

The ‘Sense and Nonsense of Maastricht’ revisited: What have we learnt about stabilization in EMU?

Willem H. Buiter^{*}

Professor of European Political Economy
European Institute, London School of Economics and Political Science,
Universiteit van Amsterdam, CEPR and NBER

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I find myself in the unusual position of having co-authored a paper (Buiter and Kletzer (1991)) criticising the fiscal-financial Maastricht criteria for EMU membership and the Stability and Growth Pact (SGP), even before the Maastricht Treaty had been signed (on February 7, 1992) or even drafted, and well before the birth of the SGP in 1997 and its revision/emasculation in 2005. We could do this because the key fiscal-financial features, and their manifest flaws, were foreshadowed quite accurately in the Delors Report (1989))

While this lecture will focus on the fiscal criteria, the excessive deficits procedure (EDP) fiscal-financial stability and macroeconomic stabilisation, I will start with a few remarks on the inflation and exchange rate criteria for EMU membership, because they are becoming highly relevant to the chances for early full EMU membership of some of the new EU members.

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The Maastricht Criteria and EMU accession by the new EU member states

The short version of the Maastricht criteria for full membership in EMU is as follows. There is a pair of fiscal/financial criteria, a ceiling on the general government deficit - to - GDP ratio of 3 percent and a ceiling on the gross general government debt - to - annual GDP ratio of 60 percent. There also is an interest rate criterion: long-term (ten year) nominal interest rates on central government debt are to be within 2 percent of the average in the three countries with the best inflation record. Next comes the inflation criterion: the annual inflation rate cannot exceed the average of the three best performing countries by more than 1.5 percent during the year prior to the examination (that is, the formal assessment as to whether a candidate has met the EMU membership criteria). Finally, there is the exchange rate criterion: the exchange rate has to respect the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System without severe tensions for at least the last two years before the examination. In particular, the Member State shall not have devalued its currency on its own initiative for the same period. The interpretation of the ECB and, until quite recently, of the European Commission, of the exchange rate criterion has been that EMU candidates will have to join an ERMII arrangement, with ± 15 percent fluctuation bands around a fixed central parity vis-à-vis the euro, for two years prior to joining EMU. There is also the requirement that the central bank of the candidate country be independent, as defined in the protocols of the Treaty.

I will not deal with the role of the fiscal-financial criteria in the EMU membership stakes. They are unlikely to be a binding constraint for the countries that, on fundamental economic grounds, are ready to join the EMU. Currently that group includes the three Baltic

states, Slovenia and Slovakia.¹ However, the combination of the inflation criterion and the exchange rate criterion could delay the EMU entry of fundamentally viable candidate countries. Estonia, probably the best functioning market economy in the EU25, is in that position, and so is Latvia. Estonia, Lithuania and Slovenia all joined ERM2 at the end of June 2004 and intend to become full EMU members on January 1, 2007. Latvia, which joined ERM2 on May 2, 2005, intends to achieve full EMU membership during 2008.

Estonia's annual inflation rate is currently running at around 4 percent per annum, Latvia's at around 6.5 percent (see Table 1).²

Table 1 here

Estonia has a currency board with a peg to the euro. Latvia has an effectively fixed exchange rate with the euro. For both these very small and very open economies, a fixed exchange rate is the appropriate choice of currency regime while in the waiting-room (or purgatory) of full EMU membership. Both countries are growing at an astounding rate (see Table 2).

Table 2 here

Estonia achieved an annual growth rate of real GDP of 6.7 percent in 2003, 7.8 percent in 2004 and 6.9 percent in 2005Q1. The corresponding figures for Latvia are 7.2 percent, 8.3 percent and 7.4 percent. Among the old EU15 member states, only Ireland has come anywhere close to the growth record achieved by the Baltic countries during the past decade (see Table 2 and Table 3).

Table 3 here

¹ The other CEE new EU members, Poland, Hungary and the Czech Republic all require up-front, large and enduring fiscal tightening to become credible candidates for Eurozone membership. Hungary's loss of fiscal control (with estimates of next year's unfunded general government deficit in excess of 12 percent of GDP), is such that, without dramatic early spending cuts and/or tax increases) a combined exchange rate collapse and public debt crisis appears likely.

² The latest (August 2005) figure for annual HICP inflation in Estonia is 4.2 percent; for Latvia the corresponding figure is 6.3 percent (ECB (2005)).

Because of the Balassa-Samuelson effect, the equilibrium real exchange rates of these two countries (and other transition countries, emerging market economies and developing countries engaged in successful real catch-up or real convergence) will experience a trend appreciation during the process of real convergence or catch-up. With a fixed nominal exchange rate, an appreciating real exchange rate means a positive inflation differential of the two candidate countries vis-à-vis the EMU as a whole. This equilibrium real exchange rate appreciation and inflation differential vis-à-vis the EMU average could well exceed the 1.5 percent permitted under the inflation criterion.³ This would preclude the countries in question from joining EMU unless they implemented one of two economically undesirable policies.

The first would be to abandon their fixed exchange rates with the Euro and to permit their currencies to appreciate vis-à-vis the Euro, this bringing down their inflation rates below the critical level. For Estonia to abandon a currency board for one or two years in order to qualify for a permanently fixed conversion rate with the Euro makes no sense. The second policy option that would permit the achievement of the inflation target would be to maintain the currency peg and deliberately create a recession which would drive actual inflation below the Balassa-Samuelson equilibrium inflation rate by enough to meet the Maastricht inflation criterion. That would be the economics of the madhouse.

It gets worse. The argument in the previous paragraph concerned ways of getting the HICP inflation rates in the candidate countries to within 1.5 percent of the average inflation rate in the Eurozone. The Treaty requires this annual inflation rate not to exceed the average

³ In a paper prepared by the CEC5 National Banks (CEC5 National Banks (2002), a range of 'guestimates' of the Balassa-Samuelson effect for these five advanced accession candidates is presented. They range from a low of 0.8 percent per annum for Slovenia (1993-99), to 1 to 2 percent per annum for Slovakia (with 3 percent per annum deemed a possibility in the future), 1.2 to 1.5 percent per annum for Poland, 1.9 percent per annum for Hungary and 1.6 percent per annum for the Czech Republic. All these estimates have the obvious shortcoming that they are based on very short datasets that do not allow the authors to filter out some of the cyclical factors. Despite these shortcomings, it is not unreasonable to estimate the impact of the Balassa-Samuelson effect on the real appreciation of the Eastern European currencies against the EMU to be in the range of 1.5 to 2.5 percent per annum for the foreseeable future. Thus, with constant nominal exchange rates, this appreciation would raise annual inflation rates in accession countries by about 1.5-2.5 percent compared to those in the EMU area.

of the three best performing EU countries by more than 1.5 percent during the year prior to the examination. This is bizarre for two reasons. First, three of the old EU15 countries and all ten new EU countries are not full participants in EMU. So Estonia could, in principle be excluded from full EMU membership even though its inflation rate was less than 1.5 percent above the Eurozone average (indeed even if it were below the Eurozone average), simply because Estonia's inflation rate happened to be more than 1.5 percent above the average rate of inflation of three EU members none of which are actually part of the Eurozone.

