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A short comment over an anti-Keynesian budget

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by *Paolo Pini* [1]

Abstract

In April this year the European Parliament in Strasbourg said "no" to the multi-annual budget which Governments of the European Union member Countries had agreed upon in February 2013. The changes may be minimal, but a strong message was sent to governments by the only institution in Europe elected by its citizens.

The budget proposal for 2014-2020 (the *Multi-annual Financial Framework . MFF*) was rejected due to both method and content. To method, because it is a deficit budget which leaves the European Commission with little margin of flexibility for anti-recession measures. To content, because it favours redistributive policies between European countries rather than policies encouraging growth and employment throughout the European Union. It is an austerity budget which is deeply anti-Keynesian in a period of serious economic crisis analogous to the great depression of the 1930s. A policy of growth at a European level is needed in order to cope with the economic depression, yet a policy of rigour and austerity was proposed. That is why it is good that it was rejected by the European Parliament.

Keywords: European budget, economic crisis, economic policy

JEL code: E6, O52, P16

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Introduction

In the European Council on 7th-8th February 2013, the Heads of State and Governments of the 27 member countries approved the Community budget for the seven-year period 2014-2020.

During the session held on 13th March 2013, the European Parliament rejected that agreement with a large majority. It held that, due to the present recession throughout European economies, the agreement was ill-suited both in substance and procedures, which will have to regulate its management on behalf of the Commission.

The agreement reached by the European Council had not escaped criticism from numerous commentators. The President of the Parliament himself, Martin Schulz, had immediately declared that he was not satisfied with what the 27 Countries had agreed.

Some believed that the European Council had achieved a realistic mediation, an honourable compromise with various *shades of grey* which saved Europe from a temporary budget. On the other hand, others believed that an agreement had been reached which "cheated" European citizens because it envisaged that *budget deficit* which, for various reasons, was blamed for the current ills afflicting so many European countries and for which cancellation had been requested. Out of these two extreme versions, the dominant theory was that it was a short-sighted accord, incapable of initiating new instruments and resources necessary to offset the crisis and foster growth and employment.

So rejection by the European Parliament was one of the possible, or rather probable, and even preferable, results. Which is what happened.

The process is obviously not complete; the Parliament's rejection initiated a difficult and probably drawn-out period of institutional confrontation and negotiation.

Three Community structures contribute to the definition of the seven-year budget, which involves a complex procedure: the European Commission, the European Council and the European Parliament.

1. **The 2014-2020 European budget: contrasting proposals on total values**

In order to understand why the Parliament rejected the inter-State agreement, we will go through the steps which led to the Council's agreement, on the basis of the initial Commission proposal. We will do so by paying attention to the figures which define the budget, rather than the procedures. For details refer to Tables 1a and 1b.

After consultation with the European Parliament which began in 2011, the European Commission under Barroso as President had proposed a seven-year budget, based on 2011 costs of 1,033.2 billion euros of expenditure commitment, and 987.6 euros of effective cover (with a deficit of 45.6 billion, equal to 4.41%). Compared to the previous budget for the period 2007-2013, this constituted a 4% increase in commitment and 4.7% increase in allocation, maintaining the share of GDP in the Member Countries just above 1%.

However, the northern countries, including the United Kingdom, Sweden, Holland, Denmark and Finland, immediately stated that that figure could not be the basis for a valid start to the debate, and immediately demanded a cut of 200 billion euros.

The European Council chaired by Van Rompuy had proposed setting up the debate in November 2012, starting with a budget of 972 billion for planned expenditure of which only 940 was actually covered, thus leaving a deficit of 32 billion euros, equal to 3.29% of commitment. This made a significant cut to the budget proposed by the Commission (-61.2 billion in planned expenditure and -47.6 billion cover) so that it was brought below 1% of Member Countries' GDP.

But the euro-sceptics did not consider this to be enough, as they wanted greater cuts and were not willing to finance their share of the Community budget. That is why the talks collapsed and the decision was referred to the European Council in February 2013.

The agreement then reached by the European Council on 7th-8th February 2013 envisaged a budget of 960 billion planned expenditure and 908.4 billion cover, thus a deficit of 51.6 billion, equal to 5.37%. Compared to the Commission's proposal, this was 73.4 billion less for planned expenditure (-7.1%) and 79.2 less cover (-8.1%), leading to the above-mentioned deficit, and higher than the forecast made by the Commission itself.

This deficit was to be added to the approximate 15 billion deficit quoted in December 2012 which anyway, according to February 2013 estimates, was due to rise to 20 billion at the end of 2013, compared to the previous seven-year budget for the period 2007-2013.

