

# Proposal for a Stabilisation Mechanism for the EU Budget\*

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*The question of how to give the European Union budget a stabilising function in the event of shocks has long been a concern for economists and economic policy-makers. Our paper proposes a mechanism that is automatic and relies on unemployment figures, similar to the role of automatic stabilisers at the national level. A novel feature of the proposal is that, instead of considering the overall unemployment rate as most studies do in the literature, it uses excess unemployment data. As a result, structural unemployment differences between countries can be discarded. A system based on excess unemployment would not involve the modification of national systems, but would introduce a complementary, top-off system. Benefits are paid in addition to payments through the national unemployment systems and are channelled into a fund set up in advance for this purpose. Annual payments to the fund are made in proportion to GDP. The payment would represent an additional cost for Member States, which could be financed by jointly guaranteed long-term loan.*

## 1. Introduction

The ability to smooth asymmetric shocks is a fundamental feature of a well-functioning economic and monetary union. Economists and economic policymakers have long been concerned with the question of how to provide the European Union budget with a stabilising function that could play a stabilising role in the event of shocks, even asymmetric shocks. Efforts have already been made to do so, notably *the European instrument for temporary Support to mitigate Unemployment Risks in an Emergency (SURE)*, set up in response to the Covid-19 pandemic, as well as the *Recovery and Resilience Facility (RRF)*. As both funds take into account the impact of country-specific shocks, the principle of solidarity is applied to some extent. However, these are one-off initiatives, with SURE terminated at the end of 2022, while amounts from the recovery fund are to be drawn down by 2026. What

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\* The papers in this issue contain the views of the authors which are not necessarily the same as the official views of the Magyar Nemzeti Bank.

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is needed is a permanent, automatic stabilisation instrument at the EU level, such those existing in national budgets. Typically, this role is fulfilled by unemployment benefit schemes. In our study, we propose a similar automatic stabilisation mechanism at the level of the euro area. We are aware that the introduction of such a system is fraught with difficulties, as it raises the delicate issues of risk sharing, solidarity and moral hazard. Our proposal would also require an additional payment from Member States. We acknowledge that such a proposal may be a distant goal, but we believe it is worth putting this new approach on the table alongside the previous proposals.

*Our proposal is for a mechanism that acts as an automatic stabiliser based on unemployment, since unemployment is the most tangible and simplest automatic stabiliser in the budget. Our paper takes excess unemployment as a starting point and calculates the level of benefits that would have to be paid out each year, and the amounts that would need to be allocated from budgets or other sources.*

## **2. Literature reviewed**

A number of economists have published papers on the concept of a stabilisation budget for the EU or the euro area, aimed at enhancing stability and resilience within the EU or the euro area. In the following, we look at a selection of publications by authors dealing with this topic, which focus specifically on unemployment as a possible automatic stabiliser. Therefore, we do not describe in detail the numerous studies that have focused primarily on the concept of a euro area stabilisation budget, rather than specifically on the provision of a common unemployment benefit. Although some authors have touched upon the issue of unemployment benefit insurance in the context of a broader debate on fiscal capacity and risk-sharing mechanisms, this has not been the focus of their research (e.g. *MacDougall et al. 1977; Thygesen et al. 2022*). In this context, however, it is worth mentioning *Nikolov (2016)*, whose study provides a good summary of the channels through which automatic stabilisers can operate at the macro level. The study distinguishes between private and social channels. The most important element of the private channel is cross-border capital flows, where consumers and investors in one country that has suffered a negative shock can access capital in other countries. The other private channel is labour migration, where workers migrate to a country that has not been hit by a negative shock. Understandably, this effect is limited among European countries compared to the United States. The Community channel would be able to work through fiscal transfers, such as cross-border grants or a European-wide unemployment scheme. *Nikolov* rightly points out that the EU budget is small compared to the national budgets of EU members, and is mainly intended to help convergence and catching up, rather than smoothing out shocks. *P. Kiss (2020)*

provides a comprehensive review and analysis of the literature related to fiscal stabilisation, and criticises the calculation of automatic stabilisers applied in the literature.

Sebastian Dullien is one of the first pioneers of studies on an EMU-wide unemployment scheme. *Dullien (2007)* presents different scenarios for a European unemployment insurance system. It takes as a basis the euro area Member States at that time and *only the short-term unemployed are covered by an insurance scheme to supplement national unemployment benefit systems*. Short-term unemployment covers persons who have lost their jobs in the last 12 months. The scheme would be financed by a tax on wages and is calculated to balance contributions and receipts over the period 1999–2005.