This would have been the case, for instance, in 2004. As can be seen from Table 1, the annual inflation rates for Denmark, Sweden and the UK (all outside the Eurozone) for that year were 0.9 percent, 1.0 percent and 1.3 percent respectively. The three lowest inflation rates for 2004 in the EU25 and in the EU15 were Finland (0.1 percent), Denmark and Sweden. The three Eurozone members with the lowest inflation rates in 2004 were Finland, the Netherlands (1.4 percent) and Germany (1.8 percent); the Eurozone average rate of inflation in 2004 was 2.1 percent. Estonia's inflation rate for that year was 3.0 percent. It would have been excluded from the Eurozone on a literal application of the inflation criterion. The same would have been true for Latvia, which had a 6.2 percent inflation rate in 2004 and Slovenia (3.6 percent).⁴ Of the 4 current ERM2 members from CEE, only Lithuania (1.1 percent) would have met the inflation criterion in 2004.

Clearly, it makes no sense to base an inflation convergence test for membership in a monetary union on a comparison of the candidate country's inflation rate with the inflation rate of countries that are not even participants in the monetary union. One can see why, historically, given that convergence to a low rate of inflation was a key objective of those who cobbled together the Maastricht criteria, the inflation rates of the three EU members with

⁴ I am not asserting that the actual inflation rates generated by the three Baltic countries is the Balassa-Samuelson equilibrium inflation rate, but only that a sustained inflation differential vis a vis the Eurozone of 1.5 percent per annum or slightly higher is well within the bounds of the Balassa-Samuelson effect estimates for these countries. Latvia and Estonia have been experiencing massive credit booms since 2003 at least, and there is no doubt a cyclical component to their current and recent inflation performance.

the lowest inflation rates would have provided the inflation benchmark for the first joining of 11 EU members in the EMU on January 1, 1999. Once EMU exists, however, the inflation performance of EU countries outside the EMU is irrelevant for inflation convergence with the Eurozone.

Would the inflation criterion make sense if it were to read: “the annual inflation rate cannot exceed the average of the three best performing Eurozone countries by more than 1.5 percent during the year prior to the examination?” Estonia, Latvia and Slovenia would not have passed this test either in 2004. In any case, it is clear that even if rephrased in this manner, the inflation criterion still would not make economic sense. The only inflation rate that matters for nominal convergence with the EMU, is the (appropriate) average rate of inflation in the Eurozone.

The ECB is very emphatic – rightly so - about the fact that it targets price stability for the Eurozone as a whole. It has no influence over or concern for, inflation developments in the 12 individual current EMU members. An illustration of this concern of the ECB with EMU-wide economic developments rather than with the economic performance of the individual member states or sub-national regions are the data it publishes in its Monthly Bulletin (MB). With two exceptions, the MB reports only Eurozone-wide aggregates. This holds true for GDP and other National Income data, price and earnings data and data on interest rates and monetary aggregates. The only blemishes are the general government deficit and the general government gross debt stock, which are reported for each of the 12 Eurozone members individually as well as for the aggregate Eurozone. This preoccupation of the ECB with the debt and deficits of the individual Eurozone member governments is mystifying as they are not part of the ECB’s mandate or domain of competence.

If inflation convergence of an EMU candidate with the Eurozone prior to full EMU participation is deemed desirable, the convergence benchmark should be defined in terms of

the average Eurozone inflation rate, not the inflation rates of any (strict) subset of the Eurozone members such as the average inflation rates of the three Eurozone members with the lowest inflation rates. Of course, the inflation benchmark should be specified not in terms of the HICP index (or any index including both traded and non-traded goods prices), but should be specified in terms of a price index for traded goods prices only. This would ensure that legitimate Balassa-Samuelson equilibrium inflation differentials do not become obstacles to EMU membership for the CEE ERM2 members.

First-best would be the absence of any inflation criterion whatsoever. Adopting an irreversibly fixed exchange rate with a very large counterparty is probably the most effective way for a small open economy to achieve convergence (up to the Balassa-Samuelson real appreciation differential) to the inflation rate of the counterparty. A full, formally symmetric monetary union such as EMU is the most credible fixed exchange rate regime. To require inflation convergence as a precondition for EMU membership truly is putting the cart before the horse.

The Stability and Growth Pact

The essence of the SGP is the commitment of all EU member states to achieve the "... medium-term objective of budgetary positions close to balance or in surplus..." which "... will allow all Member States to deal with normal cyclical fluctuations while keeping the government deficit within the reference value of 3% of GDP".⁵ Under the 97 version of the

⁵Formally, the SGP consists of three elements (what follows is cribbed with minor modifications from European Commission (2005a)):

- *a political commitment* by all parties involved in the SGP (Commission, Member States, Council) to the full and timely implementation of the budget surveillance process. These are contained in a Resolution agreed by the Amsterdam European Council of 17 June 1997. This political commitment was intended to ensure that effective peer pressure would be exerted on a Member State failing to live up to its commitments.
- *preventive elements* which through regular surveillance aim at preventing budget deficits going above the 3% reference value. To this end, Council Regulation 1466/97 reinforces the multilateral

SGP, sanctions can be imposed when the general government deficit exceeds 3 percent of GDP. However, a government deficit exceeding the reference value of 3% of GDP is considered exceptional and temporary and not subject to sanctions when it results either from an unusual event outside the control of the Member State concerned and has a major impact on the financial position of the general government, or from a severe economic downturn, defined as an annual fall of real GDP of at least 2%. Sanctions take two forms: naming and shaming (including peer pressure) and fines.

When it decides that an excessive deficit does exist, the Council makes recommendations to the offending Member State and sets a deadline of four months for effective corrective action to be taken.. If, after a progressive notice procedure, the Member State fails to comply with the Council's decisions, the Council can decide to impose sanctions, at the latest, ten months after reporting of the data indicating an excessive deficit exists.

Sanctions first take the form of a non-interest-bearing deposit with the Commission. The amount of this deposit is determined by a formula consisting of a fixed component equal to 0.2% of GDP and a variable component linked to the size of the deficit up to a maximum annual amount of 0.5% of GDP. A deposit can be converted into a fine if, in the view of the Council, the excessive deficit has not been corrected after two years. It is key to note that the ultimate judgement on whether to impose sanctions would be made by the Council, made up of the Ministers of Finance, a cabal of deeply political deal makers, not by the Commission or through the mechanical application of a numerical rule, as Germany favoured during the discussions leading up to the signing of the SGP in 1997.

surveillance of budget positions and the co-ordination of economic policies. It foresees the submission by all Member States of 'stability and convergence programmes', which are examined by the Council. The Regulation foresees also the possibility to trigger the early warning mechanism in the event a significance slippage in the budgetary position of a Member State is identified.

