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Analysis of Government Debt Dynamics in Euro Area Countries

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Whereas the internal financial resources of the state are often insufficient and do not cover its financing needs, it becomes imperative to borrow from foreign capital markets to achieve important and sometimes large objectives. Under these conditions, in the contemporary world economy more and more states register significant levels of public debt. The purpose of this article consists in the theoretical analysis of public debt, also carrying out a comparative study of the dynamics of government debt in the Eurozone countries.

Keywords: public debt, public deficit, government expenditure.

1. Introduction

It is acknowledged that every country is facing a so-called public debt which is an unavoidable event. Public debt means that debt that the state has to third parties, referring here to private individuals, banks, legal entities, businesses, from the country or abroad, who have bought bonds issued by the state to cover the financial needs of the state. In this context, it should be emphasized that to assess the sustainability of a state's economy, an important macroeconomic indicator is used, among others, namely the level of public debt relative to GDP.

Referring to the Eurozone, it is important to specify that over time the debt crisis triggered in this area has become very complex, emphasizing the need for a deeper knowledge of the related processes.

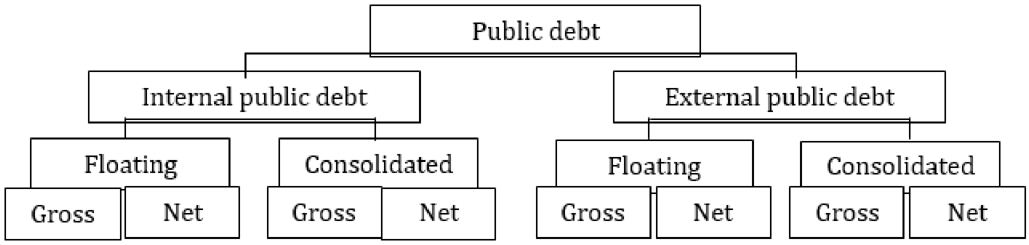
To cover all expenses that occur and are incurred during a period, the state is required to use public financial resources obtained from a series of mandatory levies such as taxes, fees, contributions. Along with these, the financing of the expenses can also be done if the state identifies the tax evasion and collects an amount from the detection of this crime. Besides, another way of financing the expenses would be from non-reimbursable external funds, as well as from the amounts borrowed directly or indirectly by the state.

2. Definition and forms of public debt

There are different definitions regarding public debt, given that the literature and certain international financial institutions have a wide variety of definitions. A suggestive definition would be that "public debt represents the total amounts borrowed by central public authorities, administrative-territorial units and other public entities from internal or external creditors or those which remained to be reimbursed at a certain period." [5]

Under these conditions, the public debt ceiling includes all the financial obligations that can be contracted and guaranteed by the central and local public administration authorities for 1 year, which is established annually by law [4]. There is both an internal public debt ceiling and an external public debt ceiling, as can be seen in Figure 1:

Figure 1. Public debt structure



Source: [1]

Regarding the forms of public debt, it is important to specify that it is established and managed separately according to its two forms:

- governmental public debt
- local public debt.

The governmental public debt expresses a "part of the public debt, which represents the totality of the internal and external financial obligations of the state, at a given moment, coming from the loans contracted directly or guaranteed by the Government, through the Ministry of Public Finance, on behalf of Romania, from the financial markets".[6]

The other form "local public debt means the totality of payment obligations, internal and external of the local public administration authority, arising from loans contracted or guaranteed by it on the internal and external capital market". [6]

Also, the public debt is classified according to the term in:

- short-term public debt (floating);
- medium- and long-term public debt (consolidated).

According to another way of classification, namely depending on the quality of creditors, the public debt can be:

- gross public debt, referring to the total value of loans;
- net public debt, which does not include the value of loans placed with state institutions.

