Central fiscal capacities

Discussion by Agnès Bénassy-Quéré

Rethinking the European Fiscal Framework, CEPR-EFB workshop, Brussels, 28 Feb. 2020

Mapping the speakers

Lars: no fiscal capacity needed (H0)

Ramon: national UI topping up EUI
(small, unlimited replacement)

Mathias: EUI topping up national UI
(reinsurance)

Understanding the differences

Is fiscal stabilization useful?

- Lars: yes, national stabilization + ESM
- Mathias: yes, EUI could have cushioned 15-25% of income losses resulting from large unemployment shocks over 2000-16 (ex ante); interregional/intertemporal
- Ramon: yes, but UI currently too large at national level given the flows of jobs; limited gains from insuring idiosyncratic shocks (ex post, general equilibrium)

Can moral hazard be controlled?

- Lars: no, rewarding "sclerotic economic structures" (p. 215)
- Mathias: yes, through ex-ante conditionality + restriction to large shocks
- Ramon: yes, endogenous behaviors accounted for; proposal is resilient to political economy arguments

Can permanent transfers be avoided?

- Lars: no, even in the long run
- Mathias: yes, limited transfers ex post (depending on shocks), ex-ante conditionality
- Ramon: yes, country-specific payroll taxes

Key points for discussion

Idiosyncratic only vs aggregate shocks

- Example 2009: who would have paid?
- Borrowing capacity vs rainy-day fund when interest rates are negative

Intertemporal smoothing at national or €area level?

- No financial frictions → intertemporal smoothing is easy → national level (Mathias) or individual level (Ramon)
- Financial frictions → risk of pro-cyclical policies, even for SGP-compliant countries, even with ESM support → €area borrowing capacity
- Chetty (JPE 2008): 60% of the increase in unemployment durations caused by UI is due to a liquidity effect rather than moral hazard → constrained households

Designing an EUI

- Baseline ≠ balanced budget at national level except (maybe) in a financial crisis; contribution rates cannot move over the cycle (pro-cyclical)
- United States: borrowing scheme + extended benefit scheme (during a large crisis)
- Interaction with social assistance which is national and with replacement >10%
- Vertical interactions, e.g. EUI 10% + national top-up 90%?
- Variable replacement rates at national level over the cycle?

Points for discussion (ctd)

Value for the €area

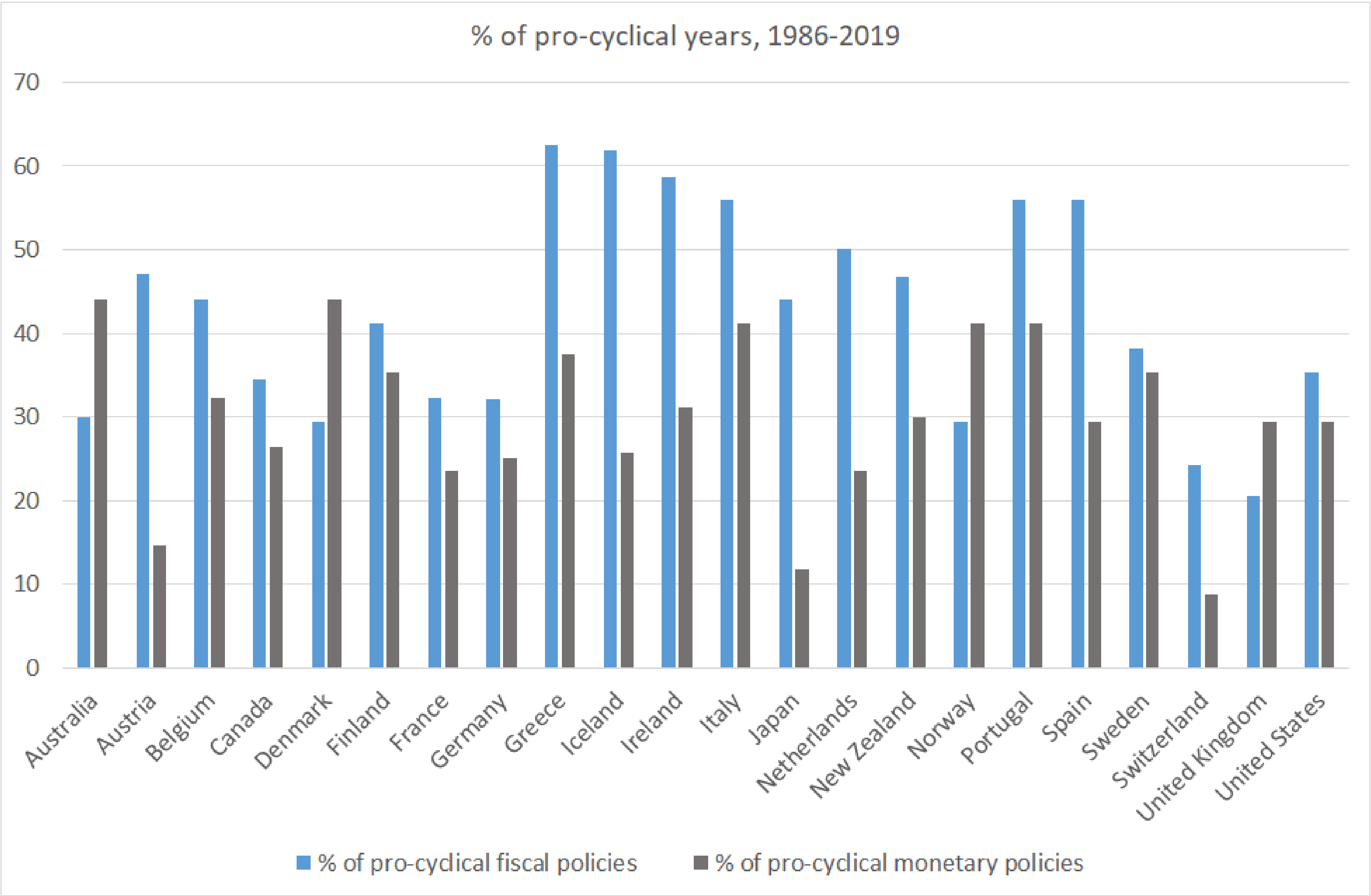
- Economic, social and political spillovers
- Impact of labor reallocations on productivity, quality of matches, unemployment duration (with declining employability)
- Impact on savings (Ramon: ambiguous, but closed economy)

