Some comments for the panel of “New Challenges for Monetary-Fiscal Policy Interactions”

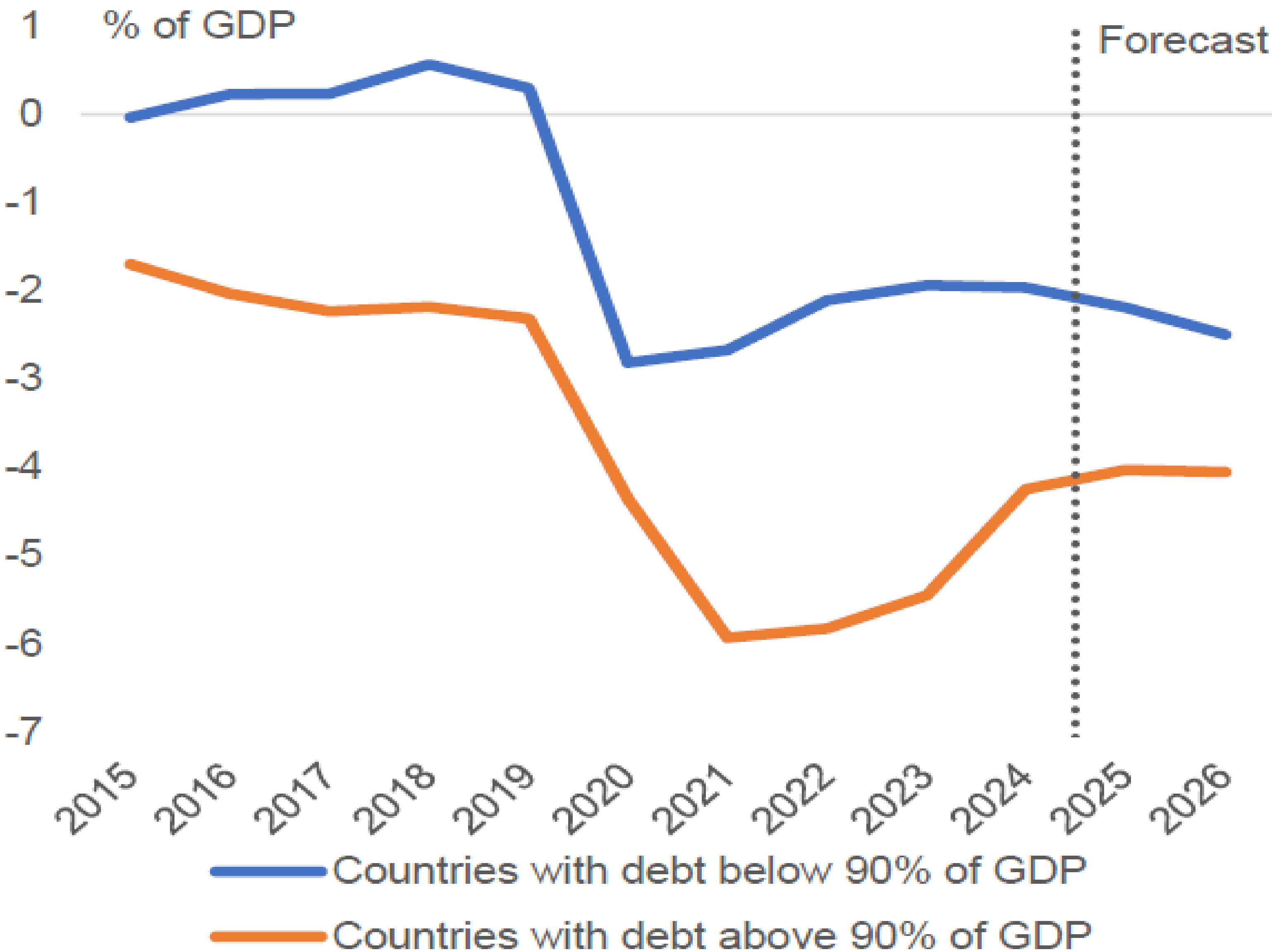
Sveriges Riksbank
Stockholm, October 6-7, 2025

