# Towards an EU Budget with an effective stabilisation function

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**Dr. David Rinaldi, Research Fellow, CEPS**

# In a Nutshell

- The crisis highlighted the need for countercyclical fiscal policies for EU economies, EMU in particular
- Strong case for a stabilisation function for the EMU, involving fiscal transfers
- At the EU level as system for fiscal transfers exist already: it's the EU Budget
- A stabilisation function exists already - at embryonal level!
  - Cohesion funds stabilise public investment levels
  - EU revenues are more responsive to income than expenditure
  - Some instruments include in their design a shock absorption function:
    - Youth Employment Initiative
    - European Globalisation Adjustment Fund
    - EU Solidarity Fund
- We recommend a more integrated approach and reforms to make those funds more automatic and ready to use

# Introductory Remarks

- What's the function of the EU Budget?

1) **provision of EU public goods**, such as research and infrastructure, defence and diplomacy;
2) **territorial cohesion**, by means of financial support to disadvantaged regions
3) **macroeconomic stabilisation**, to smooth business fluctuations.

The EU budget "*has so far been entirely devoted to the first two objectives*" (Bénassy-Quéré, Ragot, and Wolff, 2016)

- Is it clear from a policy perspective that stabilisation and stability are two different objectives?
- The case for automatic stabilisers is strong for the EMU, is it worth looking at the EU level?

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# Stability and Stabilisation

| OBJECTIVE | Macro-Financial Stability | Economic Stabilisation |
|---|---|---|
| RATIONALE | Ensuring a permanent financial backstop that prevents systemic risk and sovereign default | Support adjustment to symmetric and asymmetric shocks and stabilise the business cycle |
| POLICY TOOLS | A financial assistance facility such as the BoP Facility, EFSM, and ESM | European unemployment insurance, fiscal transfers |
| KEY FEATURES | Permanent mechanism attached to adjustment programmes and conditionality | Temporary transfers with automatic activation |

# EMU or EU?

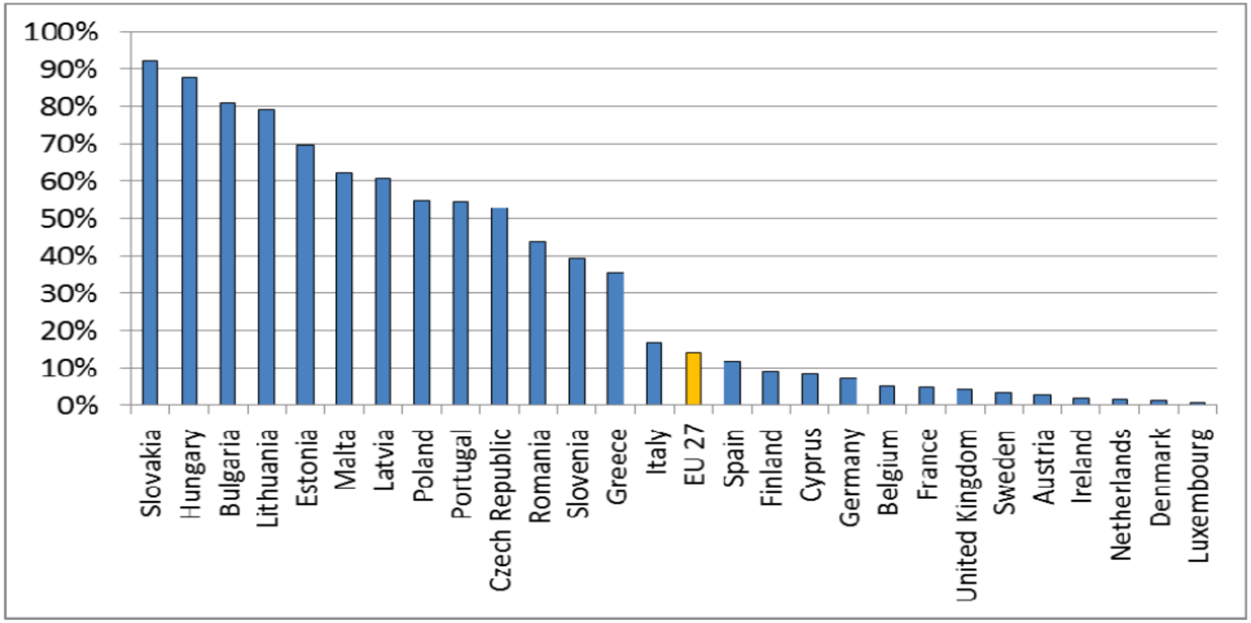
- The case for automatic stabilisers at EMU level is particularly strong:
  - No domestic monetary policy
  - No currency fluctuations
- But both EU and EMU economies:
  - High levels of interdependency
  - Subject to fiscal rules limiting room domestic fiscal policy
- Why no progress?
  - No concrete steps at the EMU levels, problems with political integration, sovereignty sharing & establishment of new transfers
  - The EU level may be a better setting as political integration and fiscal transfers are already in place

