

including the framework underpinning the EU's fiscal rules.²³ It includes the objective of debt sustainability which is at the core of the proposed EU fiscal surveillance framework (see [Box 3.1](#) on debt sustainability and its importance).

Box 3.1: Debt Sustainability

Public debt can have an important role in an economy. It can be a source of economic stimulus, a means to increase production and consumption, and ease the redistributive element in society. Capital investment financed through public debt can also be used to reform the economy to become 'greener' and stimulate digital transformation. Public debt can also finance countercyclical fiscal policy, stimulating the economy during times necessitating fiscal intervention. However, public debt cannot be increased without limit. Public debt needs to be repaid by future generations, and in the process, the economy needs to also sustain increased interest payments, i.e., the cost of borrowing.

In public finance, maintaining debt sustainability implies that the government would be able to meet not just the current obligations it has but also future payment obligations without being subject to abnormal monetary and financial assistance or, at the extreme, defaulting.

When public debt is unsustainable, or the country has very high risks of being in such a situation, market access might be hindered, whilst borrowing costs would rise, not only because of high accumulated debt but also because of the higher risk of default. In turn, economic sentiment might turn negative, leading to lower investment and economic contraction.

How much debt is sustainable, and in what ways can debt sustainability be measured is a topic of debate in economic literature. Debt sustainability levels depend on various factors and therefore differ by country. The proposed economic governance framework for the EU seeks to address issues related to the different debt positions in different countries. This is why the European Commission is proposing that each Member State has a different fiscal path toward sustainable debt levels.

²³ The official Communication by the Commission is available [here](#). The scope of the communication is broader than what is discussed in this Chapter and includes not only fiscal governance but also other aspects of macroeconomic stability.