Economic and Budgetary Outlook for the European Union 2019

STUDY

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Economic and Budgetary Outlook for the European Union 2019

This study, the third in an annual series, provides an overview of the economic and budgetary situation in the EU and beyond. It summarises the main economic indicators in the EU and euro area and their two-year trends. It explains the annual EU budget, provides an overview of its headings for 2019, and sets out the wider budgetary framework – the multiannual financial framework (MFF) – and its possible evolution after 2020. A special 'economic focus' offers a bird’s eye view of SMEs and SME policy in Europe, and of various recent EU-level initiatives in this field.
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Executive summary

In 2018, the EU and euro-area economies continued their moderate growth (2.1 %). This growth was based on domestic private and public consumption and on strong investment – itself stemming from low interest rates and high business confidence, which is, however, likely to deteriorate slightly going forward. It was also underpinned by the creation of jobs: unemployment is currently at a post-crisis low and labour market conditions are expected to continue improving over the next two years, albeit more moderately than previously.

The global outlook in which this growth is taking place, however, is less promising than it was a year ago. Indeed, for the first time in almost 30 years, the expansion of trade liberalisation came to a halt in 2018. World merchandise trade volumes grew less in 2018 than in the previous year, and are expected to decrease further in the near future, especially in the event of an escalation in current trade tensions. Partly as a result of the above, EU exports were subdued and are projected to remain so in the near future. In addition to the above, specific risks revolving around private and public finances, financial markets, monetary policies and trade, as well as the gloomier forecast for key emerging economies, such as Argentina, Brazil, Iran, Turkey, Venezuela or South Africa are signs that global expansion has peaked (3.7 %) in 2018, and should begin to decelerate in 2019 and 2020 (3.5 %). In this context, the EU and euro area is expected to continue growing, but at an even lower pace over the next two years (between 1.8 % and 1.9 %).

In this context, while the European Central Bank reduced its purchases under the purchase programmes significantly in 2018, and decided to end them by December, it decided to continue reinvesting the principal payments from maturing securities purchased under those programmes and to keep using its forward guidance. The aforementioned trends, the different pace of monetary policy normalisation in the United States and the United Kingdom on one hand and in the euro area on the other, trade tensions in world markets, but also specific fiscal issues relating to particular Member States, resulted in a mixed picture compared with last year, with the euro appreciating slightly versus emerging market currencies, while at the same time weakening versus the dollar, the yen and the pound sterling.

Following the now established pattern, the study delves into two of the tools and initiatives that European institutions use to contribute to the European response to the aforementioned developments: the European Union budget and the way it is designed to tackle challenges, and EU initiatives aimed at supporting small and medium-sized enterprises (SMEs).

The 2019 EU budget amounts to €165.8 billion, representing only 2 % of total public spending in the European Union – approximately 1 % of gross national income (GNI). Despite its volume, the overall impact of the EU budget is amplified by a number of features, including: a higher share of resources devoted to investment than in national budgets; the capacity to leverage additional funding from other sources; and attention to policy areas where the pooling of resources can provide the EU as a whole with added value (e.g. research, innovation and development cooperation).

Agreed by the European Parliament and the Council of the European Union, the 2019 budget focuses on priorities such as stimulating investment, growth and research, creating new jobs, especially for young people, as well as addressing migration and security challenges. In 2019, for the fifth year in a row, the budgetary authority had to have recourse to the flexibility provisions available under the EU’s 2014-2020 multiannual financial framework (MFF) in order to finance these persistent policy challenges.

In 2019, the shaping of the next MFF, which should cover the 2021 to 2027 period, is expected to gain momentum. EU institutions and Member States are working on the proposals put forward by the Commission in 2018, which include a number of modifications to the way the EU budget is currently financed and spent. Taking into account the expected withdrawal of the UK from the EU,
the proposed allocations for 27 Member States are organised around a new structure reinforcing priorities that emerged during the current MFF, such as research, innovation, digital transformation, climate action, borders, migration, security and defence. The objective is to reach an agreement in autumn 2019, but the start of a new political cycle for several key EU institutions might pose a challenge for this.

The EU budget devotes particular attention to SMEs, supporting them across a wide range of programmes and instruments. SMEs are crucial to European economy since they constitute 99.8% of all non-financial enterprises in Europe. In 2017, these firms employed close to 95 million people which means that two out of three workers in the EU had a job in this sector. Furthermore, European SMEs generated around €4.16 trillion, amounting to 57% of total added value. European SMEs were badly affected by the economic and financial crisis starting in 2008 and only since 2014 have employment and value added been increasing. The recovery is also manifested in the fact that between 2008 and 2017, gross value added generated by SMEs increased cumulatively by 14.3% and employment in these companies increased by 2.5%. Value added and employment are also expected to grow in 2019.

Sustaining the continued growth of European SMEs relies, not least, on ensuring sufficient access to external finance – an area where they are typically considered to be at a disadvantage relative to larger firms. However, recent evidence indicates that the environment for their access to financing is gradually improving across the EU. In 2018, only 7% of SMEs reported ‘access to finance’, as their most serious concern. This is a notable improvement when compared with the 17% reported in 2009. Notwithstanding this positive development, traditional debt finance – whether in the form of credit lines, overdrafts, trade credit or standard bank loans – continues to be the primary source of external funding for the majority of SMEs, with alternative financing instruments remaining among the least preferred options. The heavy reliance on debt finance that has traditionally characterised European SMEs contributed heavily to their increased vulnerability during the recent economic downturn. In view of the persistent challenges, public attention is increasingly drawn to the potential of capital markets to offer alternative sources of financing for SMEs. As such, diversification of sources of funding through the development of deeper and more integrated capital markets is gaining increasing traction. Providing companies, especially smaller ones, with a broader choice of market-based funding at a lower cost, can help stimulate investment, thereby promoting sustainable economic growth and job creation.
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1. Introduction

Tentative results for 2018 indicate that the EU economy is continuing to grow, albeit at a less dynamic pace, with gross domestic product (GDP) growing by 2.1% in both the euro area and the EU-28. The European Commission expects euro-area and EU-28 GDP growth to continue in 2019 at 1.9%, while the euro area is expected to lag slightly behind the EU-28 in 2020 (1.7% vs 1.8%).

Following the now established pattern, the study delves into two of the tools and initiatives that European institutions use to contribute to the European response to existing and emerging challenges: the European Union budget and the way it is designed, and EU initiatives aimed at helping the financing of European SMEs, including efforts by the European Investment Bank Group.

The economic situation in the EU and the euro area, as well as two-year projections for the main economic indicators are presented first (Section 2). In 2018 the EU economy continued to grow in terms of GDP and employment, albeit at less dynamic pace. Inflation picked up and monetary accommodation continued, though slowly tapering. Significant fragility and risks remain, however, stemming both from the international environment and from inside the EU and euro area (some being specific to certain countries, others being more general). Whether potential uncertainties materialise and the extent to which those risks are addressed ahead of any future crisis will have a significant impact on the way the EU weathers that crisis.

As in the previous edition, the study goes on to present the EU budget, its nature and its role (Section 3), before providing an overview of this year’s budget (Section 4) and the preparations that are shaping the future of EU finances after 2020 (Section 5). It is a limited budget – the €148.2 billion of total payments agreed is less than the public expenditure of a country like Austria. The commitments adopted for 2019 amount to €165.8 billion, which represents only 1.01% of EU gross national income (GNI). However, contrary to many national budgets, a significant share of the available resources is allocated to investment rather than to consumption and transfers. The EU budget focuses on promoting sustainable growth, creating jobs – especially for young people – and tackling migration and security challenges. It also seeks to trigger additional funding from other public and/or private sources to reach its goals.

Finally, the study provides an in-depth discussion of developments and challenges regarding SMEs and their financing conditions. Over the past year, the recovery of EU SMEs has continued. Their contribution to growth in value added and in employment appears to have exceeded expectations, particularly given their relative importance in the economy. This recovery has been accommodated by improvements in financing, with recent surveys confirming that fewer and fewer SMEs considered access to finance to be a major problem relative to other business concerns in 2018. Notwithstanding these improvements, SMEs remain heavily dependent on bank lending, and public discussion over the diversification of the sources of funding through the development deeper and more integrated capital markets is increasingly gaining traction.
2. The EU economy in 2019

2.1. Overview

The EU and euro-area economies are continuing their trend of moderate growth, with the euro area and the EU-28 projected to grow by 2.1% in 2018. Prospects are less bright for the coming years however (1.9% for both in 2019 and 1.7% in 2020 for the euro area (1.8% for the EU-28)).\(^1\) This growth is set against a less promising\(^2\) and potentially more turbulent context than last year, with a subdued outlook for investment,\(^3\) and trade growth projected to remain moderate at global level (from 4.1% growth in world merchandise trade volumes in 2018 to 3.5% in 2019 and 2020) but slowing down in China and other Asian economies.\(^4\)

Also, the positive trend observed last year regarding employment is continuing: the European Commission estimates that unemployment for the euro area in 2018 will hover around 8.4%, while the rate for the EU-28 is even more promising (6.9%). In the next two years, unemployment rates are expected to drop further, to 7.9% and 7.5% for the euro area and to 6.6% and 6.3% for the EU.

In 2018, both the general government deficit and the general government debt ratios are projected to continue their steady decline: from 1.6% in 2016 and 1% for 2017, the deficit stood at 0.6% for the euro area and continuing to decrease from 1.7% in 2016 and 1% in 2017, it reached 0.7% for the EU-28. While it is forecast to increase slightly in 2019, to 0.8% of GDP, both for the EU and the euro area, it should decrease further to 0.7% of GDP in 2020. As for the debt-to-GDP ratio, it decreased from 88.9% in 2016 to 86.9% for the euro area and from 83.2% to 81.4% for the EU-28. It is expected to maintain its downward trend in 2019 (84.9% and 79.5% respectively) and 2020 (82.8% and 77.6% respectively).

Inflation for the euro area is projected to reach 1.8% for 2018 and 2019, before falling slightly to 1.6% in 2020. Similarly for the EU, inflation is projected to reach 2% for 2018 and 2019, before dropping to 1.8%. Lastly, the European Central Bank maintained its asset purchase programmes in 2018, albeit at a reduced pace. While the Governing Council of the ECB declared in September 2018 that it would stop making net purchases in 2019 and onward, it also announced that it intends to reinvest the principal payments from maturing securities purchased under the programme, continue using forward guidance and continue its targeted longer-term refinancing operations (TLTRO).

Higher oil prices, reduced global trade volume growth, high geopolitical tensions;\(^5\) less accommodative macroeconomic policies in the euro area and internationally, the potential realisation of looming trade conflicts, rising long-term interest rates globally, as well as the fallout from the departure of the United Kingdom from the EU are among the many challenges the EU will be facing in the years ahead.

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\(^1\) European Commission, Autumn European Economic Forecast, November 2018, p. 184.
\(^2\) According to the Organisation for Economic Co-operation and Development (OECD) Economic Outlook of November 2018, there are signs that the global expansion has peaked: among other things, investment and trade growth are smaller than expected, incoming new order–especially in manufacturing– have weakened.
\(^3\) This is in large part due to a decline in business dynamism in several countries that was already noticed last year and to the fact that many countries hesitate to adopt regulations to increase product market competition.
\(^4\) OECD Economic Outlook, November 2018, p. 18.
\(^5\) For instance, in the Ukraine.
2.2. Main indicators

2.2.1. Gross domestic product

Tentative results for 2018 indicate that the EU economy is continuing to grow, albeit at a less dynamic pace, with gross domestic product (GDP) growing by 2.1% in both the euro area and the EU-28. The European Commission projects euro-area and EU-28 GDP growth to continue in 2019 at 1.9%, while the euro area is projected to lag slightly behind the EU-28 in 2020 (1.7% versus 1.8%). While this expansion is heartening, it has not been shared equally among Member States and, as the Commission notes, its overall effect was rather limited. Furthermore, factors such as the decrease in the price of oil, the depreciation of the euro and strong economic growth at global level (a trend since 2016), are expected to abate. At the same time, the continuation of accommodative monetary policy, low financing costs for both companies and governments owing to low interest rates, and improving corporate balance sheets, can support further growth.

This year’s modest increase is still underpinned by domestic private and public consumption, as well as employment growth (see below), while exports were subdued and are projected to remain so, on account of the weakening of foreign demand and other uncertainties pertaining international trade. Like last year, it must be noted that private consumption – the main driver of the current economic expansion – is expected to stay at around the same levels over the next two years (1.6% for the euro area and 1.7% for the EU-28 in 2020), owing, not least, to consumer confidence declining and, to a limited extent, inflation picking up and reducing households’ purchasing power.

Public consumption has contributed to economic growth too and is expected to continue doing so for the next two years (it is projected to increase to 1.6% in 2019, before returning to 1.3% in 2020 for the euro area, and to 1.5% in 2019, before dropping to 1.3% in 2020 for the EU-28). As it has already been noted in previous outlooks, these projections mask divergences between Member States, with differing consolidation needs and economic situations.

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6 ‘Between the first quarter of 2008 and mid-2018, real per capita GDP in the euro area has only increased by 4.0%’. European Commission, European Economic Forecast, op. cit, p. 26.

7 As the Commission noted in its 2017 forecast, ‘The recovery since the second quarter of 2013 has been subdued and weaker than other recoveries …, including the recovery that immediately followed the economic and financial crisis in 2009’. op. cit. p.38.

8 Private consumption is the value of goods and services (such as health and education) consumed by individuals and households that are acquired through the private sector. Public consumption, in contrast, is the value of goods and services individuals receive through the public sector.
Investment has been growing (by 3.3% in 2018 for the euro area and 3.2% for the EU-28) and is expected to remain reasonably strong. The Commission notes that while the growth in investment exceeds the growth in GDP, it remains moderate for a cyclical component during an upswing. It must also be noted that this growth matches the period before the crisis, in part as a result of low interest rates, high business confidence, and the Investment Plan for Europe, but that the trend is projected to decelerate (to 3% for the euro area in 2019 and 2020 and, similarly, to 2.9% and 2.8% for the EU-28).

### 2.2.2. Labour market

In 2018, employment in the EU (in terms of the number of people employed) continued the positive trend started in 2013 as a result of ongoing economic expansion and moderate wage growth. More specifically, employment during the 2013 to 2018 period rose by 14 million in the EU and almost 9 million in the euro area. During the same period, wage growth remained subdued – until the end of 2016, when it rose steadily, but still remained below its pre-crisis levels. Probable causes for this moderate growth are low inflation, low trend productivity growth, and high unemployment. With regard to this last element, both unemployment and underemployment continued to decline, to their lowest levels since before the crisis, a decrease stronger than expected, given the pace of economic growth. As of October 2018, it was set at 8.4% for the euro area and 6.9% for the EU as a whole. It is expected to decrease further over the next two years (to 7.9% in 2019 and 7.5% in 2020 for the euro area and to 6.6% in 2019 and 6.3% in 2020 for the EU as a whole). A further positive note is that long-term and very long-term unemployment also decreased.

However, as the European Commission points out again this year, significant differences remain between Member States for a range of different employment indicators – including the gap

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9 Numbers for November 2018 show that the main pillar of the plan – the European Fund for Strategic Investments – reached €68.8 billion, projected to trigger €359.9 billion of total investment, which will support mainly the SME, research, development and innovation, and energy sectors. For a detailed breakdown of results by country and sector see Investment Plan results, European Commission.

10 In years with comparable levels of unemployment.

11 See the 2018 Commission annual review ‘Labour Market and Wage Developments in Europe’.

12 Long-term unemployment refers to those unemployed for a year or more; very long-term unemployment refers to those who remain unemployed for at least two years.
between the highest and lowest unemployment rates (at 2.4 % for the Czech Republic versus 19.6 % for Greece in 2018), employment rates and activity rates.13

Also, while the Commission projects that labour market conditions will improve over the next two years (albeit more moderately than previously), it also notes that room for further employment growth in 2019 and 2020 becomes more limited, despite the net immigration of workers in regions with strong job opportunities and the expected integration of refugees.

2.2.3. Public finances

In 2018, the general government deficit is projected to continue its decline to 0.6 % for the euro area and 0.7 % for the EU-28 (from 1.0 % respectively in 2017). For 2019 the projected general government deficit-to-GDP ratio is projected to increase slightly to 0.8% of GDP, both for the EU and the euro area, before decreasing again to 0.7% of GDP for both in 2020, provided there is no policy change. The European Commission expects this reduction to be driven mainly by the budgetary impact of economic growth surpassing potential growth (the cyclical component14 of the budget), but also by a falling expenditure-to-GDP ratio, which is larger than the drop in the revenue-to-GDP ratio.15 As for the small uptick in 2019, it is expected to be driven by slightly looser discretionary fiscal policies and one-off measures.16

In 2018, the general government debt-to-GDP ratio of the euro area continued to decrease (86.9 % for the euro area and 81.4 % for the EU-28) since its 2014 peak (94.2 % and 88.1 % respectively) and is projected to maintain this trend in 2019 (84.9 % and 79.5 % respectively) and 2020 (82.8 % and 77.6 % respectively) for almost all Member States,17 supported by primary surpluses and a debt-decreasing snowball effect.18 Despite this encouraging trend, the ratio will remain above 60 % in 10 Member States in 2020,19 while in seven of them (Belgium, Cyprus, France, Greece, Italy, Spain and Portugal) it will be higher than 90 %.

2.2.4. Trade and developments at global level

For the first time since the 1990s, with the new wave of globalisation culminating in the creation of the WTO and more recently China’s access to the organisation, the expansion of trade liberalisation came to a halt in 2018. Indeed, following the global financial crisis and the unsuccessful Doha

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13 The unemployment rate is the number of people unemployed as a percentage of the labour force. An unemployed person is defined by Eurostat as someone aged 15 to 74 (in Italy, Spain, the United Kingdom, Iceland and Norway: 16 to 74 years); without work during the reference week; available to start work within the next two weeks (or having already found a job due to start within the next three months); and actively having sought employment at some time during the previous four weeks. The employment rate is the percentage of employed people in relation to the comparable total population. The activity rate is the percentage of active people in relation to the comparable total population. For more information on employment statistics (2016 data), see Eurostat’s dedicated page.

14 The part of the budget that tends to rise and fall in line with fluctuations in economic activity.

15 In turn owing to lower interest expenditure, but also to lower unemployment benefits, as labour markets keep improving.

16 The Commission provides the examples of revenues from sales of non-financial assets or expenditures related to short-term emergency costs or to the financial crisis.

17 Except Romania.

18 The snowball effect is the impact on the debt to GDP ratio of the difference between (nominal) growth and (implicit) interest rates paid on debt. According to the Commission, nominal GDP growth is projected to outpace the average interest rate paid on debt. As a result, the snowball effect is expected to help reduce the debt ratio in the euro area aggregate.

19 In descending order, Greece (167.4 %), Italy (131.1 %), Portugal (116.8 %), Belgium (98.7 %) France (97.2 %), Spain (95.4 %), Cyprus (91 %), the United Kingdom (82.6 %), Hungary (68.6 %), Croatia (68.2 %), Austria (67.8 %) and Slovenia (62.6 %).
Development Round, non-tariff measures started increasing and trade policy initially shifted from a global approach to regional and bilateral deals, followed by a shift towards more trade-restricting measures and discriminatory state interventions, after the recent elections in the US.

Nevertheless, world trade continued the growth trend set in previous years (albeit more moderately, at 4.1 % in world merchandise trade volumes versus 5.2 % in 2017) – in both advanced economies and emerging markets owing to an increase in global demand and manufacturing production and investment at the start of the year. The projections, however, are less optimistic and trade is set to further decrease in the next two years, as a possible escalation in current trade tensions could impact growth and trade flows.

With regard to global growth, the Commission expects it to remain at 3.7 % in 2018, but decelerate to 3.5 % in 2019 and 2020. This is in great part explained by the risks identified for the future (see point 2.4 below) and by the gloomier forecast for key emerging economies. Indeed, while economic activity in advanced economies stands to benefit from the strong growth momentum in the US, growth in emerging markets is set to diverge, as prospects for countries such as Argentina, Turkey, Iran, Venezuela, Brazil or South Africa, have weakened compared with last year’s forecast.

In China, GDP growth held out well in 2018 at 6.6%, despite the escalation of trade tensions with the US. Indeed, the frontloading of exports (i.e. the acceleration of production and shipment before the tariffs kick in) and the depreciation of the currency have mitigated the impact of tariff hikes so far. Domestic demand has remained strong and will continue to contribute to growth, as disposable incomes continue to rise. The restrictions imposed on shadow banking, have reduced credit growth and increased financial stability, but also slowed investments – especially in infrastructure and may challenge access to finance for smaller firms. In turn, slower investment and the tariffs imposed by the US, may eventually impact exports and disproportionately affect smaller firms and geographical regions relying on exports for their growth. Therefore, the projections for GDP growth are a bit more pessimistic at 6.2 % for 2019 and 5.9 % for 2020.

Investment in India is growing steadily and, along with private consumption, fuels GDP growth, which was projected to reach 7.4 % in 2018 and should remain at 7.5 % in 2019 and 2020. Despite the pressures created by rising oil prices, business investment and exports (supported by a weaker national currency) are projected to remain strong. At the same time, ratios for inflation, public deficit and debt to GDP, all remain high. In addition, the current international economic environment, with adverse terms of trade and lower growth in partner countries, could constitute a challenge to India’s further growth. Despite these headwinds, the OECD estimates that improvements in the administration of the goods and services tax and the depreciation of the rupee should provide an impetus to exports.

In Japan, economic growth was projected to reach 1.1% in 2018, supported by private consumption (increase in summer bonuses and tax incentives), business investment (due to high corporate profits

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European Commission, European Economic Forecast, op. cit, p. 12.


European Economic Forecast, op. cit, p. 16.

OECD, Economic Outlook, op. cit. p. 89.

In China, shadow banking is a major source of infrastructure financing.

OECD, Economic Outlook, op. cit. p. 90.

OECD, Economic Outlook, op. cit. p. 28.

OECD, Economic Outlook, op. cit. pp. 128-130.
and labour shortages) and exports. Government debt continues to constitute an important risk, hovering at 226 % of GDP (the highest ever recorded in the OECD area). For the time being, its impact has been mitigated by large-scale government bond purchases by the Bank of Japan, which now owns 45 % of the outstanding stock of government bonds.²⁹ Japanese GDP growth should drop slightly to 1.0 % in 2019, before decreasing further to 0.5 % in 2020.³⁰

Russia’s economic recovery continued in 2018 (1.7 %) and is projected to continue, albeit moderately (currently projected at 1.6 % in 2019 and 1.8 % in 2020),³¹ supported by the stabilisation of its macroeconomic environment and rising oil prices.³² The country’s fiscal balance is in surplus for the first time in a decade, and the pension reform it implemented is further strengthening the sustainability of its public finances. Unemployment remains low at less than 5 %, but the OECD has projected its increase, as employment demand will only partly match higher labour supply following the rise in the retirement age.³³ At the same time, projections are prudent, due to the rapidly aging population, the shrinking labour force, major geographical and social inequalities that reduce the size of the domestic market, and the uncertainty surrounding potential future sanctions and the price of oil.³⁴

Lastly, in the United States of America, the economy is strengthening owing to the substantial fiscal stimulus agreed in 2018 (2.9 % in 2018 vs 2.2 % in 2017).³⁵ However, it is projected to slow in the coming years (2.6 % in 2019 and 1.9 % in 2020), as macroeconomic policy support slowly fades.³⁶ Employment growth remains strong and, along with high consumer confidence, it is sustaining consumption and income growth. Measures of consumer and business confidence remain high.³⁷ The recent US-Mexico-Canada Agreement reduces uncertainty for North American supply chains.³⁸ Trade growth has recovered from the past appreciation of the US dollar, but the possibility exists of further trade measures being introduced.³⁹ At the same time the trade deficit is widening, as import demand remains strong (investment growth) while exports growth remains muted (reduced external demand, owing in part to tariffs).⁴⁰ The main risks identified are procyclical fiscal loosening, which may overheat the economy.⁴¹ If financial conditions tighten more quickly or harshly than expected, the risk is negative repercussions on the world economy.⁴² Rising leverage in the (non-financial) corporate sector, may result in increased vulnerability with an increase in interest rates.⁴³ Lastly reform efforts to reduce regulatory burdens in the financial sector could exacerbate vulnerabilities, particularly at the largest systemically important financial firms.⁴⁴

²⁹ OECD, Economic Outlook, op. cit. p. 145.
³⁰ European Economic Forecast, op. cit, p. 16.
³¹ European Economic Forecast, op. cit, p. 16.
³² European Economic Forecast, op. cit, p. 165.
³³ OECD, Economic Outlook, op. cit. p. 178.
³⁴ European Economic Forecast, op. cit, p. 166.
³⁵ European Economic Forecast, op. cit, p. 156.
³⁶ OECD, Economic Outlook, op. cit. p.206.
³⁷ OECD, Economic Outlook, ibid.
³⁸ OECD, Economic Outlook, ibid.
³⁹ European Economic Forecast, ibid.
⁴⁰ OECD, Economic Outlook, op. cit. p.208.
⁴¹ European Economic Forecast, ibid.
⁴² European Economic Forecast, ibid.
⁴³ European Economic Forecast, ibid.
⁴⁴ OECD, Economic Outlook, op. cit. p.209.
2.3. Inflation and monetary policy

2.3.1. Inflation

Inflation for the euro area is projected to reach 1.8% for 2018 and 2019, before declining slightly to 1.6% in 2020. Similarly for the EU 28, it is projected to reach 2% for 2018 and 2019, before dropping to 1.8%.\(^45\) Inflation in energy, service and food prices has been a key driver in changes to the harmonised index of consumer prices,\(^46\) although the impact on the index has varied from on Member State to another.\(^47\)

Aggregate rates continue to conceal significant disparities between Member States, with the Baltics, Romania and Hungary showing the highest inflation for the three-year forecast period (2.5% to 4.3% in 2018, 2.1% to 3.3% in 2020), while Cyprus, Greece Ireland and Denmark (0.7% to 0.8% in 2018, 1% to 1.7% in 2020) show the lowest, despite projections that the trend will tail off.\(^48\)

2.3.2. Monetary policy

The European Central Bank maintained its unconventional monetary policy in 2018 although, as of October 2018, it further reduced the amount of its monthly purchases under the expanded asset purchase programme to €15 billion.\(^49\) According to the latest available data, the Eurosystem holdings under the programme\(^50\) are €2.076 trillion for the public sector purchase programme (up from €1.798 trillion in November 2017), €259.3 billion for the covered bond purchase programme (up from €236 billion), €170.4 billion for the corporate sector purchase programme (up from €121.6 billion) and €26.9 billion for the asset-backed securities purchase programme (up from €24.68 billion in November 2017), for total holdings of €2.532 trillion.

