Valdis Dombrovskis

Vice-President: An Economy that works for people

Hearing due to be held on Tuesday 8 October at 09.00 hours.

European Parliament committees responsible: Economic and Monetary Affairs (ECON) and Employment and Social Affairs (EMPL).

Valdis Dombrovskis has been European Commission Vice-President for the euro and social dialogue since November 2014. From July 2016, he has also been responsible for the financial services portfolio formerly dealt with by Commissioner Jonathan Hill, who resigned following the result of the referendum on the withdrawal of the United Kingdom from the EU. Alongside his institutional role, Dombrovskis co-chaired the European People's Party (EPP) Economic and Financial Affairs Ministers' Meeting, which brings together the EPP ministers ahead of meetings of the Economic and Financial Affairs Council (Ecofin).

He was elected a Member of the Latvian Parliament and became Minister for Finance of Latvia for the 2002-2004 period. He was a Member of the European Parliament from 2004 to 2009, and Prime Minister from 2009 to 2014. In 2014, he was again elected to the Latvian Parliament and then to the European Parliament, where he sat in the EPP Group.

Born in 1971, Valdis Dombrovskis holds a Bachelor's degree in economics for engineers and a professional Master's degree in customs and tax administration, both from Riga Technical University. He also holds a Master's degree in physics from the University of Latvia. He worked as a senior economist and chief economist at the Bank of Latvia from 1998 to 2002. In 2011, he co-authored the volume *How Latvia came through the financial crisis*.

This is one of a set of Briefings designed to give Members of the European Parliament an overview of major issues of interest in the context of the hearings of the Commissioners-designate. The full set of Briefings can be found at: https://epthinktank.eu/commissioner_hearings_2019

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Members' Research Service

PE 640.172 – September 2019

Background

Valdis Dombrovskis has been designated as Executive Vice-President responsible for deploying an 'economy that works for people', enhancing the distinctive features of the **social market economy** called for in Article 3 (3) of the Treaty on European Union (TEU), and leading the work on deepening the **economic and monetary union** (EMU).

Following the 2015 Five Presidents' Report, all three European institutions, Commission, Parliament and Council, jointly endorsed the European Pillar of Social Rights (**social pillar**) in November 2017, with a view to deepening the social and employment aspects of EMU. The implementation of social pillar principles is the responsibility of Member States in cooperation with social partners. The EU has been supporting these efforts by mobilising the main policy tools to hand, namely legislation, guidance, governance and funding. Articles 151 to 156 of the Treaty on the Functioning of the European Union (TFEU) set out the rules on **social dialogue**, the main aim of which is to improve European governance by involving the European social partners in decision-making and in the implementation process. An initiative labelled a 'new start for social dialogue' was launched in June 2016, aimed at involving the social partners more closely in EU policy and law-making and in the **European Semester** process. The European Semester is the framework for economic and fiscal policy coordination within the EU, which is centred on fiscal and macroeconomic surveillance. Set up in 2010 and revamped in 2015 to strengthen EMU, it recommends inter alia several measures to address the social consequences of economic adjustments more effectively. While reorganising the process, the Commission has engaged further with the **European Parliament** through exchanges of views held at some key steps in the cycle.

Industry continues to play a critical role in the European economy. It provides jobs for nearly a quarter of European workers, contributing indirectly to the generation of numerous jobs in other sectors. In 2017, there were close to 24.5 million non-financial enterprises in the EU, of which 99.8 % were **small- and medium-sized enterprises** (SMEs). Overall, the economic contribution of SMEs to the European economy is significant. However, many find it difficult to succeed in growing their systemic presence or in gaining access to international markets. Investment and financing have been recognised by the EU as precondition for European industry to drive industrial transformation. In this respect, the European Fund for Strategic Investments (EFSI) was launched in 2015 to trigger financing for strategic projects across the continent. Beyond this, the capital markets union (CMU), launched in 2015 has further sought to reduce the cost of raising capital, minimise barriers for cross-border investments and provide new sources of funding for EU businesses, especially SMEs.