Thus the new seven-year period was to begin with a forecast deficit of 71.6 billion, equal to roughly 7.4% of planned expenditure. This percentage constitutes the expenditure share that the Commission, although committed to financing Community projects, cannot honour as the specific financial cover is lacking. Net of left-over deficit, cover for new initiatives is thus forecast at 884.4 billion. Compared to the Commission's forecast, a cut of 99.2 billion euros.

Tab.1a – European budget 2007-2013 and budget hypothesis for 2014-2020, absolute values (source: European Commission and European Council together with our calculations)

Absolute values	Budget 2007-2013	Budget 2014-2020 Commission Proposal 6/2011	Budget 2014-2020 Commission Proposal 7/2012	Budget 2014-2020 Council Agreement 2/2013
1.Smart and Inclusive Growth	446,31	490,91	494,76	450,76
1a. Competitiveness for growth and jobs	*91,5*	*154,91*	*155,52*	*125,61*
1b. Economic, social and territorial cohesion	*354,82*	*336*	*339,24*	*325,15*
2.Sustainable Growth: Natural Resources	420,68	382,93	386,47	373,18
2a. Rural development and environment	*83,99*	*101,1*	*103,42*	*95,33*
2b. Market related expenditure and direct payments	*336,69*	*281,83*	*283,05*	*277,85*
3.Security and citizenship	12,37	18,54	18,81	15,69
4.Global Europe	56,82	70	70	58,7
5.Administration	57,08	62,63	63,17	61,63
Total commitments	993,26	1025	1033,21	959,96
% GDP	1,12	1,05	1,08	1
Total payments	942,78	972,1	987,6	908,4
% GDP	1,06	1	1,03	0,95
Deficit	-50,48	-52,9	-45,61	-51,56
% Deficit	-5,08	-5,16	-4,41	-5,37

Tab.1b – European budget 2007-2013 and budget hypothesis for 2014-2020, percentage distribution (source: European Commission, European Council and our calculations)

Percentage distribution	Budget 2007-2013	Budget 2014-2020 Commission proposal 6/2011	Budget 2014-2020 Commission proposal 7/2012	Budget 2014-2020 Council agreement 2/2013
1.Smart and Inclusive Growth	44,93	47,89	47,89	46,96
1a. Competitiveness for growth and jobs	*9,21*	*15,11*	*15,05*	*13,08*
1b. Economic, social and territorial cohesion	*35,72*	*32,78*	*32,83*	*33,87*
2.Sustainable Growth: Natural Resources	42,35	37,36	37,40	38,87
2a. Rural development and environment	*8,46*	*9,86*	*10,01*	*9,93*
2b. Market related expenditure and direct payments	*33,90*	*27,50*	*27,40*	*28,94*
3.Security and citizenship	1,25	1,81	1,82	1,63
4.Global Europe	5,72	6,83	6,78	6,11
5.Administration	5,75	6,11	6,11	6,42
Total commitments	100,00	100,00	100,00	100,00

We should note that according to some experts a surplus of commitments compared with cover may be interpreted as a positive result in a situation of economic limitations to the *budget*. There is normally a lag of at least some years between the commitment to undertake an initiative and the payment for its realisation, and the growth in commitments lays down an obligation to honour commitments in future years. Moreover, this practice was adopted by the European Commission in order to influence successive budgets. However, this policy is not usually appreciated by the European Parliament, because if the *gap* between commitments and payments becomes *structural*, each government of the Member Countries, and therefore the European Council, has an extra reason to limit its *ex-ante* commitments, reducing them in order not to be dragged along by the *ex-post* behaviour of the European Commission which draws up the *budget* proposal. And this happens above all when there is strong pressure from some Member countries to reduce their finance commitments towards the European budget. This is in fact what happened with the debate on the 2014-2020 budget.

What is more, as has been observed by many, this is the first Community budget which has foreseen a reduction compared to the previous one. And this has taken place in the worst financial and economic crisis since the setting up of the European Union, and in a context in which the inter-governative policy of austerity imposes a reduction of the debt and levelling of the budget for Member countries. With this European budget, the quota of resources effectively available for the Commission is reduced from 1.06% to 0.95% of the total gross product realised in the Union Countries (in the hypothesis formulated by the Commission there was going to be 1.08% calculated for commitments and 1.03% for expenditure allocation). Compared with the budget for the period 2007-2013 (994.2 billion euros for commitments and 974.2 for cover) the reduction is 3.44% in commitments and 5.77% in cover, counting in the deficit foreseen at 20 billion at the end of 2013.

