EPICENTER
European Policy Information Center

Credit day: debt and deficit in a bipolar EU

Institut Economique Molinari[1]

6 December marks Credit Day across the European Union. This is the day when, on average, European countries' central administrations will exhaust their annual tax revenue and start living on credit to meet their spending commitments, according to a study by the Institut Economique Molinari.

Only 4 out of the 28 member states are currently in budget surplus. Among the deficit countries, France ranks worst, with both high debt and deficit levels as well as no reduction in public spending.

The EU member states' finances show two opposite poles, with the bottom quartile struggling to reduce its public spending, resulting in large deficits and escalating debt levels. The rest of the EU28 are however showing improvements, with a declining amount of unfunded spending days.

Whilst there have been improvements, EU authorities should make greater use of the preventive arm of the Stability and Growth Pact to ensure that all EU countries continue their debt and deficit consolidation.

An alternative approach to understanding government borrowing

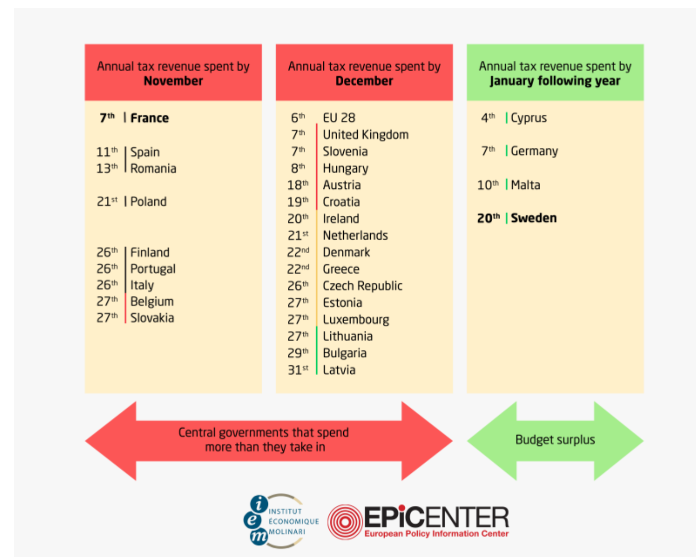
The recent study by the Institut Molinari aims to clarify for the general public the scale of public deficit and public debt. Both concepts can be difficult to grasp for multiple reasons. They are usually expressed as a percentage of GDP, they represent astronomical numbers by comparison to household budgets, and the assessment of economies by central governments is usually done by forecasts for the current year, whereas the study is an analysis of the actual data from the previous fiscal year. The study provides a straightforward measure of fiscal profligacy in the form of a central government's *credit day*. This is the day when national treasuries exhaust their annual tax revenues and begin borrowing to finance current expenditure.

16 of the EU28 are over the debt limit imposed by the Stability and Growth Pact at 60% of GDP. The deficit has been kept under the 3% threshold in 26 of the member states yet 15 of them still have a budget deficit.

The picture presented is one of a bipolar Europe, where there have been general improvements brought about by tax revenue as a share of GDP that has been relatively stable over the past 10 years, combined with reduced public spending throughout Europe. However, whilst there has been an average improvement, certain countries, notably France, Spain, Romania and Poland, have struggled to meaningfully reduce their deficits and debt, rendering them fragile to potential shocks. The EU as a whole does show an improving trend, as the average of unfunded spending days is now close to pre-2008 crisis levels.

Trends in EU28 borrowing

The EU28 have seen an average reduction of 6 credit days in the past year. In 2015, national governments borrowed for an average of 31 days, whereas the number of days in the red had declined to 25 in 2016. Four countries even managed to reduce their debt in 2016: Sweden, Malta, Germany and Cyprus. This compares to only two member countries in surplus in 2015 (Germany and Sweden). Most countries have improved their balance on a 20-year, 10-year and 5-year average. After years of spending and deficit increases in the wake of the 2008 financial crisis, we are witnessing a gradual return to pre-crisis numbers for most countries.