Bundling EUI with other elements of a job market union

- European pillar of social rights
- Mobility (portability of social rights), skills
- Insurance against structural change (European adjustment fund)

Procyclicality in OECD countries

1986-2019*



* Since 1990 for Australia and NZ, 1991 for Canada, Ireland and Switzerland, 1992 for Germany, 1996 for Greece.

Source: based on OECD EO Nov. 2019.

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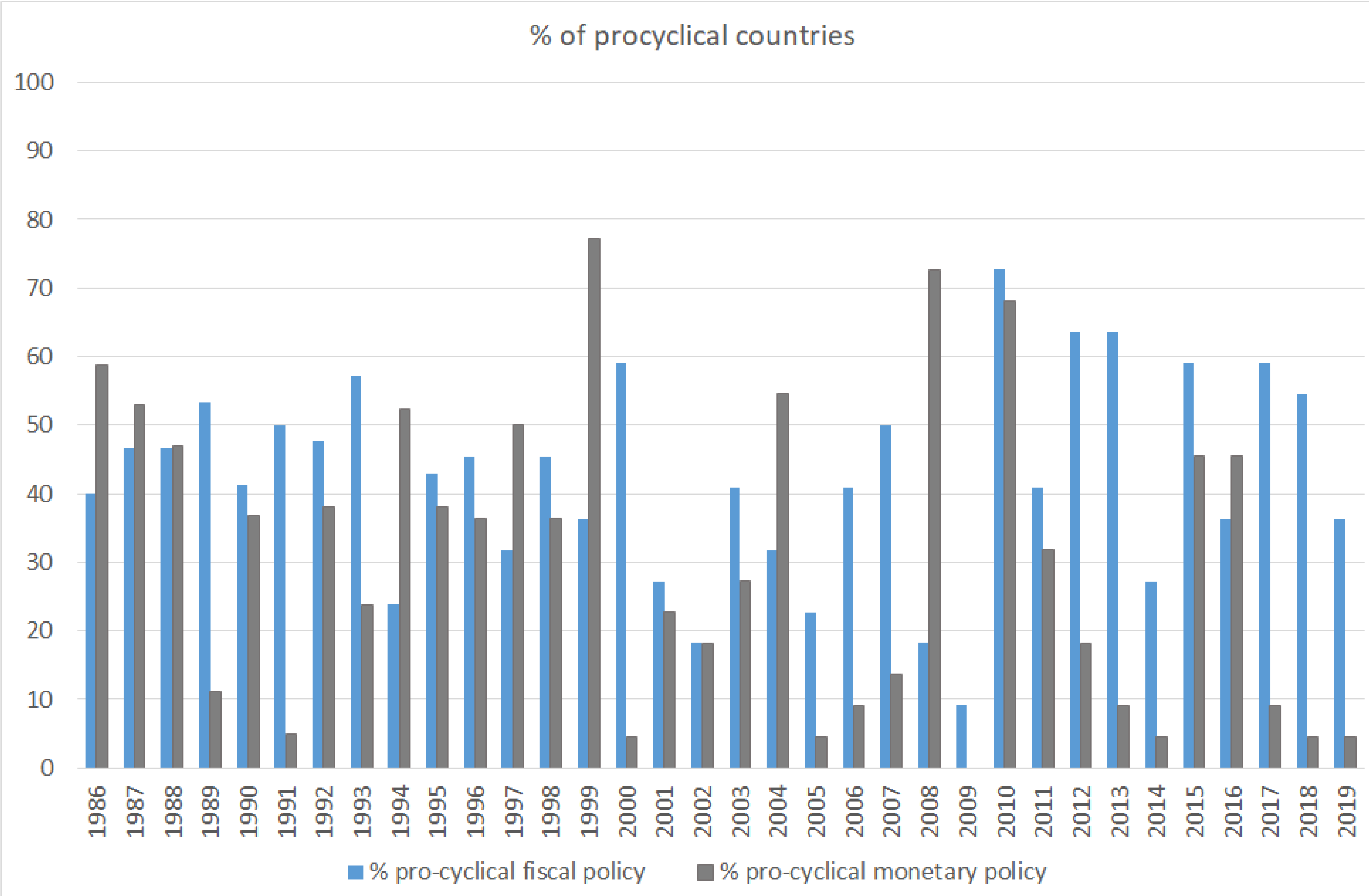

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