# EU Budget for Stabilisation

- General EU approach is on prevention rather than on ex-post mitigation: MIP, SSM
- ‘Macroeconomic stabilisation function’ of structural and cohesion fund, myth or reality?
- Pasimeni and Riso (2016) find that Own Resources stabilise the business cycle more than redistributive policies (GNA-based contributions)
  - €1 fall in p.c. GDP >> €0.008 reduction in p.c. contribution to the EU
  - Redaction in taxes to US budget is 30 times higher
  - If Brexit, stabilisation from Own Resources increases by 20%

# Does Cohesion Policy stabilize public investment?

*Share of Cohesion Policy-related financing as % of total public investment during the crisis (2010-2012)*




EU budget represent 2% of total public expenditure in EU (12.90 % for Bulgaria)

Higher shares for investment-related financing:
EU funds > 50% Hungary, Latvia, Lithuania

Positive role of pre-programming

# Between Rigidity and Flexibility

- The EU Budget is an '*Historical relic*' (Sapir Report, 2003)
  - 7 years planning with pre-allocated budgets
  - Net-balance approach
- New emerging priorities and needs
  - Economic crisis, migration, security
- The Commission is getting creative:
  1. On how to reuse and re-allocate funds which are not spent
  2. On how to shift allocations over the budgetary period
  3. On how to redirect MA appropriations towards new objectives
  4. On how to expand the ceiling of 1% of EU GDP
  5. Shifting from on MA to another (*impossible*)

# Youth Employment Initiative

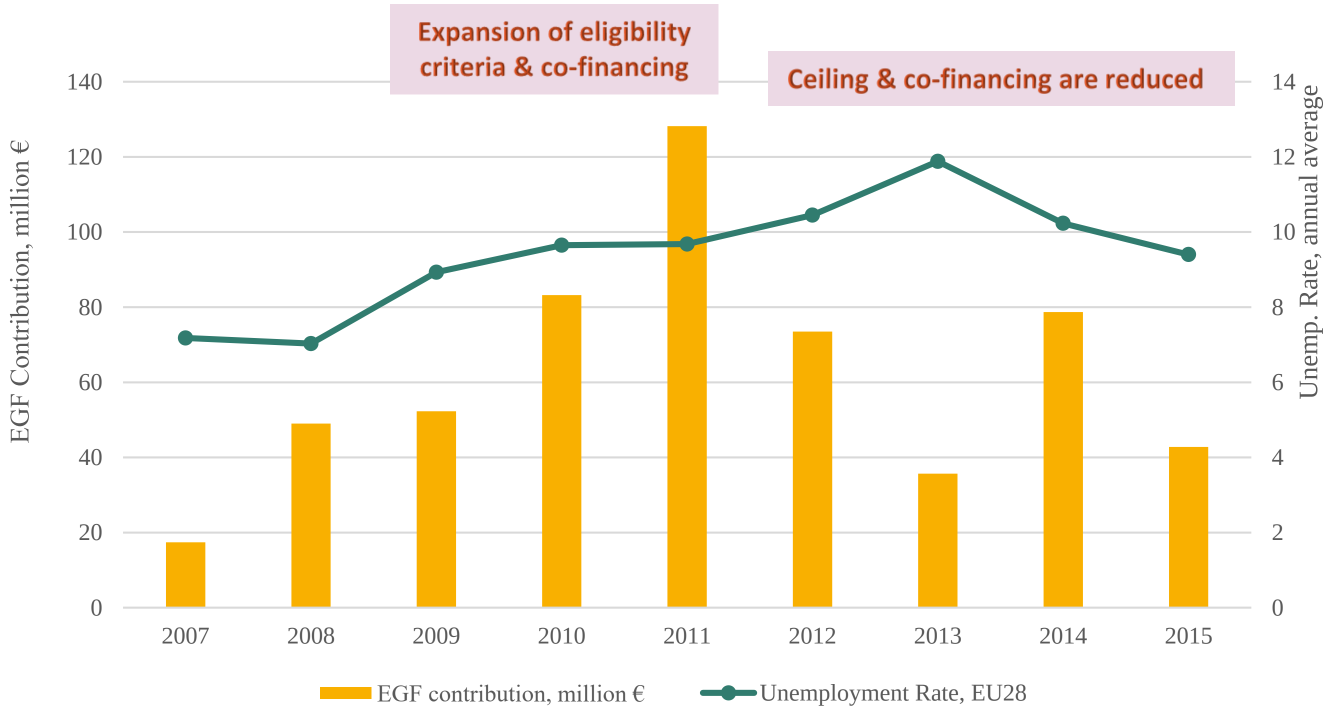
- Provide fiscal support to relaunch youth employment (Youth Guarantee)
- Open to regions with youth unemployment > 25% in 2012
- YEI (2014-2020 MFF) has €6.4 bn:
  - €3.2 bn via ESF respect common EU Budget provisions
  - €3.2 bn are through an ad-hoc YEI budgetary line for which it has been possible to introduce accelerated financing and special provisions
- ***Frontloading*** allows anticipating planned spending but did not bring results, i.e. slow implementation
- ***Prefinancing*** from 1% to 30%, i.e. €1 bn available immediately
- No national ***co-financing*** required