Yet the 4th quartile of countries, the worst fiscal performers among the EU28, warrants special attention. The quartile this year incorporates two new countries, Romania and Poland, which replace the U.K. and Greece.[2] . The five other countries in this quartile were also present in the previous study: Finland, France, Spain, Portugal and Italy. Finland (39 to 36), Portugal (54 to 35) and Italy (38 to 35) have seen a reduction

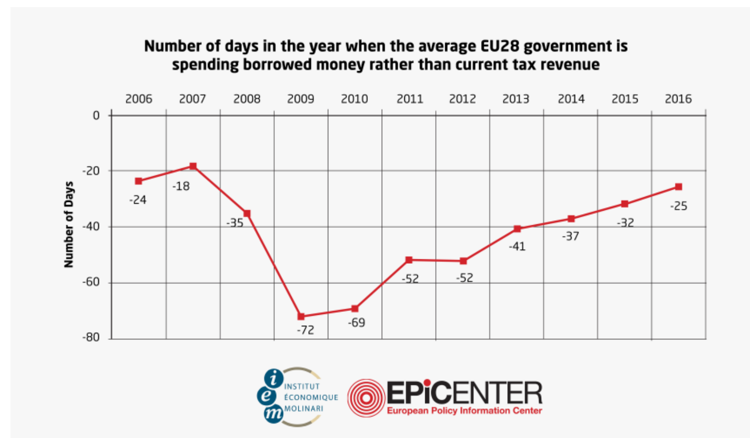
[1] IEM would like to thank EPICENTER Research Assistant Louis Rostain for valuable help compiling this briefing note.

[2] The UK and Greece both reduced their credit days in 2016, from 38 to 25 and, spectacularly, from 64 to 9, respectively.

in their credit days, whereas the four other countries in this quartile have either experienced stagnation or deterioration. Poland went from having 35 to 40 unfunded days, whilst Romania went from having 24 to 47 in just one fiscal year. Spain's balance also deteriorated, moving from 47 to 50 unfunded days. The last place goes to France, which has stalled from 53 to 54 days. France's 20-year average is approximately the same level as it is today.

France, one of the 'big three', has not reduced public spending, with its public debt increasing to nearly 100% of GDP in 2016, representing a danger for the EU economy as a whole.

No EU member state has averaged a budget surplus over the last 10 years. Yet most countries have actually improved their position. Even one of the worst crisis-hit countries, Greece, has been able to reduce its deficit along the lines of structural reform packages. The previous edition's bottom performers had been Greece and Portugal, both of which have significantly reduced their deficits over the past year. Considering the weight of the French economy in the Union, policymakers need to pay special attention to its case. The French debt-to-GDP ratio was already high at the start of the crisis and increased by 15% between 2010 and 2016 (Eurostat).



The study distinguishes between government administrations: central, regional (Austria, Belgium, Germany, Bulgaria, Spain), local and, finally, social security spending. The biggest share of spending is held by central governments. In general, social security and local administrations have budget surpluses, whereas regional administrations and central governments depend on credit for their financing.

More public spending for a better life? A comparison of public spending with HDI and the *Better Life* study

A common argument from pro-spending political parties and unions is that lower public spending leads to a decline in living standards. This is questionable, as shown by a comparison of public spending as a share of GDP with the Human Development Index and the OECD's *Better Life* study. Seven countries (Germany, Denmark, Netherlands, Ireland, Sweden, U.K., Luxembourg) with a better budget balance than France obtain better HDI scores. The OECD's *Better Life* study ranks France 11th in the EU, even though public spending as a share of GDP is the highest in Europe. This goes to show that high levels of public spending do not necessarily go hand in hand with a better quality of life.

Conclusion

The European Union member states have improved their average budgetary position over the past year, with almost all European countries reducing the amount of days funded by borrowing. The bottom quartile of the EU28 does however need special attention, with Romania drastically worsening its credit situation and France not paying enough attention to its debt and deficit levels. European countries have improved their budget balance and returned closer to pre-crisis levels, but efforts have to continue to reach Stability and Growth Pact thresholds.

References

Marques, N. and Philippe, C. (2017) *Le jour où les Etats de l'Union européenne ont dépensé toutes leurs recettes annuelles***.** Paris-Bruxelles: Institut économique Molinari.

Eurostat - General government gross debt - annual data
http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=teina225&plugin=1

Eurostat- General government deficit and surplus
http://ec.europa.eu/eurostat/tgm/table.do?tab=table&plugin=1&language=en&pcode=teina200