- *dissuasive elements* which when the 3% reference value being breached, require Member States to take immediate corrective action and, if necessary, allow for the imposition of sanctions. These elements are contained in Council Regulation 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure.

The 2005 revision of the Stability and Growth Pact (technically this involved “amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure” (Official Journal of the European Union, 7.7.2005, L 174/5 – 174/8) involved two sensible changes and a rather longer list of debilitating changes. The sensible changes were (1) greater attention to cyclically adjusted budget balance, net of one-off and temporary measures rather than to the actual budget balance, and (2) a reference to ‘debt sustainability’ which suggests that the ‘stock’ dimension of the public finances, which had effectively disappeared from the SGP process, would regain some importance in judging the (in)sustainability of the public finances.

The fatal formal weakening of the SGP came from the following modifications:

- A deficit in excess of the reference value of 3 percent will now not be deemed excessive if it is the result of unexpected adverse economic events with major negative consequences for government finances. The key missing words are: “outside the control of the Member concerned”.
- A severe economic downturn (which may excuse a violation of the deficit ceiling) is now defined not as a decline in annual GDP of at least 2 percent, but as negative annual GDP growth or ‘an accumulated loss of output during a protracted period of very low annual GDP volume growth relative to its potential’.
- Factors that are to be taken into account by the Commission take on a kitchen sink quality: ‘implementation of policies in the context of the Lisbon agenda’, ‘policies to foster R&D and innovation), public investment, pension reform and “...any other factor which, in the opinion of the Member State concerned, are relevant...”’.
- A lengthening of the periods within which decisions about excessive deficits have to be made by the Commission and within which the Member State is required to take effective action.

- It has become abundantly clear that fines will never be imposed on transgressors of the EDP. This had been predicted by many as soon as it became apparent that the sanctions of the SGP would not be triggered automatically (or even by the Commission), but only on the say so of the Council, that most political (with a very small ‘p’) of EU bodies. That leaves naming and shaming (peer pressure) as the only enforcement mechanism for EU members that are either in the EMU or are out of the EMU but have no wish to join. Only EU members not yet in EMU but wishing to join it can be subjected to effective pressure by the Maastricht gatekeeping function of the fiscal rules. For the rest, answer to the question ‘how many divisions does the Commission have?’ can only be: ‘not enough’.⁶

To all intents and purposes, this means that the EDP is dead for existing Eurozone members and for EU members that are not currently part of the Eurozone and have no desire to become members. The deficit and debt reference values can still play their ‘Maastricht’ role vis-a-vis EU members that are not yet full participants in EMU but wish to become full members. They can therefore be used by existing Eurozone members to delay the entry into full EMU participation by the 13 EU members that are not currently part of the Eurozone. They can also act as a powerful external stimulus towards fiscal-financial sustainability for candidate EMU members who are eager to join. This stimulus disappears of course as soon as membership is achieved.

If the EDP is now formally dead, was it ever truly alive in substance? Does it matter that the EDP is dead, formally and substantially?

The case for supranational fiscal rules in a monetary union

⁶ With apologies to Joseph Stalin.

It is important to note that, even if there is a case for national fiscal rules, and even if the best practicable national fiscal rules are judged to take the form of the SGP close-to-balance-or-in-surplus benchmark for the cyclically corrected deficit and of the three percent ceiling for the actual deficit, a further argument must be made that, as in the case of the SGP, such rules should be externally imposed, monitored and enforced. For national fiscal stabilisation policy (the current and future path of the government's primary financial deficits) to be a matter of common concern for the EMU members (or even all EU members) the following two arguments must be accepted.

The first argument is that there is an externality (cross-border spillover) associated with national government debt and deficits. Since we have an Excessive Deficit Procedure and not an Insufficient Deficit Procedure, the SGP Pact is based on the assumption that, in the absence of enforceable external constraints, public debt and deficits would be excessive. Unconstrained by an externally imposed, monitored and enforced fiscal rule, national government deficits would impose cross-border costs on other Union governments and citizens that are not properly allowed for and 'costed' in the national government's cost-benefit analysis of borrowing an additional euro.

The second argument is that even if there are no externalities from excessive deficits, which therefore are excessive only from the perspective of the issuing national government and its citizens, there are paternalistic reasons for compelling the national authorities to do the right thing. An appeal to paternalism could be made if an EU government is deemed either not to know what its true interest is or judged to be incapable of acting in its own interest without the benefit of externally imposed constraints. The national fiscal Ulysses is tied to the mast of credible binding commitments by the SGP to resist the siren songs of fiscal irresponsibility. It is my view that the Principle of Subsidiarity implies that without

significant externalities, there is no place for paternalism as a justification for externally imposed constraints on national fiscal policy.

What are the externalities from national government deficit financing? The following come to mind:

1. Cross-border spillovers arising from *unsustainable* national fiscal-financial programmes. This includes the following:
 - a. Cross-border contagion effects of sovereign default risk,
 - b. Spillovers from actual sovereign default,
 - c. Spillovers from actions undertaken to forestall default by other EU governments, by the EU institutions or by the ECB.
2. Cross-border spillovers that arise even when the fiscal-financial programme is sustainable. This includes the following
 - a. inflation externalities due to the response of the ECB to interest rate, output and exchange rate movements (in the effective exchange rate of the Euro) driven by national deficit financing policies.
 - b. Interest rate spillovers (through changes in default risk-free interest rates) caused by national government deficits
 - c. Suboptimal (excessive?) effective demand spillovers caused by (1) a lack of coordination among national fiscal authorities and (2) a lack of coordination between the 12 national fiscal authorities in the Eurozone and the ECB. There can be no presumption that the monetary-fiscal policy mix in the EMU area as a whole (given the monetary-fiscal policy mix in the rest of the world) is optimal in the absence of formal or informal coordination.

I can be brief about the externalities argument. Sovereign default is a distributional conflict between the owners of the sovereign debt (typically older generations), domestic and foreign, current and future tax payers (including current and future wage earners) and current and future beneficiaries of public spending programmes. The bargaining involved in the resolution of this conflict need not be efficient; costly delays can be the result of wars of attrition between badly and asymmetrically informed parties. Third party intervention in such conflicts must be timely and well-designed for it not to make matters worse.

Implicit bailout commitments by other E(M)U governments, by the EU institutions or by the ECB are unlikely, unnecessary and undesirable. The EU institutions (other than the EIB) have no serious resources with which to effect a bail-out. The Treaty specifically rules out bailouts by all three parties. The (positive) argument that EU solidarity/cohesion make a bail-out of a fiscally challenged EU government by another EU government likely is unconvincing as it would be a huge electoral liability for the bailing government. States and municipalities belonging to monetary unions possessing a much stronger sense of common identity and citizenship (in the US and Canada, for instance) routinely fail to bail each other out. The (normative) argument that EU solidarity/cohesion ought to imply a 'joint and several' attitude and approach towards the sovereign debt of its 25 member states find little resonance, even in the most Communitarian (or should that be Communautairian) constituencies.

