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A Challenge for the G20: Globally Stipulated Debt Brakes and Transnational Independent Fiscal Supervisory Councils

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Abstract:

Debt-to-GDP ratios have grown to unprecedented levels in many industrialized economies. This requires disciplined consolidation efforts which are, however, supposed to come now at the wrong time with the economic recovery being fragile. Against this background, we call for a global debt brake following the German example and discuss the political progress achieved at the most recent Euro and G20 summits. The agreement on the debt brake should be binding and hence be fixed in national constitutions and monitored by independent transnational fiscal councils. The fiscal councils could be located at the ESM and the IMF and should conduct a regular evaluation of national budget plans. In an economic and political environment which is characterized by large uncertainties concerning economic prospects and the fear of a potential spreading of the sovereign debt crisis, a global debt brake in combination with an independent transnational supervisory council would send a credible signal that a reduction of sovereign debt to sustainable levels is not further delayed into the future. The new fiscal policy framework thus leaves enough room for discretionary fiscal policy and the workings of automatic stabilizers in an economic downturn.

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[Back](#)