*Darvas et al. (2014)* provide a comprehensive assessment of the possibilities for the founding of a European unemployment insurance scheme. *The authors outline the benefits of macroeconomic stabilisation, possible solutions and the difficulties that would inevitably be encountered in setting up such a system*. In particular, they draw attention to the dual problem of solidarity and moral hazard. According to the authors, setting up such a system would be a long-term task. No precise calculations were provided on the financial implications of the envisaged system.

*Dolls et al. (2015)* also addressed the introduction, the calculation methods and the prospects of a common unemployment system. A period from 1999 to 2013 was used as a basis for examining the possible introduction of a common unemployment insurance scheme in the euro area. The focus of the study was on the redistributive and stabilising effects of the *common euro area unemployment benefit system – which partly replaces national unemployment benefit systems* – and the main difficulties and advantages of such a system. Their main findings were that a basic common unemployment scheme with a replacement rate of 50 per cent over 12 months can be implemented with a relatively small annual budget. Over the period under review, average benefits would have amounted to EUR 47 billion, financed by a contribution rate corresponding to 1.56 per cent of earned income. *The scheme would not be set up for permanent redistribution; indeed, it would only be intended to help the short-term unemployed*.

*Beblavy et al. (2015)* also address the issue of macroeconomic stabilisation through a common European unemployment benefit scheme. *The authors' model takes the number of short-term unemployed within 12 months*, compared to a ten-year moving average. The system becomes functional when the actual short-term

unemployment rate exceeds the standard deviation of the 10-year average. The study assumed a benefit period of 12 months and a replacement rate of 40 per cent of average earnings, paid to 80 per cent of the short-term unemployed eligible for the benefits. There would also be an own contribution, which equals the national unemployment benefit rate. Funding would be provided by Member States. The fund would contribute 0.1 per cent of GDP per year until 0.5 per cent of EU GDP is accumulated in a dedicated fund. Contributions will then stop and restart if the fund falls below 0.5 per cent of EU GDP. Three different scenarios and a multiplier of 1.5 per cent are used to calculate the stabilisation effect. It is stressed that their figures are only rough estimates and depend heavily on the parameters chosen.

*Arnold et al. (2018)* have also produced calculations that take into account percentage changes in unemployment. They propose the creation of a Central Fiscal Capacity (CFC) for the euro area to help smooth macroeconomic cycles. To properly build the CFC, *the authors propose the establishment of a macroeconomic stabilisation fund*, financed by regular annual contributions, to accumulate capital in good times, and to make transfers to support the countries concerned in bad times. *Borrowing is also proposed. Potential transfers would be automatically triggered by a cyclical indicator* based on the deviation of the unemployment rate in the current year from the 7-year moving average unemployment rate. EUROMOD was applied to measure the extent of stabilisation that could be delivered under different shocks in the period between 1990 and 2017. Different scenarios were examined to see how the CFC would perform in a downturn such as the great recession or the euro area crisis. Preliminary research found that annual contributions would need to fall somewhere between 0.25 and 0.5 per cent of euro area GDP to ensure that contribution rates provide sufficient resources to replenish the fund. *The analysis of the authors shows that a contribution of 0.35 per cent of GDP would already provide significant stabilisation capacity*, although it would have required borrowing for a few years after the Global Financial Crisis. It was calculated that the CFC they envisioned could significantly reduce negative macroeconomic impacts. They did not *focus* specifically on the stabilisation mechanism and *its automatic operation*, but rather investigated stabilisation effects along different parameters.

*Beblavy et al. (2015)* and *Arnold et al. (2018)* attempt to estimate a possible stabilisation effect in their studies. They point out that their calculations are only rough estimates, but give an idea of the extent to which stabilisation effects could be expected. For the purposes of our study, we wish to highlight the calculations of *Arnold et al. (2018)*, because they focus on euro area Member States. They conclude that for most Member States, with an annual GDP contribution of around 0.35 per cent, the stabilisation effect may range between 1 and 3 per cent, depending on

the shock effect, i.e. that would be the amount by which the stabilisation effect could mitigate the adverse impact of a negative shock on GDP. As we will see, this is consistent with our estimated 0.33 per cent contribution; accordingly, we may conclude that our proposed excess unemployment scheme may have a similar stabilisation effect. We wish to stress, however, that the calculation of this effect strongly depends on the parameters selected. In our paper, we do not address the modelling of possible stabilisation effects, since we propose an automatic stabilisation mechanism based on excess unemployment, the design and parameters of which can be varied arbitrarily.