Possible contagion effects of national sovereign default call for a regulatory response in the E(M)U Member States, limiting the maximum permitted exposure by systemically important financial institutions (e.g commercial banks that play a key role in the payments and settlement systems) to any sovereign. It does not call for binding macroeconomic borrowing constraints of the Maastricht variety.

As regards externalities that occur even when unsustainability and the risk or reality of sovereign default are not an issue, some brief comments will have to suffice. The ‘free riding on the ECB’ argument is that more expansionary fiscal policy (identified rather sloppily with larger national government deficits) by any national government will boost inflation throughout the monetary union, forcing the ECB to be more contractionary throughout the union. The costs of disinflation are not all borne by the government causing the inflationary impulse. Fiscal policy will be too expansionary.

The argument only holds when the central bank’s objective function penalises the output gap as well as deviations from price stability. The ECB’s objective function is lexicographic in price stability: the primary objective is price stability and only subject to or without prejudice to that price stability objective, it can support all the objectives of the EU. The ECB does not trade off price stability for anything else. Free riding on the ECB is therefore not possible.

Other than through its effect on EMU – wide inflation, expansionary national fiscal policy has cross-border effects through its effect on real interest rates. First, these effects are likely to be small, even for the larger European governments, because the relevant financial market extends beyond the boundaries of EMU and EU and consists of the global financial market. Second, interest rate spillovers are textbook examples of pecuniary externalities. Higher interest rates are bad for borrowers, and good for creditors. There is no presumption that the best real interest rate is the lowest possible one. Those concerned about government deficits raising interest rates and crowding out saving and investment must first make the case that the EU is saving and investing too little. Demonstrating that is by no means straightforward and requires a large number of contestable and controversial positive and normative assumptions.

The SGP and policy coordination.

It is clear that in world with nominal wage and price rigidities and demand-determined output, effective demand spillovers are not just pecuniary (distributional) externalities but are more akin to the technological externalities that create the potential for welfare-improving non-market interventions/solutions. Unfortunately, the SGP is completely useless as a policy coordination device: it influences and constrains each individual country's fiscal policy without any reference either to the past, present and expected future fiscal actions of other E(M)U area members, or to the past, present and anticipated future behaviour of the ECB and the other EU central banks. Nor does the SGP take account of any other past, current and anticipated future economic developments in the E(M)U area as a whole, e.g. the behaviour of output, employment and inflation in the E(M)U or the effective exchange rate of the Euro. The SGP is therefore not designed to produce an E(M)U wide fiscal stance that 'adds up' and makes sense given the monetary policy stance of the ECB and the other EU area central banks and given economic developments (including monetary and fiscal policies) in the rest of the world.

The only obvious set of circumstances for which the 'external-economic-environment-blind' approach of the SGP makes sense is when there are no international spillovers onto other members of the union from fiscal actions undertaken by individual member countries and coordination is therefore not necessary. However, without such international spillovers there would be no rationale for having externally imposed fiscal rules in the first place.

Has the SGP contributed to the sustainability of fiscal-financial programmes and to macroeconomic stability in the E(M)U?

I have argued that the supranational imposition of the fiscal-financial rules of the SGP is very hard to rationalise in terms of cross-border externalities or spillovers. For SGP is also

incapable of ensuring E(M)U-wide fiscal policy coordination, let alone fiscal and monetary policy coordination. Could it have contributed (paternalistically) to enhanced fiscal-financial sustainability and macroeconomic stability in the individual E(M)U members?

As regards sustainability, I believe that the conclusion can only be that the SGP has only made a contribution where its prescriptions were incentive-compatible for the target country. In practice this has meant that the SGP has made a contribution to sustainability only in EU members desiring to become full members of the EMU. It has made no difference to the performance of those countries (like the UK, Denmark or Sweden) that were not and are not interested in joining the monetary union. It has also made no difference to the performance of the 12 countries that did join EMU once they had been given the green light for EMU membership.

It should be no surprise that, among the 10 new EU members, the tightest fiscal ships are being run today by those already in ERMII but not yet graduated to full membership in the monetary union: Estonia, Latvia, Lithuania and Slovenia (see Table 4 and Table 6). These four countries have both the lowest government deficits and the lowest government debt stocks (as shares of GDP). Three of the four, Estonia, Latvia and Slovenia, also have the lowest primary government deficits⁷. The fourth, Lithuania is bumped by Hungary, Cyprus and Malta. Of course, government solvency (a necessary condition for sustainability) requires the present value of current and future primary surpluses to be at least equal to the outstanding stock of debt. Cyprus, Malta and Hungary have much higher debt stocks (relative to GDP) than Lithuania.⁸

Table 4 here

⁷ I am aware of potential sample selection bias here. My priors override that concern.

⁸ In addition, the massive revisions to the 2005 deficit figures for Hungary (reflecting the belated consolidation of many dodgy off-budget and off-balance sheet transactions into the general government budget) and the much higher predictions for the 2006 budget year create a strong suspicion that the 2004 deficit figures are probably understated.

Table 6 here

Table 8 here

I do not to predict that, as soon as these four countries achieve full EMU membership, fiscal discipline will be cast overboard. I only assert that once the join the monetary union, the external carrot supporting fiscal restraint is gone forever. Fiscal sustainability in a new EMU member will not be impaired if the pursuit of fiscal sustainability is incentive-compatible for the domestic polity, motivated by domestic considerations and concerns. Unless there is a viable and durable domestic political coalition in support of fiscal restraint, there will not be sufficient fiscal restraint. The SGP, once a country is in the EMU, becomes a minor irritant rather than a binding constraint if it tries to do more that the internal political processes

For the old EU members, Tables 5, 7 and 9 paint a picture supportive of my position that fiscal sustainability is made at home, once the only EU members not part of the monetary union are so out of choice rather than necessity.

Table 5 here

Table 7 here

Table 9 here

In the UK (out of EMU and happy with its opt out) the SGP has been ignored as long as the government was in compliance. When the deficit exceeded the 3 percent reference value in 2003, in 2004 and (almost surely) in 2005, despite rather robust growth in 2003 and 2004, the SGP became an irritant, but not in any way a restraining influence on UK deficit financing.

The Netherlands, in EMU but deeply attached to the SGP (perhaps the Pact's genesis in Maastricht and Amsterdam contributes to this attachment), reacted with shock to its

transgression of the 3 percent reference value in 2003 and (over-)reacted with a severe and pro-cyclical fiscal tightening which reduced the deficit to 2.1 percent of GDP the next year. France and Germany are both in their fourth successive year of non-compliance with the 3 percent ceiling. Italy is in year three of its non-compliance. Embarrassment among one's peers in Ecofin or in the Eurogroup is not much of a deterrent if one has company. The confrontation between the enforcement of the letter and spirit of the SGP and the domestic political agenda of the three largest continental EMU members was resolved by the capitulation of the Commission and the emasculation of the operating rules of the SGP reported earlier.

