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Austerity vs Stimulus: The MFF 2014-20's Role in Stimulating Economic Growth and Job Creation (ARI)

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Theme: XXXX The negotiation of the Multiannual Financial Framework (MFF) 2014-20 is a crucial feature on the EU agenda for the next few months.

Summary: The negotiation of the Multiannual Financial Framework (MFF) 2014-20 is a crucial feature on the EU agenda for the next few months. The outcome will not only determine the EU's future spending policies and the financing of its budget but also define the latter's potential role in responding to the economic crisis. In this respect, the next MFF will demonstrate the EU's responsiveness to new challenges and its capacity to contribute to solving problems. This paper analyses the key lines of the negotiation of the new MFF in the context of the debate on the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (EMU). Furthermore, it analyses the potential role of the MFF 2014-20 in stimulating economic growth and creating jobs. Finally, it presents some conclusions on the possible outcome of the negotiation and offers some recommendations on how to increase the impact of the EU budget in stimulating economic growth and job creation.

Analysis:

Introduction
After the signing of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG) and the adoption of the European agreement on the second rescue plan for Greece, the negotiation of the Multiannual Financial Framework (MFF) 2014-20 is the next crucial negotiation on the EU's agenda in 2012. The MFF will be debated during the April and June meetings of the General Affairs Council and be a central issue of the June European Council. Although a final deal on the MFF will not be reached until the end of the Cypriot Presidency during the next semester, the Danish Presidency is committed to moving the negotiations forward as much as possible.

The budgetary negotiation process started some years ago with a broad public debate on the EU budget. Several new ideas emerged, aimed at refocusing the EU's spending priorities and the financing of its budget. Some of these ideas were later incorporated by the European Parliament and, to a lesser extent by the European Commission, in their proposals for the MFF 2014-20. Furthermore, as the EU is facing a fundamental growth crisis, every available instrument should be used to stimulate growth. This would seem to lead to a change in the perception of the role the MFF 2014-2020 could play.

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In fact, after signing the new Treaty, the focus of debate is shifting towards the need to complement a balanced budget with stimulus to growth. Observers expect a more wide-ranging package of measures in order to respond to the financial and economic crisis. At the same time, countries with a strong economy would have to make greater financial transfers to countries hit by the crisis. This means that growth measures should accompany the austerity measures guaranteed by the Treaty.

The Declaration on growth and jobs approved at the informal European Council of 30 January failed to convince most observers and several reactions ahead of the 1 March European Council confirmed this impression. In a joint letter dated 20 February 2012 and addressed to the European Commission, 12 heads of government, including Spain's, urged that the EU's economic policies should focus more on growth.[1] They proposed promoting a better functioning of the single market in order to stimulate growth and the creation of jobs –in services, energy, the digital market...–, as well as promoting research and innovation, entrepreneurship and SMEs. Although the message was straightforward and was a critical assessment of the German/French concept of crisis management, there was no mention in it of the role of the EU budget in overcoming the crisis. The Danish Presidency issued a much clear message: '… we should work hard to redirect more funds from the future EU budget towards growth-enhancing areas where jobs will be created in the future... We must allow for common EU funds to be channelled directly to growth-enhancing areas in the member states'.[2] The Presidency found a common understanding on the issue at the General Affairs Council meeting of 27 January: 'The MFF can serve as an engine for growth. And that was the view expressed by quite a lot of member states'.[3]

Although the European Budget Commissioner, Janusz Lewandowski,[4] made it clear that the EU budget is not a magic wand to solve the crisis, the question remains open and crucial: how far can the MFF 2014-20 help to counteract the negative impact of the crisis and the social impact of the austerity measures implemented across Europe? Is the role of the MFF 2014-20 in the current economic crisis under debate?

While the political debate on measures to overcome the debt and growth crisis appears to be increasingly focusing on stimulus for growth, we argue that the specific characteristics of the EU budget and the negotiation process will not lead to a revolutionary new budget. Nevertheless, the MFF 2014-20 negotiation will reinforce the ongoing paradigm change in the budget's perception, from one aimed at compensating member states for their political commitments to one aimed at solving EU-wide problems, in which its means are considered investments rather than mere expenses.

