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Presidency Note

How Can Europe Pay for Things That It Cannot Afford?

Europe is facing a period of high and persistent public investment needs. According to the IMF, meeting fiscal spending needs would create a financing gap of around 5 percent of GDP across countries. The recent energy price surge highlighted once again the urgent need to accelerate the green transition and the electrification of the economy, which require substantial investments in renewable energy, electricity grids, storage capacity, energy efficiency, clean transport and industrial decarbonisation. At the same time, the geopolitical environment has increased the urgency to strengthen Europe's defence capabilities and security architecture. Additional pressures stem from demographic ageing and the associated rise in pension, healthcare and long-term care expenditure. Europe must also accelerate investments in digitalization, infrastructure, innovation and productivity-enhancing technologies, while strengthening resilience and strategic autonomy in key sectors such as critical raw materials. Lastly, common EU borrowing undertaken to address urgent needs has also increased debt servicing costs, adding further pressure on public finances.

These investment needs arise in a challenging fiscal environment. According to the latest data published by Eurostat, the EU general government deficit remained above 3%, standing at 3.1% of GDP in 2025, while the average government debt ratio increased for the third consecutive year, reaching 81.7% of GDP by the end of 2025. Several Member States continue to face elevated deficit and debt levels and remain under excessive deficit procedures, limiting fiscal buffers and increasing vulnerabilities to higher financing costs and adverse shocks.

In this context, the revised EU economic governance framework provides an important anchor for balancing fiscal sustainability with the need to support growth-enhancing reforms and investments. The new framework is designed to ensure a gradual and credible reduction in debt ratios, safeguarding fiscal sustainability over the medium term while at the same time providing fiscal space for priority investments and reforms that strengthen growth potential, resilience and competitiveness.

The credibility of the revised framework will depend critically on its strict, timely and effective implementation. Fiscal discipline remains essential to preserve market confidence, safeguard debt sustainability and maintain adequate fiscal buffers in an increasingly uncertain global environment. In this regard, any deviation from the net expenditure paths recommended by the Council risks delaying the necessary fiscal consolidation process and may lead to more demanding adjustments

in subsequent years. Similarly, the activation of national escape clauses or the general escape clause should remain limited to exceptional circumstances, given that prolonged fiscal loosening could undermine the credibility of the framework and further constrain fiscal space over the medium term.

Against this backdrop, the IMF estimates that the current consolidation plans under the revised EU framework fall well short of closing the financing gap in most EU countries and suggests that ambitious structural reforms at national and EU level can be promoted to ease the fiscal adjustment burden. Moreover, the IMF estimates that even with the implementation of an ambitious reform agenda, additional fiscal consolidation beyond what is required under the revised EU framework will be needed for the majority of the European countries[1] to keep debt in a sustainable path, while around one quarter of European countries need to rethink the Government's role in certain sectors, such as health care, education, pensions, and infrastructure in order to consolidate to levels which are very difficult to achieve through conventional consolidation efforts.

Europe should reconcile very large common investment needs with the imperative of maintaining sound public finances through coordinated actions at both national and EU levels.

Achieving this balance will require credible national fiscal policies, effective prioritisation of public expenditure and improved spending efficiency and revenue collection. In cases of significantly high debt and deficit levels, ambitious reforms aiming to improve fiscal sustainability in certain sectors, such as healthcare, education, pensions and infrastructure may be required in order to ensure compliance with the recommended net expenditure path. Moreover, economic and fiscal policy coordination, through the European Semester, is critical for promoting reforms that address fiscal risks and aligning reform agendas with the need to ensure fiscal sustainability. This approach could be complemented by an improved framework to assess the implementation of reform recommendations, especially for recommendations aiming to address fiscal risks.

At EU level, it is crucial to promote the mobilisation of private capital, continue efforts to deepen the Single Market and enhance the efficiency of EU-level financing instruments, ensuring that the EU resources are utilized in the most effective way possible. The Multiannual Financial Framework (MFF) serves as a vital instrument for common priorities, channeling EU resources toward shared challenges like defense capabilities and climate action to support these goals. Lastly, common borrowing mechanisms should be considered where justified by clear European added value, such as for joint defense procurement or large-scale infrastructure in energy and critical materials, ensuring disciplined use, risk-sharing safeguards, and alignment with fiscal rules to maintain credibility and avoid moral hazard while enabling scale that individual states cannot achieve alone. However, the longer-term implications of common borrowing warrant careful consideration, as debt servicing costs will weight on future EU budgets. According to the European Court of Auditors, by 2027, outstanding EU debt could exceed €900 billion, nearly 10 ten times the pre-NGEU level, and interest costs envisaged in the current MFF are expected to surpass €30 billion, more than double from earlier forecast. The coverage of interest costs creates a real challenge for the sustainability of the MFF and the funding of EU priorities, if not accompanied by an increase in own resources.

[1] The IMF analysis covers a broader set of European countries that expands beyond the European Union.

Questions for discussion:

1. *To what extent does the flexibility allowed within the revised EU economic governance framework and the reforms promoted at EU level contribute to addressing Europe's large investment needs without undermining fiscal sustainability? Do you share IMF's view that some member states should move beyond the EU fiscal framework and rethink the Government's role in some areas, i.e. pensions, welfare system, health care, infrastructure and education?*
2. *How can the economic and fiscal policy coordination at EU level be improved to promote national reforms that improve fiscal sustainability and ensure their effective implementation?*
3. *What role should common European financing instruments and EU-level initiatives play in supporting investments? To what extent should the efficiency of EU-level financing instruments be enhanced?*