As a final illustration, note the contrast between the three most highly indebted countries at the time of the collapse of ERM1: Belgium, Italy and Greece. All three are EMU members, Belgium and Italy since 1999, Greece since 2001. Belgium has consistently and persistently applied a sustainability-driven fiscal policy, reducing its debt-to-GDP ratio by more than 40 percentage points in 12 years. The sequence of primary surpluses, averaging well over 5 percent of GDP, is remarkable.

Italy had a period of sizeable primary surpluses between 1995 and 2000. Since then, as member of the Eurozone, Italy has markedly relaxed its fiscal stance. EMU brought lower interest rates and a much lower interest bill on Italy's sovereign debt. It spent these savings. With the longer-term fiscal fundamentals (driven by demographics and pension obligations) highly unfavourable, the current stability of the debt to GDP ratio at just under 110 percent disguises a vulnerable position. The SGP is not a constraint on the Italian fiscal authorities.

Greece's position is even more vulnerable than Italy's. With the debt-GDP ratio at around 110 percent, its financial deficits are growing and its primary surpluses have vanished altogether and turned into deficits again. An increase in interest rates, either because of an increase in the global risk-free rate and/or through an overdue increase in the Greek sovereign

risk premium could produce a drastic cumulative worsening of debt and deficit. Market confidence was not boosted by the revelations about the ways the Greek authorities of the day systematically underreported both deficits and debt during Greece's qualifying years for EMU membership and in the period 2001-2004. It is hard to discern any substantive influence of the SGP on the true evolution of Greece's fiscal-financial circumstances both before and since it joined EMU.

With the SGP out of commission as guarantor or even promoter of fiscal sustainability, it is key that the financial markets not be impeded in whatever contribution they can make to encouraging fiscal restraint. Interest rates are very similar on the euro-denominated sovereign debt instruments of the 12 Eurozone central governments, even for remaining maturities of 10 year and over. This is surprising because by 'fundamental' criteria (such as public debt burdens and capacity to generate primary surpluses) different Eurozone governments appear to represent significantly different degrees of default risk. Anne Sibert and I, in a recent paper (Buiter and Sibert (2005)), offer a contribution to an explanation of this anomaly, based on the way the Eurosystem (the ECB and the 12 national central banks of the Eurozone) treats the sovereign debt instruments of the Eurozone central governments when these are offered as collateral for Repurchase Agreements (Repos) and other collateral financing trades.

We do not argue that sovereign default risk premia determined without the Eurosystem subsidising the use of low-quality Eurozone sovereign debt used as collateral in Repos, would by themselves be sufficient to discourage unsustainable government deficits. That remains an open question. It is self-evident, however, that the suppression of euro-area sovereign default risk premium differentials inherent in the Eurosystem's current monetary policy operating procedures is a fiscal-financial sustainability own goal that can be avoided through a simple change in operating procedures, outlined in our paper.

If the markets were not to price sovereign default risk differentials among the 12 EMU area sovereigns properly even after our proposed reforms, there would be a case for further measures to correct such market failure and make up for the absence of market discipline. One possible measure would be the imposition of an *additional* hair cut (discount on the market price) on the debt offered as collateral for Repos issued by euro-zone countries violating the SGP fiscal norms. If this haircut were to be sufficiently large, it would amount to the Eurosystem declaring the sovereign debt of SGP-violating countries to be ineligible for use as collateral in Eurosystem Repo operations.

As regards macroeconomic stabilisation at the national level, it is true that the SGP permits unbridled anti-cyclical behaviour of the government deficit, provided the normal, trend or cyclically adjusted position of the deficit is sufficiently far below the three percent ceiling to prevent the ceiling from becoming a binding constraint during a cyclical downturn. It is not clear whether, for all 15 EU members, a budget '*close to balance*' over the cycle does provide enough leeway for the automatic fiscal stabilizers to operate fully. Clearly '*...or in surplus*' will always provide enough room.

The problem with the SGP as regards macroeconomic stabilisation is that it does not provide incentives for necessary (but politically unpopular) restraint during the upswing to create room for desirable (and popular) expansionary measures during the downturn. The problem that the SGP deficit rules are (almost entirely) 'memoryless', that is, a lower (flow) deficit today does not automatically/mechanically give you scope to run a larger deficit tomorrow, could be overcome by replacing or augmenting the deficit constraint with a debt constraint.⁹ A smaller deficit today ensures a lower stock of debt tomorrow, making tomorrow's debt ceiling easier to meet. However, this technical correction does not address the enforcement issue: even with a debt rule, the necessary fiscal restraint in the upswing will

⁹ The interest component of the deficit means it has a small measure of memory, given by the product of the interest rate and the change in the stock of debt. The primary deficit is completely memoryless.

still be unpopular. That the debt rule credits past surpluses against the need for future deficits is helpful, but does not eliminate the problem of the lack of external sticks and carrots for fiscal restraint. What sanctions will be imposed if a country violates a debt ceiling?

Conclusions

I would have liked to end this lecture with the exclamation: “the Pact is dead! Long live the Pact”. I cannot do so, as only the first half of the exclamation would be true.

There currently is no operational and even minimally effective supranational mechanism for encouraging fiscal-financial sustainability and macroeconomic stability either at the level of the nation state or at the level of the EMU or EU. Surveillance and Broad Economic Policy Guidelines are good because they employ large numbers of economists, but they achieve little else.

I am not convinced this is a tragedy. Price stability throughout the EMU is a fact because of the reasonably effective (albeit utterly non-transparent) monetary policy of the ECB. Steps can be taken to enhance the ability of the financial markets to discipline sovereign borrowers prone to excessive debt or deficits through a greater responsiveness of sovereign risk premia to visible hints of unsustainability. Apart from that, fiscal-financial sustainability will continue to be home-made. Apart from the international financial markets and the ratings agencies, there are no external sticks or carrots that can be waved or dangled by Brussels or Frankfurt to make fiscal restraint more incentive-compatible to politicians with an overwhelmingly domestic agenda and constituency.

Nation states will continue to pursue macroeconomic stabilisation using fiscal tools without serious attempts at international fiscal coordination, either at the E(M)U level or globally. This is regrettable, as I believe there could be gains from such fiscal coordination, as there could be from broader coordination between fiscal and monetary authorities, but it is

the way things are. There can be no fiscal co-ordination within Europe because coordinating 25 nation states would be a logistic nightmare. Even if Europe were to speak with a single fiscal voice, there can be no fiscal co-ordination with the US, because fiscal policy in the US is not made by anyone, it just emerges, mysteriously and often unexpectedly with long, variable and uncertain lags. In Japan, the monetary and fiscal authorities are only just learning to speak to each other. The two largest RICS countries, India and China do not yet have the monetary and fiscal instruments required both for market-based domestic macroeconomic management and for international monetary and fiscal policy coordination.