In the remaining part of this paper, we formulate our specific proposal and explain its details, supported by calculations. Finally, we draw policy-relevant conclusions. Like most of the literature reviewed, our focus is on the euro area. Coordinating economic policies and responding to challenges becomes more manageable when dealing with a more concentrated group of countries with a common monetary policy. Extending the calculations to the whole EU would no longer add value to the proposed mechanism. The *mechanism* is the crux of the proposal, which could be used for any group of countries; for example, it would be useful in the event of a two-speed Europe, an idea that sometimes comes up in political debates.

### 3. Proposal

*Designing and automatically operating a common unemployment benefit system for the euro area is a difficult task. We are departing from the work of the authors presented in the literature reviewed in that we propose a new approach: instead of focusing on the total mass of unemployed, excess unemployment is at the centre of our attention.* Due to differences in unemployment rates, the duration of the benefits, replacement rates and other differences, unemployment benefit systems in the countries of the euro area are varied and have evolved over decades alongside social and political commitments. Consolidating these systems does not appear realistic for the foreseeable future. In our article, we therefore propose to design the unemployment benefit system in a way that *complements already existing national schemes*. In a system based on excess unemployment, national systems would not be altered, but a complementary, *top-off* system would be introduced, i.e. payments would flow to countries in addition to the unemployment benefits received through national systems. The top-off payments would go into a fund set up in advance for this purpose; we may call this the *Unemployment Assistance Fund (UAF)*. A system based on excess unemployment would thus also

take into account structural unemployment differences; in other words, it would not provide higher support in countries where the unemployment rate is typically higher for structural or social reasons, but would *take into account the development of the excess, uniformly compared to the average of previous years* in the country concerned. It is worth noting at the outset that the top-off payments would be made to countries, not to the unemployed.

To calculate excess unemployment, we needed the unemployment rates for the year under review,<sup>1</sup> which we compared to the average unemployment rate for the preceding 7 years. Citing ECB and CEPR research, *Arnold et al. (2018) conclude that the average economic cycle in the European Union is 7 years*. Using this 7-year moving average allowed us to take into account a longer period in our calculations; this enabled us to eliminate outliers observed in a single year only, and to make the actual unemployment rate comparable with a trend. The last year of the moving average is the year preceding the calculation of the current excess unemployment. *The percentage-point value of excess unemployment can be calculated by comparing the moving average and the unemployment rate for the year under review*. In cases where the rate is lower than in the previous period, no additional benefits are paid to Member States, while in cases where the rate is higher, benefits are calculated using the percentage-point difference between the excess unemployment rate and the actual unemployment rate. The surplus percentage in the positive direction is obtained by multiplying the number of unemployed persons in the working age group (15–65 years; i.e. the age groups used to calculate the unemployment rates) by the number of unemployed persons in the working age group in the specific year.

The unemployment benefit system *has undergone significant changes in the wake of the global financial crisis*; therefore, we take into account data for the period of 2009–2022, both in terms of duration and replacement rate. *There are significant differences in the duration of the benefit period* between euro area Member States.<sup>2</sup> There are countries that only set a maximum period for claiming benefits (e.g. Cyprus, Malta), some countries have a minimum and a maximum period (e.g. Portugal, Germany), while in other countries even more factors (e.g. dates of previously claimed unemployment benefit; how many years the employee has worked in the past; how many years remained to retirement age; whether the employee has earned above a certain wage level; marital status; whether there are minor children in the family, etc.) are taken into consideration to determine how long an employee can receive the unemployment benefit and what the benefit entails. Taking into account a wide range of scenarios and the fact that basic benefits

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<sup>1</sup> Source: [https://ec.europa.eu/eurostat/databrowser/view/UNE\\_RT\\_M\\_custom\\_6679773/default/table](https://ec.europa.eu/eurostat/databrowser/view/UNE_RT_M_custom_6679773/default/table)

<sup>2</sup> Source: <https://www.missoc.org/missoc-database/comparative-tables/>

often cover 12 months and the median of the maximum values in the period under review is 12 months, *we assume a duration of 12 months for the unemployment benefits* (consistent with *Dolls et al. 2015*). As for the replacement rate,<sup>3</sup> once again, there are significant differences between the minimum and maximum values in Member States. Both the average and median values hovered around the 66-per cent mark during this period; consequently, *we calculate with a replacement rate of 66 per cent*.