Priorities and challenges

The EU's future strategic priorities for 2019 to 2024 put forward by the European Council in June 2019 talk about building a climate-neutral, green, fair and social Europe. They also call for a solid economic base in line with Europe's societal values and the principle of inclusiveness. This entails addressing fully all aspects of the digital revolution, including investment in and protection of people. Inequalities cutting across different parts of society and territories remain a challenge.

EU policies have the potential to trigger pre-distributive (e.g. policies on minimum wages) and growth enhancing measures. In this respect there are several promising avenues that might further strengthen the social dimension of the EU, such as the implementation of the **social pillar**. However, there remain fundamental issues to be clarified and addressed, including the agreement among Member States on whether an EU social dimension is necessary or opportune and the careful assessment of the instruments that the EU has available to design and implement its policies.

The complexity of the EU's social dimension is such that strengthening it requires governance mechanisms in place to allow for collective problem-solving by various actors across different sectors. As for the role of **social dialogue**, several challenges remain. These include the need to reinforce representativeness and autonomy and the links between European and national levels of social dialogue. Moreover, there is a need to further improve the social partners' capacity and involvement in public policy, as well as to ensure a stable and balanced industrial relations framework. In addition, some evaluations show how certain proposals stemming from the social pillar have caused serious collateral damage in the field of European social dialogue, impacting the relationship of trust between the European cross industry social partners.

In May 2019, Member States agreed on a forward-looking strategy with clear objectives for 2030, calling for the EU to adopt a comprehensive vision for its **industrial policy**, in order to strengthen its strategic autonomy and rise to the challenges ahead. The agreement highlighted industry as a key driver for growth, stressing the importance of swift action to maintain its competitiveness. This is also clearly reflected in the conclusions of the European Council meeting of 20 June 2019, which called for a more assertive, comprehensive and coordinated industrial policy. In view of the above, a new comprehensive European industrial strategy is likely to be a top priority during the new legislature. The challenge here will be to balance alternative views and expectations as regards openness and protection. The choice to shift the EU's strategic positioning from a defensive to an offensive policy stance will also be critical. An integrated approach may reach across a range of policy areas, including strengthening global trade rules, enhancing the **EU's trade defence** instruments and foreign direct investment screening, ensuring equal access and reciprocity in public procurement and protecting critical value chains. Creating a business-friendly environment for all enterprises, especially **SMEs** and new entrepreneurs, has remained a key objective. To this end, ongoing efforts under the Commission's cross-cutting policy on better regulation have aimed to ensure that new legislation delivers its objectives at the least cost to business and that existing legislation is checked to identify and tackle administrative burden. In her political guidelines, Commission President-elect Ursula von der Leyen took a step forward by envisaging the need for a dedicated strategy to ensure that SMEs can prosper by reducing red tape and improving access to the market.

A significant contribution to improving the business environment for EU entrepreneurs would be made by strengthening the **international role for the euro**. That would help in shaping global affairs, for example by expanding Europe's responsible trade agenda, and allow for European companies to trade all over the world, while safeguarding the European social and regulatory model at home.

Main projects

The political guidelines promise a fair transition for all towards a **green social market economy**. In this context, they put forward the idea of an action plan for the implementation of the social pillar, which Executive Vice-President Dombrovskis would be responsible for coordinating. Within this, particular focus is put on policies on a fair minimum wage, a stronger social dialogue, improved working conditions for platform workers, and a European unemployment benefit reinsurance scheme. On the same path, Dombrovskis would be entrusted with leading a refocusing of the European Semester aimed at integrating the United Nations sustainable development goals.

As part of further improving the democratic accountability of EU economic governance, Dombrovskis is required to appear before the European Parliament in regular exchanges of views to be held before each key phase of the European semester cycle.