It may be a comfort to Europe that it has company. The problem for Europe and for the world is that the company is bad.

Table 1
HICP Inflation Rates in EU Member States 1990-2004 (%)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005*
Cyprus	:	:	:	:	:	:	:	3.3	2.3	1.1	4.9	2.0	2.8	4.0	1.9	2.1
Czech	:	:	:	:	:	:	9.1	8.0	9.7	1.8	3.9	4.5	1.4	-0.1	2.6	2.0
Estonia	:	:	:	:	:	:	19.8	9.3	8.8	3.1	3.9	5.6	3.6	1.4	3.0	3.8
Hungary	:	:	:	:	:	:	23.5	18.5	14.2	10.0	10.0	9.1	5.2	4.7	6.8	3.6
Latvia	:	:	:	:	:	:	:	8.1	4.3	2.1	2.6	2.5	2.0	2.9	6.2	7.4
Lithuania	:	:	:	:	:	:	24.7	8.8	5.0	0.7	0.9	1.3	0.4	-1.1	1.1	2.6
Malta	:	:	:	:	:	:	:	3.9	3.7	2.3	3.0	2.5	2.6	1.9	2.7	2.0
Poland	:	:	:	:	:	:	:	15.0	11.8	7.2	10.1	5.3	1.9	0.7	3.6	1.8
Slovakia	:	:	:	:	:	:	5.8	6.0	6.7	10.4	12.2	7.2	3.5	8.4	7.5	2.3
Slovenia	:	:	:	:	:	:	9.9	8.3	7.9	6.1	8.9	8.6	7.5	5.7	3.6	3.2
Eurozone	:	4.1	3.6	3.3	2.7	2.4	2.2	1.6	1.1	1.1	2.1	2.3	2.3	2.1	2.1	2.6
Austria	2.8	3.1	3.5	3.2	2.7	1.6	1.8	1.2	0.8	0.5	2.0	2.3	1.7	1.3	2.0	2.6
Belgium	:	:	2.3	2.5	2.4	1.3	1.8	1.5	0.9	1.1	2.7	2.4	1.6	1.5	1.9	3.0
Finland	5.8	4.5	3.3	3.3	1.6	0.4	1.1	1.2	1.4	1.3	3.0	2.7	2.0	1.3	0.1	1.1
France	:	3.4	2.4	2.2	1.7	1.8	2.1	1.3	0.7	0.6	1.8	1.8	1.9	2.2	2.3	2.4
Germany	:	:	:	:	:	:	1.2	1.5	0.6	0.6	1.4	1.9	1.3	1.0	1.8	2.6
Greece	:	:	:	:	:	:	7.9	5.4	4.5	2.1	2.9	3.7	3.9	3.4	3.0	3.8
Ireland	:	:	:	:	:	:	2.2	1.2	2.1	2.5	5.3	4.0	4.7	4.0	2.3	2.8
Italy	6.2	6.2	5.0	4.5	4.2	5.4	4.0	1.9	2.0	1.7	2.6	2.3	2.6	2.8	2.3	2.2
Luxembourg	:	:	:	:	:	:	1.2	1.4	1.0	1.0	3.8	2.4	2.1	2.5	3.2	4.7
Netherlands	2.4	3.2	2.8	1.6	2.1	1.4	1.4	1.9	1.8	2.0	2.3	5.1	3.9	2.2	1.4	1.7
Portugal	13.3	11.4	8.9	5.9	5.0	4.0	2.9	1.9	2.2	2.2	2.8	4.4	3.7	3.3	2.5	2.7
Spain	:	:	:	4.9	4.6	4.6	3.6	1.9	1.8	2.2	3.5	2.8	3.6	3.1	3.1	3.8
Denmark	2.5	2.2	1.9	0.9	1.8	2.0	2.1	1.9	1.3	2.1	2.7	2.3	2.4	2.0	0.9	2.4
Sweden	10.2	8.7	1.3	4.8	2.9	2.7	0.8	1.8	1.0	0.6	1.3	2.7	2.0	2.3	1.0	1.1
UK	7.0	7.5	4.2	2.5	2.0	2.7	2.5	1.8	1.6	1.3	0.8	1.2	1.3	1.4	1.3	2.5

Source: Eurostat; * September 2005, % change from 12 months earlier.

Table 2
Real GDP Growth Rates in Ten New EU Member States 1991-2006 (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005*
Cyprus	0.7	9.7	0.7	5.9	9.9	1.8	2.3	5.0	4.8	5.0	4.1	2.1	1.9	3.8	3.9
Czech	:	:	:	:	:	4.2	-0.7	-1.1	1.2	3.9	2.6	1.5	3.2	4.4	4.0
Estonia	:	:	:	-1.6	4.5	4.4	11.1	4.4	0.3	7.9	6.5	7.2	6.7	7.8	6.0
Hungary	:	-2.1	-0.6	2.9	1.5	1.3	4.6	4.9	4.2	5.2	3.8	5.1	3.4	4.6	3.9
Latvia	-12.6	-32.1	-11.4	2.2	-0.9	3.8	8.3	4.7	3.3	6.9	8.0	6.4	7.2	8.3	7.2
Lithuania	-5.7	-21.3	-16.2	-9.8	3.3	4.7	7.0	7.3	-1.7	3.9	6.4	6.7	10.4	7.0	6.4
Malta	:	:	:	:	:	:	:	:	4.1	6.4	0.2	0.8	-1.9	0.4	1.7
Poland	:	:	:	:	2.7	6.0	6.8	4.8	4.1	4.0	1.0	1.4	3.8	5.3	4.4
Slovenia	-8.9	-5.5	2.8	5.3	5.5	3.7	4.8	3.9	5.4	4.1	2.7	3.5	2.7	4.2	3.7
Slovakia	:	:	7.2	6.2	5.8	6.1	4.6	4.2	1.5	2.0	3.8	4.6	4.5	5.5	4.9
EU25	:	:	:	:	:	1.8	2.7	3.0	2.9	3.7	1.8	1.1	1.1	2.4	2.0