Relying on the parameters presented above, it is possible to calculate the unemployment benefit system (*b*) required to cover the excess unemployment observed from the adoption of the euro in 1999 until 2022. Thus, the working-age population<sup>4</sup> (*p*) was multiplied by the percentage-point rate of excess unemployment (*u*) (only if the deviation from the moving average of the previous 7 years was positive), then the product was multiplied by PPP-adjusted GDP per capita<sup>5</sup> (*g*), and then by the 12-month benefit duration (*t*) and the 66 per cent replacement rate (*r*). GDP is adjusted to the PPP value in order to ensure that the unemployed in countries at different levels of development receive an appropriate amount of money relative to their own income.

The calculation is therefore:  $b = p * u * g * t * r$ .

For the countries considered, we present three years as illustrations: a calmer mid-2000s year (2004), the year 2013, which required the highest payments, and the year 2022, which has the most recent complete data series available (*Table 1*).<sup>6</sup>

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<sup>3</sup> Source: <https://www.missoc.org/missoc-database/comparative-tables/>

<sup>4</sup> Source: [https://ec.europa.eu/eurostat/databrowser/view/DEMO\\_PJAN\\_\\_custom\\_5668080/default/table](https://ec.europa.eu/eurostat/databrowser/view/DEMO_PJAN__custom_5668080/default/table)

<sup>5</sup> Source: [https://ec.europa.eu/eurostat/databrowser/view/PRC\\_PPP\\_IND\\_\\_custom\\_6701310/default/table](https://ec.europa.eu/eurostat/databrowser/view/PRC_PPP_IND__custom_6701310/default/table)

<sup>6</sup> We have completed a considerable number of calculations based on various calculations and possible approaches for different scenarios (e.g.: replacement rates, duration, cycles, excess unemployment, amount of unemployment benefits, adjustments to the moving average); however, the presentation below is limited only to the most significant and interesting calculations.

**Table 1**  
**Breakdown of excess unemployment benefits by country (2004, 2013, 2022)**

Member State	2004					2013					2022
	Deviation of unemployment moving average (pp)	Excess unemployment (persons)	Excess unemployment benefits (EUR million)	Excess unemployment benefits (GDP PPP)	Deviation of unemployment moving average (pp)	Excess unemployment (persons)	Excess unemployment benefits (million)	Excess unemployment benefits (GDP PPP)	Deviation of unemployment moving average (pp)	Excess unemployment benefits (GDP PPP)	Deviation of unemployment moving average (pp)
Austria	1.5	84,857	1,546	0.7	0.5	31,846	727	0.2	-1.1		
Belgium	0.4	25,469	440	0.2	0.8	62,919	1,308	0.4	-1.1		
Cyprus	0.5	2,494	35	0.2	9.7	59,885	870	4.6	-3.2		
Estonia	-1.6	-	-	-	-1.3	-	-	-	-0.4		
Finland	-1.4	-	-	-	0.6	22,309	440	0.3	-1.3		
France	-0.6	-	-	-	1.5	635,675	11,957	0.6	-1.7		
Greece	-0.1	-	-	-	14.8	1,084,586	13,458	6.5	-7.6		
Netherlands	2.2	242,997	4,699	1.0	2.4	272,435	6,383	1.1	-2.1		
Croatia	0.2	5,636	45	0.1	5.8	169,751	1,793	2.6	-3.2		
Ireland	-1.2	-	-	-	3.1	95,993	2,192	1.4	-2.3		
Latvia	-1.8	-	-	-	-0.9	-	-	-	-1.4		
Lithuania	-3.7	-	-	-	0.9	18,241	232	0.4	-1.5		
Luxembourg	2.3	7,243	252	1.0	1.1	4,066	195	0.5	-1.4		
Malta	0.4	1,002	12	0.2	-0.5	-	-	-	-1.2		
Germany	1.5	863,368	14,758	0.7	-2.3	-	-	-	-0.6		
Italy	-1.9	-	-	-	4.4	1,731,895	29,948	1.9	-2.5		
Portugal	1.8	130,235	1,504	0.8	5.5	382,700	5,102	2.4	-2.7		
Spain	-2.4	-	-	-	10.1	3,226,102	49,824	4.6	-4.0		
Slovakia	1.8	68,786	563	0.8	1.5	60,440	806	0.7	-1.7		
Slovenia	-0.5	-	-	-	3.6	51,906	740	1.7	-2.1		
Total (EUR million)		1,432,086	23,854			7,910,751	125,974				
Euro area GDP PPP (%)			0.3				1.3				

Note: \*Source: [https://ec.europa.eu/eurostat/data/browser/view/PRC\\_PPP\\_IND\\_\\_custom\\_6701310/default/table](https://ec.europa.eu/eurostat/data/browser/view/PRC_PPP_IND__custom_6701310/default/table)