Roel Beetsma,
University of Amsterdam, Copenhagen Business School,
former member European Fiscal Board

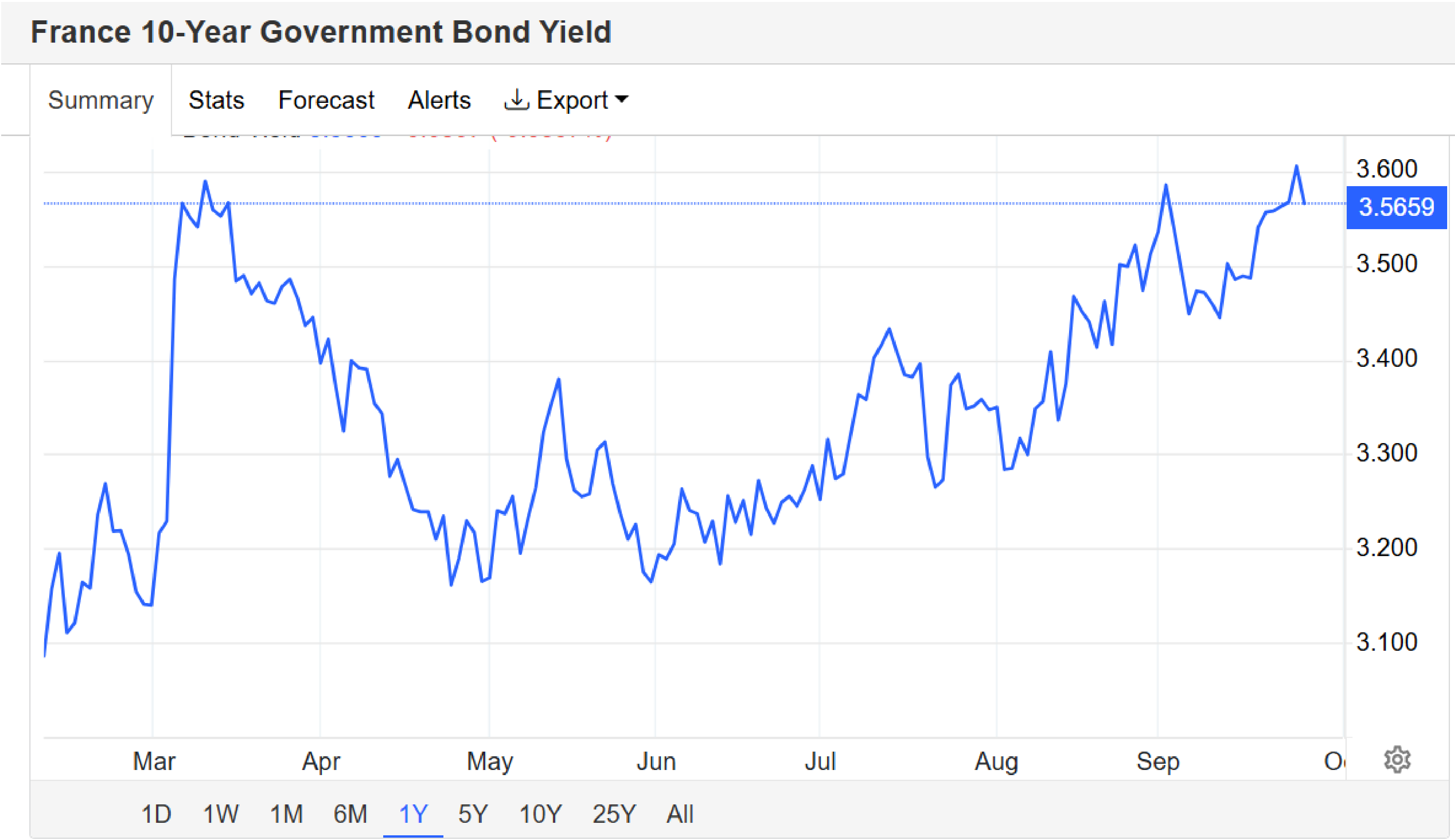
State of fiscal discipline: causes and consequences