With respect to its asset purchase programme(s), at its 13 September 2018 meeting,\(^51\) the Governing Council reiterated its intention to end its net asset purchases at the end of the year.\(^52\) It must be noted, however, that this does not mean the accommodative monetary policy of the ECB will cease after December 2018: the ECB currently holds a sizeable stock of assets acquired through the purchases programmes. These include the principal payments from maturing securities purchased, under which it intends to reinvest for a period of time after the end of its net asset purchases, to contribute both to favourable liquidity conditions and a degree of monetary accommodation.

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\(^{46}\) According to Eurostat, the harmonized index of consumer prices, abbreviated as HICP, is ‘the consumer price index as it is calculated in the European Union (EU), according to a harmonised approach and a single set of definitions. It is mainly used to measure inflation’.

\(^{47}\) The role of energy prices in recent inflation outcomes: a cross-country perspective, ECB Economic Bulletin, Issue 7/2018. See also Eurostat Inflation in the euro area, Statistics Explained.


\(^{49}\) Since inception, monthly purchases under the asset purchase programme have varied from €60 billion (March 2015 to March 2016) to €60 billion (April 2016 to March 2017), back to €60 billion (April 2017 to December 2017) to €30 billion (January 2018 to September 2018), to €15 billion since September.

\(^{50}\) According to the European Central Bank, the expanded asset purchase programme ‘includes all purchase programmes under which private sector securities and public sector securities are purchased to address the risks of too prolonged a period of low inflation’. It thus includes corporate sector purchase programme, the public sector purchase programme, the asset-backed securities purchase programme and the (third) covered bond purchase programme. For more details on those programmes see ECB – Asset purchase programmes.

\(^{51}\) Monetary policy decisions, press release, European Central Bank, 13 September 2018.

\(^{52}\) This decision has been prepared for over a year now: already in October 2017, the ECB Governing Council had signalled that, as of January 2018, monthly net asset purchases would be halved to €30 billion until September 2018. Further, as of October 2018, the ECB has reduced the purchase pace to €15 billion per month.
Furthermore, using its forward guidance,\(^5\) it has stated that key policy rates will remain at current levels at least through the summer of 2019. Lastly, since 2014, the ECB has used also another non-standard measure, targeted longer-term refinancing operations,\(^5\) under which the bank has offered long-term funding to banks at attractive conditions, to encourage them to increase their lending to the real economy.

The accommodative monetary policy in the euro area has been transmitted through the banking sector to interest rates on loans to households: in the euro area, credit to households increased by 3.3% in 2018 (3.7% in the EU) and it is projected to continue increasing by 3.5% in 2019 and 4% in 2020 respectively (3.6% and 3.9% in the EU) under strong demand and supportive credit terms and conditions by banks.\(^5\)

The aforementioned trends, the different pace of monetary policy normalisation in the United States and the United Kingdom on one hand and in the EU in the other, trade tensions in world markets, but also specific fiscal issues relating to particular Member States, resulted in a mixed picture compared with last year, with the euro appreciating slightly versus emerging market currencies, while at the same time weakening versus the dollar, the yen and the pound sterling.

### 2.4. Going forward

As mentioned at the beginning of the chapter, there are signs that global expansion has peaked. \(^5\) Going forward, all forecasts project that – for various reasons proper to each forecast – growth will slow down, in the EU and globally. A faster labour market recovery and the resulting increase in wages, or stronger confidence generated by an agreement on major euro area institutional reforms could constitute positive surprises and lead to growth that is stronger than forecasted.\(^5\)

On the other hand, however, the IMF, OECD and Commission forecasts include a few points that may create significant challenges in the future.

#### 2.4.1. Private and public finances

At 58% of GDP at aggregate level for the euro area, household indebtedness is not particularly high, but it is still elevated in some Member States.\(^5\) Corporate indebtedness however, remains high – at 82% of GDP on a consolidated basis – by both historical and international standards and is above thresholds ordinarily associated with a debt overhang.\(^5\)

When it comes to country finances, if the row sparked between the Commission and Italy over the latter’s budget eventually escalates, it could result in disorderly market reactions, which in turn could lead to an increase in global risk premiums.\(^5\) If such a scenario materialises, other high-debt

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\(^5\) For a useful backgrounder, see ECB What is forward guidance?, for more details, see the recent speech by Benoît Cœuré Forward guidance and policy normalisation.

\(^5\) For more information on TLTROs, see ECB Targeted longer-term refinancing operations (TLTROs).

\(^5\) The Commission notes, however, that despite the increase, the annual growth rate of loans to households for house purchases remains low from an historical perspective.

\(^6\) OECD, Economic Outlook, op. cit. p. 110.


Member States may have difficulties coping with higher borrowing costs and potentially causing the return of the sovereign-bank loops.\textsuperscript{60} Also, as mentioned before, public sector debt in many Member States is higher today than before the global financial crisis. In the absence of major shock absorbers at EU level, a major shock leading one or more Member States with debt ratios above 90\% to increase their fiscal deficits could place them in a dangerous situation.

### 2.4.2. Financial markets and monetary policy

The euro-area investment fund sector has expanded rapidly since the global financial crisis. According to the ECB, over the past 10 years, total assets in the euro-area investment fund sector have more than doubled from €5.7 trillion at the end of 2008 to €13.8 trillion in June 2018. The size of the sector, as well as the fact that such funds took increasing liquidity, credit and duration risks, raises concerns of possible forced selling, which could affect financial market conditions.\textsuperscript{61}

Concerning monetary policy, a future abrupt tightening would result in rising market interest rates and declining asset prices. Although those phenomena per se are normal and to be expected – given the increasingly risky investments undertaken by less-regulated entities such as hedge funds, money-market funds or insurance companies – they could amplify and/or spread to other assets, and create financial instability.\textsuperscript{62}

### 2.4.3. Trade and developments at global level

An intensification of trade restrictions would have significant costs. The tariffs already imposed are projected to slow growth and add to inflation.\textsuperscript{63} In the event of an escalation in the trade conflict between the US and China, their adverse effects would intensify considerably. Also, attention must be paid to non-tariff measures,\textsuperscript{64} which, despite not being as well-known as tariffs – if raised further – could also have spillover effects.

A rise in oil prices constitutes another risk for the future. Already in 2018, oil prices increased by approximately 30\% compared with the year before on account of supply disruption in Venezuela, uncertainty about the impact of sanctions on production in Iran and expectations that demand growth might slow, among other things. Further disruptions, such as the potential ramifications of Qatar’s recent decision to leave the Organization of the Petroleum Exporting Countries (OPEC), could enfeeble the market more and increase prices further.\textsuperscript{65}

In the US, faster monetary tightening or fiscal policy reversal could lead to deceleration of the economy.\textsuperscript{66} In China, risks of a slowdown have increased and risks of financial instability cannot yet be dismissed.\textsuperscript{67}

\textsuperscript{60} European Economic Forecast – Autumn 2018, op. cit., European Commission, p. 59.

\textsuperscript{61} In particular, the ECB notes that investment funds have increased their holdings of risky assets and of bonds with relatively low liquidity to 25\% of their bond portfolios, while at the same time cash buffers declined, raising their vulnerability to potential shocks in financial markets.


\textsuperscript{64} According to the OECD, non-tariff measures ‘comprise all policy measures other than tariffs and tariff-rate quotas that have a more or less direct effect on the price of traded products, the quantity of traded products, or both’.


\textsuperscript{67} OECD, \textit{Economic Outlook}, op. cit. p. 34.
Although, for the moment, the exposure of euro area banks as a whole to emerging markets is contained (although specific institutions still have significant exposures to turbulent markets such as Turkey) further stress in emerging markets could result in spillovers to Member States.68

Lastly, policy uncertainty – e.g. recent developments relating to Brexit – remains high and could increase further.

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3. EU budget in perspective

The EU budget represents a limited share of public spending in the European Union, but has features that can increase its impact. Challenges emerging in recent years have widened the debate on the budget's role and its possible reform.

3.1. Size and role of the EU budget

Amounting to €137.4 billion in 2017,\(^{69}\) the EU budget accounts for less than 1 % (0.90 % in 2017) of the European Union's gross national income (GNI), while Member States' public spending represents, on average, 46 % of their GNI. The EU budget therefore represents some 2 % of total public spending in the European Union (see Figure 3), reflecting the fact that spending competences and resources in most policy areas lie mainly at national and/or local levels. These data show a situation very different from that of federal entities, where federal spending usually represents some 50 % at least of final public spending (or 15 to 20 % of gross domestic product) in decentralised models, such as the US.\(^{70}\)

Figure 3 – EU budget and general government public spending in the EU (2017, € billion)

<table>
<thead>
<tr>
<th>EU Spending</th>
<th>137.4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Spends</td>
<td>7 037.0</td>
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</table>

Data source: European Commission (DG Budget and Eurostat) data. Eurostat data are provisional.

Analysts\(^{71}\) note that, to date, the EU budget has played two of the three functions that economic theory traditionally attributes to public finance: the provision of public goods (e.g. promotion of research and innovation activities), and some redistribution of resources to reduce disparities,\(^{72}\) in line with the objectives of economic, social and territorial cohesion between EU regions enshrined in the Treaty on the Functioning of the European Union (TFEU).\(^{73}\) The two functions are not mutually exclusive, since a policy area with redistributive objectives, such as cohesion, can also provide public goods.

Studies often draw attention to the relatively small size of the EU budget, concluding that this and other features limit its overall capacity to provide public goods and to play a redistributive role. For example, one paper\(^ {74}\) estimates that the annual redistribution of resources operated by the EU budget over the last 15 years corresponds to 0.2 % of the area's GNI,\(^{75}\) as compared with 1.5 % for

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69 The consolidated annual accounts of the EU for financial year 2018 are expected to be made available in June 2019.
70 C. Cottarelli and M. Guerguil (eds.), *Designing a European Fiscal Union. Lessons from the experience of existing federations*, Routledge, 2015. The authors examine the budgetary arrangements between the central and subnational levels of government in a sample of 13 federations (all those with a nominal GDP higher than US$400 billion in 2011).
72 The third function, which is not covered by the EU budget, is macroeconomic stabilisation.
73 Part Three, Title XVIII, TFEU.
75 In recent years, the figure has reached 0.3 % as a result of increasing diversity in the EU, determined on the one hand by the accession of 13 Member States with lower per capita income as of 2004, and on the other by growing divergence in economic performance and unemployment rates following the financial and economic crisis.
the federal budget in the US. In other words, 80% of resources returned to the Member State that provided them.

However, the role that the EU budget can play in the economy, and the achievement of EU policy objectives on account of a number of its characteristics, should not be underestimated. Examples include the share of the EU budget devoted to investment (as compared with national budgets, where most resources are usually allocated for consumption and transfers), its capacity to leverage complementary sources of financing (e.g. through innovative financial instruments), and to achieve advantages such as economies of scale in policy areas where the pooling of resources at EU level may help to meet objectives more effectively (e.g. in the field of development cooperation with third countries).

In some countries, the EU budget may represent a significant source of resources for investment. For example, in 13 Member States, mainly among those that joined the European Union after April 2004, the EU budget, as a share of total public spending, is significantly higher than 2%, with figures ranging between 4.47% for Portugal and 11.28% for Lithuania (Figure 4).

![Figure 4 – EU budget as a share of public spending in individual Member States (2017)](source: EPRS, based on European Commission (DG Budget and Eurostat) data.)

In addition, when focusing on investment only, the contribution of the EU budget to public investment in the Union is higher: according to the European Commission, the 2007 to 2013 cohesion policy alone represented 6.5% of government capital investment in the Union on average, with peaks of over 50% in four Member States (Hungary, Latvia, Lithuania, and Slovakia). For the 2015 to 2017 period, the pattern is confirmed with cohesion policy’s average contribution to government capital investment estimated at 8.5% in the EU and at 41% in the 13 Member States.

76 While the European Commission publishes the allocation of expenditure to Member States, it underlines that this is only an accounting exercise, which does not provide a complete overview of the benefits that each Member State derives from EU membership: Annex 1 recapitulates this allocation for each major category of EU spending in 2017.

77 The group also includes some pre-2004 Member States. For example, the case of Luxembourg (7.67%) is mainly explained by the size of the country, its role as host to a number of EU institutions, and the administrative expenditure attributed to the country on this basis. As for the EU budget, the graph does not include either spending in countries outside the EU or spending that could not be attributed to individual Member States. In 2017, this figure amounted to €25.8 billion.

78 Commissioner C. Creţu, Cohesion policy: Delivering added value to the EU and its citizens, presentation given at the ‘EU budget focused on results’ conference, 27 September 2016. It should also be noted that the benefits of cohesion policy are not limited to the Member State directly receiving the resources, since projects implementing the programmes may be awarded to companies from other Member States.
that joined the Union after April 2004.\textsuperscript{79} As regards investment in research and innovation, Horizon 2020 is the world’s largest transnational programme devoted to such activities: in 2017, the largest recipients were Germany, the United Kingdom, France, Belgium and Spain (in decreasing order according to the total amount beneficiaries located in their territories received from the programme).

From this perspective, the European Commission and the European Parliament stress\textsuperscript{80} that the EU budget is different in nature and function from national budgets, since it is mainly an investment budget with a focus on measures with European added value. The current multiannual financial framework (MFF), which sets the EU budgetary structure for the 2014 to 2020 period, seeks to focus spending priorities on sustainable growth, employment, and competitiveness, pursuant to the objectives of the Europe 2020 strategy and in line with the priorities of the Juncker Commission.\textsuperscript{81}

Co-financing is a characteristic of the EU budget that can increase its impact on job creation and growth. This means that EU spending is normally used in conjunction with funding from other public and/or private sources, thus resulting in total investments higher than the EU contribution proper. To some extent, this is already the case for traditional grants. In addition, with a view to maximising the so-called multiplier effect of the EU budget, innovative financial instruments (triggering equity, quasi-equity, debt or guarantee funding) have been developed to support economically viable investments in line with EU objectives.

While innovative financial instruments are not deemed to fit all kinds of public spending, they have features that make them attractive for some policy areas and objectives, notably by: attracting additional funding from other sources (leverage effect); and generating income through amounts repaid by beneficiaries of funding that can be used for new operations in line with the same policy objectives (revolving nature of the instruments). The leverage effect can vary significantly from one instrument to another. The European Commission reports that 2014 to 2020 period financial instruments with budgetary resources of almost €9 billion have been targeted to support total financing of more than €88 billion, representing average leverage of close to a factor of 10.\textsuperscript{82}

The High-Level Group on Own Resources (see Section 5.2) notes that, based on a study\textsuperscript{83} it commissioned, wealthier Member States have a comparative advantage in attracting resources linked to the main financial instruments.\textsuperscript{84} Therefore, the distribution of such resources differs from that in traditional EU spending areas (e.g. cohesion and agriculture). The leverage effect and evolving nature of these instruments mean that the standard representation of the allocation of EU


\textsuperscript{81} The 10 priorities of the Juncker Commission are jobs, growth and investment; the digital single market, the energy union and climate; a deeper and fairer internal market; a deeper and fairer economic and monetary union; a balanced EU-US free trade agreement; justice and fundamental rights; migration; the EU’s external action; and democratic change.

\textsuperscript{82} Report on financial instruments supported by the general budget according to Article 140(8) of the Financial Regulation as at 31 December 2016, (COM/2017/0535), European Commission, 25 September 2017. For more details on the advantages and challenges of financial instruments, please see: Implementing the EU budget through financial instruments – lessons to be learnt from the 2007-2013 programme period, European Court of Auditors, (Special Report No 19/2016); and J. Núñez Ferrer et al., Financial instruments: defining the rationale for triggering their use, Policy Department for Budgetary Affairs, DG IPOL, European Parliament, October 2017.

\textsuperscript{83} J. Núñez Ferrer, J. Le Cacheux, G. Benedetto and M. Saunier, Study on the potential and limitations of reforming the financing of the EU Budget, 3 June 2016, CEPS, Université de Pau et des Pays de l’Adour, LSE Enterprise and Deloitte.

\textsuperscript{84} Future financing of the EU: final report and recommendations, High-Level Group on Own Resources, December 2016.
expenditure to Member States (see Annex 1) provides only a partial picture of the overall benefits deriving from the EU budget and EU membership.\(^{85}\)

In some policy areas, the pooling of resources at EU level may bring advantages such as economies of scale and elimination of duplication, generating EU added value and enabling a more effective achievement of results. For example, the OECD considers the geographic reach, scale and scope of EU programmes as three comparative advantages of the EU in development cooperation.\(^{86}\) The EU, with its Member States, is the world’s biggest development aid donor. However, in addition to EU programmes, Member States channel development assistance by means of national and/or intergovernmental schemes. According to cost of non-Europe papers drafted for the European Parliament in 2013, further coordination of EU donors could save some €800 million per year in overhead costs associated with activities such as programming, implementation and monitoring of assistance, while increasing the overall impact of development measures.\(^{87}\)

In conclusion, the EU budget is relatively small in size, but has features that can reinforce its overall impact. Nevertheless, in the debate on the preparation of the post-2020 financing period, many analysts and stakeholders agree that, while the EU budget has already undergone many changes, it needs further modification and streamlining to increase its capacity to respond to the concerns of EU citizens and to the unprecedented challenges the EU is facing. For example, an analysis by the CEPS think-tank\(^{88}\) argues that there is a need to clarify the key objectives of the EU budget in today’s world, moving from a perspective in which each Member State is mainly interested in its net balance, to an approach where the EU budget complements national budgets and further increases its focus on EU objectives that can be better achieved at EU level. The debate on the post-2020 EU budget has identified the objective of concentrating resources on the policy areas with the highest EU added value, among the key principles of any reform (see Section 5.2).

### 3.2. Structure of the EU budget: revenue and multiannual planning

The ‘own resources’ system sets out how the EU budget is financed, while the structure of the expenditure side of the budget is determined, for a period of at least five years, by a multiannual planning tool – the multiannual financial framework (MFF).

Unlike national budgets, the EU budget cannot run a deficit. Its financing is ensured by three main sources of revenue: traditional own resources (customs duties and sugar levies); an own resource based on a harmonised base of value added tax (VAT); and an own resource linked to Member States’ GNIs, which plays the role of balancing the budget.\(^{89}\) The maximum level of resources available for

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85 See footnote 65.


89 Other revenue, which is not classified as own resources, includes taxes on EU staff salaries, contributions from non-EU countries to certain programmes, and fines on companies for breaching competition law.
the EU budget is set at 1.20 % of EU GNI (the ‘own resources ceiling’, which has remained virtually unchanged since the 1990s).

Currently, the bulk of revenue is provided by a GNI-based resource and a VAT-based resource, which Member States perceive as national contributions rather than EU own resources. In 2017, these two resources jointly accounted for around 68 % of EU financing (see Figure 5). The fact that the ‘other revenue’ category was exceptionally high in 2017 explains why the share of the GNI- and VAT-based resources in the EU revenue mix is usually even larger (in some years more than 80 %).

According to a number of analysts and stakeholders, including the European Parliament, the predominant role of national contributions promotes a focus in budgetary negotiations on Member State net balances and programmes with geographically pre-allocated expenditure. In the current configuration of the system, permanent and/or temporary correction mechanisms reduce the contributions of the following Member States: Austria, Denmark, Germany, the Netherlands, Sweden and the United Kingdom. Annex 2 recapitulates national contributions by Member State and traditional own resources collected on behalf of the EU in 2017.

As for the expenditure side of the budget, the 2014-2020 MFF sets the maximum level of resources (‘ceiling’) for each major category (‘heading’) of EU spending for a period of seven years. Negotiated between 2011 and 2013 against the backdrop of the economic crisis and fiscal consolidation in Member States, the current MFF is the first to have lower resources in comparison with the previous programming period (2007 to 2013). The share of EU GNI devoted to the MFF was set at 1 % for commitments and 0.95 % for payments (down from 1.12 % and 1.06 % for the 2007 to 2013 period).

The MFF resources for commitments over the entire 2014 to 2020 period amount to €1 087.1 billion in current prices (or €963.5 billion in 2011 prices). Figure 6 shows their distribution among the six major categories of EU spending (one category has two subcategories or ‘subheadings’). The MFF details the annual ceilings for new commitments in each spending category and an overall ceiling for annual payments. In addition, it contains some special instruments outside the MFF ceilings (e.g. the Emergency Aid Reserve, the European Globalisation Adjustment Fund and the European Union Solidarity Fund) and flexibility provisions, to give some room for manoeuvre in case of unexpected events. The challenge is to strike the right balance between predictability of investments and the capacity to address the unforeseen events and new priorities that can emerge during a rather long programming period.

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90 Following the entry into force of the new Own Resources Decision in 2016, the Commission carried out the technical adaptation of the ceiling to the new GNI data according to the ESA 2010 system (COM(2017) 473). The ceiling is now established at 1.20 % of GNI (down from 1.23 %). For more details on the financing system: A. D’Alfonso, How the EU Budget is financed. The ‘own resources’ system and the debate on its reform, EPRS, European Parliament, 2014.


3.3. Main institutional actors in two key phases of the budgetary cycle

The European Parliament and the Council of the European Union are the two arms of the EU budgetary authority. Their tasks include intervening at the authorisation stage, and establishing the annual EU budget and its amendments, which they negotiate on the basis of a proposal from the European Commission and within the requirements set out by the own resources system and the MFF Regulation (see Section 3.2 above).

The powers of the European Parliament and the Council differ depending on the issue at stake. For the annual budgetary procedure they enjoy an equal footing. The decision on the design of the own resources system requires the unanimity of the Member States in the Council, while the European Parliament is only consulted. The Council also unanimously adopts the regulation establishing the MFF, but in this case needs to obtain the European Parliament's consent beforehand.

This asymmetry in the powers of the two arms of the budgetary authority is said to sharpen the differences in their perspectives on budgetary issues. In addition, the requirement of unanimity in the Council for the adoption of own resources and the MFF is often seen as an obstacle to major EU budget reform. While the budget has been modified over the years, stakeholders generally acknowledge that further changes are needed. However, the veto power enshrined in the procedures would tend to favour the continuation of the status quo, which has up to now ensured an equilibrium between Member States that join forces in subgroups sharing the same interests (e.g. debates on budgetary negotiations often refer to groups, such as net contributors and net beneficiaries; and 'friends of cohesion', 'friends of better spending or correction mechanisms', and 'friends of agriculture'). The European Parliament has long pushed for EU budgetary reform,
including in areas where its powers are more limited, such as own resources and the MFF, with the aim of shifting the focus of budgetary discussions to measures with EU added value.95

As regards the implementation stage, the European Commission is ultimately responsible for the execution of the EU budget. However, implementation involves a wide range of actors under the three different management modes set out by the EU Financial Regulation. In practice, Member States implement some 80% of the EU budget in 'shared management' with the European Commission, which applies to most expenditure under subheading 1b 'Economic, social and territorial cohesion' and heading 2 'Sustainable growth: natural resources'. The remaining 20% of the budget is implemented either under 'direct management' (European Commission and EU executive agencies) or under 'indirect management' (other entities such as third-country authorities, international organisations, EU decentralised agencies and the European Investment Bank).

With the aim of ensuring correct and effective use of EU resources, the Financial Regulation applicable to the EU budget details key principles that the entities entrusted with budget implementation must respect. These include control and audit obligations for the various types of implementing methods. At political level, oversight of EU budget implementation is a key responsibility of the European Parliament (see Section 4.3).

3.4. Challenges in recent years

Since the beginning of the 2014-2020 programming period, the EU budget has been confronted with a number of challenges, including: constant pressure on the 'Security and citizenship' and 'Global Europe' headings in the context of growing instability in the EU’s neighbourhood, the migration crisis, and security threats; a continued significant investment gap in the EU many years after the outbreak of the financial and economic crisis; and a high abnormal payments backlog at the end of both 2014 and 2015.96

The immediate response of EU institutions and Member States to such challenges has included leaning heavily on the resources available under the relevant flexibility provisions of the MFF and creating budgetary tools at least partially outside the EU budget, to try to leverage funding from other public and/or private sources (e.g. the European Fund for Strategic Investments (EFSI) to address the investment gap; and EU Trust Funds and the Facility for Refugees in Turkey to deal with the migration crisis).

Resources available under flexibility provisions and special instruments were almost completely used during the first years of the current programming period. In June 2017, the mid-term revision of the MFF, for which the European Parliament had long pushed, was used to replenish and strengthen such instruments with a view to increasing the capacity of the EU budget to respond to unexpected challenges and to avoiding a repeat of abnormal payments backlogs in the last years of the framework. The mid-term revision was part of a broader package of legislative and non-legislative initiatives, whose objectives included: increasing the impact of EU funds by simplifying


96 At the worst point, in 2014, the level of payment backlog was estimated at some €26 billion. Most of this was accumulated under subheading 1b ‘Economic, social and territorial cohesion’, but some serious problems occurred also under the Erasmus and research programmes, neighbourhood and humanitarian aid programmes. For a thorough analysis of the problem see: A. D’Alfonso and M. Sapala, Payments backlog in in recent EU budgets. Lessons learnt and outlook, EPRS, European Parliament, November 2015.
the rules for their implementation; and enhancing EU instruments and resources devoted to job creation, growth, migration and security challenges, without modifying MFF ceilings.\textsuperscript{97}

A different challenge for which the possible role and contribution of the EU budget have been debated concerns the efforts to tackle the euro crisis and strengthen European monetary union (EMU). However, in its current configuration, the EU budget is deemed unable to play a stabilisation role in the case of economic shocks, on account of its size and limited flexibility in the context of MFF planning (see Sections 3.1 and 3.2 above).