Source: Eurostat

Table 3
Real GDP Growth Rates in EU15 Member States 1991-2006 (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005*
Austria	3.6	2.4	0.3	2.7	1.9	2.6	1.8	3.6	3.3	3.4	0.8	1.0	1.4	2.4	2.1
Belgium	1.8	1.5	-1.0	3.2	2.4	1.2	3.5	2.0	3.2	3.9	0.7	0.9	1.3	2.9	2.2
Finland	-6.4	-3.8	-1.2	3.9	4.4	3.8	6.2	5.0	3.4	5.0	1.0	2.2	2.4	3.6	3.3
France	1.2	1.9	-1.0	2.1	2.4	1.1	2.4	3.6	3.3	4.1	2.1	1.2	0.8	2.3	2.0
Germany	:	2.2	-0.8	2.7	1.9	1.0	1.8	2.0	2.0	3.2	1.2	0.1	-0.2	1.6	0.8
Greece	3.1	0.7	-1.6	2.0	2.1	2.4	3.6	3.4	3.4	4.5	4.6	3.8	4.6	4.7	2.9
Ireland	1.9	3.3	2.7	5.8	9.8	8.1	10.8	8.5	10.7	9.2	6.2	6.1	4.4	4.5	4.9
Italy	1.4	0.8	-0.9	2.2	2.9	1.1	2.0	1.8	1.7	3.0	1.8	0.4	0.3	1.2	1.2
Luxembourg	8.6	1.8	4.2	3.8	1.4	3.3	8.3	6.9	7.8	9.0	1.5	2.5	2.9	4.5	3.8
Netherlands	2.4	1.5	0.7	2.9	3.0	3.0	3.8	4.3	4.0	3.5	1.4	0.1	-0.1	1.7	1.0
Portugal	4.4	1.1	-2.0	1.0	8.2	3.6	4.2	4.7	3.9	3.8	2.0	0.5	-1.2	1.2	1.1
Spain	2.5	0.9	-1.0	2.4	2.8	2.4	4.0	4.3	4.2	4.4	3.5	2.7	2.9	3.1	2.7
Eurozone	:	1.6	-0.8	2.5	2.5	1.5	2.5	2.9	2.8	3.6	1.8	0.9	0.7	2.1	1.6
Denmark	1.3	2.0	-0.1	5.5	3.1	2.8	3.2	2.2	2.6	3.5	0.7	0.5	0.6	2.1	2.3
Sweden	-1.1	-1.2	-2.0	4.2	4.1	1.3	2.4	3.6	4.6	4.3	1.0	2.0	1.5	3.6	3.0
UK	-1.4	0.3	2.4	4.4	2.9	2.7	3.2	3.2	3.0	4.0	2.2	2.0	2.5	3.2	2.8
EU15	:	1.3	-0.4	2.8	2.6	1.7	2.6	2.9	2.9	3.7	1.8	1.0	1.0	2.3	1.9
Source: Eurostat															

Table 4
General Government Budget Balance of Ten New EU Member States
(% of GDP at market prices)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Cyprus	:	:	:	:	:	-4.3	-4.5	-2.4	-2.3	-4.5	-6.3	-4.1	
Czech	:	:	:	:	-2.5	-4.2	-3.4	-3.7	-5.9	-6.8	-12.5	-3.0	
Estonia	:	:	:	:	1.9	-0.3	-3.7	-0.6	0.3	1.5	2.6	1.7	
Hungary	:	:	:	:	-6.8	-8.0	-5.6	-3.0	-3.5	-8.5	-6.5	-5.4	
Latvia	:	:	:	:	:	-0.6	-4.9	-2.8	-2.1	-2.3	-1.2	-0.9	
Lithuania	:	:	:	:	-1.1	-3.0	-5.6	-2.5	-2.0	-1.4	-1.2	-1.4	
Malta	:	:	:	:	-10.7	-10.8	-7.6	-6.2	-6.6	-5.8	-10.4	-5.1	
Poland	:	:	:	:	-4.0	-2.1	-1.4	-0.7	-3.7	-3.3	-4.8	-3.9	
Slovenia	:	:	:	:	:	-2.2	-2.1	-3.5	-3.9	-2.7	-2.7	-2.1	
Slovakia	:	:	:	:	-5.5	-4.7	-6.4	-12.3	-6.6	-7.8	-3.8	-3.1	

Source: Eurostat

Table 5
General Government Budget Balance of Eurozone Member States, EU15 and EU25
 (% of GDP at market prices)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Austria	-4.2	-5.0	-5.2	-3.8	-1.9	-2.4	-2.3	-1.5	0.1	-0.4	-1.2	-1.0	
Belgium	-7.3	-5.0	-4.3	-3.8	-2.0	-0.7	-0.4	0.2	0.6	0.0	0.1	0.0	
Finland	-7.3	-5.7	-3.7	-3.2	-1.5	1.5	2.2	7.1	5.2	4.3	2.5	2.1	
France	-6.0	-5.5	-5.5	-4.1	-3.0	-2.7	-1.8	-1.4	-1.6	-3.2	-4.2	-3.6	
Germany	-3.1	-2.4	-3.3	-3.4	-2.7	-2.2	-1.5	1.3	-2.9	-3.8	-4.1	-3.7	
Greece	-13.4	-9.4	-10.2	-7.4	-4.0	-2.5	-1.8	-4.1	-6.1	-4.9	-5.7	-6.6	
Ireland	-2.7	-2.0	-2.1	-0.1	1.1	2.4	2.4	4.4	0.8	-0.4	0.2	1.4	
Italy	-10.3	-9.3	-7.6	-7.1	-2.7	-2.8	-1.7	-0.6	-3.2	-2.7	-3.2	-3.2	
Luxembourg	1.5	2.7	2.1	1.9	3.2	3.1	3.5	6.0	6.1	2.1	0.2	-0.6	
Netherlands	-2.8	-3.5	-4.2	-1.8	-1.1	-0.8	0.7	2.2	-0.2	-2.0	-3.2	-2.1	
Portugal	-8.9	-6.6	-4.5	-4.0	-3.0	-2.6	-2.8	-2.8	-4.2	-2.8	-2.9	-3.0	
Spain	:	:	:	-4.9	-3.2	-3.0	-1.2	-0.9	-0.5	-0.3	0.0	-0.1	
Eurozone	:	:	:	-4.2	-2.6	-2.2	-1.3	0.2	-1.9	-2.5	-3.0	-2.7	
Denmark	-3.7	-3.2	-3.1	-1.9	-0.5	0.2	2.4	1.7	2.6	1.4	1.0	2.3	
Sweden	-11.6	-9.3	-7.0	-2.7	-0.9	1.8	2.5	5.1	2.5	-0.3	0.2	1.6	
UK	-8.0	-6.8	-5.7	-4.3	-2.0	0.2	1.0	3.8	0.7	-1.6	-3.3	-3.1	
EU15	:	:	:	-4.2	-2.4	-1.6	-0.7	1.0	-1.2	-2.2	-2.9	-2.6	
EU25	:	:	:	:	:	-1.7	-0.8	0.8	-1.3	-2.3	-3.0	-2.6	

