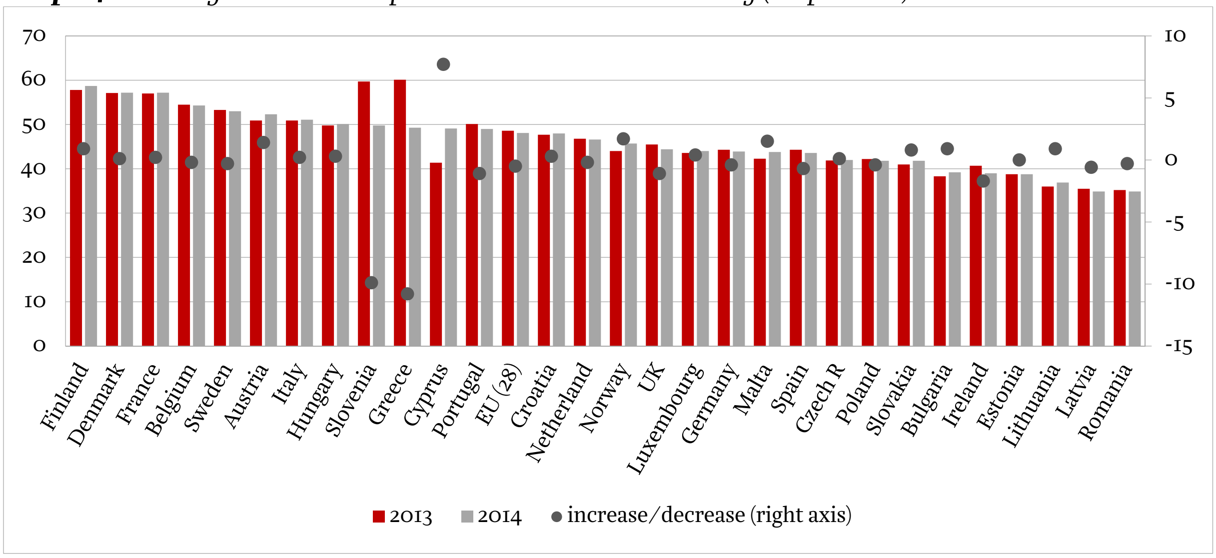
Source: Eurostat, 2015

***Graph 3** Interest expenses in EU28 and Norway, 2013 and 2014 (% of GDP)*



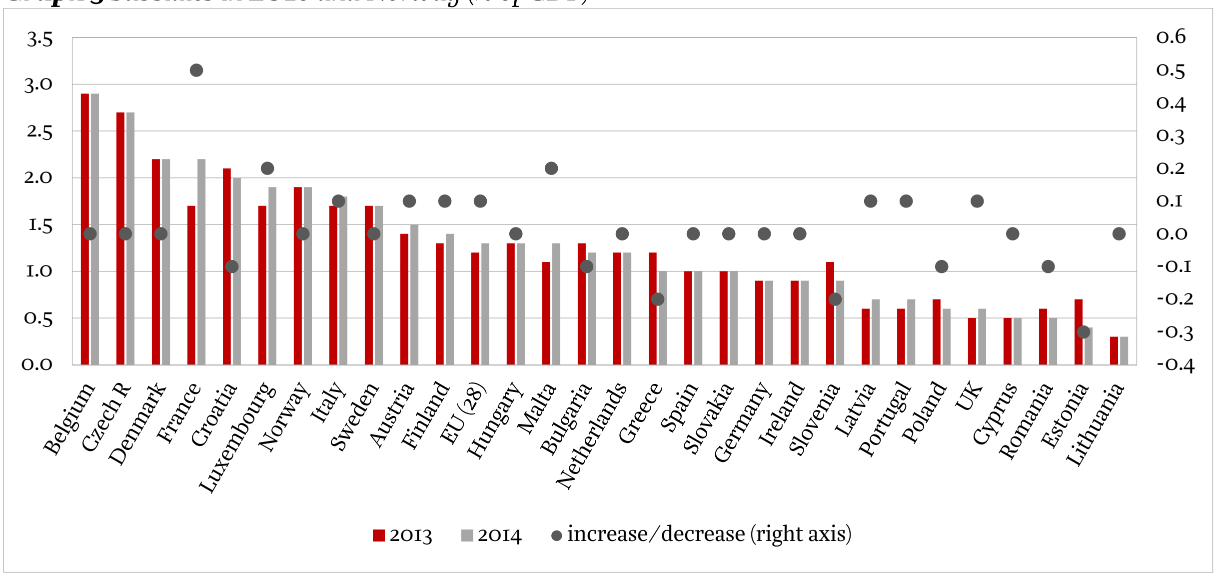
Source: Eurostat, 2015.

***Graph 4** General governments' expenditures in EU28 and Norway (% of GDP-a)*



Source: Eurostat, 2015.

***Graph 5** Subsidies in EU28 and Norway (% of GDP)*



Source: Eurostat, 2015.