One idea proposed is the creation of a specific ‘fiscal capacity’ for the euro area.\textsuperscript{98} In 2017, French President Macron called for the creation of a common budget for the euro area,\textsuperscript{99} while Commission President Jean-Claude Juncker supported the establishment of a dedicated euro-area budget line as a subsection of the EU budget itself.\textsuperscript{100} In May 2018, the European Commission put forward\textsuperscript{101} proposals for the establishment of two new budgetary instruments to deepen EMU under the post-2020 MFF (see Section 5.3). In the Meseberg Declaration of June 2018, France and Germany jointly proposed creating a euro area budget within the EU framework as of 2021, identifying the promotion of competitiveness, convergence and stabilisation in the currency area as its objective.\textsuperscript{102} In this respect, the two countries presented a proposal on the architecture of such an instrument to the Eurogroup in November 2018.

\textsuperscript{98} A. D’Alfonso and A. Stuchlik, A fiscal capacity for the euro area?, European Parliament, EPRS, September 2016.
\textsuperscript{99} E. Macron, Initiative for Europe, Sorbonne speech, 26 September 2017.
\textsuperscript{100} J.-C. Juncker, State of the Union address 2017, 13 September 2017.
\textsuperscript{101} EU budget: A reform support programme and an investment stabilisation function to strengthen Europe’s economic and monetary union, press release, European Commission, Brussels, 31 May 2018.
\textsuperscript{102} Meseberg Declaration. Renewing Europe’s promises of security and prosperity, Presse- und Informationsamt der Bundesregierung, 19 June 2018.
4. EU budget for 2019

On 10 December 2018, the European Parliament approved an agreement on the general budget of the EU for the 2019 financial year. This is the last but one annual budget in the 2014-2020 MFF and the first agreed based on the premise that the UK will withdraw from the EU on 30 March 2019 and that it will continue to contribute to and participate in its implementation as if it were a Member State until the end of the current MFF. This time the budgetary negotiations took longer than usual. Reaching an agreement was not possible within the 21-day conciliation period and the Commission had to table the second draft budget, which with some adjustments was finally approved at the last plenary session of the year. The total amount of commitments agreed is 3.2% higher than for the 2018 budget, and the distribution of resources between different EU priorities shows a number of modifications. As has been the case with all previous annual budgets in the current MFF, also this time the budgetary authority resorted to the flexibility tools provided for in the MFF Regulation with a view to financing growing needs in some areas. In 2019, the resources mobilised based on the flexibility provisions will support programmes relating to competitiveness, research, cohesion, migration and security issues.

4.1. Result of the 2019 budgetary procedure

Total commitments of the 2019 EU budget were set at €165.8 billion and total payments at €148.2 billion. In comparison with the 2018 budget this represents an increase of 3.2% and 2.4% respectively. The commitments agreed account for 1.01% of EU-28 GNI, which is a slight decrease from 1.02% of EU-28 GNI in 2018 (Figure 7; for detailed figures, see Annex 3). The margin below the 2014-2020 multiannual financial framework ceilings still available for unexpected needs in 2019 amounts to €1.3 billion in commitment appropriations.

Figure 7 – Total commitment and payment appropriations, EU budget 2018 and 2019.

Total commitments appropriations, € bn

<table>
<thead>
<tr>
<th>Year</th>
<th>Appropriations</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>160.7</td>
</tr>
<tr>
<td>2019</td>
<td>165.8</td>
</tr>
</tbody>
</table>

Total payment appropriations, € bn

<table>
<thead>
<tr>
<th>Year</th>
<th>Appropriations</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>144.8</td>
</tr>
<tr>
<td>2019</td>
<td>148.2</td>
</tr>
</tbody>
</table>

Source: EPRS.

The procedure, in accordance with Article 314 of the TFEU, started with the Commission presenting a draft budget on 23 May 2018. In the autumn the Parliament and the Council negotiated the budget based on this proposal and the Amending Letter 1/2019 (see Box 1 below). In their respective readings during the procedure, the Council cut the initial proposal of the European Commission,

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103 Data on leading European Parliament committees involved in budgetary procedures are available in Annex 4.
while the Parliament increased it (Figure 8). After 21-day conciliation procedure provided for in the Treaty the negotiations ended without agreement on 19 November 2018.

Figure 8 – 2019 EU budget (commitments, € billion, current prices)

<table>
<thead>
<tr>
<th>Budget Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Draft budget (incl. AL.1) Commission</td>
<td>€165.57</td>
</tr>
<tr>
<td>Council position</td>
<td>€164.07</td>
</tr>
<tr>
<td>EP position</td>
<td>€166.34</td>
</tr>
<tr>
<td>II Draft budget Commission</td>
<td>€165.61</td>
</tr>
<tr>
<td>Adopted budget</td>
<td>€165.80</td>
</tr>
</tbody>
</table>

Source: EPRS.

Major issues of disagreement were the financing of the EU research programmes and support for refugees via the Facility for Refugees in Turkey (FRT). Based on Article 15(3) of the recently revised Financial Regulation,\(^{104}\) the Commission and the Parliament wanted to recycle the unspent commitments for research from 2017 in the 2019 budget to increase Horizon 2020 financing. The Council, however, opposed this move on grounds of principle, so as to avoid setting a precedent. Besides, the Parliament and the Council could not reach a compromise on the level of financing from the EU budget for the second tranche of the FRT. The Parliament claimed it was not duly involved by the Council and the Commission in the discussions on the extension of the facility. It did not want to accept €2 billion transfer from the EU budget demanded by the Council for this purpose, unless satisfactory financing would be secured for priority programmes such as Horizon 2020, Erasmus+, Youth Employment Initiative and migration policy related actions.\(^{105}\) Lack of agreement on the 2019 budget before the end of 2018, would have triggered the provisional twelfths regime and could have led to delays in implementation of key policies and programmes.

On 30 November 2018, the Commission tabled the second draft budget for 2019. It took into account progress made in the Conciliation Committee and included reinforcements in commitment appropriations for the Parliament’s priority programmes and some decreases and redeployments especially in the EU’s economic and development assistance for Turkey. An increase in the allocation for Horizon 2020 was again proposed based on the application of Article 15(3) of the Financial Regulation.

Finally, an agreement was reached during the trilogue meeting of 4 December 2018. The commitments adopted in the 2019 budget are €54 million lower than the amount demanded by the Parliament and €1.7 billion higher than stipulated in the reading of the Council (compared with the initial draft budget including Amending Letter 1/2019, see Figure 8). The reinforcements obtained during the negotiations correspond to the priorities identified by the Parliament. However, the proposal to use Article 15(3) of the Financial Regulation was blocked by the Council. Instead, in the joint statement attached to the budgetary agreement, the Parliament, the Council and the Commission made a commitment to introduce an additional €100 million to the 2019 budget for Horizon 2020 and Erasmus+ through an amending budget procedure. This would be done as soon as the technical adjustment of the MFF for 2020, including the calculation of the commitments left


available below the MFF ceilings (global margin for commitments) was complete. As far as financing of the FRT is concerned, €2 billion would be contributed from the Union budget and €1 billion from the Member States.

Box 1 – 2019 budgetary procedure milestones

May 2018: The European Commission tables the draft EU budget for 2019.


October 2018: The European Parliament amends the Council’s position on the draft 2019 EU budget.


Amendments proposed in Amending Letter 1/2019:

1) An update of the estimated needs and assigned revenue and appropriations for agricultural expenditure

2) An update of appropriations as a result of the recently agreed political agreements on the creation of the European Defence Industrial Development Programme, the European Solidarity Corps and changes in the operation of the Structural Reform Support Programme;

3) Reinforcements linked to the new initiatives tabled by the Commission concerning the European Border and Coast Agency, the European Union Agency for Asylum and the Authority for European Political Parties and European Political Foundations

4) A series of administrative and technical adjustments concerning EU agencies, European External Action Service, etc.


11 December 2018: The Council adopts its reading of the second draft budget

12 December 2018: The European Parliament approves the joint text agreed by the Conciliation Committee.

In 2019, the EU budget will focus on stimulating investment and sustainable growth and creating new jobs, especially for young people, as well as addressing migration and security challenges. As compared to the draft budget proposed by the Commission in May 2018, the level of commitment appropriations for a number of programmes and activities related to these objectives will be increased, e.g. reinforcements of an additional €116.7 million for the Youth Employment Initiative, €248.8 million for research and innovation under Horizon 2020 (including €100 million through an amending budget in 2019), €240 million for Erasmus+ and €5 million for support for small and medium-sized enterprises under COSME.106

Total commitment appropriations for 2019 are up by 3.2 % in comparison with the 2018 budget. This is the result of increases in all headings, with the most significant in heading 4 'Global Europe' (+12.4 %). The overall level of payment appropriations in 2019 is 2.4 % higher and can be considered

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moderate given last year’s ambitious growth of 54.7%. In the 2019 budget, the largest increase of payment appropriations was agreed under heading 3 ‘Security and citizenship’ (+18.3%) (Figure 9).

Figure 9 – A comparison of EU budgets in 2018 and 2019 (commitment and payment appropriations, € billion)

As in previous years, the mobilisation of the flexibility tools of the MFF\(^{107}\) proved necessary to finance budgetary priorities and reinforcements, already at the initial stage of adoption. The conciliation agreement for the 2019 budget included the mobilisation of substantial amounts of two such instruments: the Global Margin for Commitments and the Flexibility Instrument (Table 1).\(^{108}\) In the resolution accompanying the mobilisation of the latter, the European Parliament reiterated its longstanding view that the EU budget needed to be made more flexible.\(^{109}\)


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\(^{107}\) Specified in Articles 9 to 15 of the MFF Regulation, these special flexibility instruments can be applied when an expenditure cannot be financed within the limits of the ceilings available under the headings. The possibility to shift available margins between headings and years, known as ‘the flexibility’, was an important issue during the negotiations on the MFF 2014-2020. Parliament strongly supported enforced flexibility provisions and the relevant articles strengthened in the MFF Regulation are an important negotiation achievement. These were already very useful during the first years of implementation of the current MFF. In its mid-term review/revision, the European Commission therefore proposed to expand the flexibility instruments and thereby increase the capacity of the EU budget to respond to unexpected challenges and new priorities.

\(^{108}\) As regards other special instruments, the agreement on the second draft budget also: included the offsetting of the Contingency Margin mobilised in 2017 against the unallocated margins under heading 5 ‘Administration’; set the level of commitments appropriations for the European Globalisation Adjustment Fund (EGF) and for the Emergency Aid Reserve (EAR) in 2019; and made available €50 million for the commitments and payment of advances under the European Union Solidarity Fund (EUSF) in 2019.

\(^{109}\) European Parliament, [resolution](https://ec.europa.eu/budget) on the proposal for a decision on the mobilisation of the Flexibility Instrument to finance immediate budgetary measures to address the on-going challenges of migration, refugee inflows and security threats, Strasbourg, 12 December 2018.
Table 1 – Flexibility tools mobilised with the adoption of the 2019 EU budget

<table>
<thead>
<tr>
<th>Instrument</th>
<th>Amount mobilised</th>
<th>Goal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Global Margin for Commitments</td>
<td>€1 476.0 million</td>
<td>to finance additional allocations under subheading 1a ‘Competitiveness for growth and jobs’ (€74.7 million), subheading 1b ‘Economic, social and territorial cohesion’ (€350 million) and heading 4 ‘Global Europe’ (€1 051.3 million).</td>
</tr>
<tr>
<td>Flexibility Instrument</td>
<td>€1 164.3 million</td>
<td>to address needs in Horizon 2020 and Erasmus+ under subheading 1a ‘Competitiveness for growth and jobs’ (€178.7 million), and migration and security challenges under heading 3 ‘Security and Citizenship’ (€985.6 million).</td>
</tr>
</tbody>
</table>


This has been a recurrent challenge since the beginning of the 2014 to 2020 MFF, because the EU budget has had to deal with many unforeseen events and crises. For the fifth year in a row, extraordinary resources had to be mobilised and/or redeployed to measures aimed at dealing with migration and refugee issues, neighbourhood policy, employment, and investment policy. Such intensive recourse to the flexibility tools proved their usefulness in the current programming period. The resources available under the flexibility provisions were almost exhausted already in the first half of the current MFF and had to be reinforced in the mid-term revision of the MFF in 2017 (see Section 3.4).

The agreement on the 2019 budget includes several additional statements, including on the close monitoring of payment appropriations in order to avoid any abnormal level of unpaid invoices at year-end; on the need for a legislative proposal for smooth implementation of increased budgetary resources for the Youth Employment Initiative; on the need to make an additional effort to reach the 20 % target for climate mainstreaming for the whole 2014 to 2020 period; and on the reinforcement of Horizon 2020 and Erasmus+ (subheading 1a) through an amending budget in 2019.

4.2. Budget headings in detail

Heading 1 ‘Smart and inclusive growth’ is the largest in the 2014 to 2020 MFF and finances investments in EU priority areas in the Member States and their regions. In the 2019 EU budget it accounts for 48.6 % of total commitment appropriations. Heading 1 is divided into subheading 1a ‘Competitiveness for growth and jobs’ and subheading 1b ‘Economic, social and territorial cohesion’.

Many programmes and initiatives under heading 1 support small and medium-sized enterprises, which are the focus of this year’s economic section of the Outlook (see Section 6). Investing in the development of SMEs fits into one of broad priorities of the 2019 budget, which is investing in a stronger and more resilient European economy. Therefore, while SMEs are often considered to be at a disadvantage regarding access to finance (see Section 6.4), they get special attention and strong support under the EU budget, and under heading 1 in particular. Relevant instruments are offered
to SMEs operating in a wide range of sectors with a priority for actions stimulating innovation, technological development, growth, competitiveness and job creation.

Figure 10 – Subheading 1a Competitiveness for growth and jobs, 2019 commitment appropriations

<table>
<thead>
<tr>
<th>12 311.5</th>
<th>3764.0</th>
<th>2766.4</th>
<th>1959.4</th>
<th>2 534.1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Horizon 2020</td>
<td>CEF (Connecting Europe Facility)</td>
<td>Erasmus+ (Education, Training and Sport)</td>
<td>Large infrastructure projects</td>
<td>other</td>
</tr>
</tbody>
</table>

Data source: European Commission. Figures for the 2019 budget were approved, and await final publication in the Official Journal of the European Union, see also Annex 3.

Subheading 1a includes EU investments in research and innovation, education and training, large infrastructure projects, trans-European networks in transport, communication and energy, social policy and enterprise development. Examples of programmes and instruments supported include Horizon 2020, the Connecting Europe Facility, Erasmus+, the European satellite navigation systems (EGNOS and Galileo), the Competitiveness of enterprises and small and medium-sized enterprises (COSME) programme and the European Fund for Strategic Investments (EFSI). The recently established (July 2018) European Defence Industrial Development Programme includes measures specifically dedicated to SMEs.¹¹⁰

As compared with 2018, the commitment appropriations under subheading 1a increased by 3.9%. Similarly, as a share of the total budget, the allocation increased from 13.7% to 14.1% (Figure 9). Almost all programmes were reinforced, in particular in the Connecting Europe Facility (+37%), the European Earth Observation Programme (Copernicus) (+36.7%), Erasmus+ (19.5%) and Horizon 2020 (+9.8%). The most spectacular increase is in the European Solidarity Corps initiative. Launched in 2017, the initiative's implementation has now reached cruising speed and it will receive an additional €100.5 million in 2019 (+235%) under subheading 1a.¹¹¹ In a number of cases, and thanks to Parliament’s firm position, additional allocations agreed in the budgetary procedure went beyond the amounts initially proposed by the Commission.

With no margin left under the expenditure ceilings of subheading 1a, in order to finance these reinforcements it was necessary to use €74.7 million from the Global Margin for Commitments and mobilise €178.7 million through the Flexibility Instrument. This was facilitated by the adoption of the mid-term revision of the MFF¹¹² (see Section 3.4), which included an agreement on the allocation of additional resources for the 2017 to 2020 period to programmes and instruments that have proved successful in promoting growth and job creation (e.g. Horizon 2020, Connecting Europe


¹¹¹ Some complementary resources for the initiative come from the programmes under other headings, such as the European Social Fund or LIFE programme, Statement of estimates of the European Commission for the financial year 2019, SEC(2018) 250 - May 2018.

Facility – Transport, Erasmus+ and COSME).\textsuperscript{113} The boost in these allocations has also an impact on sums dedicated to SME support (see Box 2).

### Box 2 – Instruments addressing SMEs under heading 1a

Many instruments under subheading 1a 'Competitiveness for growth and jobs' contribute to growth and stimulate SME innovation and competitiveness. SMEs can be supported individually or as members of a consortium. They secure access to finance in various forms, including grants, loans, microfinance, guarantees or equity instruments (see Section 6.6.). In 2019 EU financial support for programmes dedicated to SMEs will intensify. The Horizon 2020 framework programme for research and innovation (€12.3 billion of commitments in 2019) includes strands specifically relevant to small and medium enterprises. For instance, under the 'Industrial leadership' pillar, a specific 'Innovation in SMEs' objective supports the innovation capacity of small businesses. It will receive €92.6 million in 2019 (3.1 % more than in 2018). Furthermore, as part of Horizon 2020 and under the umbrella project grouping 'European Innovation Council', the sum of €641.6 million is dedicated to the SME instrument (€100 million more than proposed by the Commission). It will support the most innovative enterprises in their efforts to get their ideas on the market or scale up.

The COSME programme has a 2019 allocation of €367.2 million (3.7 % increase) to achieve objectives such as improving access to finance and to markets for SMEs as well as the framework conditions for the competitiveness and sustainability of EU enterprises. Some other programmes partly support SMEs, for instance the Connecting Europe Facility (CEF), which invests in transport, energy and digital infrastructure, and the Employment and Social Innovation (EaSI) Programme, which offers microloans to micro-enterprises and investments to social enterprises.

SMEs are an important target group for investments under the European Fund for Strategic Investments (EFSI) (see also Section 6.6.5). In accordance with the decision on the extension of the EFSI till the end of 2020 (\textit{Regulation (EU) 2017/2396}), given the particularly quick absorption of the allocation for the dedicated SME Window and exceptional demand for SME financing, the support for SME Window was enhanced. In 2019, the allocation for EFSI totals €186.9 million in commitment appropriations.

### Figure 11 – Subheading 1b Economic, social and territorial cohesion, 2019 commitment appropriations

\begin{center}
\begin{tabular}{lcccc}
\hline
 & 27 875.2 & 9 753.6 & 8 648.9 & 5 848.7 & 5 065.5 \\
Regional convergence (less developed regions) & Cohesion Fund & Competitiveness (more developed regions) & Transition regions & other \\
\hline
\end{tabular}
\end{center}

Data source: European Commission, see above and Annex 3.

Subheading 1b covers EU expenditure on cohesion policy and supports the harmonious economic, social and territorial development of EU regions and cities. Most of the expenditure in the subheading is pre-allocated to the Member States and implemented through three European structural and investment (ESI) funds, namely the European Regional Development Fund (ERDF), the European Social Fund (ESF) and the Cohesion Fund.\textsuperscript{114} Moreover, the subheading 1b includes a

\begin{footnotesize}
\textsuperscript{113} In the first years of the current MFF, programmes such as Horizon 2020 attracted numerous, high-quality applications. However, on account of the level of available resources, only part of the positively evaluated proposals could be financed. European Commission SWD(2016) 299 final, 14 September 2016 p. 7.

\textsuperscript{114} The remaining two of the five ESI funds are the European Fund for Rural Development (EFRD) and the European Maritime and Fisheries Fund (EMFF), which are included under heading 2 'Sustainable growth: natural resources'.
\end{footnotesize}
specific contribution from the Cohesion Fund to the Connecting Europe Facility, a specific allocation for the Youth Employment Initiative, and the Fund for European Aid to the most Deprived (FEAD).

ESI fund resources are distributed between two objectives: ‘Investment for growth and jobs’ and ‘European territorial cooperation’ and make a significant contribution to initiatives supporting SMEs. One of the 11 thematic objectives supported by the ESI funds in the 2014 to 2020 programming period is specifically dedicated to enhancing the competitiveness of SMEs (see Box 3).

In 2019, total commitment appropriations for subheading 1b are set at €57.2 billion and represent a 3 % increase compared with the previous year. The amounts agreed for the ESI funds under this subheading are based on the envelopes set in the relevant legal bases and in the operational programmes adopted. As there was no margin left under the expenditure ceiling of this subheading, it was necessary to mobilise the Global Margin for Commitments for an amount of €350 million. It will be used to finance the Youth Employment Initiative (see Table 1).

The level of payment appropriations for subheading 1b, rose significantly in the 2018 budget (+54.7 %) and will remain stable for 2019 (+1.1 %). Even though the implementation of the 2014 to 2020 programmes seems finally to be reaching cruising speed and the payment requirements are increasing, the Commission estimates a significant decline in payment needs for the programmes started in the 2007 to 2013 period, which are at the closure stage. However, as emphasised in the joint statement by the European Parliament, Council and Commission attached to the budgetary agreement, it is necessary to continue close monitoring of the situation with payment requirements in 2019 in order to avoid risk of accumulation of abnormal backlog of unpaid bills. Should the figures show that the agreed payment appropriations are not sufficient, the Commission is invited to present an appropriate solution as soon as possible and the budgetary authority declared that it would take into account the urgency of the matter. According to the Commission, the bottlenecks that hindered the implementation of the ESI funds in the previous years have been removed. There has been significant progress in the designation of national managing authorities, in project selection and in the financial implementation of the 2014 to 2020 programmes.

Subheading 1b includes a new Structural Reform Support Programme (SRSP). Created in 2017, and designed to support institutional, administrative and growth-sustaining structural reforms in the Member States, the programme has quickly proven to be highly popular. Its initial budget amounting to €142.8 million over the 2017 to 2020 period (deducted from existing technical assistance resources under the ESI funds) was exhausted already in the course of 2018 (24 countries benefiting from the scheme). Therefore, it was agreed to mobilise the Flexibility Instrument and enforce the SRSP with additional €80 million until 2020. Out of this amount, €40 million will be mobilised for the SRSP in the 2019 budget.

In addition to the ESI funds, subheading 1b includes an allocation for the Youth Employment Initiative (YEI), which is specifically targeted at the regions most affected by youth unemployment, complementing other actions supported by the ESF. The continuation of the YEI, which was strongly supported by the European Parliament, was agreed in the framework of the mid-term revision of the MFF in 2017. In 2019, commitment appropriations for the YEI total €350 million, in line with Parliament’s reading of the budget and up from the €233 million initially proposed in the first draft budget. The specific allocation to the YEI, which is financed by the Global Margin for Commitments,

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118 European Parliament, Resolution on the proposal to increase the financial envelope of the Structural Reform Support Programme and adapt its general objective, Strasbourg, 11 September 2018.
is to be coupled by at least a corresponding amount financed from targeted investment from the ESF.119

**Box 3 – SMEs in the ESI funds**

SMEs are one of the key investment priorities under the ESI funds in the 2014 to 2020 MFF (see also Section 6.6.4). One of the key thematic objectives defined for spending in the framework of cohesion policy is dedicated to 'Enhancing the competitiveness of SMEs' (thematic objective 3) and amounts to €64.3 billion over the seven-year period (23 % of ESI funds). This, coupled with the national co-financing of projects, makes for a total amount of €96.4 billion to be invested in European SMEs. The EU contribution to this goal is financed from the European Regional Development Fund (52.7 %) (subheading 1b) and from the European Agricultural Fund for Rural Development (43.2 %) and European Maritime and Fisheries Fund (4.1 %) (the last two under heading 2).

Support for SMEs is also implemented under other thematic objectives, in particular 'low-carbon economy' and 'research and innovation'. The European Social Fund contributes to SME growth under thematic objectives 'educational and vocational training', 'sustainable and quality employment' and 'social inclusion'.

The ESI funds support SMEs operating on different markets and various sectors, including the agricultural, fishery and aquaculture sectors. Support can be granted for a broad variety of actions affecting SMEs, from investments in equipment, small-scale infrastructure (including in the area of culture and tourism), technology and research to networking, exchange of experience, studies and capacity-building and entrepreneurship, education and vocational training. This is done for example in form of grants, loans, advisory services and financial instruments. According to European Commission data, under the thematic goal 'Competitiveness of SMEs' alone 816 754 enterprises will have been supported over the 2014 to 2020 period.120

**Figure 12 – Heading 2 Sustainable growth: natural resources, 2018 commitment appropriations**

<table>
<thead>
<tr>
<th>43191.9</th>
<th>14727.3</th>
<th>1772.9</th>
</tr>
</thead>
<tbody>
<tr>
<td>EAGF (European Agricultural Guarantee Fund — Market related expenditure and direct payments)</td>
<td>EAFRD (European Agricultural Fund for Rural Development)</td>
<td>other</td>
</tr>
</tbody>
</table>

Data source: European Commission, see above and Annex 3.

Heading 2 finances the common agricultural policy, which focuses on three priorities for the 2014-2020 period: viable food production; sustainable management of natural resources; and balanced development of rural areas throughout the EU. The two funding tools available for these objectives are the European Agricultural Guarantee Fund (EAGF), which deals with market measures and direct payments, and the European Agricultural Fund for Rural Development (EAFRD), which is one of the five European structural and investment (ESI) funds.

In addition, heading 2 covers EU expenditure on common fisheries policy and environmental measures, by means of such instruments as the European Maritime and Fisheries Fund (EMFF), which is also an ESI fund, and the LIFE programme for environment and climate measures. Most of

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120 European Commission, Cohesion Data, January 2019.
the 2019 budget includes pre-programmed commitments for market measures, direct payments, rural development and fisheries programmes. The EAFRD and the EMFF include initiatives that support SMEs operating in the agricultural and maritime sectors (see Box 3).

In comparison with 2018, total commitments for heading 2 are stable (+0.7%). According to the Commission, the market situation does not require any exceptional support and the implementation of the direct payments to farmers is back to normal after temporary delays in the initial stage. The implementation of the rural development measures under the EAFRD has reached cruising speed, and the EMFF, which was slow at the beginning of the current MFF, is now accelerating. In addition, the allocation agreed under heading 2 includes €15 million in EU support for Member States affected by African swine fever.121

The objectives of the LIFE programme, updated after the mid-term evaluation, will be more concentrated on financing of nature and biodiversity and the mitigation of climate change.122 The programme will be reinforced, with €35.5 million more than in 2018 (+6.7%). This is in line with the Parliament’s insistence on reaching the target of 20% climate-relevant spending over the 2014-2020 period. Private entities, including SMEs can be beneficiaries of the LIFE programme, for instance through the financial instruments offered in the framework of the natural capital financial facility and private finance for energy efficiency instruments.123

Figure 13 – Heading 3 Security and citizenship, 2018 commitment appropriations

![Figure 13](Image)

Data source: European Commission, see above and Annex 3.

