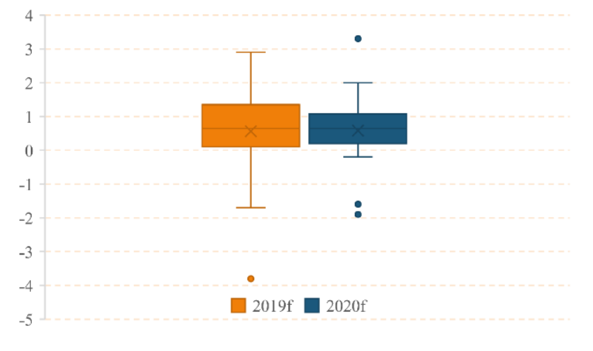
Overview

This edition of the European Fiscal Monitor covers 24 EU economies as seen through the lens of national Independent Fiscal Institutions (IFIs).

The economic cycle is thought to have peaked in most EU economies. Most IFIs see their national economies performing somewhat above or, in a few cases, significantly above their potential but expect the output gap to close in the medium term as headline growth decelerates (see Figure). Italy and Greece are two notable exceptions. In both cases, national watchdogs estimate the output gaps to be large and persistently negative.

Figure: Output gap forecast distribution (pct of pot. GDP)



Source: EU IFIs, AMECO database

The risks to this benign outlook continue to be tilted towards the downside. The economies of the EU are highly open economies sensitive to external demand conditions. These are ultimately linked to global trade dynamics currently threatened by political fall-outs between key actors. Ireland has been facing particularly uncertain times with the possibility of significant overheating of the economy on the one hand, and the possibility of facing the economic consequences of a disorderly Brexit on the other.

Despite favourable economic conditions, reports of (likely) non-compliance with fiscal rules – national or EU-level - are relatively frequent. Rapid growth in public spending has been identified as problematic from the perspective of compliance with rules in Austria, Bulgaria, Italy, Ireland, Lithuania and Slovakia. Should France follow the path planned in the 2019 Stability Programme Update, it would likely find itself in significant deviation from a rules-based consolidation path which would trigger the correction mechanism set out in law. In a similar vein, in Italy, the budgetary watchdog identified insufficient structural adjustment in 2018, and sees a risk of significant deviation, in 2019, from a consolidation path that already involves an extensive use of the room for maneuver granted by the EU authorities. Moreover, the debt-to-GDP ratio has not been falling in line with rule-based requirements. Romania has been found in violation of rules governing convergence towards a medium-term objective but the IFI is also concerned that headline deficit is being kept below the 3-percent threshold through one-off revenue measures. In the cases of Estonia and Slovakia, the likely non-compliance with numerical rules and targets has triggered attempts to change them.

The Latvian and Slovak IFIs **call explicitly for a more prudent fiscal stance** not only to meet medium-term objectives but also **to create fiscal space** to cope with the looming pressures arising from a rapidly ageing population.

Several IFIs re-iterate their calls for more structural reform, especially those aimed at increasing the quality of public spending and in areas affected by population ageing, **and more medium-term orientation in the budgetary process.**

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