- High structural deficits and projected debt increases
- Likelihood debt crisis determined by the extremes
- Source of fiscal discipline problems is largely political
  - Vanishing culture of fiscal discipline
  - Populism plus demography forcing governments to spend on welfare etc. (at the cost of discipline and growth-promotion, such as education)
- Financial markets seem to largely ignore the risks, history shows sudden eruptions are possible
- ECB as a de facto backstop, potentially disincentivising measures

Structural balance (EFB June 2025 report)



Yield French 10-year bonds (source: Trading Economics)



Policy coordination in EU and euro area is largely "implicit"

- Fiscal coordination "implicit" via fiscal rules and ECOFIN
  - Commission provides guidance
  - Informal concept of euro-area aggregate fiscal stance
- Fiscal and monetary policy interact through ECB asset purchase programs
  - Large shocks in combination with fiscal profligacy may force ECB to step in
- Is there a case for explicit fiscal coordination?

Revised EU fiscal framework

- Net primary expenditures main guiding variable
  - Directly observable indicator
  - Largely unaffected by the business cycle
  - Alleviates pressure on ECB's counter-cyclical policy – especially valuable when countries business cycles are not aligned
- Medium-term fiscal-structural plan sets nominal path of net primary expenditures in advance:
  - Ratio of public spending to GDP may gradually change – effect is potentially large over 4- or 7-year period
  - Could gradually shift macro demand relative to supply, with potential implications for price stability and ECB policy

Transmission protection instrument

- Criteria:
  - Compliance with the EU fiscal framework: not under EDP or assessed to have failed to take effective action when under EDP
  - Absence of severe macroeconomic imbalances: not under an excessive imbalance procedure or not being assessed as having failed to take recommended corrective action
  - Fiscal sustainability: based on DSA by own and various policy institutions
  - Sound and sustainable macroeconomic policies: complying with the commitments in the RRPs and with Commission's country-specific recommendations in the fiscal sphere under European Semester

Transmission protection instrument

- No specification of limit on amount, nor on type of securities.

- Criteria not hard – Lagarde: “These criteria will be an input into the Governing Council’s decision-making and will be dynamically adjusted to the unfolding risks and conditions to be addressed.”

  - It should be made clear that when capital market access comes under pressure and the criteria are not fulfilled, countries would need to turn to the ESM for an adjustment program