Source: Authors' calculations

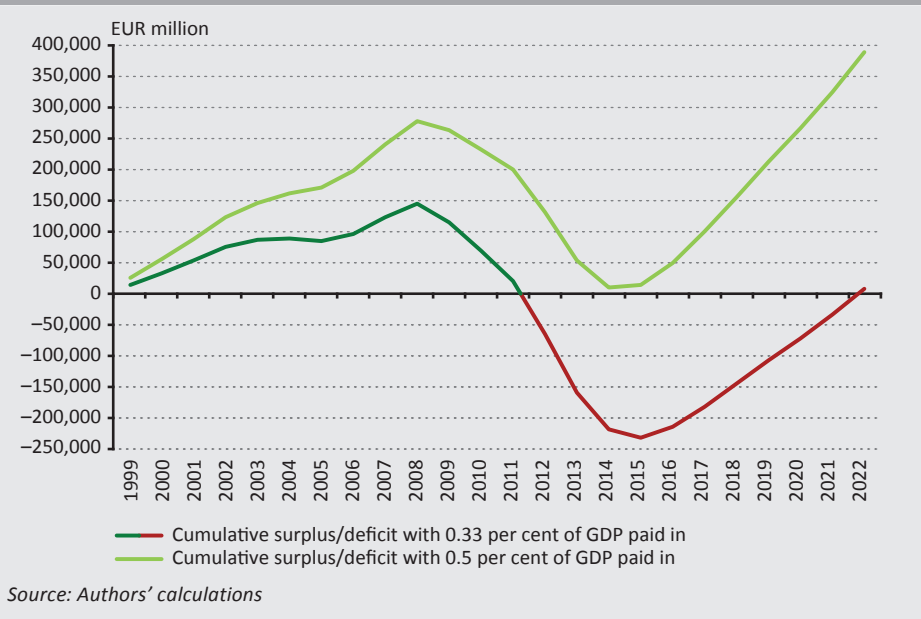


The first data series presented above – for the year 2004 – contains typical data for the decade preceding the 2008 crisis. The decade was characterised by falling unemployment, rising GDP and a lack of major downturns and crises; it was a more peaceful period of growth. Accordingly, only half of the Member States would have received top-off payments. By contrast, following the global crisis and the euro area crisis, conditions worsened significantly, with rising unemployment and stagnating or falling GDP. In 2013, a year when unemployment was hit hardest by the crises, 80 per cent of euro area Member States – 16 countries – would have received payments from the excess unemployment benefit scheme. Mediterranean countries, in particular, would have benefited from substantial unemployment assistance. As a percentage of GDP, Greece would have received 6.5 per cent, Spain 4.6 per cent, Portugal 2.4 per cent and Italy 1.9 per cent. In 2013, excess benefits would have represented 1.3 per cent of the euro area's total GDP; i.e. EUR 126 billion. After the crisis wore off, by 2022 all countries had a lower unemployment figure than in the previous 7 years, which means that no extra payments would have been needed. This is why *Table 1* shows only one column for 2022, presenting the percentage-point deviation of unemployment from the moving average (all values are negative).

The example of the three years shown as an illustration demonstrates that the distributions of *excess unemployment benefit payments and the beneficiary countries can widely vary from year to year*. In practice, it would be impractical to fund a system where in some years there would be no payments or receipts at all, or where years with low payments would alternate with years exhibiting a sharp increase, as in 2013. In practice, *a feasible system would be one where a flat rate of contributions would be made each year* to the common fund (UAF). This would make the system simpler, more transparent and easier to predict. In years when the payments for excess unemployment benefits are lower than the constant rate contributions, the money accumulated in the UAF would be utilised in years of higher unemployment.

The next question to be answered is the optimal level of annual payments as a percentage of GDP to cover the amount of excess unemployment benefits. Based on the above parameters, the average annual payment for the period of 1999–2022 is 0.33 per cent of euro area PPP-adjusted GDP. However, such annual payments would have been insufficient to cover the high payment needs observed in the period of 2012–2021. In order to cover the payments for the whole period, 0.5 per cent of euro area GDP would have been required (see *Figure 1*). In this case, the funds in the UAF would have swelled substantially from 2015 onwards.