The green transition should rest on private and public investment. With this in mind, Dombrovskis would be entrusted with coordinating the work on the Sustainable Europe Investment Plan, which is supposed to unlock €1 trillion of climate-related investment over the next decade. He would also take care of relations with the European Investment Bank (EIB), helping to turn part of it into Europe's climate bank, with the aim of having half of EIB total financing dedicated to climate investment by 2025.

The political guidelines highlight that social rights and Europe's climate-neutrality must go hand in hand with a **competitive industry**. For this purpose, Executive Vice-President Dombrovskis would co-lead the Commission's work on a new long-term strategy for Europe's industrial future and the SME strategy, in particular by enhancing SMEs' access to finance. As outlined above, economic relations are crucial to strengthen EU industry competitiveness, therefore Dombrovskis would follow trade and economic relations with EU competitors and strategic partners.

To **deepen EMU**, Dombrovskis would have to coordinate the work on delivering a budgetary instrument for convergence and competitiveness in the euro area, as part of the work on supporting Member States' structural reforms aimed at fostering inclusive growth and territorial cohesion. The completion of the banking union will also be crucial (see more detail below).

European Parliament

During the 2014-2019 legislative term, the European Parliament called for new measures to modernise the world of work, social protection and access to education. On the subject of governance and funding, in 2017 Parliament returned to the idea of introducing a 'social imbalances procedure' to the drawing up of country-specific recommendations. Several issues connected with strengthening the social aspects of the Semester process have still to be tackled, including the importance of democratic control while deepening EMU. Parliament has made several proposals to secure financial support for new priorities, higher payment ceilings, and more synergies between the different funds, while linking spending and performance. In 2018, Parliament called for a European social economy label to establish a broader EU-level legal basis for various types of social economy players and create a more favourable legal and funding environment for them. While the Commission agreed on the importance of the proposal, it wished to look further into the feasibility of creating an EU-wide label with the stakeholders.

In the last term, Parliament took a general position on EMU in a number of resolutions. Three in particular, all adopted in February 2017, concern improving the functioning of the European Union building on the potential of the Lisbon Treaty; possible evolutions of and adjustments to the current institutional set-up of the European Union; and budgetary capacity for the Eurozone. In these resolutions, Parliament called for a wide range of competencies to be transferred from the national to the EU level, and recommended that the central executive role in economic governance be transferred from Council to the Commission. In the context of the annual growth survey (AGS) for the years 2015 to 2019, Parliament called, among other things, for Member States to continue to pursue growth-friendly fiscal consolidation and to implement productivity-enhancing and socially balanced structural reforms. In addition, it called on the Commission to make the necessary proposals to address the lack of proper democratic accountability in EU economic governance, for example through closer collaboration between the European Parliament and national parliaments in the context of the European Semester. Lastly, on several occasions, it expressed concern regarding the extremely low rate of Member State compliance with the country-specific recommendations. In the context of the employment and social aspects of the AGS (for the years 2015 to 2019), Parliament called, not least, for (i) measures to assist SMEs and start-ups; (ii) measures to improve employment sustainability and quality; (iii) flexibility measures within structural reforms to maintain employment and ensure job quality and security in bad economic times; (iv) socially responsible reforms; (v) measures to tackle youth unemployment and long-term unemployment; and (vi) a holistic approach to addressing the consequences of the ageing of the EU population.

During the last term, Parliament contributed systematically to the policy debate over industry, entrepreneurship and SMEs with resolutions and own initiative reports on key issues. Moreover, it continued, as co-legislator, to advocate the creation of favourable conditions for the private sector to grow and improve its competitiveness. Parliament has long recognised the importance of reinvigorating European industry through comprehensive joined-up action. This was reflected in its 2017 resolution on building an ambitious EU industrial strategy as a priority for growth, employment and innovation in Europe. Breaking down barriers to the digitalisation of enterprises (especially innovative SMEs, start-ups and scale-ups) has been a key priority for Parliament with a view to completing the digital single market. In this respect, it advocated swift implementation of the proposals included in the Commission's digital single market strategy. In February 2019, Parliament adopted a resolution calling for a comprehensive European industrial policy on artificial intelligence (AI) and robotics in order to boost innovation and the free movement of AI-driven services and smart goods.

