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Short analysis of the Communication of the Commission "A European Economic Recovery Plan"

nce) - Économie - La politique macroéconomique et sociale de l'Europe -

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Preliminary remarks :

1. Tools at the disposal of the EU as regards economics :

The Commission stresses on the need for Europe to use all the tools at its disposal. But the European Economic Recovery Plan comes down basically to coordinate "national action plan" for the following reasons :

1) Lack of tools :

By immediately recalling that most of the economic policy levers, and in particular those which can stimulate consumer demand in the short term, are in the hands of the Member States, the Commission acknowledges its lack of leverage power to launch an ambitious Economic Recovery Plan.

Therefore, the spreading of the financial crisis into the real economy is the occasion to question EU competences in the field of economics, in view of its inability to offer a European solution to the problem.

2) Existing tools :

Till now, one of the major critics to have on the macro-economic framework of the EU is that there was a far too-limited use of the economic tools at their disposal. It is especially the case of "coordination of economic policies", which is far from being satisfactory. In this respect, the Greens have by and large recalled the need to coordinate economic policies more closely, especially within the Eurogroup.

At present, the fact that Member States have very different starting points in terms of fiscal room for manoeuvre, makes it indeed all the more necessary to coordinate at the European level !

2. Supporting the real economy

General remark : The Communication of the Commission stresses the role to be played by counter-cyclical macro-economic policies to relaunch the economy, through public authorities' intervention.

Considering the faith of the Commission in the virtues of the market, and its negative bias towards the role of the State in the economy, this change of tune is rather positive. Indeed, it is in contrast with the usual approach of the Commission according to which :
Competitiveness automatically translates itself into growth, and therefore prosperity and wellbeing for all.
The faith in the markets leads the European Commission to develop more and more an approach of "better regulation" being identified as "deregulation" or "self-regulation" of the markets.

In its "Proposal of Economic Recovery Plan", the change of tune takes the following forms :

2.a Monetary policy as a tool to boost economy.

The Commission welcomes the fact that ECB has cut its interest rates (while it usually sticks to the principle of ECB independence, and encourages it to combat inflation, in complement to the pursuance of structural reforms).

The Greens agree this new stance, since they always defended the idea that ECB, whose primary goal is to maintain price stability, should pay equal attention to the fulfilment of the objectives of the Lisbon-Göteborg Strategy.

The role of banks

According to the Commission : "Member States should use the major financial support provided to the banking sector to encourage a return to normal lending activities and to ensure that central interest rates are passed on to borrowers".

Considering that Mc Creevy is a strong advocator of self-regulation and "better regulation" has been associated during whole his mandate to "less regulation", this statement is of course a step in the right direction.

This is in line with the position of the Greens : the bailing out of banks by the State to avoid the crackdown of the financial system could be support, provided the respect of strict conditions in respect with governance, compensation scheme, investment strategies, realistic accounting norms, adequate change of business models and a strong accountability to public authorities.

However, the "European Economic Recovery Plan" must not consist of an alibi to carry on "business as usual" in the ambit of finance !!! The Commission needs to take into account the origin of the crisis, i.e. excess of deregulation in the financial market. In order words, although being positive, the proposal of the Commission to conduct a counter-cyclical macro-economic policies through monetary and fiscal stimulus are not enough, if the status quo is globally maintained in the financial sector, especially as regards European supervision.

As a matter of fact, a "Green New Deal" does not only upgrade the role of public authorities as an investor, but also as a regulator (see proposals expressed in the first report of the Green New Deal Group, discussed at the Conference of financial crisis the 13th of November 08).

2. b. Budgetary policy :

Commission position : Budgetary policy should boost demand by making use of the flexibility offered by the revised Stability and Growth Pact.

This budgetary stimulus should be timely, temporary, targeted and coordinated.

On this line, the Commission agrees that it may lead some Member States to breach the 3% GDP deficit reference value.

Comments :

This statement is in contrast with the usual tone of the Commission, whose stance was basically to insist on fiscal discipline as if it turned into a goal in itself, while minimizing the fact that the need to contain public debts may also clash with the achievement of Lisbon objectives that call for an intelligent private and public investment policy to address major society concerns, such as climate change.

REMIND : The Greens were always strong advocators of the reform of the Stability and Growth Pact as initially conceived (it forced upon national governments to follow the simple rule of a balanced budget or a slight surplus, without taking into account the complexity of economic and monetary policies).

In so doing, the SGP forced EMU countries to conduct procyclical policies in period of economic recession (the strict interpretation of the Pact could imply the cutting down of crucial expenditures like education, basic research and investment in times of economic downturns).

by imposing to ALL countries the observance of the 3% limit, it led to a "one-size-fits-all approach", since the SGP made no differences between "mature" and "catching-up" countries, was regardless of the rate and variability of growth, of investment needs (such as the need for infrastructures or the population age structure, which greatly vary across countries), etc.

Last but not least, the SGP overlooked important parameters in assessing the "soundness of the budgetary position" such as investment expenditures (e.g. education) whose return is spread over long periods.

The reform of the Stability and Growth Pact implemented in 2005 aimed to tackle these main shortcomings and introduced flexibility so as to take into account the quality of public finance (and not just merely quantitative targets) and cyclical conditions (to afford more flexibility in bad times, and demand more fiscal discipline in good times).