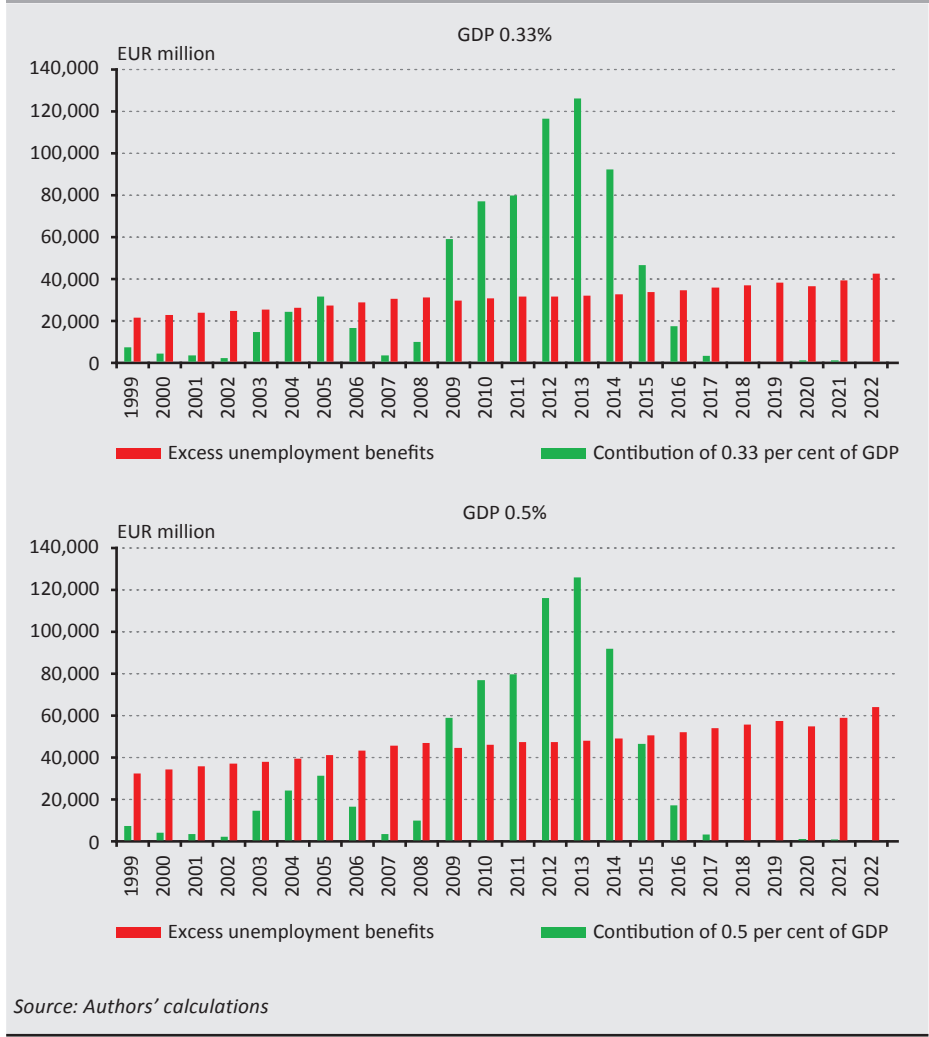
**Figure 1**  
**Cumulative excess unemployment benefits and contribution of 0.33 per cent vs. 0.5 per cent of GDP in the euro area**



These calculations show that it is difficult to define a constant contribution rate that would always cover the payment of excess unemployment benefits in the long run. Much will depend on how unemployment develops in the coming years. The amount of the contribution can also be set on the assumption that severe crises, such as the global financial crisis, are likely to occur in the future, and accordingly, the annual contributions should also be higher in preparation for this. If this were to lead to excessive accumulation in the UAF, a maximum accumulation could be set, after which payments into the UAF would temporarily be suspended. Considering the data we examined where unemployment benefit claims would be the highest for 5 consecutive years – i.e. the 5-year period of 2010–2014 –, a total of EUR 490 billion would have been paid out in unemployment benefits and accordingly, a ceiling of EUR 500 billion would be a reasonable threshold to replenish the unemployment fund. If we consider that such major crises will be very rare, then we could decide on making smaller payments, and if these did not cover the benefits in some years, then UAF could borrow money for those years, the repayment of which would be jointly guaranteed by the Member States, as in the case of the Recovery Fund (RRF). The aim is to create an automatic stabiliser based on unemployment that is self-sustaining in the long term.

The annual breakdown of the scheme would be as follows, with contributions of 0.33 per cent and 0.5 per cent of GDP:

**Figure 2**  
**Annual evolution of euro area excess unemployment benefits and contributions of 0.33 vs. 0.5 per cent of GDP**



For the three years illustrated above, the payments per country based on 0.33 and 0.5 per cent of GDP are shown in *Table 2*.