The EU Budget's Role in Stimulating Economic Growth and Job Creation

The EU budget is at a special moment as regards the role it can play over the next few years in the European integration process. However it is not easy to define its scope. Despite its limitations, accounting for 1% of the EU's GNP, the EU budget finances the EU's policies and numerous activities in its member states. While small and insufficient to address the crisis in Europe, the EU budget is the member states' principal financial

[1] Of the UK, the Netherlands, Ireland, Italy, Estonia, Latvia, Finland, the Czech Republic, Slovakia, Spain, Sweden and Poland.
[2] Prime Minister Helle Thorning-Schmidt's speech at the Centre for European Policy Studies, 29/II/2012.
[3] 'Talks on long-term EU budget framework gain momentum', http://www.consilium.europa.eu/homepage/showfocus?lang=en&focusID=79656.
[4] This message was implicit in the Conference on the EU Multiannual Financial Framework and Own resources, Brussels, 22/III/2012.

instrument for joint action when facing challenges. In relation to national budgets, the EU budget's distinctive role is to finance investments where significant economies of scale can be achieved, steering national policies and also co-generating investments from the private and public sectors. In fact, the EU budget consists of up to 95% of policy-related investment expenditure and only 5% of administrative expenditure (Serrano & Kölling, 2011).

The EU budget has historically played an important role in the European integration process, making it acceptable to member states through specific financial compensations and by financing major instruments such as CAP and regional policy. These compensations were fixed in the EU budgetary resources structure, making it relatively inflexible and resistant to reform. Nevertheless the EU budget has also evolved, adapting its financing and spending structure to the EU's integration process. The first MFF was agreed for the period 1988-92 (Delors I) in order to provide the resources needed for the budgetary implementation of the Single European Act and the single market. The MFF 1993-99 (Delors II) contained a significant increase in structural and cohesion funds as a basis for preparing the member states for the single currency. The MFF for the period 2000-06 (Agenda 2000) secured the necessary resources to finance the enlargement process and the present MFF 2007-13 has followed the main objective of reducing the gap between new and old member states (Serrano, Kölling 2009). Important reforms have also been made, symbolising the EU budget's reaction to specific challenges and steadily consolidating it as a prime economic instrument.

The Commission recently underlined this dimension[5] and made clear references to the EU budget's role in crisis management, both in the current MFF 2007-13 (for instance, in the European Economic Recovery Programme, the adaption of the Structural Funds, the Globalisation Adjustment Fund and the role of the European Investment Bank) and in its proposals for the MFF 2014-20. Regarding the latter, the Commission proposes a number of measures which could be supported by the EU budget. First, it could contribute to the implementation of the single market. Innovative financial instruments could multiply its impact in strategic sectors where important economies of scale can be fostered. For example, Project Bonds are seen as a way of attracting private investment for key projects in the fields of energy, telecommunications and transport. Furthermore, as part of the next MFF, the Commission presented proposals to invest EU budget resources in projects such as the Connecting Europe Facility, which will help fill the missing links in Europe's infrastructure networks and generate benefits in the near future.

Secondly, the EU budget could also take up a more direct role in creating jobs, especially in mobilising and training young people in member states with high youth unemployment. This would not be a new task, but would highlight the instruments available. Since 1957 the European Social Fund (ESF) helps people to improve their skills and job prospects. During the MFF 2014-2020 all Cohesion Fund instruments, the European Social Fund (ESF) and the European Regional Development Fund (ERDF) will be especially directed at combating unemployment and fostering investments in growth, not only in the less developed regions but throughout Europe. Furthermore, investments in the CAP, especially rural development measures, will play an increasing role in fostering and maintaining growth and jobs in rural areas, according to the proposals presented by the European Council.

[5] In the answer to the above mentioned letter of the 12 heads of government.

Third, Small and Medium-sized Enterprises (SMEs) are an important contributor to growth and employment in the Union. The EU budget has traditionally supported SMEs and will also do so in the next MFF. During the current MFF 2007-13 the Competitiveness and Innovation Framework Programme (CIP) supports innovation activities and provides better access to finance for enterprises and SMEs. The new MFF 2014-20 also foresees a specific programme for SMEs: the 'Programme for the Competitiveness of Enterprises and SME' (COSME) to strengthen the competitiveness and sustainability of the Union's enterprises in areas such as international markets and tourism.