Heading 3 is the smallest in the 2014 to 2020 MFF, but finances EU actions of high and growing importance in policy areas such as border control, migration and asylum, public health, consumer protection, culture, information and dialogue with citizens. The biggest funds under this heading are the Asylum, Migration and Integration Fund (AMIF) and the Internal Security Fund (ISF). An important part of heading 3 is allocated to the EU decentralised agencies. Among them in particular the European Border and Coast Guard Agency (Frontex) and the European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice (eu-LISA).

Addressing the challenges of migration, border management and security is one of the financing priorities in the 2019 budget. This is expressed in the 8.4% increase in the allocation under heading 3 in comparison with the 2018 budget. The total approved commitment appropriations of around €3.8 billion exceed by €985.6 million the annual ceiling set in the MFF for the heading. As in 2018, this gap, representing around one quarter of expenditure under heading 3, had to be financed from the

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123 For more see: LIFE financial instruments, European Commission [accessed on 17 January 2018].
Flexibility Instrument. This would have not been possible without the reinforcement of the special and flexibility instruments agreed in the mid-term revision of the MFF in 2017 (see Section 3.4).

The Flexibility Instrument will cover the financing of such actions as emergency assistance, relocation, resettlement, integration of refugees and asylum-seekers, and the return of those not entitled to international protection. Additional resources will be spent on the European Border and Coast Guard, the EU Agency for Asylum, and other agencies dealing with border and visa issues. As a result, the Commission estimates that €2.3 billion in total under heading 3 will be required in order to address the challenges of migration and security issues (the external dimension of these policy areas is financed under heading 4).

The remaining part of heading 3 is dedicated to different programmes promoting justice, citizens’ rights, democracy, health, consumer protection and culture. Among them, in line with the Parliament’s reading of the budget proposal, the Creative Europe programme will receive €14.5 million more than in the 2018 budget (see Box 4).

**Box 4– Creative Europe support SMEs**

The Creative Europe programme is the only EU programme focusing exclusively on cultural and creative activities and enterprises and has been successfully implemented since 2014. Among the most important beneficiaries of the programme are SMEs in the audiovisual, media and cultural sectors. Since July 2016, apart from non-refundable grants, the Creative Europe supports SMEs through financial instruments. The Cultural and Creative Sector Guarantee Facility (CCS GF), implemented by the European Investment Fund, improves financial capacity of micro, small and medium-sized businesses offering them affordable debt financing. The CCS GF initial budget of €121 million for years 2014-2020 was increased with €60 million allocation from the EFSI and is expected to leverage €692 million in loans and other financial products for about 10 000 SMEs in the cultural and creative sectors.

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allocations go to the Development Cooperation Instrument (DCI), European Neighbourhood Instrument (ENI) and Instrument for Pre-accession assistance (IPA II).126

Expenditures secured under heading 4 in 2019 will continue to support development cooperation (73.2 % of the allocation) and humanitarian aid (14.6 %). In addition, most instruments under heading 4 contribute to addressing the external dimension of the migration challenges, by directly assisting the countries and communities hosting refugees and tackling the root causes of migration in the regions of origin.

Compared to the 2018 budget, there have been significant increases in the envelopes for the Instrument for Pre-accession assistance (IPA II) (+16.6 %) and Humanitarian aid (+52.2 %). They are mostly related to a decision to finance the second tranche of the Facility for Refugees in Turkey (€1 450 million)127 and the budgetary consequences of the pledges made to support humanitarian actions, development and resilience in Syria, Jordan and Lebanon (€560 million).128 In addition to this, the Union Civil Protection Mechanism (known as rescEU) has been increased by 46.1 % to provide funding for the expected uptake for actions following the Commission’s proposal to improve civil protection capabilities in third countries.129

The financial needs for actions covered in heading 4 exceeded the available margin and required the use of the Global Margin for Commitments for an amount of €1 051.3 million. As a result, heading 4 gets a significant boost of 12.4 % in comparison with the 2018 budget. Accordingly, its share in total commitment appropriations agreed for 2019 increases from 6.0 to 6.8 %.

In line with the decision included in the 2018 budget, the budgetary authority decided to reduce the pre-accession funds for Turkey. As the situation continues to deteriorate in terms of democracy, rule of law and human rights, the financial planning was revised downwards by €146.7 million.130

Figure 15 – Heading 5 Administration, 2018 commitment appropriations

Data source: European Commission, see above and Annex 3.

Heading 5 covers the administrative expenditure of all EU institutions, pensions for former staff and former Members of the institutions, as well as financing for European schools. The share of the budget allocated to this heading remains stable at 6 % of the total commitments, the same level as in 2018.

126 In addition to the programmes and funds allocated under heading 4, EU Member States also provide financial support for third countries and regions through the European Development Fund (EDF). This intergovernmental fund, however, is not part of the EU budget.

127 The total EU budget contribution to the second tranche of the FRT amounts to €2 billion. Of this, an initial amount of €550 million was financed under the 2018 budget, based on Amending Budget 3/2018 and from the existing Humanitarian Aid budgetary envelope.

128 Brussels conference ‘Supporting the future of Syria and the region’ in April 2018.


The 2019 budget for the EU administration reflects the strict measures that have been taken to ensure that this category of expenditure integrates all possibilities for rationalisation and savings. Drivers of the 2.9% increase in appropriations in comparison to the previous year include the increase in the pensions bill for former staff and Members (with a growing number of pensioners expected).131

4.3. Scrutiny of EU spending: procedures in the European Parliament

In accordance with the cycle of scrutiny of the EU annual budget, the management and execution of the 2019 budget will be evaluated during the course of 2020 and 2021 (Figure 16). The procedure will begin in the middle of 2020 after adoption of final accounts by the European Commission (stage A), and finish with a decision of the European Parliament adopted before 15 May 2020 (stage D) or in October 2020 in case of postponement (stage E).132

In 2019, the European Parliament is expected to take a discharge decision on the 2017 financial year. The ongoing discharge procedure is at the stage of hearings with respective commissioners and representatives of EU institutions and bodies, conducted by the European Parliament’s Budgetary Control Committee (CONT) (stage C). Following this stage, and after receiving the Council recommendation on the discharge, the European Parliament is expected to take its decision by mid-May (stage D). However, with the European elections taking place in May, this year the decision will have to be taken by April, most likely at the last plenary session of the current Parliament.133

The European Parliament is also responsible for initiating the next discharge procedure in 2019, covering the 2018 budgetary year. The procedure will begin with the publication of a series of budgetary reports and evaluations by the European Commission. Following this stage, the European Court of Auditors (ECA) will present its annual report with the statement of assurance (DAS)134 on the implementation of the 2018 financial year. In addition, in the course of 2019, the ECA will publish various special reports and other products on topics selected on the basis of its assessment of the main risks to EU spending and policy delivery. The five priority areas identified by the ECA for its 2019 work programme are: sustainable use of natural resources and addressing climate change; investment for cohesion, growth and inclusion; migration, security and global sustainable development challenges; functioning single market and sustainable monetary union; and financing and administering the Union accountably and efficiently.135

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132 The discharge procedure is based on Articles 317 to 319 of the Treaty on the Functioning of the EU. The timeframe of the procedure is determined in the Financial Regulation, in particular Articles 258 to 263. Regulation (EU, Euratom) 2018/1046 of 18 July 2018.
133 The discharge procedure for the 2017 financial year can be followed on the European Parliament’s Budgetary Control Committee website.
134 The statement of assurance (known as the DAS) is the official opinion issued by the ECA on the reliability of the accounts and on the legality and regularity of the underlying transactions (Article 287 TFEU and Article 148 Financial Regulation).
135 For the list of high priority and priority topics to be covered by the ECA in 2019, please see the ECA 2019 Work Programme.
The European Parliament plays a crucial role in the democratic scrutiny and control of the implementation of the EU budget. Within the annual discharge procedure it not only signs off the financial year, but also makes recommendations for improving the financial management and implementation of the EU budget. After receiving a recommendation from the Council, it ascertains whether the European Commission upheld the principles of sound financial management, and abided by the applicable rules and regulations when implementing the budget. The Parliament grants separate discharge to the other EU institutions for the management of their sections of the general budget, and to the decentralised agencies and joint undertakings for their budgets.

Apart from scrutinising the regularity and legality of the budget’s implementation, the discharge procedure increasingly focuses on performance culture, performance information and achievement of goals. The principles of performance orientation have gradually permeated many aspects of the management, implementation and control of the EU budget. Since 2015, the principles have been included in the Commission’s ‘EU budget focused on results’ initiative. This wider approach to the assessment of EU spending is strongly supported by the European Parliament and the ECA. Many of the improvements introduced so far in this respect were triggered by opinions and demands expressed during the budgetary discharge procedure, for instance in the ECA’s annual and special reports and the European Parliament’s resolutions.

The possibility to accelerate the discharge procedure and close it within the year following the accounting year in question (N+1) is a longstanding demand of the CONT committee. However, the revision of the EU’s Financial Regulation adopted in July 2018 did not introduce any significant changes that could shorten the time lag between the implementation of the budget and its political scrutiny.

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**Figure 16 – EU discharge procedure from the perspective of the European Parliament**

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<td><strong>A</strong></td>
<td><strong>B</strong></td>
<td><strong>C</strong></td>
<td><strong>D</strong></td>
<td><strong>E</strong></td>
</tr>
<tr>
<td>COMMISSION</td>
<td>ECA</td>
<td>HEARINGS</td>
<td>EP</td>
<td>IF POSTPONEMENT</td>
</tr>
<tr>
<td>by 31 Jul n+1</td>
<td>by 15 Nov n+1</td>
<td>between B and Jan n+2</td>
<td>by 15 May n+2</td>
<td>Oct n+2</td>
</tr>
</tbody>
</table>

**COMMISSION**
Commission adopts final accounts and a synthesis report on its management activities.

**ECA**
ECA transmits its annual reports including the statement of assurance (DAS).

**HEARINGS**
Hearings of Commissioners and senior officials from EU institutions and bodies before EP’s Budgetary Control (CONT) Committee.

**EP**
EP decides whether to grant or postpone discharge (following Council’s adoption of its recommendation).

**IF POSTPONEMENT**
EP decides whether to grant or refuse discharge.

Source: EPRS.

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137 For the methods of implementation of the EU budget please see Section 3.3.

5. EU budget in the medium and long term

The current MFF sets out the structure for EU spending up until 2020. In 2019, negotiations on the next programming period are expected to advance further and possibly result in an agreement by the end of the year. The expected withdrawal of the UK from the EU means that the negotiations are taking place against a different background from the one that characterised the current MFF.

5.1. The final year of the 2014-2020 MFF and the expected withdrawal of the UK from the EU

Table 2 compares commitments in the adopted EU budget for 2019 and the ceilings available for each heading in the remaining year of the current MFF. The figures in bold highlight the categories of spending for which the budgetary authority resorted to special instruments (the Flexibility Instrument and the global margin for commitments) when adopting the 2019 budget: subheading 1a ‘Competitiveness for growth and jobs’, subheading 1b ‘Economic, social and territorial cohesion’, heading 3 ‘Security and citizenship’ and heading 4 ‘Global Europe’. In 2020, pressure on the expenditure ceilings may be expected to recur for some of these categories, in particular ‘Security and citizenship’, which receives around one quarter of its 2019 financing from special instruments (repeating what happened in 2018).

Table 2 – EU 2019 budget commitments and 2020 MFF ceilings by heading (€ million, current prices)¹³⁹

<table>
<thead>
<tr>
<th>Heading/subheading</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>1a Competitiveness for growth and jobs</td>
<td>23 335</td>
<td>25 191</td>
</tr>
<tr>
<td>1b Economic, social and territorial cohesion</td>
<td>57 192</td>
<td>58 470</td>
</tr>
<tr>
<td>2 Sustainable growth: natural resources</td>
<td>59 642</td>
<td>60 421</td>
</tr>
<tr>
<td>3 Security and citizenship</td>
<td>3 786</td>
<td>2 951</td>
</tr>
<tr>
<td>4 Global Europe</td>
<td>11 319</td>
<td>10 510</td>
</tr>
<tr>
<td>5 Administration</td>
<td>9 943</td>
<td>11 254</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>165 218</td>
<td>168 797</td>
</tr>
</tbody>
</table>

Data source: European Commission, DG Budget.

An issue that was particularly difficult during the final period of the previous MFF and the beginning of the current one was that of unpaid claims¹⁴⁰ at the end of the year. An intense interinstitutional dialogue to tackle the problem resulted in the decision to resort to the MFF flexibility provisions and to improve the forecasting and management of payment needs, which helped to normalise the year-end backlog.¹⁴¹

¹³⁹ The total for 2019 is lower than the overall appropriations for the 2019 EU budget, since it does not include the instruments that are outside the MFF ceilings.

¹⁴⁰ At the worst point, in 2014, the level of payment backlog was estimated at some €26 billion. Most of this was accumulated under subheading 1b ‘Economic, social and territorial cohesion’, but some serious problems also occurred under the Erasmus and research programmes, and neighbourhood and humanitarian aid programmes. For a thorough analysis of the problem see: A. D’Alfonso and M. Sapala, Payments backlog in in recent EU budgets. Lessons learnt and outlook, EPRS, European Parliament, November 2015.

¹⁴¹ It is worth noting that forecasting the payments, especially in Heading 1b is very difficult. The Commission estimates that in this heading a +/- 1% of change in the pace of implementation leads to a +/- €4 billion change in payment...
However, this challenge may recur in the coming years. Although the pressure on payments has decreased significantly, this is also due to the delayed start and slow implementation of the 2014-2020 programmes, especially in cohesion policies. In fact, at the end of the fifth year of the current programming period (i.e. in December 2018), only 27% of the €461 billion of investments planned under the 2014 to 2020 European Structural and Investment Funds (ESIF) had actually been disbursed. This suggests that payment claims will again tend to be concentrated in the final years of the current MFF and the first years of the next one.

While the mid-term revision of the MFF is helping to address possible problems (see Section 3.4), close monitoring of payment needs will nevertheless be needed so as to avoid a repeat of abnormal payments backlogs at year-end, as stressed by Parliament, Council and Commission in a joint declaration accompanying the 2019 EU budget. Expressing its concern about the under-execution of payments in cohesion expenditure over the last three years, Parliament has urged Member States to accelerate the implementation of relevant programmes to catch up with delays.

A factor that may have an impact on the EU budget by 2020 and/or beyond is the expected withdrawal of the United Kingdom (UK) from the EU. Following the triggering of the Article 50 procedure by the UK in 2017, its EU membership should cease as from 30 March 2019.

The unprecedented request of one Member State to withdraw from the EU has posed the challenge of disentangling the ongoing financial liabilities of the withdrawing country from those of the other 27 Member States, which will continue to honour their obligations through the mechanisms agreed to this effect. The settlement of the UK’s financial obligations towards the EU was one of the three priorities identified for the first phase of the negotiations on the withdrawal agreement.

During the negotiations, the UK has agreed to honour its share of the financing of all the obligations undertaken during its EU membership. Among other points, this implies in relation to the EU budget and the 2014-2020 MFF that the UK ‘will contribute to, and participate in, the implementation of the EU annual budgets for the years 2019 and 2020 as if it had remained in the Union. It will also contribute its share of the financing of the budgetary commitments outstanding on 31 December 2020 (i.e. reste à liquider) as well as its share of the financing of the Union’s liabilities incurred before 31 December 2020, except for liabilities with corresponding assets. In addition, the United Kingdom will remain liable for its share of the EU’s contingent liabilities as established at the date of withdrawal’.

Chapter 2 of the Withdrawal Agreement translates the conclusions on the financial settlement reached during the first phase of the negotiations into legal provisions. In practice, the Agreement, if approved by the UK House of Commons and the European Parliament, should result in the UK withdrawal having no impact on the 2019 and 2020 EU budgets. Neither would the overall 2014-


European Structural and Investment Funds, Data portal, data consulted on 3 January 2019.

2019 general budget: all sections, Legislative Observatory (OEIL), European Parliament.


The MFF and the annual EU budget are immediate examples of financial liabilities to be disentangled, but the landscape of financial obligations jointly undertaken by EU Member States is broader and more complex than that. For more details, please see A. D’Alfonso, E.-M. Poptcheva, J. McEldowney and L. Tilindyte, The Brexit negotiations: Issues for the first phase, EPRS, European Parliament, June 2017.

2020 MFF be affected. The UK Treasury has estimated the total amount of the financial settlement at €40-45 billion, which would be paid over a number of years.

Should the EU-UK joint committee in charge of implementing and applying the Withdrawal Agreement agree an extension of the transition period by one or two years (i.e. up to 31 December 2021 or 2022), the UK will make a contribution to the EU budget during the extended period of the transition for an amount to be determined by the joint committee itself.

In December 2018, given the uncertainty surrounding the approval of the Withdrawal Agreement in the UK House of Commons, both the EU and the UK stepped up work on preparedness for the consequences of the UK withdrawal, taking into account all possible outcomes. With regard to the EU budgets 2019 and 2020, the European Commission said that it would propose the continuation of the PEACE and INTERREG programmes that promote cross-border cooperation between the Republic of Ireland and Northern Ireland even in the event of a withdrawal without a deal (no-deal scenario).

The Commission communication does not provide any further details on the possible consequences of a no-deal scenario for the 2019 and 2020 EU budgets and related responses. The Bruegel think tank estimates that, should the UK not honour its financial obligations, the missing resources for the EU budget would amount to up to €16.5 billion until the end of 2020, but suggests that the margin available under the current own resources ceiling could cover this gap.

As regards the next generation (post-2020) of EU programmes, the possibility of UK participation in some of them remains to be seen and could be discussed during the negotiations on the future EU-UK relationship that should take place during the transition period. Preparations of the proposals for the next MFF have factored in the expected withdrawal of the UK from the EU (see Sections 5.2 and 5.3).

5.2. The preparation of the proposals for the post-2020 MFF

The debate on the post-2020 MFF and possible reform of the EU budget began at the very beginning of the current programming period. Unsatisfied with the limited changes to the EU’s financing system agreed by the European Council in 2013, the European Parliament included the creation of an interinstitutional High-Level Group on Own Resources (HLG) among the conditions to give its consent to the 2014 to 2020 MFF regulation. The HLG, which was created by Parliament, Council and Commission already in 2014, reviewed not only the revenue side of the budget, but also EU expenditure, stressing how closely related the two aspects are. Presenting its final report in January 2017, the HLG recommended in-depth reform of both revenue and expenditure to increase the ability of the EU budget to respond to priorities.
Confirming its salience, the reflection on the next MFF has become part of the broader debate on the future of the EU, which was kick-started by the Bratislava Declaration agreed by 27 EU Heads of State and Government in the wake of the UK referendum, a Commission White paper and the Rome Declaration adopted on the 60th anniversary of the Treaties of Rome. This development reflects the deeply political nature of the MFF, which translates agreed EU policy priorities into budgetary figures.

The expected withdrawal of the UK from the EU means that the preparations of the proposal for the next MFF took place against a different backdrop, which a number of analysts have identified as an opportunity for broader reform of the EU budget. Over the years, critics of the current EU financing system have often argued that its complexity and opacity also result from the UK rebate and other correction mechanisms that hinder the reform of both the revenue and the expenditure sides of the EU budget.

While the proposal for the post-2020 MFF was originally due by December 2017, the European Commission decided to postpone it until mid-2018. Various contributions have fed the preparation of the next MFF, including important mid-term evaluations on a number of EU sectoral policies and spending programmes, such as the seventh cohesion report published in October 2017.

The June 2017 reflection paper on the future of EU finances, which the European Commission presented as part of the wider debate on the future of the EU, made a significant input to the process. Taking into account the conclusions and recommendations of the HLG on own resources, the document identifies the key principles that should drive any reform, irrespective of the way forward that the EU decides to pursue. In particular, these principles are: 1) concentrating resources on the policy areas with the highest EU added value, selected through criteria such as Treaty objectives and obligations, economies of scale, and public goods with a EU dimension; 2) continuing simplification efforts with a view to further streamlining implementation; 3) keeping the creation of tools outside the EU budget to a minimum so as to ensure democratic accountability and transparency; and 4) strengthening the flexibility provisions with a view to reducing the rigidity inherent in a framework covering many years. The reflection paper adds that, with the withdrawal of the UK from the EU, the revenue side of the budget should be simplified by eliminating all current correction mechanisms. The text concludes that the EU will certainly change after 2020, and that its budget will evolve accordingly, depending on the path that is chosen for the future of the EU.

In February 2018, the European Commission produced its contribution to an informal European Council, illustrating the financial impact of various possible policy choices that had been evoked in the vivid debate surrounding the next MFF. The text estimated the resources that the EU budget would need in domains such as external border control, defence, mobility of young people, digital

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156 For example, this criticism has been expressed on many occasions by the European Parliament (e.g. legislative resolution of 16 April 2014 on the draft Council decision on the system of own resources of the European Union legislative resolution and by the European Court of Auditors (e.g. Opinion No 4/2005).  

157 See for example: F. Zuleeg, Britain outside Europe? Fewer EU concessions to UK post-Brexit, European Policy Centre, 2014; and Q. Peel, ‘A fair deal demands that Britain rethink the rebate’, Financial Times, 8 December 2005.

158 Initially, the proposal was due before 1 January 2018 on the basis of Article 25 of the MFF Regulation.


transformation, research and innovation, economic and monetary union, agriculture and cohesion under different policy options. In addition, the Commission outlined ways to modernise the EU budget, for example by streamlining the use of financial instruments and promoting a stronger link between EU resources and respect for the EU’s fundamental values.\textsuperscript{161}

EU institutions have contributed ideas and views to the discussion on various occasions. Following its first official reaction to the reflection paper,\textsuperscript{162} the European Parliament detailed its input on both the expenditure and revenue sides of the post-2020 EU budget ahead of the Commission’s proposals.\textsuperscript{163} In a briefing note on the mid-term review of the MFF, the European Court of Auditors made a number of recommendations on the preparation of the post-2020 framework.\textsuperscript{164} The European Committee of Regions, meanwhile, presented its opinion on the reform of the financing system of the EU and commissioned a study on key challenges and opportunities for cities and regions.\textsuperscript{165}

In addition, the European Commission consulted stakeholders, including all Member States, on their expectations for the next MFF, with a view to preparing a balanced proposal that was both ambitious and realistic. EU leaders held a debate on political priorities for the new MFF at an informal European Council meeting on 23 February 2018.

As regards the possible impact on the EU budget of the UK withdrawal from the Union, European Commissioner Günther H. Oettinger in charge of Budget and Human Resources has quantified it in lower resources for the budget amounting to €12-15 billion per year. He suggested that part of this gap be covered by fresh resources and the remainder by cuts to expenditure.\textsuperscript{166}

Many other stakeholders are involved in the debate. There is general agreement that the EU budget needs reform. A focus on results, leverage, synergies, conditionality and European added value is often mentioned among the principles that should underpin any changes. Stakeholders from academic, expert and political circles underline that in a rapidly evolving world, the design of the EU budget has to ensure the right balance between predictability of investments and capacity to respond to new challenges and priorities. The problems that the current MFF has faced demonstrate how difficult the task is, and the weaknesses of the EU financing system.\textsuperscript{167}

The main issues for consideration and possible modifications that have emerged from the debate include: the own resources system; the size, structure and priorities of the MFF; its duration; its flexibility provisions; the unity of the budget (following the recent proliferation of instruments at


\textsuperscript{163} European Parliament, Resolution on the next MFF: Preparing the Parliament’s position on the MFF post-2020, Strasbourg, 14 March 2018; and Resolution on reform of the European Union’s system of own resources, Strasbourg, 14 March 2018.


\textsuperscript{165} European Committee of Regions, Reform of EU own resources within the next MFF post-2020, COTER-VI/026, 125th plenary session; J. N. Ferrer, D. Rinaldi, A. Hassel, M. Nesbit, A. Illes and K. Paque, Key challenges and opportunities for Cities and Regions and MFF post 2020, 2017.


least partially outside the budget); the streamlining of financial instruments; the role of the budget in EU economic governance and respect for the rule of law; and the creation of instruments with a stabilisation function for the euro area (see Section 3.4).

5.3. Proposals for the 2021-2027 MFF and its financing

In May and June 2018, the European Commission presented its package of proposals for the next MFF, the related implementing programmes and a reform of the own resources system. The package is designed for a Union with 27 Member States on account of the expected withdrawal of the UK (see Section 5.1). The proposed MFF covers the 2021 to 2027 period and its commitments amount to €1 134.5 billion in constant 2018 prices, which corresponds to 1.11 % of EU27 GNI (i.e. with UK GNI subtracted). Payment appropriations are set at €1 104.8 billion (1.08 % of EU27 GNI).

Table 3 provides an overview of the MFF proposal and its new structure, comparing it with expenditure in the current period after deduction of the amounts related to the UK. The main issues for consideration to have emerged in the MFF debate ahead of the proposals are discussed below.169

- Duration – the European Commission has again proposed a seven-year framework, which is not aligned to the five-year political cycle of the European Commission and the European Parliament. Ideas for changes include a five-year MFF synchronised with the political mandates of these two EU institutions; five + five years with a compulsory mid-term review; and ten years with compulsory mid-term revision for programmes requiring long-term programming and five years for the others.

- Unity of the budget – the Commission has proposed to bring the European Development Fund (EDF), an intergovernmental tool for development cooperation with the African, Caribbean and Pacific Group of States (ACP), into the EU budget and the MFF.

- Size – according to the Commission, the total resources are broadly similar to the current programming period in real terms, when taking into account the inclusion of the EDF into the EU budget.170 The expected withdrawal of the UK makes comparisons harder than in previous negotiations and the conclusions depend on the perspective adopted (e.g. amounts in constant or current prices, with or without the UK). For example, when deducting the amounts relating to the UK in the current period, the proposal represents a 5 % increase in absolute figures, but a decrease from 1.16 % to 1.11 % as a share of EU27 GNI. In any case, total allocations are well below 1.3 % of EU27 GNI, the level estimated necessary by Parliament for the EU to address all its priorities and objectives.