Member State	2004		2013		2022	
	Contribution at 0.33 per cent of GDP (EUR million)	Contribution at 0.5 per cent of GDP (EUR million)	Contribution at 0.33 per cent of GDP (EUR million)	Contribution at 0.5 per cent of GDP (EUR million)	Contribution at 0.33 per cent of GDP (EUR million)	Contribution at 0.5 per cent of GDP (EUR million)
Austria	744	1,127	968	1,466	1,317	1,995
Belgium	901	1,365	1,161	1,758	1,629	2,468
Cyprus	51	77	63	95	97	148
Estonia	53	81	86	131	135	204
Finland	440	666	537	814	704	1,067
France	4,913	7,443	6,212	9,412	8,081	12,244
Greece	752	1,139	679	1,028	835	1,266
Netherlands	1,572	2,382	1,971	2,986	2,644	4,006
Croatia	171	258	224	340	332	503
Ireland	425	644	527	798	1,386	2,100
Latvia	75	114	109	164	161	245
Lithuania	119	180	188	285	294	446
Luxembourg	80	121	131	198	199	301
Malta	23	35	33	50	63	96
Germany	6,971	10,561	8,641	13,092	11,406	17,281
Italy	4,596	6,964	5,209	7,892	6,553	9,928
Portugal	607	920	696	1,054	923	1,399
Spain	3,025	4,584	3,602	5,458	4,684	7,097
Slovakia	221	334	361	547	437	662
Slovenia	123	186	147	223	226	343
Total (EUR million)	25,860	39,182	31,542	47,792	42,106	63,797
Euro area GDP PPP %	0.33%	0.5%	0.33%	0.5%	0.33%	0.5%

*Source: Authors' calculations*

*The next question is how excess unemployment benefits would be financed and from what source.* Raising funds at the EU level does not seem realistic because it would mean earmarking funds for euro area members to pay into the unemployment fund. Member States would be free to decide how to raise the money: they could raise taxes, introduce new taxes or cut spending, but they would always have to respect the EU's fiscal rules under the Stability and Growth Pact.

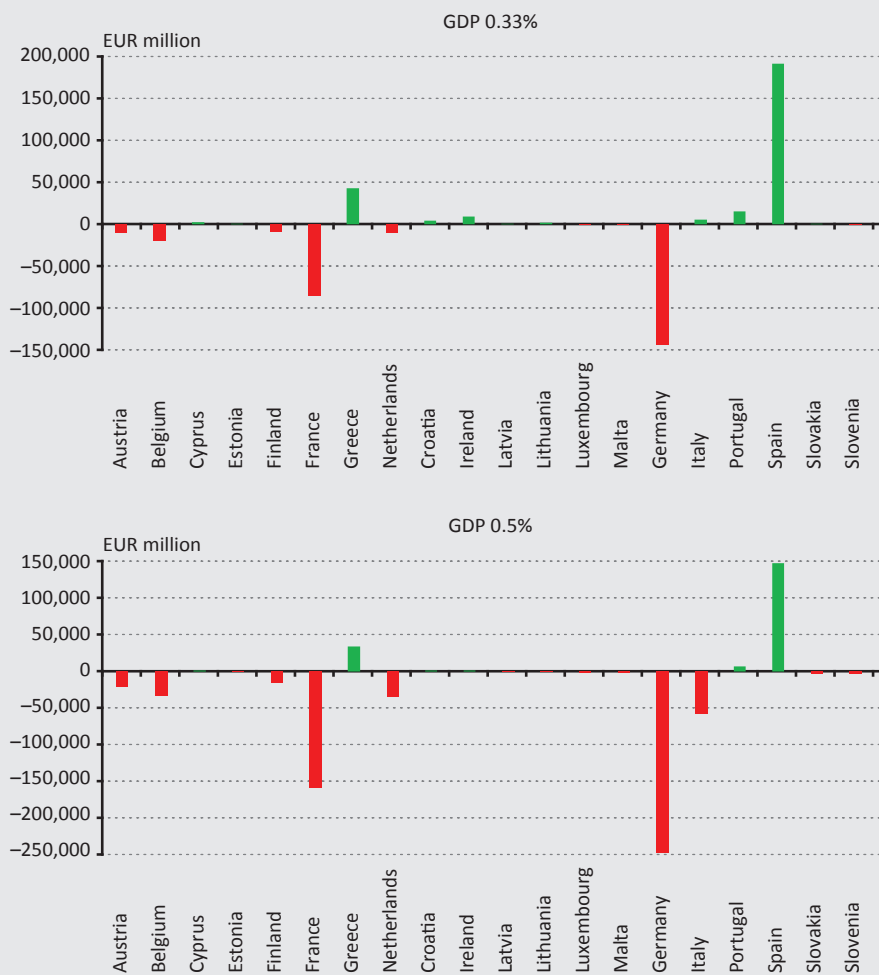
The best solution would be for the UAF to issue long-term bonds, similar to the Recovery Fund, with repayments guaranteed by Member States in proportion to their GDP. If 10-, 20- or 30-year bonds were issued, the interest burden on national budgets would be reduced and there would be several years available to gain experience on how the automatic stabiliser works.