Finally, the EU budget has a special role in Research and Innovation. The European Research Area Framework is one of the commitments of the Innovation Union flagship initiative (Europe 2020). The financing of excellence research projects and infrastructures, in addition to the support for researcher career development, are already included in the Seventh R+D Framework Programme, but will continue under the new programme Horizon 2020 for the next period 2014-20. The proposed budget for Horizon 2020 has been raised to €80 billion, and the programme's scope is far greater than in the Seventh Framework Programme (€50 billion for 2007-13). The novelty in the approach of MFF 2014-20 is that the whole chain of innovation, from fundamental research to the market, will also be supported through spending on traditional headings, such as Cohesion policy and CAP, in order to improve Europe's future competitiveness.

The Negotiation of the New Multiannual Financial Framework

In contrast to earlier procedures, the negotiation of the MFF 2014-20 will take place in a context of economic crisis and of the first major crisis of the Euro and public debt markets. The negotiation is also complex for other reasons:

- It will be the first time that 27 member states will negotiate a MFF. The enlargements of 2004 and 2007 resulted in a significant shift in the balance of net contributors and net beneficiaries, especially in cohesion policy, where Poland has become the largest recipient. Croatia will join the EU on 1 July 2013 as the 28th member state.
- The MFF 2014-20 must fulfil the objectives of the EU 2020 Strategy.
- The Lisbon Treaty introduces new objectives for the EU which require financing, such as territorial cohesion, policies on migration and climate change, in addition to the creation of a European External Service.
- There will be a greater role for the European Parliament, which will have to adopt the Regulation before the Council makes its decision (co-decision procedure).
- There is no effective ongoing parallel negotiation on resources which would allow compensating member states for certain commitments.
- Negotiations are carried out in a political climate in the EU marked by increasing Euroscepticism, not only among citizens but also the political class.

In its first reflections of October 2010, the European Council proposed designing a future budget that would be closer to the goals of the EU 2020 Strategy and to convert it into a toolbox for good economic governance.[6] This approach was considered innovative because it did not envisage new budget instruments but mainly focused on improving the performance of the existing budget. Furthermore, traditional EU policies such as CAP and Cohesion should widen their scope to contribute to common EU priorities.

[6] COM(2010) 700 final.

Under this approach, the Commission presented its proposals, 'A Budget for Europe 2020',[7] in June 2011. The structure and duration proposed by the Commission are largely a continuation of the MFF 2007-13. The two most significant changes are that certain items have been placed outside the MFF (ITER and EDF) and that the Commission implemented the principles already outlined in the 2010 budget review.[8] The main lines of the proposal can be summarised as follows:

- EU spending should concentrate on a limited number of actions and contribute to key policy priorities, above all those of the Europe 2020 Strategy.
- EU spending should offer clear 'European added value' and should be conditional on the achievement of EU policy priorities, including the reduction of instruments and administrative burdens.
- Regarding the financing of the budget, a new own-resource system based on a Financial Transactions Tax has been proposed.
- Cooperation with the private sector on innovative financial instruments should be increased.

The proposals do not envisage a radical change in the structure of the EU budget, although the proposed system of own resources introduces innovative elements which were widely demanded during the public consultation process. In other areas the proposals try to accommodate the austerity demands of some member states, even if the margins beyond the MFF have been extended considerably. At the same time there are significant efforts to concentrate resources on the Europe 2020 objectives as well as a prime focus on European added value and the effectiveness of EU expenditure. In addition, the strong commitment to the objective of knowledge-based growth and investment in European public goods underlines the European Council's serious attempt to give the EU budget more capacity to face current and future challenges.

After the presentation of the main legislative proposals in October 2011, representatives of the EU governments have exchanged their views on future policies and have come closer on the less conflictive budget issues. Nevertheless, the crucial conflicts on the CAP and the cohesion policy, which together are responsible for approximately 74% of the MFF, as well as the differences regarding the new own-resources and the 'correction mechanisms'[9] are still to be resolved. Following the logic of former MFF negotiations based on net payment balances, several governments have already strongly expressed the areas on which they are unwilling to compromise.

