**Fiscal Follies: How new EU rules miss the mark on climate and prosperity**

Fiscal Matters, a coalition of civil society organisations, think tanks and trade unions, are deeply concerned about the political agreement on the revision of the EU fiscal rules. The rules do not constitute an adequate response to the challenges ahead: accelerating climate change, economic and social divergence, poverty and inequality, fundamental changes to the world of work, and war on EU's borders. All these challenges require more, not less, public investment.

The rules focus on achieving arbitrary debt and deficit-to-GDP ratios. Instead, they should have moved towards more effective criteria for ensuring debt and deficit sustainability and recognised the contribution of quality public investments and reforms to economic prosperity and debt sustainability.

Recent research suggests the EU needs at least an increase of €260bn of public investments annually to meet its climate obligations alone. The EU also has an annual social infrastructure investment gap of €192bn. To tackle Europe's pressing challenges, these gaps must be filled with urgency. Delayed action will be more expensive, less effective, increase fiscal risks and undermine debt sustainability.

The new rules will severely restrict Member States' capacity to invest in a socially just transition to a more sustainable and inclusive future. Some might have to implement significant expenditure cuts to follow the rules. The first impacts of the rules restricting fiscal space for crucial public investments can already be seen. For example, France has announced a €1.4 billion cut to its green transition budget as part of broader budget cuts. Denmark's Prime Minister is reportedly considering cuts to welfare to bolster defense spending. Germany has significantly cut its budgets, including cuts to green investments, which will have a negative impact on the economy. By severely restricting fiscal space, the rules also risk increasing economic and social divergence, meaning those with higher debt or deficits have less fiscal space to invest towards solving pressing environmental, social or geopolitical challenges. Especially those which were hit hardest by the economic and financial crisis are, according to research, already less prepared for future challenges.

While adequately regulated private finance has a role to play, it has proven to be largely insufficient over the last decades to fill green and social spending gaps and to deliver on the transition. We see no reason why this would change. Allowing private companies to control essential public goods, such as health, education, social housing and energy networks, risks prioritising profit over equitable access and long-term societal benefit, and faster decarbonization. It could potentially exacerbate inequalities and compromise the quality and accessibility of these vital services. The fossil fuel price increase, and corporate-led inflation have shown that governments need to play a greater role to steer our economy.

**Significant fiscal adjustment requirements incompatible with solving Europe's challenges**

The final compromise is a setback from the Commission's original proposal, which allowed for more - albeit still insufficient - flexibility to trigger quality public investments. Applying the debt sustainability analysis (DSA) methodology requires significant fiscal adjustments from Member States. The inclusion of new arbitrary numerical safeguards - particularly a requirement for those countries above 3% or 60% to reduce their structural deficit to below 1.5% of GDP - is further tightening existing arbitrary and problematic constraints. Overall, the combination of different requirements leads to very heterogeneous and extremely demanding fiscal adjustment for Member States. Initial ETUC calculations indicate that following the new rules will require substantial deficit reduction that will impose severe constraints on public expenditures. The exclusion of all national co-financing towards EU programmes from the calculation of net expenditure is commendable, but it does not create additional fiscal space. It only reorients investments towards EU priorities, as national co-financing still counts towards debt & deficit levels that many Member States must reduce.

**Minor qualitative improvements**

The qualitive improvements compared to the old rules are limited without serious consideration of environmental and climate challenges. On the positive side, Member States must develop multi-annual national fiscal-structural plans, implementing country-specific fiscal trajectories as well as resilience-enhancing reforms and investments. In their plans, Member States must explain how they will respond to the country-specific recommendations under the European Semester and make sure that reforms and investments are aligned with common EU priorities. However, the wording is non-committal (the plans should simply "explain how they will address" common priorities – art 11), which severely limits the potential of the new rules to improve the quality of public finances and to bridge investment gaps. It is welcome that Member States must report on national investment needs and involve stakeholders in the development of national fiscal-structural plans.

**Lack of clarity on the impact of the deal**

Added numerical safeguards lead to confusing, unequal rules. For instance, the deficit resilience safeguard would impose very different obligations on Member States who are just above 60% of debt-to-GDP and 3% of deficit-to-GDP than for Member States just below. This also functionally weakens the flexibility from existing relevant factors in the corrective arm regulation, which allows the Commission to accept temporary spending increases above the 3% deficit-to-GDP ratio.

**No official information has been published as to what the rules require from each country in terms of debt & deficit reduction and related public expenditure cuts and limits compared to the old rules. We do not find it responsible for Member States and the European Parliament to sign off on rules without clear information on what their impact will be.**

**Our call for action for the EU institutions**

- **European Commission**: Before the votes in Parliament and Council, publish the official simulations indicating by how much each Member State would need to limit the growth of their net expenditures and reduce their debt & deficit ratios in their first fiscal-structural plan.
- **European Parliament**: Before voting, get full clarity on the consequences of the rules and take sufficient time to ensure an improved agreement that avoids a return to austerity and enables the necessary fiscal space for investments, including towards common EU priorities.
- **European Commission/Council**: Ensure that the upcoming revision of the DSA methodology allows realistic and sustainable adjustment paths. Risks, including fiscal risks, of delayed action or inaction on climate, nature and economic & social convergence should be considered to allow increased fiscal space for proactive investments.
- **Next European Commission/Council/European Parliament**: Create a dedicated and long-term EU public investment fund post-2026 to drive the socially just transformation of our economy towards net-zero and a circular economy. Provide companies and people with confidence in the transition and strengthen economic and social cohesion by ensuring that governments can make long-term investments towards social and green objectives.

The well-being of people and the future of our planet depend on bold and decisive action taken now. Delayed action will greatly increase costs and worsen economic, environmental, social, and political outcomes. EU fiscal rules must support, not hinder Member States in achieving their objectives. We ask decision-makers to safeguard a just transition and a stable, democratic, prosperous, and thriving Europe for all.