- Structure and priorities – the Commission is proposing a new structure with seven headings instead of six, with a view to aligning the presentation and nomenclature of the budget to an evolving set of EU priorities (see Table 3). Two separate headings are created for policy areas that have played a major role in the EU debate in recent years: ‘Migration and border management’ and ‘Security and defence’. Within headings, expenditure is presented around 17 policy clusters, including ‘European public administration’. An increase in resources is planned for activities related to various domains such as: research, innovation and digital transformation;

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168 Or €1 279 billion in current prices that take into account a 2 % annual inflation rate.
169 Some of these elements do not come from the draft MFF regulation, but from other proposals in the package. For other details, see: M. Parry and M. Sapala, 2021-2027 multiannual financial framework and new own resources: Analysis of the Commission’s proposal, EPRS, European Parliament, 2018; and A. D’Alfonso, Multiannual financial framework for the years 2021 to 2027, EPRS, European Parliament, (forthcoming).
young people; external border control; security; defence; migration; and external action. According to the European Commission, 80% of these reinforcements would come from fresh resources, while redeployments from other policy areas would provide the remaining 20%. In this respect, traditional policies such as agriculture and cohesion would see their resources decrease by around 15% and 11%, respectively (in constant prices). In addition, some EU instruments would move to a different heading as compared to the current MFF. This change has implications for the flexibility of the framework since shifting resources is easier within headings than between them.

Flexibility – various elements of the proposals seek to ensure that the MFF is able to tackle rapidly unforeseen events and needs, by reinforcing its flexibility. Examples are provisions to increase the possibility to move resources between headings and financial years, as well as within and between individual programmes. Unallocated margins under the headings are in general higher than in the current MFF. In addition, higher annual amounts would be available for special instruments outside the MFF ceilings, including the Flexibility Instrument, the European Union Solidarity Fund and the Emergency Aid Reserve. The scope of the latter would be extended to cover also emergencies within the EU. The transformation of the Global Margin for Commitments into a Union reserve would increase the possibilities to resort to unused margins and decommitted resources from previous financial years.

Simplification – the number of implementing programmes would be significantly reduced from 58 to 37, in an effort to increase efficiency of spending and streamline fragmented sources of funding. In this spirit, for example, the InvestEU programme would cover loans, guarantees and other innovative financial instruments currently dispersed across various programmes, with a view to maximising economies of scale, providing a single set of requirements and eliminating overlaps. In addition, the Commission aims to promote further simplification in implementing rules, with the objective of having a single rule book for resources implemented under direct, indirect and shared management to the extent possible.

The creation of specific instruments for economic and monetary union (EMU) – against the background of the debate on a possible fiscal capacity with a stabilisation function for the euro area (see Section 3.4), the Commission has proposed the establishment of two new instruments aimed at contributing to a stable and resilient EMU. Endowed with €25 billion and included under the ‘Cohesion and values’ heading of the new MFF, a reform support programme has been designed to offer financial and technical support to Member States that carry out key reforms to increase national resilience, especially in the context of the European Semester. Outside the MFF, a European investment stabilisation function (EISF) would provide a tool to help euro-area and European exchange rate mechanism-participating Member States stabilise investment levels in the event of large asymmetric shocks. The EISF would play this role by means of a mechanism capable of disbursing loans guaranteed by the EU budget (for a total amount of up to €30 billion for the 2021 to 2027 period).

Stronger link between the budget and the respect for the rule of law – a new mechanism would suspend, reduce or restrict access to EU funds if general deficiencies to the rule of law put at risk their sound financial management or the financial interests of the EU. The mechanism is designed to not affect final beneficiaries of the funds, since Member States remain responsible for implementing the programmes.

As regards defence, the Commission is also proposing a European peace facility that would be endowed with €9.2 billion over the 2021 to 2027 period.
Table 3 – Proposal for the 2021-2027 multiannual financial framework (commitments, 2018 prices, € million)

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<tbody>
<tr>
<td>1. Single market, innovation and digital</td>
<td>116 361</td>
<td>11.0 %</td>
<td>166 303</td>
<td>14.7 %</td>
<td>+43 %</td>
<td></td>
</tr>
<tr>
<td>1. Research and innovation</td>
<td>69 787</td>
<td>6.4 %</td>
<td>91 028</td>
<td>8.0 %</td>
<td>+30 %</td>
<td></td>
</tr>
<tr>
<td>2. European strategic investments</td>
<td>31 886</td>
<td>2.9 %</td>
<td>44 375</td>
<td>3.9 %</td>
<td>+39 %</td>
<td></td>
</tr>
<tr>
<td>3. Single market</td>
<td>5 100</td>
<td>0.5 %</td>
<td>5 672</td>
<td>0.5 %</td>
<td>+11 %</td>
<td></td>
</tr>
<tr>
<td>4. Space</td>
<td>11 502</td>
<td>1.1 %</td>
<td>14 404</td>
<td>1.3 %</td>
<td>+25 %</td>
<td></td>
</tr>
<tr>
<td>Margin</td>
<td>-1 913</td>
<td></td>
<td>10 824</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Cohesion and values</td>
<td>387 250</td>
<td>35.8 %</td>
<td>391 974</td>
<td>34.5 %</td>
<td>+1 %</td>
<td></td>
</tr>
<tr>
<td>5. Regional development and cohesion</td>
<td>272 647</td>
<td>25.2 %</td>
<td>242 209</td>
<td>21.3 %</td>
<td>-11 %</td>
<td></td>
</tr>
<tr>
<td>6. Economic and monetary union</td>
<td>273</td>
<td>&lt;0.1%</td>
<td>22 281</td>
<td>2.0%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Investing in people, social cohesion and values</td>
<td>115 729</td>
<td>10.7%</td>
<td>123 466</td>
<td>10.9%</td>
<td>+7%</td>
<td></td>
</tr>
<tr>
<td>Margin</td>
<td>-1 399</td>
<td></td>
<td>4 018</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Natural resources and environment</td>
<td>399 608</td>
<td>36.9 %</td>
<td>336 623</td>
<td>29.7%</td>
<td>-16%</td>
<td></td>
</tr>
<tr>
<td>8. Agriculture and maritime policy</td>
<td>390 155</td>
<td>36.0 %</td>
<td>330 724</td>
<td>29.1%</td>
<td>-15%</td>
<td></td>
</tr>
<tr>
<td>9. Environment and climate action</td>
<td>3 492</td>
<td>0.3%</td>
<td>5 085</td>
<td>0.4%</td>
<td>+46%</td>
<td></td>
</tr>
<tr>
<td>Margin</td>
<td>5 960</td>
<td></td>
<td>814</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Migration and border management</td>
<td>10 051</td>
<td>0.9 %</td>
<td>30 829</td>
<td>2.7%</td>
<td>+207%</td>
<td></td>
</tr>
<tr>
<td>10. Migration</td>
<td>7 180</td>
<td>0.7%</td>
<td>9 972</td>
<td>0.9%</td>
<td>+39%</td>
<td></td>
</tr>
<tr>
<td>11. Border management</td>
<td>5 492</td>
<td>0.5%</td>
<td>18 824</td>
<td>1.7%</td>
<td>+243%</td>
<td></td>
</tr>
<tr>
<td>Margin</td>
<td>-2 621</td>
<td></td>
<td>2 033</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Security and defence</td>
<td>1 964</td>
<td>0.2%</td>
<td>24 323</td>
<td>2.1%</td>
<td>+1 138%</td>
<td></td>
</tr>
<tr>
<td>12. Security</td>
<td>3 455</td>
<td>0.3%</td>
<td>4 255</td>
<td>0.4%</td>
<td>+23%</td>
<td></td>
</tr>
<tr>
<td>13. Defence</td>
<td>575</td>
<td>0.1%</td>
<td>17 220</td>
<td>1.5%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>14. Crisis response</td>
<td>1 222</td>
<td>0.1%</td>
<td>1 242</td>
<td>0.1%</td>
<td>+2%</td>
<td></td>
</tr>
<tr>
<td>Margin</td>
<td>-3 289</td>
<td></td>
<td>1 606</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Neighbourhood and the world</td>
<td>96 295</td>
<td>8.9%</td>
<td>108 929</td>
<td>9.6%</td>
<td>+13%</td>
<td></td>
</tr>
<tr>
<td>15. External action</td>
<td>85 313</td>
<td>7.9%</td>
<td>93 150</td>
<td>8.2%</td>
<td>+9%</td>
<td></td>
</tr>
<tr>
<td>16. Pre-accession assistance</td>
<td>13 010</td>
<td>1.2%</td>
<td>12 865</td>
<td>1.1%</td>
<td>-1%</td>
<td></td>
</tr>
<tr>
<td>Margin</td>
<td>-2 027</td>
<td></td>
<td>2 913</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. European public administration</td>
<td>70 791</td>
<td>6.5%</td>
<td>75 602</td>
<td>6.7%</td>
<td>+7%</td>
<td></td>
</tr>
<tr>
<td>TOTAL commitments</td>
<td>1 082 320</td>
<td>100%</td>
<td>1 134 583</td>
<td>100.0%</td>
<td>+5%</td>
<td></td>
</tr>
<tr>
<td>In % of GNI (EU-27)</td>
<td>1.16%</td>
<td></td>
<td>1.11%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>TOTAL payments</td>
<td>1 104 805</td>
<td></td>
<td>1.08%</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: EPRS, based on annexes to the European Parliament resolution on the MFF of 14 November 2018.

In addition, as expected following the work of the interinstitutional High-Level Group on Own Resources, the MFF package includes proposals to reform the revenue side of the EU budget.\(^{172}\) Some of the main changes proposed by the Commission concern: 1) the streamlining of existing resources, through a simplification of the VAT-based resource and a reduction of the amounts that Member States retain as collection costs on customs duties; 2) the abolition of the UK rebate with that country’s expected withdrawal, and the phasing out of all other correction mechanisms; 3) the

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\(^{172}\) For a detailed overview, see: A. D’Alfonso, Own resources of the European Union: Reforming the EU’s financing system, EPRS, European Parliament, November 2018.
introduction of three new genuine own resources linked to EU policies on climate (part of the revenue stemming from the ETS, the existing EU emissions trading system), environment (a resource based on the quantity of non-recycled plastic packaging waste generated by Member States) and the single market (a resource assigning to the EU budget 3% of the taxable profits of a CCCTB, a common consolidated corporate tax base still to be introduced); and 4) the increase of the own resources ceiling for payments from 1.20% to 1.29% of EU GNI, which takes into account the inclusion of the EDF within the EU budget and the automatic reduction of total EU GNI that the expected withdrawal of the UK implies.

Based on European Commission data, Figure 17 shows how the proposal would modify the revenue mix, with 12% of total revenue expected to accrue from the three new own resources. The European Commission estimates that, once the changes proposed in the package are implemented, the GNI-based resource would provide 50-60% of total revenue, which is well above the 40% share that the European Parliament has advocated in various resolutions.

Figure 17 – Mix of EU revenue in 2018 and estimated average for 2021 to 2027 period

Source: A. D’Alfonso, Own resources of the European Union: Reforming the EU’s financing system, EPRS, European Parliament, November 2018.

5.4. Initial reactions to the proposals and the road to their adoption

The proposals for the next MFF and the own resources system have received a mixed response. They do not represent a radical redesign of the current provisions, but rather their evolution. Defining its package as pragmatic and modern, the European Commission appears to suggest that it has taken into account the extensive consultations carried out beforehand (see Section 5.2) to propose a degree of reform on which an agreement is deemed politically achievable.

Analysts and observers have differing views on the extent of the modifications that the proposals imply and their effectiveness. The Bruegel think tank gives a prudently positive assessment, noting the major constraints with which the European Commission was confronted in preparing the proposal. According to this analysis, the positive elements of the package include: higher allocations for policy areas that provide European public goods (border control, defence, research and innovation, digital sector, and migration); higher national co-financing for cohesion and rural

173 EU budget: Commission proposes a modern budget for a Union that protects, empowers and defends, press release, European Commission, 2 May 2018.
development; stronger flexibility provisions; an attempt to link the EU budget to respect for the rule of law; and the proposed changes to the revenue side. Conversely, the authors assess negatively other elements of the package, such as: insufficient efforts to simplify the budgetary system; a too limited increase in resources for external policies; and ineffective design of the two new instruments put forward to reinforce economic and monetary union.\(^\text{174}\)

According to a policy brief by the Jacques Delors Institute, the planned rebalancing of resources between traditional policies (agriculture and cohesion) and new priorities is more ambitious than in the Commission’s proposals for previous MFFs, but not radical. While recalling the various factors that make comparability with the size of the current MFF difficult, the authors conclude that the economic environment helps to smoothen the impact of the expected withdrawal of the UK. The document notes some conceptual innovations in spending programmes such as the streamlining of the use of financial instruments by means of the InvestEU programme. However, the proposed basket of new own resources is criticised as insufficiently bold when compared with the recommendations of the High-Level Group.\(^\text{175}\)

The European Policy Centre (EPC) assesses some developments as positive such as: increased resources for new priority areas, climate mainstreaming across all EU programmes with the target of devoting 25% of the MFF to climate-related objectives, the proposed abolition of all correction mechanisms on the revenue side, and the endeavour to tie the budget to respect for the rule of law in Member States. However, continuity is deemed to prevail and the author calls for more ambitious reform that, despite the limited size of the EU budget, would align its expenditure more closely to the Union’s principles and goals.\(^\text{176}\)

The CEPS think tank sees the proposed MFF as old-fashioned. Considering the novelties overall to be minor, the commentary points to elements of continuity such as the absence of provisions introducing national co-financing for income support to farmers in agricultural expenditure.\(^\text{177}\) In another commentary, the same think tank outlines the limitations of the EU budget, including the proposed European investment stabilisation function, in fulfilling a stabilisation role against economic shocks (see Section 3.1). The authors conclude that the Commission proposals do not provide a political process to identify stabilisation as a necessary component of EU expenditure.\(^\text{178}\)

In addition to the content of the next MFF, one factor that has attracted immediate attention is the timeline for the negotiations. While past experience has shown the complexity of the process, a new layer is added for the post-2020 MFF by the fact that 2019 marks the beginning of the new institutional cycle for various EU institutions, starting with the European Parliament elections at the end of May.

When presenting its MFF proposals in May 2018, the European Commission called for swift negotiations to take maximum one year, with a view to having an agreement before the European Parliament elections and the European summit in Sibiu in May 2019. It recalled the negative knock-on effect that late adoption of the current MFF had on the start of its implementation, pointing to the objective of avoiding a repeat of the situation. This timeline looked ambitious from the outset,


\(^\text{177}\) J. Núñez Ferrer and D. Gros The multiannual financial framework, where continuity is the radical response, CEPS, Commentary, 4 May 2018.

\(^\text{178}\) J. Núñez Ferrer and C. Alcidi, Should the EU budget have a stabilisation function?, CEPS, Commentary, 30 May 2018.
considering that it took around two and a half years to negotiate and adopt the MFF Regulation for the 2014 to 2020 period.\textsuperscript{179}

Work on the proposed package for the post-2020 MFF and own resources started soon after the Commission tabled it. On 30 May 2018, the European Parliament outlined its first reaction to the proposals in a resolution that reflected the mandates previously adopted on the topics (see Section 5.2), urging the Council to ensure that the next MFF endowed the EU with sufficient resources to deliver on its objectives and priorities.\textsuperscript{180} In the Council, the rotating presidencies started to steer the examination of the proposal at technical level.

The European Economic and Social Committee (EESC) and the Committee of the Regions (CoR) delivered their opinions, in September and October 2018 respectively.\textsuperscript{181} Both advisory committees welcomed a number of positive elements in the package, but were critical of the cuts proposed for cohesion and agriculture. They recommended that the EU budget should reach 1.3 % of EU-27 GNI to be able to tackle all EU objectives, in line with the position already expressed by the Parliament on the appropriate size of the post-2020 MFF. The EESC welcomed the investment support function envisaged for the InvestEU Fund, but considered that more resources would be needed to tackle the investment gap in the EU, while the new investment stabilisation mechanism proposed for the euro area was deemed unable to make a difference in the event of an asymmetric shock owing to its limited size. The EESC supported the timeline for the negotiations proposed by the Commission and the CoR urged EU institutions to reach a swift agreement.

In November 2018, the European Parliament stood ready to start negotiations with the Council following the adoption of a resolution that details its position.\textsuperscript{182} The text, which builds on previous resolutions that provided Parliament's input and an initial reaction to the Commission proposals,\textsuperscript{183} translates Parliament's mandate into budgetary figures and proposes amendments to the draft MFF regulation and accompanying interinstitutional agreement. The resolution expresses concern that proposed MFF resources as a share of EU-27 GNI are lower than in the 2014 to 2020 period (1.11 %, down from 1.16 %), and would not enable the EU to tackle its commitments. Taking Brexit into account, Table 4 recap's the main changes requested. These include further reinforcing priorities such as: research and innovation (Horizon), youth (Erasmus+ and measures against unemployment), transport, space, small businesses, environment, climate, neighbourhood, and development; and restoring resources for agriculture and cohesion to their 2014 to 2020 levels. The proposed modifications would bring the next MFF to €1.32 trillion (1.3 % of EU-27 GNI). The text welcomes proposals for increased flexibility and own resources, supporting even more ambitious reform. In addition, Parliament reiterates that negotiations should tackle the MFF and EU revenue jointly, urging the Council to start them rapidly. The timeline proposed by the Commission with an agreement before the European elections is considered positively, with a view to avoiding the negative impact of late adoption on the implementation of the next generation of EU programmes.

\textsuperscript{179} The Council’s adoption of the accompanying Own Resources Decision, which introduced minor changes to the EU’s financing system, took even longer, i.e. almost three years.

\textsuperscript{180} European Parliament, Resolution on the 2021-2027 multiannual financial framework and own resources, Strasbourg, 30 May 2018.

\textsuperscript{181} European Economic and Social Committee, Multiannual financial framework post 2020, Opinion, ECO/460, 19 September 2018; and European Committee of the Regions, The multiannual financial framework package for the years 2021-2027, Opinion, COTER-VII/042, 9 October 2018.

\textsuperscript{182} European Parliament, Resolution on the multiannual financial framework 2021-2027 – Parliament’s position with a view to an agreement, Strasbourg, 14 November 2018.

\textsuperscript{183} European Parliament, Resolution on the next MFF: Preparing the Parliament’s position on the MFF post-2020, Strasbourg, 14 March 2018; Resolution on reform of the European Union’s system of own resources, Strasbourg, 14 March 2018; and Resolution on the 2021-2027 multiannual financial framework and own resources, Strasbourg, 30 May 2018.
and funds. However, a mandatory mid-term revision should enable the Parliament elected in May to have its say on the post-2020 MFF. A seven-year duration should apply for one last time, before moving to five-plus-five-year frameworks with compulsory mid-term revisions to align the EU’s budgetary and institutional cycles more effectively.

Table 4 – New MFF: Parliament resolution, Commission proposal and 2014-2020 allocations (€ million, 2018 prices, EU-27)


---

1. Single market, innovation and digital

| 116 361 | 166 303 | 216 010 | +29.9 % |

- Horizon Europe, InvestEU Fund, Connecting Europe Facility (CEF) Transport, Decentralised agencies, Single Market Programme, Fiscalis, EU Anti-Fraud Programme, Sustainable tourism, European Space Programme

2. Cohesion and values

| 387 250 | 391 974 | 457 540 | +16.7 % |

- European Regional Development Fund (ERDF) and Cohesion Fund (CF), Support to the Turkish-Cypriot Community, European Social Fund+ (including a Child Guarantee), Erasmus+, Creative Europe, Justice, Rights and Values (including Union values strand), Decentralised agencies

3. Natural resources and environment

| 399 608 | 336 623 | 404 718 | +20.2 % |

- European Agricultural Guarantee Fund (EAGF) and European Agricultural Fund for Rural Development (EAFRD), European Maritime and Fisheries Fund, Other, Programme for Environment and Climate Action (LIFE), Just Energy Transition Fund, Decentralised agencies

4. Migration and border management

| 10 051 | 30 829 | 32 194 | +4.4 % |

- Decentralised agencies

5. Security and defence

| 1 964 | 24 323 | 24 639 | +1.3 % |

- Nuclear decommissioning, Decentralised agencies

6. Neighbourhood and the world

| 96 295 | 108 929 | 113 386 | +4.1 % |

- Instrument(s) in support of neighbourhood and development policies, Overseas countries and territories (including Greenland), Decentralised agencies, Pre-accession assistance

7. European public administration

| 70 791 | 75 602 | 75 602 | = |

- Total MFF ceilings

| 1 082 320 | 1 134 583 | 1 324 089 | +16.7 % |

- In % GNI (EU-27)

| 1.16 % | 1.11 % | 1.30 % |

- Instruments outside ceilings

| N/A | 26 023 | 38 623 | +48.4 % |

- Emergency aid reserve, EU Solidarity Fund, Flexibility Instrument


---

184 In addition, the interim report increases the margins for headings 1, 2, 3 and 6 as compared to the Commission proposal.

185 The interim report maintains the financing of the common agricultural policy for the EU-27 at the 2014 to 2020 level in real terms, while budgeting the initial amount of the agricultural reserve.
In December 2018, the European Council discussed the details of the next MFF for the first time, welcoming the intensive preparatory work carried out by the Council in 2018. In addition to a progress report, the Austrian presidency produced a draft negotiating box, a technical tool that lists issues to be addressed and related options with a view to facilitating an agreement.\(^{186}\) EU leaders invited the Romanian presidency to continue this technical work and develop an orientation for the negotiations during the first semester of 2019, setting the objective to reach an agreement in the European Council in autumn 2019.\(^{187}\)

The December 2018 conclusions of the European Council mean that the ambitious timeline initially proposed by the Commission and supported by the European Parliament in its resolutions will not be met. In its contribution ahead of the summit, the Commission acknowledged progress made on the negotiations so far, but already outlined an updated timeline. The document urged leaders to reach agreement on the MFF in October 2019 and to work closely with Parliament, recalling the negative impact that a delayed adoption would have on the implementation of future programmes.\(^{188}\)

According to some observers, the new timeline with an agreement planned for autumn 2019 (see Figure 18) may prove equally difficult. Such analyses point not only to the various challenging issues on which an agreement has to be reached (e.g. size of the budget, spending priorities and conditionality linked to the rule of law), but also to possible institutional delays, since decisions on five key EU appointments have to be made in the second half of 2019.\(^{189}\)

The unanimity requirement for the adoption of the MFF regulation in the Council remains an important challenge for such a broad proposal, with groups of Member States traditionally reported to have differing views on various elements. In addition, some analysts argue that the new background characterising the negotiations for the post-2020 period could trigger cleavages within traditional coalitions.\(^{190}\) The European Parliament has called on the European Council to make the process smoother, by activating the passerelle clause of the Treaty, which would allow the Council to act by qualified majority in this domain.\(^{191}\)

\(^{186}\) Council of the European Union, Multiannual financial framework (MFF) 2021-2027: Presidency progress report (14346/18), Brussels, 30 November 2018; and Multiannual financial framework (2021-2027): draft negotiating box (14759/18), Brussels, 30 November 2018.

\(^{187}\) European Council, Conclusions of the meeting (EUCO 17/18), Brussels, 14 December 2018.

\(^{188}\) European Commission, Towards a swift agreement on a long-term budget for Europe’s priorities, COM(2018)814 final, 4 December 2018.

\(^{189}\) Janis A. Emmanouilidis, The need to ‘Re-unite EUrope’: the results of another Brexit summit, European Policy Centre, 17 December 2018.

\(^{190}\) J. Haas, E. Rubio and P. Schneemelcher, op. cit.

Figure 18 – Timeline of the 2021 to 2027 MFF

2018

- 2 May: European Commission: proposals for post-2020 MFF and own resources
- 14 November: European Parliament adopts its detailed negotiating position
- 30 November: Council: Presidency produces progress report and draft negotiating box
- 13 December: European Council: first discussion on the content of the proposals
- January: Council: regular discussions planned in the first half of the year

2019

- 9 May: Informal European Council on the future of the EU in Sibiu
- 23-26 May: European Parliament elections
- 20-21 June: European Council: debate on the proposals
- Autumn: European Council: new target date for a political agreement

European Parliament: consent vote on the MFF agreement reached in Council and European Council

2021

Start of post-2020 MFF

Source: EPRS.
6. Economic focus: Financing small and medium-sized enterprises (SMEs) in the EU

Figure 19 – Key figures on SMEs in the European Union

SMEs and large enterprises in the EU-28

<table>
<thead>
<tr>
<th>Enterprises</th>
<th>Value added</th>
<th>Employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>In 1 000</td>
<td>€ trillion</td>
<td>In 1 000</td>
</tr>
<tr>
<td>SMEs (&lt;250 employees)</td>
<td>24,483</td>
<td>99.8%</td>
</tr>
<tr>
<td>Large (&gt;250 employees)</td>
<td>47,000</td>
<td>0.2%</td>
</tr>
<tr>
<td>All enterprises</td>
<td>24,530</td>
<td>100%</td>
</tr>
</tbody>
</table>

Evolution of SMEs in the EU-28 (2008=100)

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of SMEs</th>
<th>Value added</th>
<th>Employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>114.3</td>
<td>113.8</td>
<td>102.5</td>
</tr>
<tr>
<td>2009</td>
<td>115.3</td>
<td>114.8</td>
<td>103.5</td>
</tr>
<tr>
<td>2010</td>
<td>116.3</td>
<td>116.1</td>
<td>104.5</td>
</tr>
<tr>
<td>2011</td>
<td>117.3</td>
<td>117.1</td>
<td>105.5</td>
</tr>
<tr>
<td>2012</td>
<td>118.3</td>
<td>118.1</td>
<td>106.5</td>
</tr>
<tr>
<td>2013</td>
<td>119.3</td>
<td>119.1</td>
<td>107.5</td>
</tr>
<tr>
<td>2014</td>
<td>120.3</td>
<td>120.1</td>
<td>108.5</td>
</tr>
<tr>
<td>2015</td>
<td>121.3</td>
<td>121.1</td>
<td>109.5</td>
</tr>
<tr>
<td>2016</td>
<td>122.3</td>
<td>122.1</td>
<td>110.5</td>
</tr>
<tr>
<td>2017</td>
<td>123.3</td>
<td>123.1</td>
<td>111.5</td>
</tr>
</tbody>
</table>

Number of SMEs (per 1,000 inhabitants, 2017)

EU-28: 57 SMEs per 1,000 inhabitants

Number of SMEs (in 1,000, 2017)

<table>
<thead>
<tr>
<th>Country</th>
<th>SMEs</th>
</tr>
</thead>
<tbody>
<tr>
<td>IT</td>
<td>3,746</td>
</tr>
<tr>
<td>FR</td>
<td>2,961</td>
</tr>
<tr>
<td>ES</td>
<td>2,663</td>
</tr>
<tr>
<td>DE</td>
<td>2,483</td>
</tr>
<tr>
<td>UK</td>
<td>2,157</td>
</tr>
<tr>
<td>PL</td>
<td>1,693</td>
</tr>
<tr>
<td>NL</td>
<td>1,416</td>
</tr>
<tr>
<td>CZ</td>
<td>1,001</td>
</tr>
<tr>
<td>PT</td>
<td>897</td>
</tr>
<tr>
<td>SE</td>
<td>722</td>
</tr>
<tr>
<td>BE</td>
<td>619</td>
</tr>
<tr>
<td>HU</td>
<td>498</td>
</tr>
<tr>
<td>RO</td>
<td>481</td>
</tr>
<tr>
<td>SK</td>
<td>444</td>
</tr>
<tr>
<td>Other MS</td>
<td>2,143</td>
</tr>
</tbody>
</table>

SMEs by Member States (top 5, 10 and 15)

Other MS: BG (337), AT (331), IE (255), FI (236), DK (208), LT (184), HR (149), SI (142), LV (114), BE (74), CY (51), LU (34) and MT (29)

Contribution of SMEs to EU-28 added value and employment (% 2017)

Value added

SMEs produce 57 cents of every euro of value added (56.8%)

Employment

SMEs employ 2 out of every 3 employees (66.4%)

Value added = net contribution of the company to the economy
6.1. European SMEs at a glance

SMEs comprise three different categories of firms: micro-enterprises, small enterprises and medium-sized enterprises (see Table 5). The official EU definition of SMEs includes three different indicators: the number of employees and either the level of turnover or the total size of the balance sheet.