The position defended by the Commission as regards the flexibility offered by Stability and Growth Pact implements in practise the spirit of its reform in 2005. This change must be welcomed, since it makes it easier to finance high - quality public investments, such as the ones aiming at the de-coupling of growth from energy consumption, transport and resource use, as well as investments needed to meet the Kyoto targets.

2. c. A public investment policy geared towards the four priorities set in the Lisbon agenda (people, business, infrastructure and energy, research and innovation)

Statement of the Commission : although defending the idea of a mix of public spending and tax reduction, the Commission makes it plain that public spending has a stronger positive impact on demand in the short run compared with tax cuts.

The Commission deems that a coordinated investment policy should aim at creating a "low carbon economy". Infrastructure and energy package are considered to be one of the four priority areas.

The Greens have a predilection for a strong public investment policy which could benefit SMEs and could support long-term public policy goals such as the energy-climate package. Any tax reduction must be targeted, and the overall objective is to ensure a shift of taxation from labour to environmental degradation.

Considering that Barroso Barroso' initiative in 2005 was to abandon the original spirit of the Göteborg Strategy (which aimed to put on a equal base economic, social and environmental concerns) to refocus on growth and employment, the fact that he advocates a strong investment policy in economic sectors related to the fight against climate change is a step forward in the "recovery" of the initial "spirit Göteborg Strategy", provided that it is not used to promote nuclear energy.

Indeed, for the Greens, abandoning the green strategies at a time of economic austerity would be disastrous, all the more that a vast programme to fight climate change is part of the solution to counter an economic recession.

2.d. Structural policies + working towards global solutions.

"Structural reforms" to be implemented :

No change to signalise in the proposal of the Commission : they are still geared towards the objective of increasing labour market flexibility.

The same goes true for the usual request of the Commission to open up even more the market around the globe, and to create a network of deep and comprehensive free trade agreements.

Comments :

The whole European construction since its inception is based on the belief that the removal of barriers to free trade and the implementation of the internal market will boost growth and therefore human wellbeing. The fact that the same old recipes are given as regards "structural reforms" and trade gives a hard evidence that the economic model remains the same...

Beside, implementing reforms in the context of intensifying competition from emerging countries with low production costs, such as China and India, will put even more the so-called European Social Model under pressure, and will consist of other pressing reason to implement further structural reforms in the EU, with a clear focus to develop the "flexibility" aspect of the so-called "flexicurity" model.

2. e. Taxation policy

The Recovery Plan includes a number of measures that fall within the taxation area. Some of these measures have already been proposed by the Commission, whereas other measures are still to come.

General taxation measures

a) Lower taxes and social contributions :

The idea is twofold : 1) to promote job creation by lowing social contributions paid by employers ; 2) to lower taxation of labour income so as to support purchasing power in particular for low wage earners.

b) Temporary reductions in the level of the standard rate of VAT (in so far as they remain above the Community minimum level (15%).

Comments :

a) As for the first proposals, these measures fall outside the competence of the EU and it is for Member States to decide whether they introduce them or not.

b) As for the second proposal, UK has already announced a general reduction of the VAT, while France and Germany oppose such moves. In so far as the reduction covers all goods and services and remains above the Community minimum level (15%), there is no need for a Council's decision. Two main kind of problems arise from such proposals :

This VAT cut aims at providing a fiscal impulse to support consumption (not to change its pattern). However, it remains to be seen if such move will lead to more consumption, or if consumers may prefer to save rather than spent.
Indirect tax, such as VAT, is regressive tax. However, it remains to be seen how low income can be targeted better. Other political actions to lighten the burden on the most vulnerable sections of the population might be more appropriate than undifferentiated VAT cuts, that will put further constraint to the budget.

Targeted reduced VAT rates

The Commission has already proposed a Directive to make permanent reduced VAT rates for labour intensive services and locally supply services. The Recovery Plan calls on the Council to adopt this proposal as soon as possible (before the 2009 Spring European Council).

Comments : The Greens have always defended this idea of reduced VAT on labour intensive services. This directive gives Member States the possibility of applying reduced VAT rates to renovation and repair works, with a view tot increased energy-saving and efficiency. However, the current proposal does not include provisions on the use of VAT reduced rates for environmental purposes (Energy-efficiency-related taxation measures).

Remind :

The European Council in March 2008 to examine areas where economic instruments, including VAT rates, can have a role to play to increase the use of energy-efficient goods and energy-saving materials. The proposal of the Commission was scheduled to be adopted in November 2008. However, the services of the European Commission informed the ECON Secretariat earlier in November that the Energy Taxation Package will not be adopted in November 2008, as scheduled. This delay needs to be criticized !
Car-related taxation measures

The Commission proposes to accompany the Recovery Plan with demand-side measures such as a reduction by Member States of their registration and circulation taxes for lower emission cars.

Conclusions :

Considering that the rationale of EU's approach on economics is on the same line as the "Washington consensus", according to which the development of countries supposes : further trade liberalisation ; privatisation and deregulation, the "Economic Recovery Plan" proposed by the Commission is a step in the good direction.

But the fact that it still contains "old traditional recipes" gives hard evidence that we are still far from a situation where the Commission would turn its back on his rooted belief that growth, measured by GDP, and delivered through competitiveness, will automatically ensure prosperity, social cohesion and sustainable development.

However, the fact that it develops now a more "Keynesian" approach to the economy is worth mentioning... But it still needs to be consistent with the overriding objective to tackle the triple crisis "financial crunch, climate crunch, and coming global energy crunch" as proposed by the "Green New Deal".