2. The structure of the 2014-2020 budget: some comparisons with the previous budget and between proposals of the Commission and the Council

The criticisms of the seven-year budget made by the European Commission cannot however be limited to the total figures, but are also addressed to the very structure of the budget.

We now come to the structure of the budget for the next seven years and examine the weight of each main expenditure item. We again refer to Table 1a and 1b as well as Table 2.

With respect to the 2006-2013 period, the budget available for "agricultural policies, rural development and environmental sustainability" has been reduced from 420.7 to 373.2 billion euros (-11.3%), that for "economic, social and territorial cohesion" (including *structural funds*) from 354.8 to 325.1 (-8.4%) That for "competitiveness for growth and employment" has instead been increased from 91.5 to 125.6 (+37.4%) for "administration (that is, *European burocracy*) from 57 to 61.6 (+7.9%), for "Global Europe" from 56.8 to 58.7 (+3.3%), for "security" (including European defence) from 12.4 to 15.7 (+26.85%). The new fund for "youth unemployment" has a budget of 6

billion euros, in Countries where the youth (under 25 years) unemployment rate is above 25%.

It appears that the reduction for "cohesion" is more than compensated for by the increase for "competitiveness", even though Agriculture and Cohesion still remain as extremely important items: they alone cover 72.7% (compared with 78.1% in the preceding budget) even though they lose more than 5 percentage points.

On the whole, it would thus seem that the inter-State agreement has produced results which are not negative for the structure of the budget, with more growth and less redistribution compared with the previous long-term budget.

However, it certainly does not constitute a positive result, if we bear in mind what the Commission had originally proposed.

An examination of the items and respective figures in fact reveals many negative signs, if we take into account the hypotheses put forward by the European Commission which, compared with previous budgets, lead us to speak of a *budget* of "austerity" rather than growth.

The resources for transport networks, energy networks and digital networks, part of the "*Connecting Europe*" programme, have been decreased from 50 billion in the budget proposed by the Commission to 29.3 billion euros. Only 1 billion is devoted to digital networks. The resources committed for competitiveness, including resources for growth and employment by means of innovation, investment, infrastructures and network connection etc, amount to 125.7 billion euros against the 155.5 proposed by the Commission, representing a drastic cut compared to the initial political intentions.

The policies for rural development and the environment, although their budget has been increased, have a marginal role compared to redistributive agricultural policies in the strict sense (contributions to producers and market support), which account for 74.4% of this total item. On the other hand, the expenditure for the burocratic structure of the Commission has been increased, despite the fact that cuts had been foreseen. In addition, of the 6 billion devoted to coping with youth unemployment, 3 come from the European Social Fund, which is part of the policies for social cohesion.

Tab.2 –European budget 2007-2013 and hypothesis for the 2014-2020 budget, absolute increases/decreases and in percentage terms (source: European Commission, European Council and our calculations)

Differences between Commission and Council budget proposals for 2014-2020 and 2007-2013 budget.	Absolute values Commission 6/11 v. 2007-2013	Absolute values Commission 7/12 v. 2007-2013	Absolute values Council 2/13 v. 2007-2013	% Commission 6/11 v. 2007-2013	% Commission 7/12 v. 2007-2013	% Council 2/13 v. 2007-2013	Absolute values Council 2/13 v. Commission 7/12	% Council2/13 v. Commission 7/12
1.Smart and Inclusive Growth	44,60	48,45	4,45	9,99	10,86	1,00	-44,00	-8,89
1a. Competitiveness for growth and jobs	63,41	64,03	34,12	69,31	69,98	37,29	-29,91	-19,23
1b. Economic, social and territorial cohesion	-18,82	-15,57	-29,67	-5,30	-4,39	-8,36	-14,09	-4,15
2.Sustainable Growth: Natural Resources	-37,76	-34,21	-47,50	-8,97	-8,13	-11,29	-13,29	-3,44
2a. Rural development and environment	17,11	19,43	11,34	20,37	23,13	13,50	-8,09	-7,82
2b. Market related expenditure and direct payments	-54,86	-53,63	-58,83	-16,29	-15,93	-17,47	-5,20	-1,84
3.Security and citizenship	6,17	6,44	3,32	49,89	52,10	26,85	-3,12	-16,60
4.Global Europe	13,19	13,19	1,89	23,21	23,21	3,32	-11,30	-16,14
5.Administration	5,55	6,08	4,55	9,72	10,66	7,97	-1,54	-2,43
Total commitments	31,74	39,95	-33,29	3,20	4,02	-3,35	-73,25	-7,09
% GDP	-0,07	-0,04	-0,12				-0,08	
Total payments	29,32	44,821	-34,378	3,11	4,75	-3,65	-79,20	-8,02
% GDP	-0,06	-0,03	-0,11				-0,08	
Deficit	-2,42	4,87	-1,08	4,80	-9,64	2,15	-5,95	13,05
% Deficit	-0,08	0,67	-0,29	1,55	-13,14	5,69	-0,96	21,67

