Rainy days in Europe

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The debate on how to advance towards greater integration in Europe is intensifying with the approach of June, the self-imposed deadline for Europe's leaders to come up with specific new reforms for the euro zone. The International Monetary Fund, which is often more forthright than commonly supposed in its recommendations on fiscal policy, has recently joined the fray with a proposal for a stabilisation fund to cushion fluctuations in the economic cycle. The idea is not new. The European Commission (EC) suggested it in December, offering three alternatives: a common unemployment insurance, a fund for investments (to ensure that investment does not come to a halt in recessions), and a less specific alternative with the down-home name of "rainy day fund" in which to save up resources in growth periods for use during periods of recession. The IMF comes down on the side of this last alternative.

Although there is already fiscal room for manoeuvre to stabilise the economic cycle (such as the 3% deficit limit), the argument is that asymmetric shocks affecting a single country of a monetary union like the euro zone can be significant and that there is no independent monetary policy with which to counter them. Furthermore, even when recessions are common to the whole zone, monetary policy may not be sufficient to combat them, as was the case in the period 2011-2013, when nearly all euro zone countries, even those not under market pressure, applied restrictive fiscal policies.

The IMF's document shows that a small annual contribution from countries (0.35% of GDP) may be enough to apply countercyclical policies that will avoid a typical recession in the euro zone. For major crises such as the last one, the fund would need to be able to borrow, and this could lead to rejection by northern European countries. In order to maintain fiscal discipline, as well as making the tax rules simpler and more transparent (already proposed by the IMF on other occasions, and also defended by the EC), the fund would be applied only to countries that complied with the rules on deficit and debt. And to make it fiscally neutral - no permanent transfers among countries, which is the great fear of the northern European countries in this regard, contributions in excess to countries in difficulties would be returned in subsequent years.

The mechanism seems well designed and politically viable in the current economic situation, but doubts linger as to whether it is really an essential instrument for normal crises - the shocks are not so asymmetrical in Europe - and whether it would have sufficed to avoid the European crisis of ten years ago, which was of a more systemic nature. Clearly not, and therefore we need more ambitious proposals that move towards some form of mechanism for mutualising debt.

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