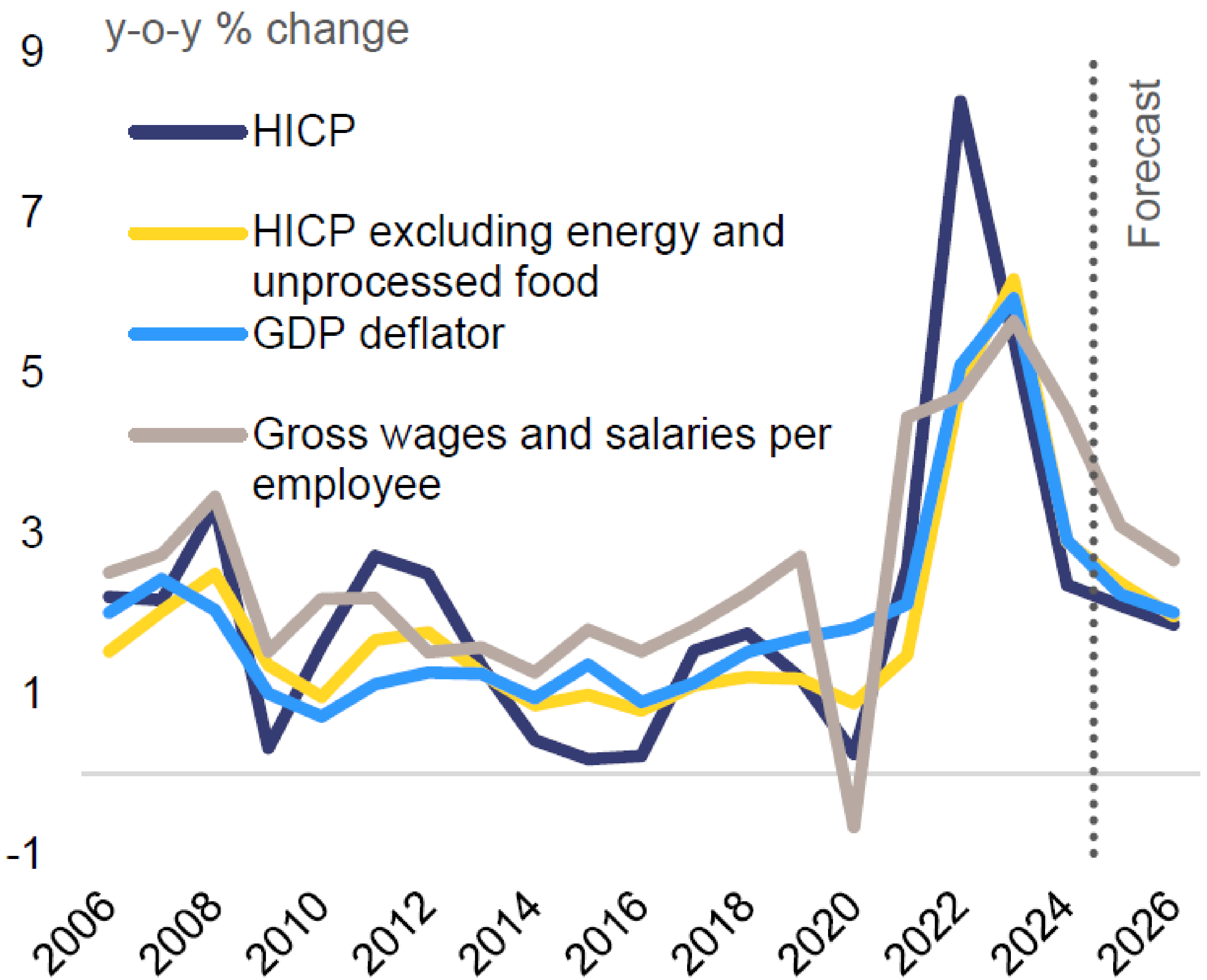
  - Political stakes to avoid EDP or further steps in the EDP have increased

Explicit coordination of fiscal policies?

- Politically difficult to achieve
- Explicit fiscal coordination can be harmful or beneficial:
    - Strengthens strategic position of fiscal authorities as a collective against ECB – higher danger of "fiscal dominance" and less fiscal discipline (Beetsma and Bovenberg, 1999)
    - Coordinating on appropriate combination of fiscal stances could benefit all
- As an example, take the current situation:
    - Inflation approximately at target (ECB completed its job)
    - Output gap close to zero
    - Combination of tighter fiscal stances in combination with further monetary easing might benefit investment climate through lower interest rates

Inflation (forecast) (source: EFB)