Financial services portfolio

Executive Vice-President Dombrovskis will lead the financial services portfolio and will be supported by the Directorate-General for Financial Stability, Financial Services and the Capital Markets Union. The financial system plays a key role in supporting the EU economy. Financial institutions grant loans to households and businesses, help firms to raise capital, allow individuals to save and invest, offer insurance against risks and facilitate payments. Financial infrastructure enables market participants to conclude transactions with one another in an effective and orderly manner.

Before the 2008 financial crisis, financial services within the EU had been integrating at a rapid pace. In particular, the Commission launched the financial services action plan in 1999, a set of measures to improve the single market for financial services, which became one of the key elements of the Lisbon Strategy. The ensuing reforms focused on strengthening integration on retail markets and filling regulatory gaps. When the crisis broke out, the EU shifted the focus of its financial regulatory agenda to driving recovery and forestalling future crises, by means of improving market transparency, strengthening financial institutions, improving corporate governance and offering better protection to consumers. The need for stronger EU-wide supervision emerged, and the European system of financial supervision (ESFS) was created in 2010, followed by the establishment of the banking union in 2014.

The financial crisis particularly emphasised the global dimension of financial markets. The 2008 G20 summit in Washington agreed on a common roadmap for financial regulatory reform to tackle the global financial crisis and to ensure a level playing field. Since then, the intensity of international cooperation on financial regulation has increased, and the EU has stepped up its activity in international financial regulatory fora (such as the G20 and the Financial Stability Board) and in global standard-setting bodies (such as the Basel Committee on Banking Supervision).

Recent developments

As a response to the financial crisis, the Parliament and the Council adopted key pieces of legislation in 2014 to build the **banking union**, which currently rests on two pillars: the single supervisory mechanism, created to supervise major banks established in the euro area Member States and in other participating Member States, and the single resolution mechanism, aimed at ensuring that failing banks in the banking union undergo orderly resolution procedures. In November 2015, the Commission tabled a proposal, currently under discussion, to establish a euro area-wide integrated deposit guarantee scheme (the European deposit insurance scheme, EDIS), which would be the third pillar of the banking union. Negotiations at the political level were postponed until 'sufficient further progress has been made on the measures on risk reduction' in the banking sector. In endorsing a comprehensive package on strengthening the economic and monetary union, the European Council's Euro Summit of December 2018 paved the way for further steps.

As part of the Commission's ongoing work to **reduce risks in the banking sector**, a set of proposals building on existing EU banking rules have been adopted. They aim to complete the post-crisis regulatory agenda and to transpose international regulatory standards into EU law, while ensuring that banks can continue to support the real economy. The legislative package amends the prudential requirements for banks and investment firms, and the rules on the recovery and resolution of failing institutions including some features of the single resolution mechanism.

The recession resulting from the financial crisis has caused economic difficulties for an increasing number of EU companies and citizens in recent years, leaving them unable to repay their loans. As a result, many EU banks have accumulated high volumes of **non-performing loans (NPLs)** on their balance-sheets. To tackle this issue, the Commission adopted a comprehensive package of measures in March 2018, including a proposal for a regulation introducing common minimum loss-coverage levels for NPLs, and a proposal for a directive aimed at fostering NPL secondary markets and easing the recovery of collateral from secured loans. The Regulation was finally adopted by co-legislators in April 2019, while the proposal for a directive is currently under discussion.