Table 5 – Definition of SMEs

<table>
<thead>
<tr>
<th>Company category</th>
<th>Employees</th>
<th>Turnover</th>
<th>Balance sheet</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro</td>
<td>&lt;10</td>
<td>&lt; €2 million</td>
<td>&lt; €2 million</td>
</tr>
<tr>
<td>Small</td>
<td>&lt;50</td>
<td>&lt; €10 million</td>
<td>&lt; €10 million</td>
</tr>
<tr>
<td>Medium-sized</td>
<td>&lt;250</td>
<td>&lt; €50 million</td>
<td>&lt; €43 million</td>
</tr>
</tbody>
</table>

This definition, which dates from 2003, is currently under evaluation to see if it is still relevant in the current business and financing environment. Being classified as a SME allows enterprises to have access to many specifically-targeted EU business-support programmes such as research and innovation funding (Horizon 2020), competitiveness funding (COSME), structural and investment funds and similar national support programmes that could, in cases of bigger enterprises, be considered as unfair government support (state aid). SMEs are also subject to lighter requirements or reduced fees for EU administrative compliance. Since European legislation affects SMEs in multiple fields from taxation, through competition, to company law, the EU strives to create framework conditions that are small-business friendly. Apart from programmes and actions specifically targeted at SMEs, it does so by systematically considering the impact its policies have on this type of firm.

In 2017 there were almost 24.5 million SMEs in the European Union constituting 99.8% of all non-financial enterprises. Owing to their importance, SMEs are often referred to as ‘the backbone of the European economy’. In 2017 these firms employed close to 95 million people, meaning that two out of three workers in the EU had an occupation in this sector. Furthermore, European SMEs generated around 57% of total added value which amounts to €4.16 trillion.

The SME segment is heterogeneous across the EU. While the number of small and medium-sized category firms varies relatively little among EU-28 Member States, the number of micro-enterprises is much more diversified. Looking at the whole EU, these smallest companies constitute 93.1% of all firms (see chart ‘SMEs by size (2017)’). At the same time they employ almost 30% of all workforce and generate one-fifth of the value added in the EU. The largest numbers of SMEs are active in the biggest Member States – total numbers vary from Italy with 3 746 000 to Slovakia with 434 000 (see chart ‘Number of SMEs in 2017’). Furthermore, the prevalence of SMEs also varies enormously, with the EU average at 57 per 1000 inhabitants, while Czech Republic has 115, Portugal 98, Germany 34 and Romania 29 (See map ‘Number of SMEs, per 1 000 inhabitants(2017)’). Important differences exist in terms of the contribution to value added and employment of different sub-categories of SME. Interestingly, the Commission estimates that in national economies where micro-enterprises

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192 It was introduced by Commission Recommendation 2003/361/EC. The Commission impact assessment explains the main reasons behind the ongoing evaluation related to financial thresholds and legal certainty.


194 Eurostat defines gross value added (GVA) as output (at basic prices) minus intermediate consumption (at purchaser prices); it is the balancing item of the national accounts’ production account.
capture a significant amount of value added and employment, medium and large SMEs typically account for only a small share. In 2017, value added created in the total economy by all SMEs varied from 41% in Ireland to 81% in Malta, and employment from 54% in the UK to 85% in Greece (see charts ‘Contribution of SMEs to EU-28 added value and employment (% 2017)’).

European non-financial business SMEs are heavily concentrated in five sectors: wholesale and retail trade, accommodation and food services, business services, construction and manufacturing (see chart ‘SMEs by sector 2017’). As much as 71% of total value added generated in 2017 by SMEs as well as 77% of employment came from the sectors mentioned above. A challenging issue with the competitiveness of European SMEs is the fact that three out of four are active in either low knowledge-intensive service industries or low-tech manufacturing industries. Similarly, 93% of SMEs are active in industries characterised by very low or low export intensities.

6.2. Performance of SMEs

The financial and economic crisis, followed in some Member States by the sovereign debt crisis, significantly affected European SMEs. Over the 2008 to 2014 period, as many as 20 Member States reported net employment reduction among SMEs, and eight Member States faced double-digit net employment losses. However, the recovery gradually set in, and 2014 marked the first year since the beginning of the crisis in which both employment and value added have both increased (See chart ‘Evolution of SMEs in the EU-28’). Between 2008 and 2017, gross value added generated by SMEs increased cumulatively by 14.3% and employment in these companies increased by 2.5%. At the same time economy as a whole generated a slightly higher cumulative increase of 16.5% in value added and a slightly lower increase of 1.8% in employment.

While the recovery of European SMEs is indisputable, national level data reveals divergent developments across the Union: in 2017 six Member States had not yet reached the 2008 SME added value levels, while five Member States exceeded it by at least 40%. In terms of employment recovery has been more muted with 15 Member States still below 2008 levels and only three exceeding pre-crisis levels by more than 20%.

The number of SMEs in the EU grew by 13.8% between 2008 and 2017. The number of new SMEs is much higher than the actual increase in SME population because many SMEs, particularly young ones, close down and leave the markets each year. While 10 new enterprises were created for every existing 100 SMEs in the 2012 to 2015 period, 8.5 of them ceased to operate. Research has established that young and high-growth firms can be key drivers of innovation by increasing pressure on incumbents to innovate and improve their productivity. Correspondingly, high business entry rates can be conducive to development

International comparison

From 2009 to 2016 the United States achieved more than double cumulative growth in SME value added and employment. The increase in the number of SMEs in the EU was about 30% higher than in the US. The gap in terms of value added may gradually be narrowing as over the 2016-2017 period the EU’s SMEs had higher growth rates, but in terms of employment the opposite is true. The EU’s SMEs are also less dynamic since there are fewer scale-up and high-growth firms than in the US. This may indicate that the barriers to growth are higher in Europe than in the US. In contrast, SME employment and the number of SMEs fell noticeably in Japan over the 2009-2016 period.

195 The first group comprises Cyprus, Greece, Spain, Croatia, Italy and Portugal, while the second, Bulgaria, Estonia, Latvia, Luxembourg and Malta.

196 The first group comprises Bulgaria, Cyprus, Czech Republic, Denmark, France, Greece, Spain, Croatia, Ireland, Italy, Latvia, Lithuania, Portugal, Romanian and Slovenia. The second includes Germany, Luxembourg and Malta.
and diffusion of technology. The ECB noted that the rate of replacement of old firms by new ones has been declining in the EU which may adversely affect technological diffusion and productivity.197

In its latest SME performance review198 the Commission reported that growth in SME employment over the 2015 to 2016 period occurred across all economic sectors but with varying intensity. In 2017 the SME sector continued to grow at a moderate pace. Growth in value added of 1.5 % in 2016 was followed by a stronger 3.5 % increase in 2017.199 After increasing by 2.3 % in 2016, employment meanwhile grew further by 2.0 % in 2017. These increases were relatively well balanced across the main sectors and the Member States.

The European Association of Craft, Small and Medium-Sized Enterprises (UEAPME) evaluates the business climate for SMEs twice a year. Its latest report from October 2018 shows that the positive economic climate in Europe continued, based on robust domestic demand, steady GDP growth rate and decreasing unemployment.200 This is also reflected by high and stable levels of SME confidence (albeit more pronounced in the north than in the south of Europe). SMEs polled broadly report increases in turnover, employment, orders, prices and investments since 2013. Also in the first half of 2018 all of these indicators apart from the number of orders were on an upward trajectory.

6.3. Start-ups and scale-ups

Many economists agree that start-ups that manage to scale up (grow quickly) are key to economic growth.201 While the large majority of micro start-ups that survive the crucial first two years do not grow, a small group of those that do grow create a disproportionate amount of jobs. For example, an OECD study showed that only 4 % of micro-start-ups grow on average, but they are responsible for between 22 % (the Netherlands) and 53 % (France) of job creation in this segment.202 These companies are both young and record high growth rates and the bulk of research shows that they are significant generators of jobs, taxes and wealth and often drive innovation. On the other hand, as discussed in detail in the following sections, many start-ups struggle with access to finance since they often do not have sufficient collateral, have limited credit history and lack the expertise needed to obtain funding. In the EU, most start-ups offer a product or service online and are active across diverse sectors such as IT/software development, software as a service, bio- nano- and medical technologies, industrial technology, production and hardware, consulting and financial technology. While the number of scale-ups in the EU increased by 24 % between 2014 and 2016 it is still relatively small as a proportion of all SMEs and concentrated in larger countries – seven out of 10 come from one of six Member States.203 Furthermore, compared with countries like Switzerland, South Korea, Japan, China or the US, the EU has proportionately fewer companies able to substantially scale up their operations.

197 For more details see European Central Bank, The slowdown in euro area productivity in a global context, and OECD, Entrepreneurship at a glance 2016, Chapter 3.
199 The Commission explains that the weaker value added growth of 1.5 % generated by EU SMEs in 2016 masked robust underlying economic fundamentals and occurred entirely due to the significant exchange rate movements of the euro vis-à-vis the pound sterling.
201 The EU defines start-ups on the basis of criteria such as age (younger than 10 years), innovation (in product or business model) and aim to scale up. Scale-ups, or high growth firms have at least 10 employees at the beginning of their growth spurt and increase the number of their employees annually by 10 % or more in three consecutive years.
202 OECD discussion paper on Enabling SMEs to scale up, March 2018.
203 Germany, United Kingdom, Spain, France, Italy and Poland.
6.4. Landscape of financing European SMEs

Figure 20 – European SME financing landscape

Important problems faced by SMEs in the EU (2018)

Access to finance is the most important concern for 7% of EU SMEs

Access to finance as important problem in the Member States (% of EU SMEs)

Access to finance is the most important concern for 7% of EU SMEs

Sources of SME finance in the EU (2018)

Purpose of SME financing in the EU (2018)

SMEs requesting a new credit line (2018)

Perceived change in the external financing gap by SMEs and large firms

Note: The finance gap indicator, created by the European Central Bank (ECB), shows how SMEs perceive their external financing situation. It shows the perceived changes in the needs and availability of external financing. It is a composite indicator constructed using data from the survey on the access to finance of enterprises (SAFE) carried out by the European Commission. The indicator has a value between -1 and 1, and then it has multiplied by 100 to obtain a percentage. The indicators has 100 (-100) if the need increases (decreases) and the availability decreases (increases). Therefore a positive value of the indicator suggests an increasing financing gap while a negative value implies a perceived shrinking financing gap. From the graph, it can be noted that from the second semester of 2014, both SMEs and large firms perceived a shrinking financing gap.
Sustaining the continued growth of European SMEs relies, not least, on ensuring sufficient access to external finance. The provision of financing is indeed crucial at all stages of firms’ development from start-up to scale-up and well into their further growth, laying the foundations for the broadening of productive capacities and the creation of new jobs.

SMEs are typically considered to be in disadvantaged position regarding access to finance.204 Their smaller scale and level of sophistication implies that they also tend to face disproportionate challenges relative to larger firms, when it comes to securing credit from banks or raising capital from public markets. These relate to difficulties regarding the signalling of their creditworthiness to lenders, the irregularity in cash flows and thereby inability to follow fixed repayment schedules, as well as their limited capacities in collateral provision.205

Recent evidence, however, indicates that despite inherent weaknesses and persistent market imperfections the environment for SME access to financing is gradually improving across the EU. This suggests that the ongoing economic recovery and the improved performance by SMEs has also been accommodated by improvements in their financing conditions. According to the latest findings of the Survey on Access to Finance of Enterprises (SAFE) conducted annually by European Central Bank (ECB) and the European Commission,206 the importance of ‘access to finance’, as a critical concern for EU SMEs has diminished substantially over the last five years, as compared to other business challenges. In 2018, only 7 % of SMEs reported ‘access to finance’, as their most serious concern (see chart ‘Access to finance as an important problem for SMEs’). This is a notable improvement, as compared to the 17 % reported in 2009, or even 15 % reported in 2013.207

Today, SMEs’ most pressing problem appears to be the availability of skilled staff and experienced managers. In the context of the latest SAFE, such access to skilled and experienced personnel was identified as a critical problem by 25 % of respondents across the EU – up from 14 % in 2013 (see chart ‘Important problems faced by SMEs in the EU). Finding customers remains an equally important issue for 23 % of respondents, while 13 % of SMEs also reported difficulties due to the regulatory burden as their most important concern.

However, the overall improvement in the perception of ‘access to finance’ among EU SMEs has been rather uneven across countries and different types of enterprise. For example, data from SAFE indicate that those countries that experienced a more stable economic recovery, such as France, Germany, the Netherlands, the UK and Austria, tend to report results close to, or below, the EU average. Countries that were more severely hit by the economic downturn, over the last decade, such as Greece, Italy, Cyprus and Ireland continue to report access to finance as among the more serious concerns for SMEs (see chart ‘Access to finance as an important problem in the Member States’). Similarly, 9 % of SMEs already listed in stock markets reported access to finance as a prime concern, as compared to 11 % of venture capital- or business angel-reliant SMEs.

Notwithstanding these variations, on aggregate, the perception of financing conditions has indeed improved, among SMEs, in recent years. This is further confirmed by the ECB’s external financing gap indicator, which measures the difference between perceived needs and perceived availability

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204 European Commission, An action plan to improve access to finance for SMEs, 2011.


207 This ranking is calculated based on scores respondents were asked to assign to a fixed set of problems in response to the following question ‘How important have the following problems been for your enterprise in the six past months?’. The problem given the highest importance was then designated the most pressing problem.
of external financing by SMEs in the euro area. A negative indicator value implies that the financing gap perceived by enterprises is shrinking and thereby conditions are improving (see chart ‘Perceived change in the external financing gap by SMEs and large firms’).

For the period of April 2018 to September 2018, both SMEs and large enterprises perceived the increase in the external financing needs to be smaller than the improvement in the access to external funds. This resulted in a negative external financing gap for SMEs and larger enterprises (-5 % for SMEs) which is a positive development. A similar trend can be observed in the results of the last seven consecutive semesters, which would indicate a gradual improvement in financing conditions for enterprises.

Country level results display some disparities in perceptions among European SMEs. In the majority of countries, the financing gap is negative. For example, in Germany and Spain, the indicator reaches -9 % and in the Netherlands -8 %. At the same time, SMEs in Greece continued to be financially constrained, exhibiting a positive financing gap, albeit with a notable improvement reaching 5 % from 14 % in the previous semester.

Turning to the mix of financing, the SAFE results indicate that traditional debt finance – whether in the form of credit lines, overdrafts, trade credit or standard bank loans – continues to be the primary source of external funding for the majority of SMEs and small entrepreneurs. The defining characteristic of these straight debt instruments, as noted by the OECD, is that ‘they represent an unconditional claim on the borrower, who must pay a specified amount of interest to creditors at fixed intervals, regardless of the financial condition of the company or the return on the investment’. The techniques and methods employed to determine credit worthiness or repayment ability can vary considerably, while information asymmetries between SMEs and lenders can have a major bearing on both the approval of credit by lenders and the cost of its repayment.

Among the various debt financing instruments available to SMEs, credit lines and overdrafts are the types used most often, followed by leasing, trade credit and loans. As illustrated in the figure on sources of financing, in 2018 about 35 % of SMEs indicated that they had resorted to credit lines or overdrafts to cover their financing needs within the past six months. Leasing appears to have picked up in SMEs preferences accounting for 24 % of all EU28 SMEs. Simple bank loans have declined slightly although they continue to be among the most preferred sources of SME financing, accounting for 17 % of respondents.

In line with the findings of previous years external financing was obtained by SMEs mainly for the purposes of fixed investment (reported by 41 % of respondents) followed by inventory and working capital (37 %) and hiring and training of employees (22 %). Developing and launching new products or services and refinancing or paying off obligations came last in SME responses (20 % and 14 % respectively).

As regards the cost of financing, SMEs reported that interest rates increased slightly between 2017 and 2018. Over the last four years of the SAFE survey, the reverse was true, which may indicate a

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208 The **financing gap indicator** is based on SAFE data and combines both financing needs and availability of financing (bank loans, bank overdrafts, trade credit, equity and debt securities) at firm level. For each of the five financing instruments, an indicator of a perceived financing gap change takes the value of 1 (-1) if the need increases/decreases and availability decreases/increases. The composite indicator is the weighted average of the financing gap related to the five instruments. Values are multiplied by 100 to obtain weighted net balances in percentages.

209 ECB, *Survey on the Access to Finance of Enterprises in the euro area – April to September 2018*.

210 This finding emerges from SMEs responses to the question ‘Are the following sources of financing relevant to your enterprise, that is, have you used them in the past or considered using them in the future?’.

shift in the cost of financing. At the same time, in 2018 more SMEs also reported increases in the non-interest rate costs of financing, such as charges, fees and commissions and in collateral requirements.

SAFE further provides numerous interesting insights into the specifics of the debt financing of EU SMEs. For example, the results confirm that in 2018, applications for new credit lines or new loans by SMEs were for the most part successful: 212 74 % of all applications were granted in full by financial institutions, while another 6 % granted most of the sum applied for. Moreover, the results indicate that of the external financing obtained by SMEs, 38 % related to amounts of less than € 100 000. As for other areas, the scale and size of loans varied considerably across Member States and depending on firms' characteristics. In particular, smaller loans (less than €25 000 or between €25 000 and €100 000) were reported by SMEs in Spain and Poland, whereas larger loans (between €250 000 and €1 million or even above €1 million) were most frequently reported by SMEs in Denmark and the Netherlands. Finally, the majority of SMEs that did not apply for a loan, indicated that they did not do so because of the availability of sufficient internal funds.

The figures above also show the evolution of small loans, namely loans bellow € 0.25 million, for the euro area over the 2010 to 2018 period (see chart 'New loans to SMEs by European banks'). Following analysis by the European Investments Fund (EIF), these are employed as a proxy to shed further light on the development of debt financing for SMEs. The data are consistent with SAFE results over the last five years. The volume of small loans for new business initially contracted in 2010, but gradually picked up and has been growing consistently since early 2014. By October 2018 it reached a total of € 41.5 billion.

Notwithstanding the gradual recovery of credit, bank loans and related debt-based funding, alternative financing instruments continue to be among the least preferred options of financing for EU SMEs. Equity (2 %), other sources (1 %), and debt securities (1 %) remained among the least popular types of financing – a finding that is consistent with results from previous years. Capital markets continue to be fragmented for smaller enterprises – for various reasons including a disproportionate regulatory burden – and the recent financial and sovereign debt crisis has taken a big toll on SMEs' ability to raise capital on public markets.

Developments in SME-dedicated stock markets213 are relevant in this context. Listings on stock exchanges offer an important alternative route for SMEs to access additional finance and can bring important benefits to enterprises. However, European public markets for SMEs have been struggling to attract issuers since the outbreak of the crisis. Initial public offerings (IPOs) by SMEs have been in constant decline in Europe over the past decade. The European Commission estimates that the number of IPOs on SME-dedicated stock market venues fell from 478 on average per year in the 2006-2007 period to 218 between 2009 and 2017.214 The result of this decline is also reflected in the value of capital raised by SMEs. From 2009 to 2017, an average of €2.55 billion per year was raised through IPOs, down from an average of €13.8 billion annually in the 2006 to 2007 period.

This negative trend is further exacerbated by the fact that the bulk of IPO activity, or more than 70 % of total proceeds over the 2006 to 2017 period, was concentrated in one venue – AIM – which is owned and operated by the London Stock Exchange. Although this proportion has decreased over time, it still highlights an important dimension in the European landscape for SMEs' initial public

212 European Commission, Survey on the access to finance of enterprises (SAFE), Analytical Report, 2018.
213 Specialised stock markets for SMEs, such as Alternext/Euronext Growth and AIM.
offerings, namely that activity remains highly concentrated in the UK, with other markets struggling or virtually inactive by comparison.215

Similarly, venture capital (VC) investments may have started to recover in recent years, but the size of the market remains too small to allow EU start-ups to scale-up and become bigger companies.216 Indeed, as emphasised by the EIF, venture capital investments in the EU jumped by 34 % between 2016 and 2017 and this affected investments for all enterprise development stages. For example, seed investments217 grew by 49 %, start-up investments by 46 % and later stage venture by 17 %.218 However, the amount of venture capital invested in the EU in start-up companies remains six times less than in the US, namely €6.5 billion as compared to €39.4 billion in the US. At the same time venture capital funds in the US are nearly three times bigger than in those the EU. They have an average size of €156 million, as compared to €56 million in the EU.219

Finally, comes corporate debt. Although SMEs can theoretically access the market, they are much less frequent issuers as the market is wholesale and mainly focused on mid to large issuers. As emphasised by a recent report from the Commission Expert Group, bond markets remain largely untapped by European SMEs, despite the creation of specialised platforms in Europe with simpler, less costly processes and requirements.220

As regards their future outlook, the latest SAFE survey highlights that about 45 % of SMEs in the EU28 do not foresee any limitations in their access to financing in the coming years. Others that did express the possibility of facing difficulties in accessing financing in the future, sit high interest rates and the price of financing, as well as insufficient collateral or guarantees as the principal sources of limitation. Geographically, SMEs in Belgium and Finland appear to expect no obstacles more frequently than other EU Member States, while the country where this is least observed is Greece. On balance, however SMEs according to the SAFE survey expect the availability of all types of financing to improve in the six months from October 2018 to March 2019. Concerning the main factors that can affect their future financing, SMEs cite tax incentives and making existing public measures easier to obtain as the most important factors. Business support services and guarantees for loans follow in importance, while measures to facilitate equity investments and export credits or guarantees come at the end of the scale.

6.5. Diversifying SME financing

Over the last decade, the global financial and sovereign debt crisis exposed the challenges and risks involved for European companies, especially SMEs, from their over-dependence on bank-based financing. The heavy reliance on debt finance in the form of bank loans, overdrafts and leasing, that

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216 European Commission, VentureEU: €2.1 billion to boost venture capital investment in Europe’s innovative start-ups, press release, Brussels, 10 April 2018.
217 Seed capital refers to the initial capital used when starting a business, often coming from the founders’ personal assets, friends or family, for covering initial operating expenses and attracting venture capitalists.
219 European Commission, Factsheet VentureEU: Boosting venture capital investments in Europe’s innovative start-ups.
has traditionally characterised European SMEs, contributed heavily to their increased vulnerability during the recent economic downturn.

Figure 21 – Reliance on bank financing by non-financial corporations (in %)

As the need for banks to deleverage increased and as capital requirements on European financial institutions became stricter – through for example the adoption of the Capital Requirements Regulation and Capital Requirements Directive (CRR/CRD) – the banks’ ability and willingness to take risks as well as to extend new lending to companies narrowed.

Across the EU, this resulted in the tightening of credit standards and the subsequent credit crunch, which inevitably affected the financing of SMEs disproportionately relative to bigger enterprises. Beyond their traditional dependence on bank lending, smaller companies tend to lack collateral and have more irregular cash flows than larger firms, and are heavily affected during times of economic stress. This raises the costs of financing and makes it difficult to impose specific repayment schedules thereby further hampering access to financing.

The gradual improvement of the economic environment across the EU, facilitated by the ECB’s monetary policy stance, since 2014, has led to a significant easing of financing conditions for consumers and firms, while SMEs on average have also stared to recover. The introduction of further regulatory changes also contributed, including the adoption of the SME Supporting Factor, which reduced the capital requirements for exposures to SMEs in comparison with the pre-CRR/CRD IV framework.

The recovery, however, has been uneven across Member States reflecting differing degrees of development of financial markets between countries, in terms of diversity of financial institutions,

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221 Europe’s economic recovery and implications for monetary policy, Remarks by Peter Praet, Member of the Executive Board of the ECB, at the International Conference of Commercial Bank Economists (ICCBE) in France, Paris, 6 July 2017.

as well as their product offerings and risk appetite. Contrary to larger firms, SMEs tend to rely more on local or national providers of finance. Cross-border lending remains at a rather embryonic stage despite the recent growth of financial technology companies across Europe. Access to finance, therefore, remains a critical challenge for many SMEs in the EU. According to a recent Commission report the debt finance gap for SMEs is estimated at €30 billion annually.223

In view of the persistent challenges, public attention is increasingly being placed on the potential of capital markets to offer alternative sources of financing for SMEs. While policies to support bank-based financing (such as credit guarantee schemes) continue to be widespread in many EU countries, diversification of the sources of funding through the development of deeper and more integrated capital markets is increasingly gaining traction. This is why, building a capital markets union (CMU) constitutes a priority for the EU.