Apart from the general strong defence of the status quo, two groups of opinions can be identified: member states that underline that the next MFF should reflect the fiscal consolidation efforts undertaken at the national level and those that stress the importance of adequately financing the EU's common policies in order to help overcome the crisis and address common challenges. The first group seems to have lost momentum over the past few months compared to September 2011, when eight member states –the main net contributors– demanded a reduction in the EU budget. In February 2012 only Germany, the UK, the Netherlands, Sweden and Austria reiterated this demand and insisted on a reduction of at least €100 billion in the Commission's proposal (mainly through cuts in the CAP and cohesion policy). Regarding the other group, most of the new member states

[7] COM(2011) 500 final.
[8] COM (2011) 510.
[9] Including the British rebate and the specific compensations for Denmark, Sweden, the Netherlands and Austria.

defend a powerful cohesion policy, while 18 member states consider the proposal of the European Council balanced, defend the overall size of the MFF 2014-20 as proposed and call for a stronger focus on jobs and growth, in particular by placing the Europe 2020 Strategy at the heart of the MFF.

During the Danish Presidency the working method of the negotiation has been changed from a bottom-up to a top-down approach. This means that the Presidency prefers to discuss first the overall amounts and only afterwards the specific policy priorities. This approach clearly favours the most reluctant member states and fosters the status quo instead of bringing forward a debate on the new role of the EU budget. Although it is expected that this will narrow the gap among member states' positions, the final decisions will be taken during the Cypriot Presidency, probably at the end of 2012. However, these will only be adopted after their approval by the European Parliament, which will probably support –or even increase– the figures proposed by the European Council and try to ensure that the latter does not water them down.

Conclusions: The 15-pages of conclusions of the European Council of 1-2 March 2012 mentions the word 'growth' 24 times, but the word 'crisis' only once, in relation with the problems of the Euro zone.[10] This clearly shows in which direction most European politicians would like to go. Nevertheless, the crucial role of the MFF 2014-20 and the EU budget in this process remains undefined.

The current negotiation procedure and the persistence of several member states' 'red lines' seem to lead to a MFF 2014-20 that again maintains the status quo of the European budget structure and allows little scope for manoeuvre over the coming months.

Nevertheless, already during the first meetings at the ministerial level it seems to be clear that a large number of member states are resisting further austerity demands and would prefer to focus the MFF 2014-20 on growth and job creation. Furthermore, the European Council's proposals for the MFF 2014-20, which are in part legitimised by the broad-ranging public debate, are a balance between, on the one hand, increasing the efficiency of EU expenditure and, on the other, enhancing measures. Although the proposals are very likely to be altered during the negotiations, they have been accepted by all member states as the basis for negotiation and, apart from the issue of new own resources, the final agreement might be close to them. Finally, the European Parliament will have a new and crucial role in the negotiations and will strongly defend an EU budget which actively supports growth and includes measures to fight unemployment.[11]

This analysis confirms our hypothesis that the MFF 2014-20 will not be revolutionary as regards new spending and financing instruments, but will nevertheless reinforce the ongoing paradigm change towards considering EU expenditure an active investment. The current negotiation shows that there will not be a substantial change in the structure of the EU budget, but a clear redefinition of specific spending headings regarding investments in growth and job creation.

[10] Conclusions of the European Council (1-2/III/2012).
[11] EP Resolution of 8/VI/2011; Lamassoure (2010), Financing Agenda 2020, EP Working Document, Budget Committee, 6/V/2010.

The following conclusions and recommendations can be made:

(1) Increasing the budget seems very unlikely, but new additional own resources could help boost it and gradually displace national contributions, reducing the burden on national treasuries.
(2) It is necessary to have a greater flexibility regarding EU funding that has not been fully used (eg, transfers between different headlines and use of unspent funds).
(3) A crisis-specific and post-crisis budget should be created. Payments in the first years of the MFF 2014-20 should be increased at times of crisis and, after a mid-term revision, adapted to what is hoped will be a better economic environment in subsequent years.
(4) Regarding spending, there should be general shift to assignations in relation to common challenges:
    - The impact of EU funds on 'crisis' countries should be increased –meaning that the most developed countries, facing fewer problems, should receive less, while countries undergoing an economic crisis should receive more resources–.
    - Funds should be concentrated on specific problems (eg, the old or the unemployed). Active use should be made of Cohesion funds in regions with high unemployment.
    - Cohesion Funds should be redefined to help member states with transitory budgetary problems linked to the economic crisis.
(5) Regarding spending, assignations should shift from a sector-specific to a problem-specific approach:
    - Sectoral spending, like CAP, should be connected to growth-related spending, which means farmers should receive funding from other non-CAP funds in order to improve productivity and to be competitive in new markets, taking into account the changing market for agriculture products.
(6) There should be a clear reduction in administrative costs. EU agencies should be reinforced by national civil servants, limiting the burden on the EU budget.

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