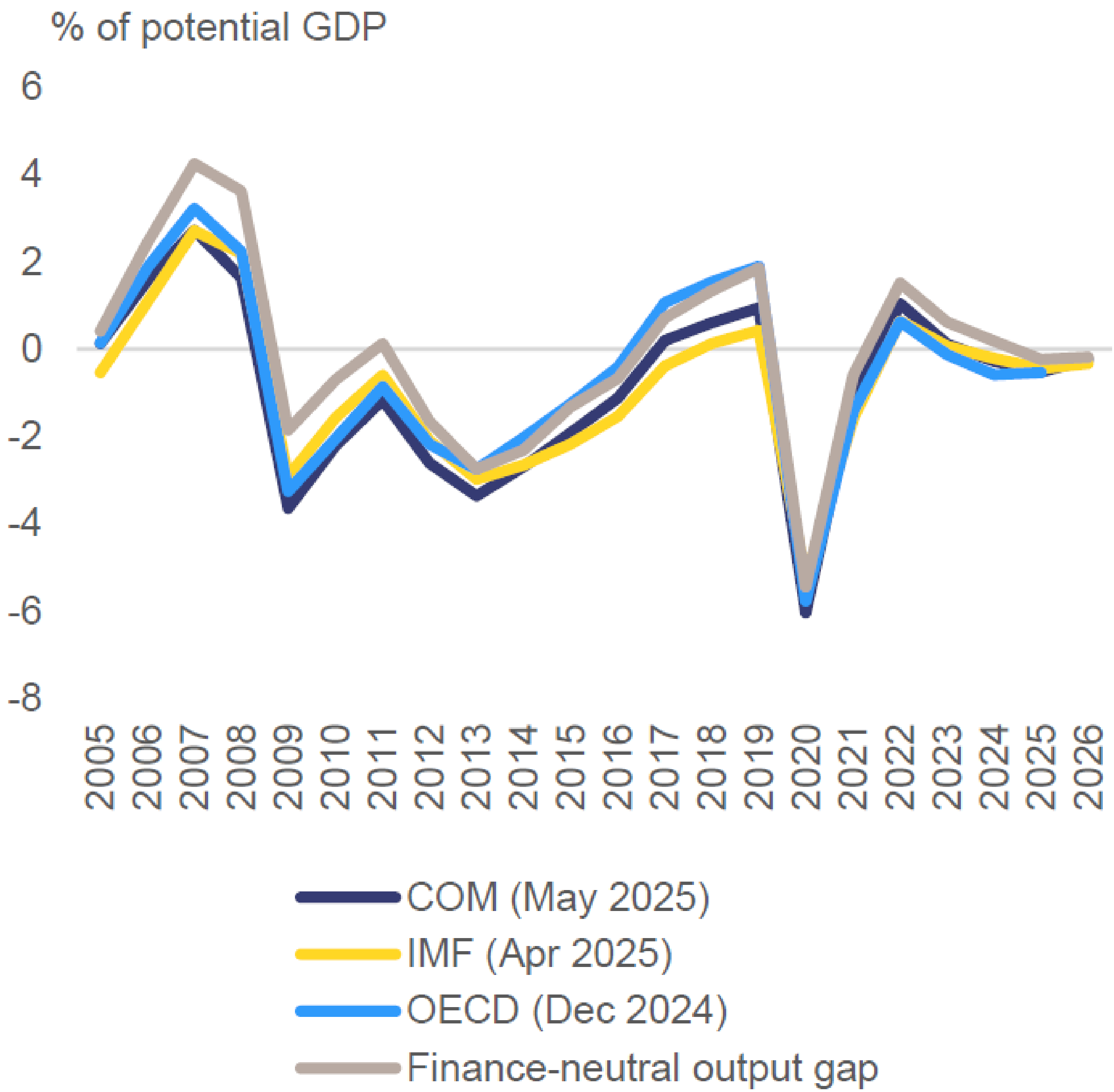
Graph 1.8: Inflation and wages, euro area



Source: European Commission.

Output gap (source: EFB)

Graph 1.10: Output gap, euro area



Extra slides

Role of “financial landscape”

- US has integrated capital market with much smaller role for banks
- EU capital market integration has long way to go
  - CMU / SIU might reduce role of banks, limiting their risks
- Creation of European safe asset will stimulate capital market integration.
- Gradual expansion EU budget and EU investments financed through EU debt may create such an asset; supported by increased own resources seems essential to back the debt.
- Such a process will take time, as EU debt will compete with other debt, in particular bunds, in investor portfolios

Choices in case of crisis

- TPI with less conditionality
- OMT conditional on ESM adjustment
  - Macroeconomic adjustment programme is baring fruits in case of Greece, although process has been painful and long
  - But in case of a large country, will the rest of the euro-area be able to provide enough resources?

Thank you for your attention