Providing companies, especially smaller ones, with a broader choice of market-based funding at a lower cost, can help stimulate investment, thereby promoting sustainable economic growth and job creation. Importantly, as emphasised by a recent OECD report, such market financing 'should not be seen as a way to disengage banks from SME financing, but rather as a way to complement bank lending and other financing alternatives'.224

The scope for the market financing of SMEs is wide ranging and faces unique challenges largely reflecting the diversity and complexity of SMEs themselves. It is therefore often argued that there is no silver bullet answer to the SME financing problem. Addressing the matter necessitates a more granular approach. As such, market solutions would need to be tailored to reflect the different characteristics of enterprises, as regards scale (micro, small or medium), degree of market capitalisation (micro or mid cap), maturity and level of sophistication (start-up or scale up) and growth levels (high-growth and gazelles) among other things. For example, medium-sized family business may recognise the growth potential from expanding their shareholder base, but may lack the sophistication and capacity to pursue their listing in stock markets, issuing of bonds or indeed introduction of private placements.

Similarly, high-risk start-ups and high growth companies require significant long-term investments, but usually have limited, if any, collateral and have unpredictable cash flows, making it difficult to service debt repayments. Understanding the broad range of underlying SME characteristics and the business challenges they face is therefore critical, in order to shape different financing instruments appropriately and thereby address both demand and supply-side shortfalls more effectively.

Against this background, one area that is increasingly gaining prominence in providing access to funding for SMEs globally is that of equity financing. This can take different forms and is generally complementary to bank lending. As stressed by the OECD, equity financing goes hand in hand with debt financing and the existence of both ‘well-functioning equity and debt markets are required for efficient and effective SME financing’.225

Equity is especially relevant for SMEs that have a high risk-return profile, as it is often the case of new, innovative and high growth firms.226 Equally, equity finance at early stages of development can help boost the creation of new firms, while specialised platforms that facilitate the public listing of

224 OECD, Opportunities and constraints of market-based financing for SMEs, Report to the G20 Finance Ministers and Central Bank Governors, September 2015.
225 ibid.
SMEs can help to inject liquidity and provide further alternatives in boosting access to finance for small firms.

In the EU, SMEs wishing to raise capital on public markets – through the issuance of shares or bonds – can pursue this through specialised public markets, namely multilateral trading facilities (MTF). Unlike regulated markets, MTFs are friendlier towards smaller companies placing less burdensome regulatory requirements on them in order to become and remain listed.

A recent report commissioned by the European Securities and Markets Authority (ESMA) identifies 146 MTFs across the EU. Moreover, under the capital markets union action plan and more specifically the recent Markets in Financial Instruments Directive (MiFID) II, a new sub-category of MTFs was introduced, namely SME growth markets. These are MTFs where one of the critical requirements is for at least half of the companies that have issued shares or bonds on them to be SMEs. Their aim is to 'to facilitate access to capital for smaller and medium sized enterprises and to facilitate the further development of specialist markets that aim to cater for the needs of smaller and medium-sized issuers'.

The promotion of capital market financing for SMEs through their listing on appropriate MTFs can be instrumental in triggering investment and economic growth across the EU. Data suggest that newly listed SMEs in such venues tend to outperform other private companies as regards both overall growth and job generation. Analysis by the OECD further emphasises that the benefits can extend beyond initial public offerings (IPOs), to longer-term repeat access to financing through secondary or follow-on capital raisings. By broadening their investor base and gaining access to more stable financing, SMEs can achieve healthy balance sheets, develop a higher public profile and get broader recognition for their brand. This helps them develop the conditions and the potential to grow faster and eventually scale up their productive capacity further.

Similar to the above, venture capital (VC) can also play a critical role in improving access to finance for SMEs. It is an important source of funding, especially for higher risk and innovative projects and companies. VC’s impact, however, is generally considered go beyond the simple provision of financing.

Venture capital can generate additional value for SMEs by introducing capabilities and sophistication in areas that a company was previously lacking, including management upskilling, improvement of governance, or capacities in project realisation. Equally, venture capitalists often act as anchor investors remaining in the supported SME even after a company's flotation on public markets.

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227 An MTF is a system, or 'venue' that brings together multiple third-party buying and selling interests in financial instruments in a way that results in a contract, MTFs can be operated by investment firms or market operators and are subject to broadly the same overarching regulatory requirements as regulated markets (e.g. fair and orderly trading) and the same detailed transparency requirements as regulated markets; in this sense they are more like a traditional regulated market than a broker crossing network or a systematic internaliser.

228 Europe Economics, Data Gathering and Cost Analysis on Draft Technical Standards Relating to the Market Abuse Regulation, 6 February 2015.

229 I. Zachariadis, Enabling SMEs' access to capital markets, EPRS, November 2018.

230 MiFID II, Recital.


markets. This, in turn, brings stability and can signal confidence to the market, which may further improve a company’s viability, as evidenced by the lower insolvency rate of smaller growth companies backed by VC during the crisis. The key institutional investors among venture capital funds appear to be insurance companies and pension funds.

**Business angel investments** can help narrow the financing gap for start-ups and early stage SMEs. Driven by groups or standalone high net worth individuals, business angel investors in essence provide SMEs with their own private funds, giving them the opportunity to scale up and grow before they can access other more complex types of equity financing such as venture capital. Similar to venture capitalists, the support of angel investors can go well beyond capital, by providing business management experience, skills and contacts for the early stage entrepreneurs. The UK leads the European business angel market with Spain, Germany and France following.

Finally, more recent developments, such as **crowdfunding platforms** are also important to emphasise, although it is still too early to assess their full potential. Crowdfunding refers to the process of raising external finance from a large audience rather than one financial intermediary or investor, where each individual provides a small amount of the funding requested.

In the EU, the market for crowdfunding is still fairly underdeveloped as compared to other major world economies. One of the key underlying problems relates to the degree of market fragmentation in the EU and the lack of common rules across Member States. The absence of cross border harmonisation in the market tends to raise the costs of compliance and, as emphasised by the Commission, prevents crowdfunding platforms from expanding. Equally, analysis indicates the need to enhance more the protection of investors in such contexts. Risks can be generally under-priced in crowdfunding platforms leaving investors – especially retail investors – unprotected against high default rates.

Notwithstanding the importance of equity financing in the EU a number of challenges remain. Initial public offerings by SMEs have been in constant decline over the past decade. The European Commission estimates that from 2009 to 2017, an average of €2.55 billion per year was raised through IPOs on SME-dedicated MTFs, down from an average of €13.8 billion annually in the 2006-2007 period. Equally, evidence on European VC funds also suggests that they lack scale and are only half the size of their US equivalents. According to the EIB, matching US levels of venture capital financing as a share of GDP would require around €35 billion a year in additional EU venture capital activity.

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240 Underestimation of the quantity of risks borne by market players.


€4.2 billion was successfully raised through crowdfunding platforms in the EU. In the US, by comparison crowdfunding has been expanding rapidly reaching US$16.2 billion in 2014, up by 167% in 2013, when it was US$6.1 billion.

In addition to equity, SME bond finance has also been identified as an area of potential growth in recent years, because it does not dilute the ownership (or control) of the company and it can provide an effective way to inject liquidity into the market, especially in periods of low interest rates.

However, the literature recognises the continuing difficulties for SMEs in this field. Bond finance is an instrument traditionally used by larger corporations to raise capital. As emphasised by the EIF, although called SME bonds – the issuing companies are often not SMEs in the sense of the EU definition, but rather bigger mid-caps or small corporates. This is because the costs of bond issuance and reporting requirements, as well as, the credit history and earnings record required to meet repayment obligations, necessitate a level of sophistication that is difficult for a smaller company to attain. Notwithstanding these shortcomings, successful examples of small-scale bond issuance do exist. This for example is the case of mini-bonds already issued in many EU countries.

A notable case in this context is Italy, where mini-bonds issued by non-listed SMEs have been in operation since 2012. The number of issuing companies grew to 106 enterprises in 2016 from 85 in 2015, raising €3.57 billion in total.

Finally, SME securitisation is increasingly gaining ground and reputation as a way to help financial intermediaries broaden their funding base, thereby improving liquidity, as well as allowing banks to free up capital and increase their SME lending. Securitisation refers to the process whereby a financial instrument is created, typically by a lender such as a bank, which allows for the pooling of assets for investors to purchase. In the case of SME loan securitisation, a bank extends loans to its SMEs, which are then bundled in a pool, establishing a portfolio. This portfolio is then sold to capital market investors through the issuance of notes, by a special purpose vehicle (SPV) backed by the loan portfolio.

The European SME securitisation market grew steadily from the beginning of the previous decade until the outbreak of the crisis, after which it initially retained high levels before subsidising to 2003 to 2004 levels by 2016. Securitisation came under increased scrutiny and criticism at the outset of the global financial crisis, with particular reference to the US subprime securitisation market.

However, according to EIF analysis de-stigmatisation is under way, as public perception is gradually improving.

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245 A. Thomadakis, Developing EU Capital Markets for SMEs: Mission impossible?, ECMI Commentary No 46, 4 September 2017.
247 ESMA, Access to public capital markets for SMEs, Securities and Markets Stakeholder Group, 8 November 2017.
248 A. Thomadakis, Developing EU Capital Markets for SMEs: Mission impossible?, ECMI Commentary No 46, 4 September 2017.
251 H. Kraemer-Eis, SME securitisation in Europe – a short summary.
moving to one where SME securitisation is increasingly viewed as an instrument that could help overcome the negative effects of the crisis.\textsuperscript{253}

6.6. EU policies and initiatives to boost SME financing

In view of the above, the EU supports SME access to finance in a number of ways – legislative acts create framework conditions, while various programmes and initiatives target specific financing needs, for example supporting the innovation activities or providing guarantees for bank loans. Since European SMEs operate mostly in sectors characterised by either low knowledge or technology intensities or low export intensities, there is substantial policy interest in encouraging them to become more innovative and export. Expanding beyond borders is thought to increase SME growth and innovation. They also can benefit from new market opportunities, as well as new resources and improved efficiency. The economic literature supports the view that the most productive and innovative usually firms engage in internationalisation.\textsuperscript{254}

6.6.1. Capital markets union

The CMU is one of the flagships of the current Commission. As emphasised earlier it was launched with the aims of deepening financial integration, increasing the stability of the financial system, attracting investment and developing local capital markets. It is also intended to increase the availability of market-based sources of finance (currently underused at less than 15\%) for start-ups and SMEs, which need more funding for innovation and growth. Furthermore, the aim of the CMU is to lower the high fixed costs of access to the stock market (currently up to 15\% of the amount raised) to enable small businesses to use this important financing possibility.

The prospectus rules adopted in June 2017 exempt the smallest capital raisings from the costly obligation to prepare a prospectus. Start-ups and SMEs will be allowed to raise up to \euro 1 million in capital on local markets without having to publish one. It will become mandatory from \euro 8 million only, and Member States will be able to set their own obligation as long as the capital raised is between \euro 1 million and \euro 8 million.

In December 2017 the EU adopted a securitisation package to boost lending via SME asset-backed securities and commercial papers. Furthermore, new rules facilitate the transfer of risk from banks’ balance sheets, making more capital available for SMEs. The costs of securitisation for SMEs should also be lowered by resulting improved consistency and standardisation on the markets.

In order to boost investment in innovative start-up and scale-up companies the EU adopted the revision to the regulation on European venture capital funds (EuVECA) in October 2017. This set up the rules to help investment firms support SMEs by means of increased flexibility on eligible investments, an enlarged scope and lower costs for funds. Furthermore, the European Commission and the European Investment Fund (EIF) launched a pan-European Venture Capital Fund-of-Funds Programme (VentureEU) in April 2018. The Union will back the participating funds with \euro 410 million of funding. In turn, these funds are designed to raise up to \euro 2.1 billion of public and private investment, which is to trigger an estimated \euro 6.5 billion of new investment in innovative SMEs. Expected results include greater diversification of funding, promotion of innovation and non-listed companies, and more SMEs financed for a longer period of time.


\textsuperscript{254} See for example C. Altomonte, T. Aquilante, G. Békés, G. Ottaviano, Internationalisation and innovation of firms: Give them one roof, CEPR Policy Portal, 2014.
There are SME-focused proposals as part of the CMU that still need to be adopted by the co-legislators. In March 2018, in order to increase access to finance for entrepreneurs, start-ups, scale-ups and SMEs in general, the Commission proposed new rules on crowdfunding. The aim is to create an alternative to bank lending, which, while being the main source of external finance for SMEs, is often costly or difficult to access owing to the absence of credit history or a lack of tangible collateral. The Commission is proposing to establish an EU regime that would be voluntary for crowdfunding service providers. The new rules would ensure that participating providers comply with one set of rules only, whether operating in their domestic market or across the EU. This is expected to attract more investors and projects for funding and provide legal certainty, which should all help to boost SME financing via the crowdfunding channel.

In May 2018, the Commission proposed new rules on SME growth markets which are a new category of trading venue created by the Markets in Financial Instruments Directive II (MiFID II) to improve SME access to capital. This initiative is expected to increase the number of initial public offerings (IPOs) by SMEs, attract more investors to SMEs listed on those markets and increase liquidity so that SME shares can be traded more easily. Furthermore, the new rules would reduce the administrative burden for SMEs, facilitate the registration of bond issuing trading venues, and allow a lighter prospectus for issuers with at least three years of listing on SME growth markets when they transfer to a regulated market.

The proposal of May 2017 on a European market infrastructure regulation aims to introduce simpler, transparent and more efficient rules on over the counter (OTC) derivatives. The Commission expects SMEs to benefit from improved access to derivatives clearing, simplified reporting requirements and reduced regulatory requirements.

In March 2018, the Commission adopted a proposal on the cross-border distribution of collective investment funds, which is designed to eliminate the current regulatory barriers to the growth of such funds and as such is likely to increase their investments in SMEs, in particular by venture capital funds. The same month it also tabled new legislation on the third-party proprietary effects of the cross-border assignment of claims, which would harmonise laws at EU level providing legal certainty for parties involved in factoring, collateralisation and securitisation and as such facilitating access to cheaper finance for SMEs.

6.6.2. Programme for competitiveness and SMEs (COSME)

The EU’s programme for competitiveness and SMEs (COSME) has a total budget of €2.3 billion for the 2014 to 2020 period. At least 60% of the financial envelope, which totals €1.4 billion, is earmarked to facilitate SMEs’ access to finance. Using the high leverage effect, COSME is expected to mobilise around €20 billion in guaranteed loans and around €4 billion for equity finance. The programme uses two financial instruments managed by the European Investment Fund (EIF) in cooperation with financial intermediaries in the Member States.

The COSME loan guarantee facility (LGF) supports guarantees and counter-guarantees to financial institutions, so that they can provide SMEs with more loans and leases. It also supports the securitisation of SME debt finance portfolios. The LGF enables risk sharing so that financial intermediaries can serve a wider range of SMEs and support more types of financial transaction. The latest available data shows that 92 guarantee contracts for a total guarantee of more than €1 billion have been signed. The instrument enables support for almost 350,000 SMEs (half of them start-ups) and 1.6 million jobs. The LGF is now expected to provide SMEs with more than €29 billion

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255 I. Zachariadis, Enabling SMEs’ access to capital markets, EPRS, European Parliament, November 2018.

256 European Investment Bank, Competitiveness of enterprises and SMEs – Loan Guarantee Facility, June 2018.
in total financing. Furthermore, the Commission estimates that 90% of beneficiaries will be from the category that currently faces the most difficulty obtaining finance: companies with 10 or fewer employees.

The second instrument, the **COSME equity facility for growth**, invests in selected risk capital funds that focus on providing venture capital and mezzanine finance. They support SMEs with significant potential and those operating across borders during their expansion and growth stages. As of the end of June 2018 the facility was active in nine countries with more than €115 million in financial support offered.

6.6.3. Horizon 2020

The EU funds many SMEs through its largest framework programme offering direct financial support for their research, development and innovation projects. Horizon 2020 is expected to help over 7 500 companies with innovation support under the current multiannual financial framework. The Commission initially expected that 20% of the total combined budget for all the ‘Societal Challenges’ Europe 2020 policy priority and for the specific Horizon 2020 ‘Leadership in Enabling and Industrial Technologies’ objective would go to SMEs. This was however exceeded by the end of 2017 by more than 4 percent points, with SMEs having received €4.13 billion in grant money under these two objectives. By the time the programme ends in 2020 the Commission expects that as much as €8 billion will have financed either consortia in which SMEs collaborate with other firms and research organisations or individual innovative firms. In fact the main programmes supporting SMEs, such as Horizon 2020 and COSME, received a high number of eligible submissions, exhausting their resources and as a result the envelope for the ‘Competitiveness for growth and jobs’ the budget heading was increased during the mid-term revision of the 2014 to 2020 MFF by €875 million.

As part of the Horizon 2020 programme, the EU set up a **European Innovation Council (EIC)** that supports market-creating innovation and the rapid scale-up of European enterprises, in particular SMEs. Between 2018 and 2020 the EIC pilot will make €2.7 billion available to breakthrough innovations. The EIC was launched in October 2017 as an umbrella project grouping together the **SME Instrument**\(^{257}\), **Fast Track to Innovation (FTI)**, **Future and Emerging Technologies (FET) Open, and Horizon Prizes**, to provide a ‘one stop shop’ for funding for high potential innovations in the EU. Importantly, the SME Instrument addresses the financing gap in developing the high-potential and high-risk innovative ideas of small companies and helping to market them. Furthermore, the Horizon 2020 ‘Innovation in SMEs’ specific objective supports the innovation capacity of firms, including through the **Eurostars Joint Programme** – with a budget of €1.14 billion – which focuses on promoting the transnational collaboration of SMEs dedicated to research and development activities.

**InnovFin** is a joint initiative launched by the European Investment Bank Group (EIB and EIF) in cooperation with the Commission that covers the entire value chain of research and innovation. By 2020 it is expected to make over €24 billion of debt and equity financing available to innovative enterprises, which will support a further €48 billion of final investments. Innovfin is active in 42 countries supporting over 11 000 companies, 110 innovative projects, 590 000 jobs and offering €14.2 billion in financing. SME funding is being dispersed via multiple instruments: (i) **InnovFin SME Guarantee**, a debt facility providing loans, guarantees and other forms of debt finance mainly to research and innovation-driven SMEs (which has increased the pool of loans available for SMEs

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\(^{257}\) The Commission estimates that around 4 000 SMEs will be selected to receive funding under the SME instrument call with lump sums of €50 000 per project. The total budget of the instrument is close to €3 billion for the 2014 to 2020 period.
and small midcaps across both the EU and Horizon 2020 associated countries by more than €10 billion since its launch in 2014), (ii) **InnovFin Equity**, which comprises equity facilities providing funding for mostly early-stage investments, with focus on early-stage SMEs with high-growth potential, (iii) **InnovFin Technology Transfer** supporting companies active in key enabling technologies field, (iv) **InnovFin Business Angels**, targeting investments in business angel managed funds or co-investment funds, (v) **InnovFin Venture Capital** focusing on investments in venture capital funds that provide funding for firms in their early-stages, (vi) **InnovFin Fund-of-Funds**, which provides funding for the Pan-European Venture Capital Fund(s)-of-Funds Programme and (vii) **InnovFin Advisory**, which helps SMEs to structure their research and innovation projects in order to improve their access to finance. More specifically focused programmes supporting SMEs include **InnovFin Energy Demo projects**, **InovFin Infectious Diseases Facility** and **InnovFin Thematic Investment Platforms** which deal with the bioeconomy and the circular economy.258

### 6.6.4. European structural and investment funds

One of the 11 thematic cohesion policy objectives is ‘improving the competitiveness of SMEs’. Investments and assistance for SMEs are also accessible under other thematic objectives, particularly under ‘research and innovation’, ‘the low-carbon economy’ and ‘information and communication technologies’. The total budget for the competitiveness of SMEs theme is almost €95 billion for the 2014 to 2020 period259 and the objective is to target 800 000 SMEs. Cohesion policy is implemented mainly through the **European structural and investment funds** (ESIF funds). These funds are delivered through nationally co-financed multiannual programmes, and managed by Member States and regions.

The ESI funds facilitate access to finance through facilities such as grants, loans, loan guarantees and venture capital. The funds also focus on facilitating SME access to global markets and international value chains and exploiting new sources of growth such as the green economy, sustainable tourism, health and social services. Furthermore, they support investment in human capital and vocational education and training, and forge links between SMEs, research centres and universities. The rules enabling SMEs to access cohesion policy funds have been simplified by measures such as online reporting on the use of funds, clearer eligibility rules, and less frequent audits for small operations. Cohesion policy helped more than 95 000 start-ups and helped generate more than 300 000 jobs. The **European Regional Development Fund** (ERDF) is the largest EU financial tool supporting SMEs. As much as €57 billion or around 20 % of funding from the fund is dedicated exclusively to SMEs. It helps SMEs and entrepreneurs in areas such as research, technological development and innovation, access to and use of ICT, competitiveness, employment promotion and labour mobility.

The **European Social Fund** (ESF) has for the first time been linked with SME and entrepreneurial policies in the current financial framework. It supports employment, labour mobility, investment in education and skills, and enhancing business friendly public administration. It also is used for provision of microfinance.

In the context of SMEs the **European Agricultural Fund for Rural Development** focuses on co-investment in competitiveness, innovation, modernisation, know-how, ICT skills and diversification of activities (e.g. from rural into non-rural ones).

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258 For more details please refer to the [InnovFin: EU Finance for innovators](#) booklet.

259 The EU funds two thirds of the projects and the Member States one third.
The **European Maritime and Fisheries Fund** (EMFF) supports SMEs by helping them to diversify the coastal economies and by financing projects that make fishing profitable, support small-scale fisheries, develop sustainable aquaculture and improve scientific knowledge.

Within the ESI framework projects can be financed via grants and financial instruments. The scope for use of the latter has been broadened in the 2014 to 2020 period. The new financial instrument, called the 'co-investment facility to provide funding to start-ups and SMEs', was launched in 2016 with the aim of combining public and private financial resources and increasing fund take-up by Member States. It will help SMEs to develop their business models and draw additional funding through a collective public-private investment scheme that can amount to as much as €15 million per SME.

### 6.6.5. The Investment Plan for Europe

The plan's main instrument is the **European Fund for Strategic Investments** (EFSI), which provides EU guarantees to trigger private investment. One of the main targets of EFSI is to provide support for SMEs. Its main added value is to take on a part of the risk of new projects through a first-loss liability, through which the fund enables private investors to take part in projects under favourable conditions. Data from November 2018 shows that almost €360 billion worth of investments are expected to be mobilised, providing assistance for around 850,000 SMEs. Available funding includes loans, microfinance and guarantees or equity funding through venture capital funds, business angels or social investors supporting SMEs with high growth potential. These companies are often characterised by a higher risk profile, and are active in research and innovation or undertaking social activities. Later stages of SME development are supported by the **expansion and growth window** of the European Investment Fund. It provides equity financing for more vulnerable SMEs, targeting social enterprises and social sector organisations.

In response to a Commission proposal, the European Parliament and the Council agreed to extend the duration of the fund until 31 December 2020 and increase the EU guarantee from €16 to 26 billion and EIB capital from €5 to €7.5 billion, which is expected to trigger private and public investment of €500 billion over the extension period. EFSI has already a dedicated **SME Window** that offers up to a total of €5.5 billion of either funding resources or guarantee capacity. The Commission recognised a need to dedicate a larger part of financing to SMEs since 'the market absorption has been particularly quick under the SME window where the EFSI is delivering well beyond expectations'. Consequently, the SME window has been scaled up under the present framework with €500 million transferred from the infrastructure and innovation window in July 2016. Increased focus on SMEs would be ensured by directing 40% of the increased risk bearing capacity towards these type of firms. According to the proposal, particular attention would be paid to social enterprises and to EFSI's social dimension.

### 6.6.6. The SME initiative

This initiative is a joint financial instrument of the European Commission and the EIB Group that aims to mobilise SME financing by providing partial risk cover for the SME loan portfolios of financial institutions (risk-sharing). It uses funds from COSME, Horizon 2020 and the European structural and investment funds combined with resources from the EIB and EIF. The financial intermediaries selected to take part can gain access to loss protection and potential capital relief at an

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advantageous cost. In return they provide SME loans, leasing and/or guarantees at favourable terms. The initiative is currently operating in five Member States.261

6.6.7. Microfinance and social entrepreneurship

One of the three axes of the Programme for Employment and Social Innovation (EaSI) is to support access to microfinance and social entrepreneurship.262 It does so by providing micro-loans and equity (less than €25 000) for micro-enterprises and people unable to become self-employed because of difficulties in accessing traditional banking services. In the EU, as many as 91 % of all start-ups are micro enterprises. Under the programme, the European Investment Fund is managing two financial tools: (i) the EaSI guarantee instrument, designed to increase access to finance for social enterprises, micro-enterprises and vulnerable groups with a budget of €96 million, and (ii) the EaSI capacity building investments window, to enhance the institutional capacity of micro-credit and social finance providers with a budget of €16 million. Data from October 2016 shows that since 2014 the EIF has signed 33 transactions in 18 countries, generating €660 million of financing for over 50 000 micro-enterprises and social enterprises.

6.6.8. SMEs in cultural and creative sectors

Access to finance can be challenging for SMEs operating in the cultural and creative sectors, mainly on account of the intangible nature of their assets and collaterals, the relatively small size of the market, demand uncertainty and the shortage of financial intermediary expertise. Therefore, in order to increase lending to SMEs and enable them to scale up their activities, the EU has established a cultural and creative sectors guarantee facility under the Creative Europe programme. This scheme, with a budget of €121 million, is expected to create more than €600 million worth of bank loans in the 2014 to 2020 period. So far, financial intermediaries from Spain, France and Romania have signed agreements with the EIF.

6.6.9. Long-term investment funds

In 2015 the EU adopted a regulation on European long-term investment funds (ELTIFs).263 These funds allow investors to finance companies and projects that require long-term capital. Importantly, listed SMEs that issue equity or debt instruments can be financed using ELTIFs. The regulation established standard ELTIF operation rules, in particular specifying requirements on the composition of their portfolios and the investment instruments that they are permitted to use to secure exposure to long-term assets, such as equity or debt instruments issued by both listed and unlisted SMEs.