# European Globalisation Adjustment Fund (EGF)

- Introduced in 2006 to address trade shocks, reformed in 2009 to include shocks from economic crisis
- Activated at MS request if 500 people loose job + grey area
- Focus on ALMPs with reactivation rate ranging from 3% to 90%
- Ceiling reduced from €500 ml a year to €150 ml
- It remains out of the MFF budget!
- Implementation rate of only 55% meaning that significant shares of allocated budget went unused

# European Globalisation Adjustment Fund (EGF)

- Activated 167 times, total EU contribution of €588.4 mn, which tops up a total €422 mn of national co-financing.
- Over 141’800 beneficiaries receiving, on average, €4’180 each



# EU Solidarity Fund (EUSF)

- Introduced in 2002 in the aftermath of a massive flooding
- EU financing kicks in to provide assistance to MS in case of shocks due to major natural disasters
- ‘*major disasters*’: it must originate a direct damage of at least 0.6% GDP or €3 bn excess expenditure
- Ceiling of €500 ml/y but out of the MFF budget
- 70 disasters in 24 MS, €3.7 bn spent against the €7 bn available
- The operability of the fund is a crucial problem
  - Lenghty application procedure, grants paid after 12 months

# The EU budget has a stabilisation function

- The EU financial envelop dedicated to shock absorption and emergency measures amounts to €10.95 billion along the 2014-2020 period
  - EUSF assistance for natural disasters (€500 million a year)
  - YEI for labour market imbalances linked to youth unemployment (approximately €910 million a year)
  - EGF for trade-related economic crisis  shocks
- The fact however that a stabilisation function is present within the EU budget does not imply that it actually works or is sufficient to respond to the several shocks affecting the economy of European countries

# How to make the stabilisation function more effective?

- Stabilisation objectives and outcomes are present in the EU budgetary architecture but are definitely not integrated or structured in a way to perform shock absorption effectively
- Due to latter *incidental* creation linked to *cohesion* and *net balance* logics
- The are ways to enhance the stabilisation function of such funds by:
  - ✓Ensuring the possibility of a prompt disbursement
  - ✓Triggering is as automatic as possible
  - ✓Design a dynamic set of beneficiaries

# Ongoing Reform Process

- Mid-term MFF review (European Commission, 2016) proposes:
  - supplementing YEI with €2 bn (till 2020)
  - measures to '*to respond to unforeseen circumstances*'
    - a more efficient activation of the EGF and EUSF,
    - a new instrument to provide emergency assistance (migrants)
    - a European Union Crisis Reserve (humanitarian or security crisis
- White Paper (European Commission, 2017) most ambitious scenario: "*additional EU financial support is made available to boost economic development and respond to shocks at regional, sectoral and national level*"

# Recommendations

- Integrated vs Fragmented approach
  - Provides better visibility
  - Enhance stakeholders' capacity
  - Simplification and effectiveness
- EU Fund for Employment (€1.1 bn/y)
  - With two windows: for imbalances & shocks
  - Special fonttloading, pre-financing and co-financing
- Expansion of the EU Solidarity Fund
  - One window for natural disaster, one for other shocks

Thanks for your attention.

Contact:
david.rinaldi@ceps.eu

@CEPS_thinktank
@Rinaldi_David