The European Council and the European Parliament adopted the Stability and Growth Pact (SGP) reform in April 2024. The main objective of the reform is to ensure sound and sustainable general governments, while promoting sustainable and inclusive growth and job creation in all Member States through structural reforms and investments. The SGP's general objectives of reducing debt and deficit ratios in a gradual, realistic, sustainable and growth-friendly manner was agreed upon, while safeguarding reforms and investments in strategic areas and providing adequate room for counter-cyclical policies and addressing macroeconomic imbalances. The main novelty of the reform is that a differentiated approach is applied to each Member State to take into account the heterogeneity of fiscal positions, public debt and economic challenges across the EU. Thus, the new framework would allow for multi-annual, country-specific fiscal paths for each Member State, while ensuring effective multilateral surveillance and respecting the principle of equal treatment. A new feature would be that Member States could request an extension of the fiscal adjustment period by up to seven years. With these proposals, there would be more room for country-specific reforms. The reformed SGP is expected to stimulate reforms within the framework of the European Semester. The new SGP can provide a wider scope for the reforms that will be required to make the proposed unemployment assistance mechanism work in a sustainable manner.

There is no getting around the moral hazard issue stemming from the fact that the higher a country's GDP, the more it would pay in euros, but also the more assistance it would receive. Therefore, the *net position should be considered*. Figure 3 shows the cumulated net balance by each country for the period of 1999–2022. For most countries, the net position is around zero or shows a small positive or negative balance. However, two countries – Germany and France – would have been significant contributors because their excess unemployment rates were low throughout the period. Spain and Greece, however, would have been significant net beneficiaries due to their high excess unemployment rates. This aptly illustrates the problem of *moral hazard*: high performers pay more to the benefit of low performers. This is a serious obstacle to the adoption of an assistance system that is based on unemployment. This has been pointed out by most authors focusing on the EU-wide unemployment benefit system (e.g. *Arnold et al. 2018; Dolls et al. 2015; Darvas et al. 2014*). Nevertheless, an unemployment benefit scheme with an *automatic budgetary stabilisation* role would be particularly necessary

for the economic stabilisation of the euro area. Furthermore, it is not necessarily the case that it is always the same countries that will be net contributors and net beneficiaries, as this will depend on the number of excess unemployed. For example, in 2004 (see *Table 1*), Spain and Greece would not have received assistance, while Germany would have.

**Figure 3**  
Cumulative net balance by country based on contributions of 0.33 per cent and 0.5 per cent of GDP, 1999–2022



Source: Authors' calculations

In theory, the money from the UAF received by a country could be used for any purpose. This is why conditionality is essential: to develop a set of conditions that would reduce chronically high unemployment levels and curb the growth of unemployment in a crisis. It is important that the conditionality rules focus on a few narrowly defined reforms, which would be easy to monitor and would not undermine the automatic role of the system. The UAF should be managed by one of the institutions of the Union. The most obvious would be *the European Stability Mechanism*, because it already has the infrastructure to manage assets, borrow and enforce conditionality.

#### **4. Conclusion**

Our paper *presents a new approach focusing on excess unemployment*, which is intended to *complement national systems* without the need to change them. The proposal includes a supplementary Unemployment Assistance Fund (UAF), which would pay countries based on the excess unemployment calculated as a percentage-point deviation from the 7-year moving average. The system aims to smooth shocks, manage economic fluctuations and structural unemployment differences between Member States.

The study proposes annual contributions ranging between 0.33 and 0.5 per cent of euro area GDP to an unemployment benefit fund in order to cover excess unemployment benefits. Funding would be provided by Member State contributions or by issuing long-term bonds guaranteed jointly in proportion to GDP. We believe that the latter solution is probably the most realistic.

However, the proposal also faces the challenge of moral hazard, as consistently better performing countries pay in more, while countries with high excess unemployment levels benefit more, which in itself could undermine the incentive for reforms. To mitigate this, measures would also be needed to encourage specific, verifiable reforms to reduce chronically high excess unemployment without jeopardising the automatic stabilising role of the system. Long-term borrowing may give some extra time to implement these reforms.

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