On 30 September 2015, the Commission published its action plan on building a **capital markets union** (CMU), containing a list of over 30 actions and related legislative and non-legislative measures aimed at establishing more integrated capital markets in the EU by 2019. The CMU aims to increase funding choices for Europe's businesses and SMEs, create more opportunities for investors, and facilitate infrastructure and cross-border investment. Among the legislative proposals adopted in this context, there is a proposed regulation that introduces a lighter regime for the prospectus of instruments issued by SMEs. Improvements were introduced in the regulatory framework for EU venture capital and high-quality securitisations. Measures to facilitate cross-border distribution and supervision of investment funds were also adopted.

In its mid-term review of the CMU action plan, published in June 2017, the Commission updated the proposed actions and added complementary measures in response to new challenges affecting EU financial markets, such as the departure of the largest financial centre from the EU due to the expected withdrawal of the UK from the EU. To make it easier for SMEs to raise capital on the markets, the legislation on prospectus and market abuse has been subject to a proposal for further amendments aimed to reduce the administrative burden and compliance costs faced by companies issuing securities on SME growth markets. Furthermore, more proportionate and risk-sensitive prudential rules for investment firms were laid down by amending the relevant existing provisions. A framework was also established for a pan-European personal pension product (PEPP), with a view to increasing investment in the EU, and to enhancing the features, cross-border provision and portability of personal pension products.

As part of the EU's project for a CMU, an action plan on financial technology (fintech) was tabled in March 2018 with the aim to enable the EU financial sector to make use of the rapid advances in new technologies that are transforming the industry and revolutionising the way people access financial services. In this context, the Commission put forward new rules, currently under discussion, to help crowdfunding platforms scale up across the EU single market.

The Commission published an action plan on financing sustainable growth in March 2018, with the aim of boosting the role of finance in achieving the EU goal of a more sustainable economy. The action plan is a key step towards implementing the Paris Agreement and the EU agenda for sustainable development. To implement the plan, the Commission adopted three legislative proposals, two of which have reached an agreement, the third – a proposal for a regulation on the establishment of a framework to facilitate sustainable investment – is currently under discussion.

In the context of the CMU mid-term review, co-legislators agreed on a comprehensive package aimed at reviewing the ESFS by strengthening the powers, governance and funding of the European Supervisory Authorities (ESAs), and introducing targeted amendments to the European Systemic Risk Board Regulation. This initiative followed a proposal for a regulation introducing a more pan-European approach to the supervision of EU central counterparties (CCPs) and at ensuring further supervisory convergence. This framework should be complemented by a proposal for a regulation establishing a recovery and resolution regime for EU CCPs, which is currently under discussion.

In 2015, the EU adopted a modernised regulatory framework to prevent **financial crime** such as money laundering and terrorist financing, taking into account the 2012 recommendations of the Financial Action Task Force. This framework was further strengthened with the adoption of the fifth Anti-Money Laundering Directive in 2018.

Priorities and challenges

Risks in the banking sector have decreased significantly in recent years, thanks to more stringent supervision and to EU banks having reinforced their capital base and improved their liquidity management since 2014. The NPL stock is now close to pre-crisis levels. This made it easier for the December 2018 Euro Summit to pave the way for the next steps in the completion of the banking union. The Commission's proposal for an EDIS would complement the EMU, improve the protection of bank customers, and further increase the stability and resilience of the financial system in the euro area and beyond. At the June 2018 Euro Summit, an agreement was reached that the European Stability Mechanism (ESM) would provide a common backstop to the Single Resolution Fund (SRF) providing a credit line to the SRF and further minimising the risk of taxpayers having to support failing banks; however, the details of the ESM's operation have yet to be agreed.

Recovery from the financial crisis is well underway, yet achieving more supervisory convergence at the international level and preserving a level playing field with other jurisdictions (notably in view of the UK's withdrawal from the EU) remains of utmost importance. As for the banking sector, actions should include completing the transposition of international standards on capital requirements (Basel III finalisation), while also preserving the specificities of the EU banking sector, reviewing the bank resolution framework and strengthening the anti-money laundering/counter-terrorism financing supervisory framework.