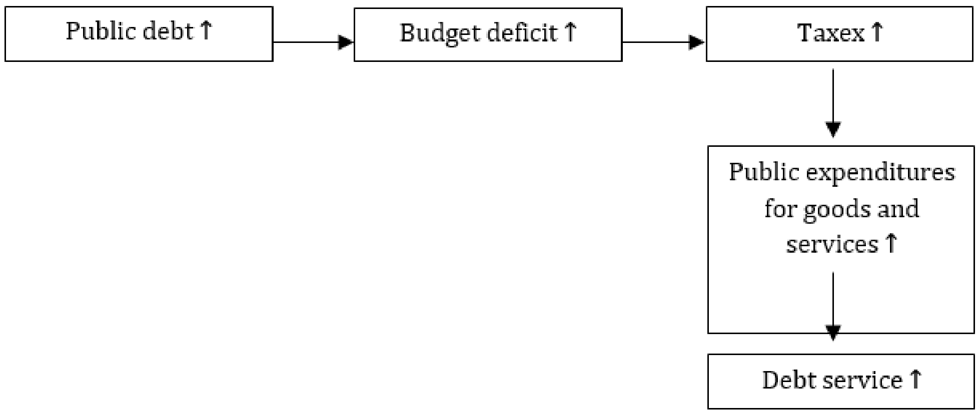
If the creditors' headquarters is taken into account, the following forms are distinguished:

- internal public debt (occurs when the debtor and the creditor are from the same country);
- external public debt (when the creditor is from another country).

An important aspect is that "the minimum rule for responsible governance says that public debt should not grow faster than nominal GDP. Every time when this rule is broken, the percentage of public debt in GDP will increase, as well as the interest rate in GDP, and the tax burden on citizens will also increase." [3]

Figure 2 shows the impact of public debt. Thus, if this indicator increases, then there is an increase in the budget deficit. At the same time, there may be an increase in taxes, but also public spending on goods and services. And the important thing is that debt service increases.

Figure 2. Public debt impact



Source: [3]

The impact of increasing public debt on short-term investment is reflected in the so-called phenomenon of decommissioning. According to the theory of dislocation, it is assumed that an expansionist policy, generating a budget deficit, will have as a consequence a dislocation of private investments. A major negative effect in the case of a large public debt is that of the substitution of private capital by public debt. Against this background, it is considered that in the long run, the replacement of capital harms the economic growth of the country in question and implicitly on the living standard of the citizens. [2]

3. Evolution of government debt in Euro Area countries

It is known that at the European Union and Eurozone level, there is a carefully developed fiscal policy framework, which includes a series of rules designed to ensure fiscal discipline, to emphasize and maintain the stabilizing role of public finances. An important role is played by the fiscal provisions of the Maastricht Treaty, including in particular the excessive deficit procedure (EDP). This refers, inter alia, to the reference values for the general government deficit ratio (which should not exceed 3% of GDP) and the government debt ratio (which should not exceed 60% of GDP). At the same time, the above-mentioned Framework also includes the Stability and Growth Pact, which promotes the coordination of economic policies and defines the conditions under which the excessive deficit procedure can be applied. To deter unsustainable deficits, several sanctions are provided, which are part of the main mechanisms used in the Stability and Growth Pact.

As can be seen in Table 1, in 2014, 6 of the 19 Eurozone countries had a government debt level that exceeded 100% of GDP (Belgium 107%, Ireland 104.4%, Greece 178 .9%, Spain 100.7%, Italy 135.4%, and Cyprus 109.2%). In the period that followed, the vast majority of these countries managed to reduce the level of government debt, so that in 2019 only Italy (134%) and Greece (176.6%) still registered a government debt over 100% of GDP. On the other hand, Estonia recorded during the analyzed period, the lowest level of government debt in the Eurozone and it should be noted that year after year it managed to reduce it (from 10.6% in 2014 to 8, 4% in 2019).