6.7. Outlook for 2019

In the 2018 SME performance review the Commission estimates that SME value added in the EU-28 non-financial business sector will increase by 4.3 % in 2019 (the same as in 2018). This figure is slightly higher than the 4 % growth predicted for large enterprises in 2019. Similarly, in terms of employment, SMEs with an expected growth rate of 1.3 % in 2019 are expected to marginally outperform large enterprises, which are forecasted to grow by 1 %.

261 Bulgaria, Finland, Malta, Romania and Spain.
262 The other two concern modernisation of employment and social policies as well as job mobility.
Furthermore, the Enterprise Europe Network published its annual SME survey in November 2018. Overall, European SMEs manifested an upswing in confidence. The survey showed that two out of three SMEs which internationalise were expecting to increase their turnover in the following 12 months, while one in three also expected to create new jobs. More than half of SMEs surveyed expected to increase their market share and more than a third also anticipated realising improvements in their products or services through innovation. The most confident group of SMEs were those with global ambitions – two thirds of them expected to increase their market share in 2019.

As regards financing, the latest SAFE survey highlights that about 45 % of SMEs in the EU28 do not foresee any limitations in their access to future financing. Others that did express the possibility of facing difficulties in accessing financing in the future, cited high interest rates and financing prices, as well as insufficient collateral or guarantees as the principal sources of limitation. Geographically, SMEs in Belgium and Finland appear to expect no obstacles more frequently than other EU Member States, while the country where this is least observed is Greece. On balance, however, according to the SAFE survey, SMEs expect the availability of all types of financing to improve in the six months from October 2018 to March 2019. Concerning the main factors that can affect their future financing, SMEs cite tax incentives and making existing public measures easier to obtain as the most important factors. Business support services and guarantees for loans follow in importance, while measures to facilitate equity investments and export credits or guarantees come at the end of their scaling. Finally, it remains to be seen how the end of quantitative easing in the euro area, especially if followed by a rise in the interest rates, will affect SMEs and their capacity to access new financing in the future.

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## 8. Annexes

Annex 1 – EU spending allocation by Member State in 2017 (€ million)

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### Economic and Budgetary Outlook for the European Union 2019

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### Annex 2 – Own resources by Member State in 2017 (€ million and % of GNI)

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<th>Lump sum reduction granted for DK, NL, AT &amp; SE</th>
<th>Total national contribution</th>
<th>Traditional own resources (TOR), net (80 %)</th>
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<td>4</td>
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<td>6=1+2+3+4+5</td>
<td>% GNI</td>
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### Economic and Budgetary Outlook for the European Union 2019

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Data source: European Commission, [Financial report 2017](#).
### Annex 3 - the EU budget 2018, 2019

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<td>CA</td>
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## Economic and Budgetary Outlook for the European Union 2019

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<th>57 192.000</th>
<th>47 035.410</th>
<th>3.0%</th>
<th>1.1%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment for growth and jobs</td>
<td>50 797.976</td>
<td>43 447.389</td>
<td>52 357.460</td>
<td>43 736.616</td>
<td>3.1%</td>
<td>0.7%</td>
</tr>
<tr>
<td>Regional convergence (less developed regions)</td>
<td>27 012.258</td>
<td>23 387.572</td>
<td>27 875.240</td>
<td>24 042.312</td>
<td>3.2%</td>
<td>2.8%</td>
</tr>
<tr>
<td>Transition regions</td>
<td>5 738.604</td>
<td>4 040.463</td>
<td>5 848.702</td>
<td>4 370.076</td>
<td>1.9%</td>
<td>8.2%</td>
</tr>
<tr>
<td>Competitiveness (more developed regions)</td>
<td>8 426.792</td>
<td>7 394.060</td>
<td>8 648.891</td>
<td>7 441.507</td>
<td>2.6%</td>
<td>0.6%</td>
</tr>
<tr>
<td>Outermost and sparsely populated regions</td>
<td>226.473</td>
<td>169.014</td>
<td>231.005</td>
<td>176.442</td>
<td>2.0%</td>
<td>4.4%</td>
</tr>
<tr>
<td>Cohesion fund</td>
<td>9 393.849</td>
<td>8 456.279</td>
<td>9 753.622</td>
<td>7 706.279</td>
<td>3.8%</td>
<td>-8.9%</td>
</tr>
<tr>
<td>Connecting Europe Facility (CEF) — CF contribution</td>
<td>1 655.141</td>
<td>625.755</td>
<td>1 700.429</td>
<td>851.591</td>
<td>2.7%</td>
<td>36.1%</td>
</tr>
<tr>
<td>European territorial cooperation</td>
<td>1 934.269</td>
<td>1 234.672</td>
<td>1 972.954</td>
<td>1 190.567</td>
<td>2.0%</td>
<td>-3.6%</td>
</tr>
<tr>
<td>Youth Employment initiative (specific top-up allocation)</td>
<td>350.000</td>
<td>600.000</td>
<td>350.000</td>
<td>631.500</td>
<td>0.0%</td>
<td>5.3%</td>
</tr>
<tr>
<td>Technical assistance and innovative actions</td>
<td>230.285</td>
<td>199.613</td>
<td>239.702</td>
<td>212.747</td>
<td>4.1%</td>
<td>6.6%</td>
</tr>
<tr>
<td>European Aid to the Most Deprived (FEAD)</td>
<td>556.875</td>
<td>401.400</td>
<td>567.780</td>
<td>401.200</td>
<td>2.0%</td>
<td>0.0%</td>
</tr>
<tr>
<td>Pilot projects and preparatory actions</td>
<td>350.000</td>
<td>600.000</td>
<td>350.000</td>
<td>631.500</td>
<td>2.0%</td>
<td>36.1%</td>
</tr>
</tbody>
</table>

### SUSTAINABLE GROWTH: NATURAL RESOURCES

<table>
<thead>
<tr>
<th></th>
<th>59 238.558</th>
<th>56 040.991</th>
<th>59 642.078</th>
<th>57 399.857</th>
<th>0.7%</th>
<th>2.4%</th>
</tr>
</thead>
<tbody>
<tr>
<td>European Agricultural Guarantee Fund (EAGF)</td>
<td>43 233.117</td>
<td>43 187.277</td>
<td>43 191.947</td>
<td>43 116.399</td>
<td>-0.1%</td>
<td>-0.2%</td>
</tr>
<tr>
<td>European Agricultural Fund for Rural Development (EAFRD)</td>
<td>14 380.314</td>
<td>11 852.226</td>
<td>14 727.263</td>
<td>13 148.188</td>
<td>2.4%</td>
<td>10.9%</td>
</tr>
<tr>
<td>European Maritime and Fisheries Fund (EMFF)</td>
<td>933.361</td>
<td>514.547</td>
<td>942.055</td>
<td>570.725</td>
<td>0.9%</td>
<td>10.9%</td>
</tr>
<tr>
<td>Sustainable Fisheries Partnership Agreements (SFPAs) and compulsory contributions to Regional Fisheries Management Organisations (RFMOs) and to other international organisations</td>
<td>94.535</td>
<td>88.297</td>
<td>147.900</td>
<td>142.035</td>
<td>56.4%</td>
<td>60.9%</td>
</tr>
<tr>
<td>Environment and climate action (LIFE)</td>
<td>522.797</td>
<td>316.101</td>
<td>558.071</td>
<td>341.561</td>
<td>6.7%</td>
<td>8.1%</td>
</tr>
<tr>
<td>Other actions and measures</td>
<td>0.000</td>
<td>6.000</td>
<td>0.000</td>
<td>0.000</td>
<td>∞</td>
<td>-100.0%</td>
</tr>
<tr>
<td>Pilot projects and preparatory actions</td>
<td>15.600</td>
<td>17.708</td>
<td>13.500</td>
<td>19.607</td>
<td>-13.5%</td>
<td>10.7%</td>
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<tr>
<td>Decentralised agencies</td>
<td>58.834</td>
<td>58.834</td>
<td>61.342</td>
<td>61.342</td>
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<td>4.3%</td>
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### SECURITY AND CITIZENSHIP

<table>
<thead>
<tr>
<th></th>
<th>3 493.241</th>
<th>2 980.707</th>
<th>3 786.629</th>
<th>3 527.435</th>
<th>8.4%</th>
<th>18.3%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asylum, Migration and Integration Fund</td>
<td>719.155</td>
<td>594.385</td>
<td>1 120.814</td>
<td>952.604</td>
<td>55.9%</td>
<td>60.3%</td>
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<tr>
<td>Internal Security Fund</td>
<td>719.986</td>
<td>481.234</td>
<td>533.498</td>
<td>663.722</td>
<td>-25.9%</td>
<td>37.9%</td>
</tr>
<tr>
<td>IT systems</td>
<td>26.334</td>
<td>13.167</td>
<td>0.100</td>
<td>0.000</td>
<td>-99.6%</td>
<td>-100.0%</td>
</tr>
<tr>
<td>Justice</td>
<td>47.149</td>
<td>35.871</td>
<td>44.625</td>
<td>38.137</td>
<td>-5.4%</td>
<td>6.3%</td>
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<td>Rights, equality and citizenship</td>
<td>63.382</td>
<td>46.600</td>
<td>65.721</td>
<td>57.950</td>
<td>3.7%</td>
<td>24.4%</td>
</tr>
<tr>
<td>-------------------------------------------------------------------------</td>
<td>-------</td>
<td>-------</td>
<td>-------</td>
<td>-------</td>
<td>---------</td>
<td>---------</td>
</tr>
<tr>
<td>— Union Civil Protection Mechanan</td>
<td>33,246</td>
<td>34,270</td>
<td>149,556</td>
<td>81,660</td>
<td>349.8%</td>
<td>138.3%</td>
</tr>
<tr>
<td>— Europe for Citizens</td>
<td>27,555</td>
<td>28,634</td>
<td>28,682</td>
<td>29,222</td>
<td>4.1%</td>
<td>2.1%</td>
</tr>
<tr>
<td>— Food and feed</td>
<td>280,178</td>
<td>248,375</td>
<td>289,691</td>
<td>239,272</td>
<td>3.4%</td>
<td>-3.7%</td>
</tr>
<tr>
<td>— Health</td>
<td>66,374</td>
<td>55,907</td>
<td>68,308</td>
<td>61,250</td>
<td>2.9%</td>
<td>9.6%</td>
</tr>
<tr>
<td>— Consumer</td>
<td>27,966</td>
<td>23,091</td>
<td>29,255</td>
<td>23,608</td>
<td>4.6%</td>
<td>2.2%</td>
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<tr>
<td>— Creative Europe</td>
<td>230,386</td>
<td>180,685</td>
<td>244,843</td>
<td>194,780</td>
<td>6.3%</td>
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<td>— Instrument for Emergency Support within the Union (IES)</td>
<td>200,000</td>
<td>220,583</td>
<td>0.250</td>
<td>69,537</td>
<td>-99.9%</td>
<td>-68.5%</td>
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<tr>
<td>— Actions financed under the prerogatives of the Commission and specific competences conferred to the Commission</td>
<td>98,757</td>
<td>91,713</td>
<td>105,790</td>
<td>99,881</td>
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<tr>
<td>— Of which ‘Communication actions’</td>
<td>73,393</td>
<td>72,341</td>
<td>77,118</td>
<td>74,000</td>
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<td>2.3%</td>
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<tr>
<td>— Pilot projects and preparatory actions</td>
<td>12,650</td>
<td>17,922</td>
<td>15,075</td>
<td>18,261</td>
<td>19.2%</td>
<td>1.9%</td>
</tr>
<tr>
<td>— Decentralised agencies</td>
<td>940,124</td>
<td>908,271</td>
<td>1,090,422</td>
<td>997,551</td>
<td>16.0%</td>
<td>9.8%</td>
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<tr>
<td>GLOBAL EUROPE</td>
<td>10,068,842</td>
<td>8,906,075</td>
<td>11,319,266</td>
<td>9,358,296</td>
<td>12.4%</td>
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<tr>
<td>— Instrument for Pre-Accession Assistance (IPA II)</td>
<td>2,078,771</td>
<td>1,451,614</td>
<td>2,423,420</td>
<td>1,707,516</td>
<td>16.6%</td>
<td>17.6%</td>
</tr>
<tr>
<td>— European Neighbourhood Instrument (ENI)</td>
<td>2,436,637</td>
<td>2,278,002</td>
<td>2,677,281</td>
<td>2,060,307</td>
<td>9.9%</td>
<td>-9.6%</td>
</tr>
<tr>
<td>— Development Cooperation Instrument (DCI)</td>
<td>2,976,020</td>
<td>2,734,530</td>
<td>3,189,899</td>
<td>2,796,283</td>
<td>7.2%</td>
<td>2.3%</td>
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<tr>
<td>— Partnership instrument for cooperation with third countries (PI)</td>
<td>140,187</td>
<td>100,715</td>
<td>154,004</td>
<td>99,605</td>
<td>9.9%</td>
<td>-1.1%</td>
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<tr>
<td>— European Instrument for Democracy and Human Rights (EIDHR)</td>
<td>192,750</td>
<td>169,347</td>
<td>196,658</td>
<td>159,311</td>
<td>2.0%</td>
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</tr>
<tr>
<td>— Instrument contributing to Stability and Peace (cSP)</td>
<td>370,010</td>
<td>325,265</td>
<td>376,737</td>
<td>321,300</td>
<td>1.8%</td>
<td>-1.2%</td>
</tr>
<tr>
<td>— Humanitarian aid (HUMA)</td>
<td>1,085,394</td>
<td>1,094,987</td>
<td>1,651,824</td>
<td>1,603,043</td>
<td>52.2%</td>
<td>46.4%</td>
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<tr>
<td>— Common Foreign and Security Policy (CFSP)</td>
<td>328,010</td>
<td>292,021</td>
<td>334,857</td>
<td>305,500</td>
<td>2.1%</td>
<td>4.6%</td>
</tr>
<tr>
<td>— Instrument for Nuclear Safety Cooperation (INSC)</td>
<td>32,967</td>
<td>45,461</td>
<td>33,630</td>
<td>41,476</td>
<td>2.0%</td>
<td>-8.8%</td>
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<tr>
<td>— Macro-financial Assistance (MFA)</td>
<td>42,086</td>
<td>42,086</td>
<td>27,000</td>
<td>27,000</td>
<td>-35.8%</td>
<td>-35.8%</td>
</tr>
<tr>
<td>— Guarantee Fund for external actions (GF)</td>
<td>137,801</td>
<td>137,801</td>
<td>0.000</td>
<td>0.000</td>
<td>-100.0%</td>
<td>-100.0%</td>
</tr>
<tr>
<td>— Union Civil Protection Mechanan</td>
<td>16,121</td>
<td>15,467</td>
<td>23,546</td>
<td>20,665</td>
<td>46.1%</td>
<td>33.6%</td>
</tr>
<tr>
<td>— EU Aid Volunteers initiative (EUAV)</td>
<td>20,328</td>
<td>16,874</td>
<td>19,537</td>
<td>16,054</td>
<td>-3.9%</td>
<td>-4.9%</td>
</tr>
<tr>
<td>— European Fund for Sustainable Development (EFSD)</td>
<td>25,000</td>
<td>25,000</td>
<td>25,000</td>
<td>25,000</td>
<td>0.0%</td>
<td>0.0%</td>
</tr>
<tr>
<td>— Other actions and programmes</td>
<td>83,452</td>
<td>74,903</td>
<td>83,606</td>
<td>72,954</td>
<td>0.2%</td>
<td>-2.6%</td>
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<tr>
<td>— Actions financed under the prerogatives of the Commission and specific competences conferred to the Commission</td>
<td>74,352</td>
<td>67,555</td>
<td>75,452</td>
<td>73,684</td>
<td>1.5%</td>
<td>9.1%</td>
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<tr>
<td>— Pilot projects and preparatory actions</td>
<td>8,900</td>
<td>14,391</td>
<td>6,325</td>
<td>8,109</td>
<td>-28.9%</td>
<td>-43.7%</td>
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<tr>
<td>— Decentralised agencies</td>
<td>20,056</td>
<td>20,056</td>
<td>20,489</td>
<td>20,489</td>
<td>2.2%</td>
<td>2.2%</td>
</tr>
</tbody>
</table>
### Administration

<table>
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<tr>
<th>Description</th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
<th>Change</th>
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</thead>
<tbody>
<tr>
<td>— Of which: administrative expenditure of the institutions</td>
<td>7,579,921</td>
<td>7,580,726</td>
<td>7,747,286</td>
<td>7,749,216</td>
<td>2.2%</td>
</tr>
<tr>
<td>— Pensions and European Schools</td>
<td>2,085,593</td>
<td>2,085,593</td>
<td>2,195,689</td>
<td>2,195,689</td>
<td>5.3%</td>
</tr>
<tr>
<td></td>
<td>— Pensions</td>
<td>1,892,806</td>
<td>1,892,806</td>
<td>2,003,592</td>
<td>2,003,592</td>
</tr>
<tr>
<td></td>
<td>— European schools</td>
<td>192,787</td>
<td>192,787</td>
<td>192,097</td>
<td>192,097</td>
</tr>
<tr>
<td>— Administrative expenditure of the institutions</td>
<td>7,579,921</td>
<td>7,580,726</td>
<td>7,747,286</td>
<td>7,749,216</td>
<td>2.2%</td>
</tr>
<tr>
<td>— European Parliament</td>
<td>1,950,242</td>
<td>1,950,242</td>
<td>1,996,363</td>
<td>1,996,363</td>
<td>2.4%</td>
</tr>
<tr>
<td>— European Council and Council</td>
<td>572,894</td>
<td>572,894</td>
<td>581,895</td>
<td>581,895</td>
<td>1.6%</td>
</tr>
<tr>
<td>— European Commission</td>
<td>3,565,497</td>
<td>3,566,302</td>
<td>3,632,742</td>
<td>3,634,672</td>
<td>1.9%</td>
</tr>
<tr>
<td>— Court of Justice of the European Union</td>
<td>409,985</td>
<td>409,985</td>
<td>429,410</td>
<td>429,410</td>
<td>4.7%</td>
</tr>
<tr>
<td>— European Court of Auditors</td>
<td>146,016</td>
<td>146,016</td>
<td>146,891</td>
<td>146,891</td>
<td>0.6%</td>
</tr>
<tr>
<td>— European Economic and Social Committee</td>
<td>135,631</td>
<td>135,631</td>
<td>138,503</td>
<td>138,503</td>
<td>2.1%</td>
</tr>
<tr>
<td>— European Committee of the Regions</td>
<td>96,101</td>
<td>96,101</td>
<td>98,751</td>
<td>98,751</td>
<td>2.8%</td>
</tr>
<tr>
<td>— European Ombudsman</td>
<td>10,628</td>
<td>10,628</td>
<td>11,279</td>
<td>11,279</td>
<td>6.1%</td>
</tr>
<tr>
<td>— European data protection Supervisor</td>
<td>14,449</td>
<td>14,449</td>
<td>16,639</td>
<td>16,639</td>
<td>15.2%</td>
</tr>
<tr>
<td>— European External Action Service</td>
<td>678,479</td>
<td>678,479</td>
<td>694,813</td>
<td>694,813</td>
<td>2.4%</td>
</tr>
<tr>
<td>APPROPRIATIONS FOR HEADINGS</td>
<td>159,997,953</td>
<td>144,216,678</td>
<td>165,218,397</td>
<td>147,787,440</td>
<td>3.3%</td>
</tr>
</tbody>
</table>

**Data source:** European Commission. Figures for the 2019 budget have been approved (see Section 4), and await final publication in the Official Journal of the European Union. See also: European Parliament, Resolution on the Council position on the second draft general budget of the European Union for the financial year 2019, Strasbourg, 10 December 2018.
Annex 4 – List of rapporteurs of main budgetary procedures relevant for 2019

**Committee on Budgets (BUDG)**

<table>
<thead>
<tr>
<th>Chair: Jean Arthuis (ALDE, France)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Multiannual financial framework 2021-2027</strong></td>
</tr>
<tr>
<td>Rapporteurs: Jan Olbrycht (EPP, Poland), Isabelle Thomas (S&amp;D, France)</td>
</tr>
<tr>
<td>Shadow rapporteurs: Gérard Deprez (ALDE, Belgium), Marco Valli (EFDD, Italy)</td>
</tr>
<tr>
<td><strong>System of own resources of the European Union</strong></td>
</tr>
<tr>
<td>Rapporteurs: Janusz Lewandowski (EPP, Poland), Gérard Deprez (ALDE, Belgium)</td>
</tr>
<tr>
<td>Shadow rapporteurs: Younous Omarjee (GUE/NGL, France), Marco Valli (EFFD, Italy)</td>
</tr>
</tbody>
</table>

**2019 general budget**: all sections

| Rapporteurs: Paul Rübig (EPP, Austria), Daniele Viotti (S&D, Italy) |
| Shadow rapporteurs: Monika Hohlmeier (EPP, Germany), Bernd Kölmel (ECR, Germany), Gérard Deprez (ALDE, Belgium), Líadh Ní Riada (GUE, Ireland), Stanisław Złotek (ENF, Poland), Eider Gardiazabal Rubial (S&D, Spain), Nedzhmi Ali (ALDE, Bulgaria), Younous Omarjee (GUE, France), Indrek Tarand (Greens/EFA, Estonia), Marco Valli (EFFD, Italy), Marco Zanni (ENF, Italy) |

**Budgetary Control Committee (CONT)**

<table>
<thead>
<tr>
<th>Chair: Ingeborg Grässle (EPP, Germany)</th>
</tr>
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<tbody>
<tr>
<td><strong>2017 discharge – EU general budget, European Commission</strong></td>
</tr>
<tr>
<td>Rapporteur: Inés Ayala Sender (S&amp;D, Spain)</td>
</tr>
<tr>
<td>Shadow rapporteurs: Ingeborg Grässle (EPP, Germany), Ryszard Czarnecki (ECR, Poland), Martina Dlabajová (ALDE, Czech Republic), Luke Ming Flanagan (GUE/NGL, Ireland), Bart Staes (Greens/EFA, Belgium) Jean-François Jalkh (ENF, France)</td>
</tr>
</tbody>
</table>

| **2017 discharge – ECA’s special reports** |
| Rapporteur: Inés Ayala Sender (S&D, Spain) |
| Shadow rapporteurs: Ingeborg Grässle (EPP, Germany), Ryszard Czarnecki (ECR, Poland), Martina Dlabajova (ALDE, Czech Republic), Luke Ming Flanagan (GUE/NGL, Ireland), Bart Staes (Greens/EFA, Belgium) Jean-François Jalkh (ENF, France) |

| **2017 discharge – European Development Funds (EDFs)** |
| Rapporteur: Marco Valli (EFFD, Italy) |
| Shadow rapporteurs: Joachim Zeller (EPP, Germany) Iris Hoffmann (S&D, Germany), Ryszard Czarnecki (ECR, Poland), Gerben-Jan Gerbrandy (ALDE, Netherlands), Younous Omarjee (GUE/NGL, France), Indrek Tarand (Greens/EFA, Estonia), Barbara Kappel (ENF, Austria) |
### 2017 discharge – EU general budget, European Parliament

Rapporteur: Claudia Schmidt (EPP, Austria)

Shadow rapporteurs: Gilles Pagnieux (S&D, France), Ryszard Czarnecki (ECR, Poland), Nedzhmi Ali (ALDE, Bulgaria), Dennis De Jong (GUE/NGL, Netherlands), Benedek Javor (Greens/EFA, Hungary), Marco Valli (EFDD, Italy), Jean François Jalkh (ENF, France)

### 2017 discharge – other institutions

Rapporteurs: Arndt Kohn (S&D, Germany)

Shadow rapporteurs: José Ignacio Salafranca Sánchez-Neyra (EPP, Spain), Raffaele Fitto (ECR, Italy), Wolf Klinz (ALDE, Germany), Dennis de Jong (Netherlands, GUE/NGL), Benedek Jávor (Greens/EFA, Hungary), Marco Valli (EFDD, Italy), Jean-François Jalkh (ENF, France)

### 2017 discharge – agencies

Rapporteur: Petri Sarvamaa (EPP, Finland)

Shadow rapporteurs: Karin Kadenbach (S&D, Austria), Ryszard Czarnecki (ECR, Poland), Nedzhmi Ali (ALDE, Bulgaria), Monica Macovei (ECR, Romania, for EFSA), Dennis de Jong (Netherlands, GUE/NGL), Marco Valli (EFDD, Italy), Bart Staes (Greens/EFA, Belgium), Barbara Kappel (ENF, Austria)

### 2017 discharge – joint undertakings

Rapporteur: Martina Dlabajová (ALDE, Czech Republic)

Shadow rapporteurs: Tomàs Zdechovský (EPP, Czech Republic), Miroslav Poche (S&D, Czech Republic), Notis Marias (ECR, Greece), Younous Omarjee (GUE/NGL, France), Indrek Tarand (Greens/EFA, Estonia), Marco Valli (EFDD, Italy), Barbara Kappel (ENF, Austria)

Source: European Parliament [Legislative Observatory.](#)
This EPRS study, the third in an annual series, provides an overview of the economic and budgetary situation in the EU and beyond. It summarises the main economic indicators in the Union and euro area, and their two-year trends. The figures show that growth was moderate in 2018, at 2.1%, although this is expected to deteriorate slightly in the coming months, given the poorer global outlook than a year ago. That said, unemployment is at a post-crisis low, and is expected to improve further, given positive labour market conditions.

The study explains the annual EU budget, providing an overview of its headings for 2019, with the total amounting to €165.8 billion (or around 1% of EU gross national income). The budget focuses on priorities that include stimulating investment, growth and research, the creation of new jobs – especially for young people – and addressing migration and security challenges. The wider budgetary framework – the multiannual financial framework (MFF) – is also analysed in the study, with key decisions on spending for the 2021-2027 period due to be taken during 2019.

In this year’s edition, the special ‘economic focus’ offers a bird’s eye view of SMEs and SME policy in Europe, and of various recent EU-level initiatives in this field. The EU budget devotes particular attention to SMEs, given their central role in the European economy and in job creation. The EU needs to continue devoting efforts to improving European SMEs’ access to finance, since despite recent improvements, they are still too heavily reliant on debt financing which puts them at risk in a downturn.