3. The position of Italy

If viewed from a strict accounting logic, Italy benefits from the budget, as its net contribution to costs has decreased. The average negative balance which was equal to 4.5 billion in the previous budget, or 0.28% of GDP, has been reduced to 3.8 billion, equal to 0.23%. Italy will benefit from funds for youth employment, as its unemployment rate for under 25 year olds exceeds 25% (400 billion foreseen); also from the item “cohesion” (an increase of 200 million for structural funds compared to the previous budget) which envisages 29.6 billion for Italy of which 20.5 billion are to go to the South: and this is perhaps the result of the efforts made by the Italian Ministry for territorial cohesion in accelerating the utilisation of structural funds foreseen in the previous budget and the reduction of national co-financing. Moreover, further benefits will derive from resources for rural development, but we may observe that these are more than compensated for by the reduction of agricultural aid to companies and market support.

On the whole, Italy has obtained a “privileged” position in the definition of the “austerity” budget; in other words, in an agreement which has cut the Community budget, in advantage over countries which were more in favour of cuts (the UK) and not favouring countries which opposed cuts (FR) it has reduced its negative balance as net contributor, acquiring resources in areas where it was seriously behind in utilisation and for actions to cope with social problems. A sort of “damage repair” policy. On one hand

our Government has reduced damage deriving from the reduction in the European budget and changes in its structure, on the other it does not seem to have been particularly incisive in opposing the euro-sceptics' desire for an even lighter budget, when in fact it should have been. In other words, it has been at the "redistribution" table rather than the "growth" one.

4. An overall evaluation: more redistribution and less growth

If considered in the context of an economic crisis lasting since 2008, with 26 million now unemployed in Europe, or 12% of the working population, then the agreement on the European budget marks something far worse than "damage relief". We must compare what the European Commission forecast in July 2012 with what the European Council decided in February 2013 (a comparison indicated in the last two columns of Table 2).

The item indicating the greatest cut is most important one for growth measures: *Competitiveness for growth and jobs* -19%. This section includes resources for both tangible and intangible infrastructures, innovation, research and training. On the other hand, there has been a very slight reduction in contributions to farmers and in support of agricultural markets, while the greater cuts appear for environmental issues and rural development. This confirms that in an attitude towards austerity, the supporters of an archaic vision of the *budget* have retained their position, bringing about change in a downward direction

The European Council has thus reduced the budget as a whole with respect to what was proposed by the European Commission, which had formulated a more expansionist hypothesis. Moreover, the cuts have not been distributed proportionately among the various items of the budget. In fact, they have been limited to the "redistributive" items in the budget, which are most at risk of veto by single Member countries in the Union, that is, in direct aid to agricultural production and cohesion policies between European countries. Instead the axe has been aimed at the "growth" items which support both a direct public demand from the European Commission as the quality of growth and development centred on knowledge, research and innovation, that is, on those items which directly support aggregate demand and factors of common and collective competitiveness. The exact opposite of what was in the intentions of the Commission which, with a view to a growth budget, wanted to encourage "growth" for all and penalise "redistribution" for the few. Unfortunately, this result is nothing new in the confrontation between the European Commission and the European Council; also in the past the Council, whose role as governor of the Member Countries is much greater than the Commission, has downsized and re-balanced the budget towards redistribution more than growth. What is new is that the European Council has intervened, due to pressure from "euro-sceptical" governments and with the abetting of those "pro-austerity", reducing the absolute value of the seven-year budget not only compared with the Commission's proposal but also compared with the previous 2006-2013 period.

5. The European Parliament rejects the agreement

Thus the budget approved by the European Council was passed in this form to the European Parliament table. The latter was merely able to approve or reject the budget but not make any amendments.

Many people asked: what will the Parliament decide? Will it be happy enough with the two clauses that the President Schulz requested from the Council? A) the review clause and b) the flexibility clause, as they have been formulated by the Council? What is the meaning of the "bland" possibility of annually reviewing the budget, shifting resources from one year to the next, and the even "blander" possibility of shifting resources from one expenditure section to another according to Europe's economic and social conditions? Do they envisage realising this with a qualified majority and no longer with a unanimous vote? Or will the Parliament reject the budget and initiate negotiations between the three European institutions: the Council, the Commission and Parliament?