The scheduled review of the relevant legislation adopted in recent years will offer an opportunity for a further acceleration in the integration of EU capital markets. A deep and liquid European capital market will enhance private risk-sharing, make the EU more competitive and resilient, and ensure a stronger international role for the euro. The potential of the CMU to facilitate SMEs' access to capital will be raised by the private-public fund specialising in initial public offerings of SMEs.

Following the adoption of the Commission's action plan, the EU has already started emerging as a global leader in the area of sustainable finance. However, implementing the action plan will be a challenging task in the coming years. It will also be instrumental to the Commission's announced strategy for green financing and the Sustainable Europe Investment Plan.

In the EU, attention is being paid to the contribution that fintech could make to increasing efficiency, strengthening financial integration and enhancing the EU's role in financial services. Meanwhile, there is a pressing need for safe and effective common rules supporting innovation and protecting consumers. Together with the ESAs, the Commission is monitoring the development of crypto-assets and initial coin offerings, to assess whether EU-level regulatory action is required. As EU standards for new technologies (such as blockchain) are developed, their use for post-trade and for securities issuance will attract increasing attention. Furthermore, potential applications of artificial intelligence in financial services require consideration.

European Parliament

Treaty basis and European Parliament competence

Articles 49, 51, 53, 56, 59, 63, 64 and 65 of Title IV of the Treaty on the Functioning of the European Union (TFEU) relate to the right of establishment and free movement of services and capital; Article 75 TFEU concerns measures to control capital movements to combat terrorism; Articles 113, 114 and 115 TFEU address the approximation of laws; and Article 127(6) TFEU allows the European Central Bank to be entrusted with supervisory tasks for financial institutions. The Parliament acts under the ordinary legislative procedure (formerly 'co-decision') with the Council.

In its capacity as co-legislator, the Parliament has contributed significantly to the laying down of risk-reducing rules for the EU banking sector while preserving its ability to support the real economy. In its resolution adopted in view of the finalisation of the Basel III framework, the Parliament stressed that upcoming changes should not lead to a significant overall increase in the capital requirements for banks and should not harm their ability to finance the real economy, in particular SMEs. In addition, in its annual resolutions on the banking union for 2016 and 2017, the Parliament called on the Commission to take the proportionality principle into account. When reviewing the prudential framework, the Parliament consistently pushed for making requirements proportionate to the size and risk profile of banks, by reducing compliance obligations for 'small, non-complex institutions'. It also insisted that the scope of the favourable prudential treatment of SME loans be broadened and a similar treatment be introduced for exposures to certain infrastructure projects. In negotiations concerning the rules on minimum loss coverage for NPLs, the Parliament consequently secured that the requirements increase at a more gradual pace, so that banks can deal with NPLs smoothly without disruptive effects on the real economy.

In a resolution of May 2016, the European Parliament stressed that virtual currencies and blockchain have the potential to positively contribute to citizens' welfare and economic development, including in the financial sector. However, they entail risks that need to be addressed appropriately so as to enhance trustworthiness. A proportionate regulatory approach at EU level is therefore required. The Parliament also called on the Commission to promote a shared and inclusive governance of the distributed ledger technology. In May 2017, the Parliament adopted a resolution on the influence of FinTech on the future of the financial sector, focusing on six main areas: data, cybersecurity, blockchains, interoperability, financial stability, financial and IT skills.

The European Parliament also engaged in shaping the ESFS review undertaken by the Commission in 2017. In fact, in response to a March 2014 European Parliament legislative initiative aiming to strengthen the ESAs, the then outgoing Commission identified some areas where further improvements were required in order to allow the ESAs to fully exploit their mandate. Moreover, in its resolution of 9 July 2015 on building a capital markets union, the Parliament underlined that a strong CMU needs to be accompanied by robust EU-wide and national supervision, including adequate macro-prudential instruments. Among possible options, it indicated that a stronger role in improving supervisory convergence could be attributed to the European Securities and Markets Authority (ESMA).

FURTHER READING

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