Source: Eurostat

Table 6
General Government Consolidated Gross Debt of Ten New EU Member States
(% of GDP at market prices)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Cyprus	:	:	:	:	:	61.6	62.0	61.6	61.9	65.2	69.8	72.0	
Czech	:	:	:	:	12.2	12.9	13.4	18.2	26.3	29.8	36.8	36.8	
Estonia	:	:	:	:	6.4	5.6	6.0	4.7	4.7	5.8	6.0	5.5	
Latvia	:	:	:	:	:	9.8	12.6	12.9	15.0	14.2	14.6	14.7	
Lithuania	:	:	:	:	15.2	16.5	23.0	23.8	22.9	22.4	21.4	19.6	
Hungary	:	:	:	:	64.2	61.9	61.2	55.4	52.2	55.5	57.4	57.4	
Malta	:	:	:	:	51.5	64.9	56.8	56.4	63.5	63.2	72.8	75.9	
Poland	:	:	:	:	44.0	39.1	40.3	36.6	36.7	41.2	45.3	43.6	
Slovakia	:	:	:	:	28.6	28.6	43.8	49.9	49.2	43.7	43.1	42.5	
Slovenia	:	:	:	:	:	23.6	24.9	27.4	28.4	29.8	29.4	29.8	

Source: Eurostat

Table 7 General Government Consolidated Gross Debt of EU15 Member States (% of GDP at market prices)													
	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Austria	61.8	64.7	69.2	69.1	64.7	64.8	67.5	67.0	67.0	66.7	65.1	64.3	
Belgium	137.9	135.9	134.0	130.2	124.8	119.6	114.8	109.1	108.0	105.4	100.0	95.7	
Finland	55.9	58.0	57.1	57.1	54.1	48.6	47.0	44.6	43.6	42.3	45.2	45.1	
France	45.3	48.4	54.6	57.1	59.3	59.5	58.5	56.8	56.8	58.8	63.2	65.1	
Germany	46.9	49.3	57.0	59.8	61.0	60.9	61.2	60.2	59.6	61.2	64.8	66.4	
Greece	110.1	107.9	108.7	111.3	108.2	105.8	105.2	114.0	114.4	111.6	108.8	109.3	
Ireland	95.1	89.6	81.8	73.3	64.5	53.8	48.6	38.3	35.9	32.4	31.5	29.8	
Italy	118.7	124.8	124.3	123.1	120.5	116.7	115.5	111.2	110.9	108.3	106.8	106.5	
Luxembourg	6.8	6.3	6.7	7.2	6.8	6.3	5.9	5.5	6.7	6.8	6.7	6.6	
Netherlands	79.3	76.4	77.2	75.2	69.9	66.8	63.1	55.9	51.5	51.3	52.6	53.1	
Portugal	59.1	62.1	64.3	62.9	59.1	55.0	54.3	53.3	53.6	56.1	57.7	59.4	
Spain	58.4	61.1	63.9	68.1	66.6	64.6	63.1	61.1	56.3	53.2	49.4	47.0	
Eurozone	65.6	68.4	73.1	74.6	74.3	73.6	72.2	69.6	69.3	69.2	70.4	70.8	
Denmark	81.1	77.4	73.2	69.7	65.7	61.2	57.7	52.3	48.0	47.6	45.0	43.2	
Sweden	:	73.9	73.7	73.5	70.6	68.1	62.7	52.8	54.3	52.4	52.0	51.1	
UK	45.4	48.6	51.8	52.3	50.8	47.7	45.1	42.0	38.7	38.2	39.7	41.5	
EU15	:	66.4	70.8	72.6	71.0	68.9	67.9	64.1	63.1	62.5	64.0	64.3	
EU25	:	:	:	:	:	67.5	66.7	62.9	62.0	61.4	63.0	63.4	
Source: Eurostat													

Table 8
General Government Primary Budget Balance of Ten New EU Member States
(% of GDP at market prices)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Cyprus	:	:	:	:	:	1.1	1.0	1.1	1.1	-1.3	-2.8	-0.9
Czech	:	:	:	:	:	:	-2.5	-2.8	-4.8	-5.2	-10.3	-1.8
Estonia	:	:	:	:	:	:	-3.4	-0.3	0.5	1.7	3.3	2.0
Hungary	:	:	:	:	:	:	1.9	2.6	1.0	-4.5	-2.2	-0.2
Latvia	:	:	:	:	:	:	-4.1	-1.8	-1.1	-1.9	-0.7	0.0
Lithuania	:	:	:	:	:	:	-4.1	-0.8	-0.4	-0.1	-0.6	-1.5
Malta	:	:	:	:	:	:	-4.0	-2.5	-2.8	-1.9	-6.7	-1.1
Poland	:	:	:	:	:	-0.2	0.6	1.4	-0.7	-0.7	-1.6	-2.2
Slovenia	:	:	:	:	:	:	0.2	-1.0	-0.4	0.0	0.1	0.0
Slovakia	:	:	:	:	:	:	-3.1	-8.2	-2.0	-2.1	-1.2	-1.1
Source: Eurostat												

Table 9 General Government Primary Budget Balance of Eurozone Member States, EU15 and EU25 (% of GDP at market prices)												
	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Austria	0.1	-0.9	-0.9	0.4	2.0	1.4	1.3	2.1	3.8	3.1	2.0	1.7
Belgium	3.8	4.6	4.9	5.1	6.0	6.8	6.6	6.9	7.2	6.1	5.7	4.8
Finland	-2.8	-1.5	0.3	1.1	2.7	5.1	5.3	10.0	7.9	6.5	4.5	4.0
France :	:	:		-0.1	0.7	0.9	1.4	1.7	1.6	-0.2	-1.3	-0.8
Germany	0.2	0.9	0.3	0.3	0.9	1.4	2.0	4.7	0.4	-0.5	-0.7	-0.6
Greece	-2.0	3.1	1.0	3.1	4.2	5.3	6.5	4.0	3.7	2.2	0.6	-0.4
Ireland	3.9	4.1	3.3	4.4	5.3	5.7	4.7	6.4	2.4	1.0	1.5	2.5
Italy	2.8	2.1	3.9	4.4	6.7	5.2	5.0	5.8	3.6	3.2	2.4	2.0
Luxembourg	1.9	3.1	2.4	2.3	3.6	3.4	3.8	6.2	6.5	2.6	0.8	-0.9
Netherlands	3.4	2.3	1.7	3.8	4.1	4.1	5.1	6.0	3.3	1.1	-0.3	0.4
Portugal :	:	:		1.4	1.3	0.9	0.4	0.4	-1.2	0.3	0.0	-0.1
Spain :	:	:		0.4	1.6	1.2	2.4	2.4	2.6	2.6	2.8	1.9
Eurozone :	:	:		1.4	2.5	2.5	2.9	4.2	2.2	1.2	0.6	0.6
Denmark	3.6	3.4	2.7	3.6	4.2	4.6	6.3	5.3	6.3	4.5	3.8	5.1
Sweden	-5.7	-2.9	-0.3	3.8	5.3	7.4	7.1	9.2	5.7	2.8	2.3	3.2
UK	-4.9	-3.4	-2.1	-0.6	1.7	3.8	3.9	6.6	3.1	0.3	-1.3	-1.1
EU15 :	:	:		1.3	2.5	2.9	3.3	4.8	2.5	1.2	0.4	0.4
EU25 :	:	:	:	:	:		3.2	4.6	2.4	1.0	0.3	0.4
Source: Eurostat												

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