Yet the possibility of reviewing the budget also leads to risks, under the present conditions of equilibrium between the governments of the various Countries, that is, there is the possibility of a review which worsens the situation rather than improves it. The risk is high and the Parliament does not like a budget with a deficit which risks becoming permanent. Will it therefore decide to reject the budget? It would certainly be a not just rare but unique decision, and also a strong message to the European governments which had signed the agreement, judged by most as pejorative, short-sighted and even fraudulent.

However, it is not the first time that the Parliament has sent strict messages to Member Countries and to the European Council in particular. It expressed a negative opinion in January 2006 when debating the 2007-2013 budget. Parliament has also a procedural tool: one fifth of Parliament members could request a secret ballot and this would open up a favourable scenario for rejecting the budget. The seven-year plan must be approved by an absolute majority in Parliament, made up of 378 members, and both absence in the chamber and abstention count as a vote against the motion. Parliamentary members representing the parties in government in each country, governments in the European Council which may threaten to veto the motion fostering "redistributive" interests rather than growth, may, in a secret ballot, feel less bound to restrictions of their governing mandate which weigh less in Parliament, or governative parliamentarians who believe that their Country has obtained few redistribution advantages from the budget equilibrium achieved in the European Council could reject such a hypothetical agreement. At the same time, the parliamentarians representing parties which are not in single Countries' governments may confirm their preferences for a more expansionist budget and often, in the present scenario of each European Country's government, adopt a progressive attitude rather than a moderate or conservative one. Moreover, the growing opposition towards austerity measures in the south of Europe, but also social problems in some countries in north Europe, may make further pressure on parliamentarians for a "no" to the seven-year austerity budget. However, it might have been just a hope, that the facts would then unfortunately be able to deny.

But things did not go that way. On 13th March 2013 an outstanding majority in the European Parliament voted against the proposal for the seven-year plan, with 506 votes against, 161 in favour and 23 abstentions. In the Parliament's opinion, the proposal cannot be approved because it is too restrictive for the management of policies in the next seven years.

Parliament laid down five conditions for the future approval of the budget, thus passing it back to debate by the European Council. The conditions are: 1) flexibility in the management of the budget from one year to the next and between one budget to the next; 2) possibility of review during the financial period; 3) a qualified majority in the European Council and not unanimity during the review phase; 4) greater resources for the management of the budget to be added to those available to member States; 5) review of the deficit between commitments and payments.

The first condition would allow the European Commission greater flexibility in the management of the budget in order to adapt commitments and payments according to the European economic situation and the political priorities believed to be important for "economic growth" rather that "redistribution among countries". In other words, the Commission would have the power to intervene again in the structure of the budget.

The second condition would ensure a review of the seven-year budget at the half-way stage in order to adapt it to the mid-term evolution of the European economy.

This condition is closely linked to the third condition, which envisages suppression of the veto by some Countries, introducing the review procedure by the Countries' qualified majority, thus reducing the power of "euro sceptical" Countries which have strived to weaken the propositive role of the European Commission in definition of the budget.

The fourth condition aims at increasing the European Commission's available resources, envisaging that greater resources may arrive directly by means of taxation, for example, on financial transactions or on polluting emissions which are responsible for the greenhouse effect.

Finally, the fifth condition, a further critical aspect where Parliament has intervened, is that of the *gap* between commitments and payments, as it is noted how this practice of *programmed deficit* risks questioning the sustainability of expenditure programmes which have not total cover, and which at the same time make it unacceptable to shift the payment of the debt to future financial periods. Therefore this means rejecting the structural deficit which would risk leading to a downward shift of future commitments.

6. A temporary conclusion

The rejection by the European Parliament therefore concerns not just content but also method. Not only does it request more flexible procedures which can be utilised by the Commission in the multi-year budget management, but there also lies an intention to grant the Commission with the power of intervention in the structure of the budget, thus restoring the Commission's political will to create *more growth* and less *redistribution*.

Now negotiations are open between the European Council, consisting of member Countries' Presidents and Heads of Government on one hand, and the European Parliament and European Commission on the other. We cannot expect that the Council

will make a major review of the long-term plan, at least in its absolute values, but it is certain that the European Parliament, the only European institution directly elected by the citizens, has sent a strong message to the Governments of Europe.

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