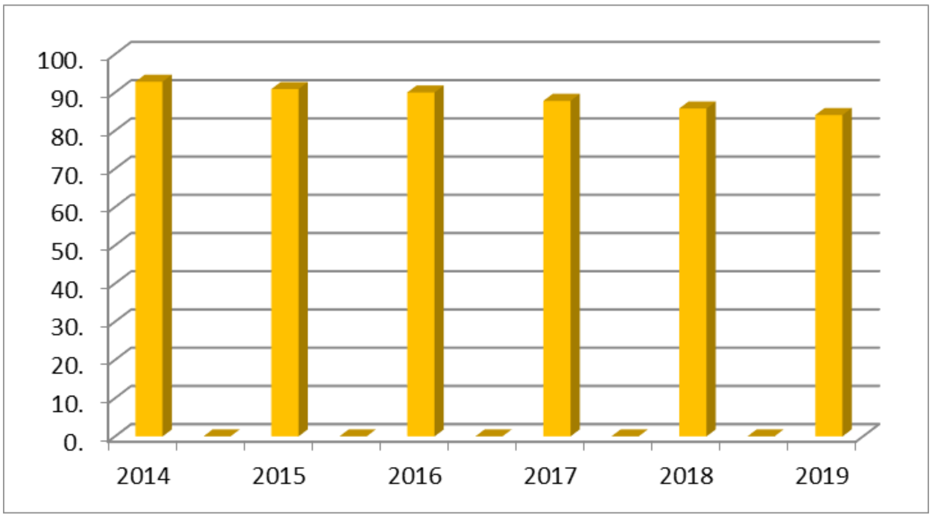
Table 1. The level of government debt in Eurozone countries in the period 2014-2019 (% of GDP)

	2014	2015	2016	2017	2018	2019
Euro area - 19 countries (from 2015)	92.8	90.9	90	87.8	85.8	84.1
Belgium	107	105.2	104.9	101.7	99.8	98.6
Germany	75.7	72.1	69.2	65.3	61.9	59.8
Estonia	10.6	10	10.2	9.3	8.4	8.4
Ireland	104.4	76.7	73.8	67.7	63.5	58.8
Greece	178.9	175.9	178.5	176.2	181.2	176.6
Spain	100.7	99.3	99.2	98.6	97.6	95.5
France	94.9	95.6	98	98.3	98.1	98.1
Italy	135.4	135.3	134.8	134.1	134.8	134.8
Cyprus	109.2	107.5	103.4	93.9	100.6	95.5
Latvia	41.6	37.3	40.9	39.3	37.2	36.9
Lithuania	40.6	42.6	39.7	39.1	33.8	36.3
Luxembourg	22.7	22	20.1	22.3	21	22.1
Malta	63.4	58	55.5	50.3	45.6	43.1
Netherlands	67.8	64.6	61.9	56.9	52.4	48.6
Austria	84	84.9	82.9	78.3	74	70.4
Portugal	132.9	131.2	131.5	126.1	122	117.7
Slovenia	80.3	82.6	78.7	74.1	70.4	66.1
Slovakia	53.5	51.9	52	51.3	49.4	48
Finland	59.8	63.6	63.2	61.3	59.6	59.4

Source: Eurostat

With a public debt level up to 60% in 2019 are also the countries: Luxembourg (22.1%), Latvia (36.9%), Lithuania (36.3%), Malta (43.1%) , Netherlands (48.6%), Slovakia (48%), Ireland (58.8%), Finland (59.4%) and Germany (59.8%). It should be noted that, compared to 2014, in 2019 all Eurozone countries, except France, managed to reduce their government debts.

Figure 3. Government Debt in Euro Area - 19 countries (from 2015)



Source: Eurostat

If we analyze the average government debt at the level of the entire Eurozone, we can notice its downward trend from 2014, when it recorded 92.8% of GDP, until 2019, when it registered a share of 84.1% of GDP. However, this indicator is still high.

4. Conclusions

Both nationally and internationally, public debt management, in general, exceeds the boundaries of necessity, thus becoming an obligation. In the absence of sustained fiscal consolidation efforts, there will be significant increases in public debt, and in the long run, this is a major impediment to a sustained recovery and balanced economic growth. Thus, in this case, the situation becomes very sensitive and can even generate a large crisis of public debt.

Another important aspect is that the effect of public debt on the short-term economy takes the form of unleashing or stimulating investment. The expansionary budgetary policy generating a budget deficit has a significant impact on the economy. In the conditions in which the state increases the public expenditures, applying a series of economic policies based on the deepening of the budget deficit and the increase of the public debt, the national economy is decapitalized, registering a negative effect on investments. Both capital and national production are affected in the long run.

The sustainability of public debt is influenced both by the general macroeconomic framework and the vulnerabilities present at the level of the private sector and by the level, dynamics, the structure of the portfolio, and its cost.

Some Eurozone countries have managed to reduce their government debt levels over the period under review, which could be a consequence of robust economic growth and unprecedented declines in interest rates, but replenishing budgetary reserves remains particularly important reducing vulnerabilities to future shocks.

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