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POLICY DEPARTMENT A
ECONOMIC AND SCIENTIFIC POLICY

Economic and Monetary Affairs

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Internal Market and Consumer Protection

Joint Interparliamentary Meeting
8-9 November 2010
'Beyond the crisis: how should Europe respond to the challenges ahead'
Compilation of Working Documents

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WORKING GROUP 1: WHAT KIND OF GROWTH AND JOBS FOR THE EUROPE OF TOMORROW?

Abstract

This briefing note provides an introduction to the priorities of Europe 2020, the new strategic policy framework the European Union has set itself for the next ten years, and attempts at highlighting the way the current economic context has impacted on the design of the strategy. It subsequently stresses the implications of such choices for the labour market and employment policies. An overview of the role of structural and cohesion policies in recession and current recovery is also given. The note stresses how an active role of the European Parliament and national parliaments in Europe 2020 could be key to improving the effectiveness of the strategy's implementation. Finally, the reform will be as successful as it is able to stimulate the EU's external trade.

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1. The crisis and beyond: a new strategy for the European Union

All the efforts deployed by the European Union since 2000 to reach the ambitious Lisbon targets were wiped away in a few months by the financial and economic crisis in 2008.

The Lisbon strategy had already been the subject of much debate and criticism and its failure was definitively declared as soon as the impact of the crisis became apparent. One of the deplorable effects of this was that discussions on post-Lisbon could not be based on a clear-cut evaluation of the merits and deficiencies of its predecessor.

1.1. Economic and employment prospects

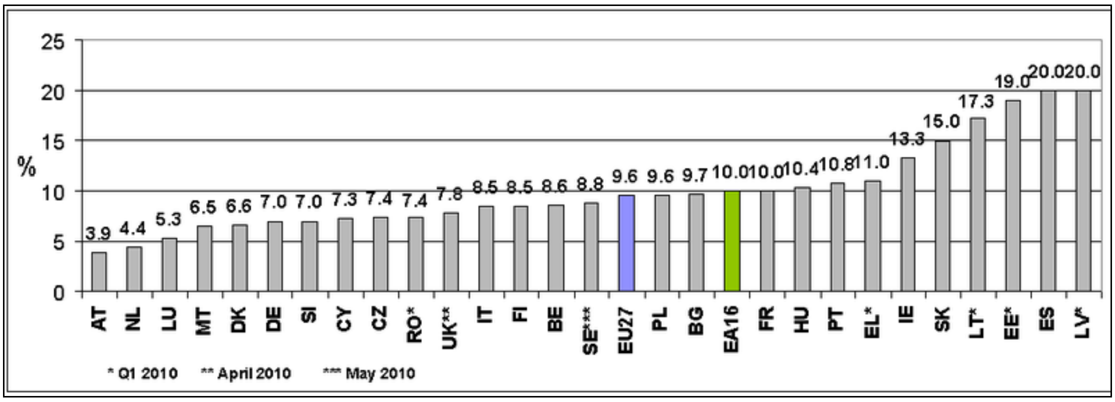
Following a heavy downturn in economic activity in 2008 and especially 2009, it seems that growth is returning to Europe. According to Eurostat, euro area (EA16) and EU27 GDP (gross domestic product) increased by 1.0% during the second quarter of 2010, compared with the previous quarter. This is a remarkable increase from the situation in 2009, with negative growth rates in all EU Member States except for Poland. In the second quarter of 2010, Lithuania (+3.2%) recorded the highest growth rate compared with the previous quarter, followed by Germany (+2.2%), Estonia, Finland and Sweden (all +1.9%).

The average EU economic growth at this juncture is slightly higher than both that of the US or Japan (both 0.4%) in the second quarter of 2010. Although GDP growth is on a returning path, there is no room for complacency as the crisis is not resolved yet with ongoing financial sector tensions and unsustainable public deficits in Greece and Ireland, as well as to a lesser extent Portugal, Spain and Italy.

One main indicator for the recovery is industrial production. Industrial production rose in all Member States, except Greece (-3.0%) and Denmark (-0.9%). The highest increases were registered in Estonia (+22.9%), Latvia (+20.5%), Poland (+13.2%), Luxembourg (+11.8%), Germany and Slovenia (both +11.5%).

Following the drop in GDP growth, the unemployment rate in all of the EU has grown since the first quarter of 2008. However, the increase in unemployment has been smaller than in the US. According to the latest available data (covering the period up to last August, see Table 1) the labour market in the EU is finally showing signs of stabilisation and, in some Member States, slight recovery. The deterioration in employment numbers seems to have come to an end in the second quarter of 2010, when the situation remained basically unchanged for the first time in nearly two years. Eurostat estimates that 23.066 million men and women were unemployed in the EU27 in August 2010, around 7 million more compared to the lowest level reported in 2008.

Table 1 - Unemployment rate in EU Member States August 2010



Source: Eurostat

However, it can be expected that employment will not rebound at the same pace as GDP growth. Economic theory predicts that GDP growth and employment evolve differently, as employment levels react to GDP growth with a certain time-lag.

Consequently, it is normal for unemployment rates to stay on a high level despite positive GDP growth rates in the aftermath of the crisis. The reasons for the time lag are various, but the main explanation for it is the existence of underutilised human resources during a period of recession.

Employers can make use of arrangements such as putting employees on 1) short-time work or 2) reducing the hours the number of hours worked in other ways (production stops, obligations to take annual leave, leave rotation, sabbaticals) so as to avoid to fire people and thereby protecting their human capital.

In some countries, the crisis has given rise to more firing and loss of jobs in low-skilled sectors (e.g. construction in Spain), in others more flexible measures (such as *Kurzarbeit* in Germany) have been introduced that reduce labour costs.

As fiscal tightening is expected to take place soon, governments might withdraw their financial support from the labour market which may increase the problem of unemployment in the next months, unless the economic rebound will be strong enough to foil that negative shock.

A reasonable expectation therefore is that improvements in unemployment figures may appear only gradually in 2011-2012, and given that economic and financial stability returns more robustly.

1.2. Europe 2020

Discussions on post-Lisbon were inevitably conditioned by recession and EU policy-makers' need to show responsive to it. Therefore, in developing its proposals for a post-Lisbon strategy, the European Commission had to face a double challenge: keeping in mind current constraints while putting forward an ambitious agenda to direct EU's and Member States' reform programmes for the next ten years.

However, those who claimed that the economic downturn should bring about a complete paradigm shift in EU policies had to lower their sights and accept a much less original outcome than they had hoped for.

Europe 2020's structure based on the three priority areas identified as "smart" (developing an economy based on knowledge and innovation), "sustainable" (promoting efficient use of resources while building a greener, more competitive economy) and "inclusive" growth (fostering a high-employment economy that delivers social and territorial cohesion) echoes the well-known formula that would make Europe "the most dynamic and competitive knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion, and respect for the environment".

One of the main sources of criticism on the Lisbon strategy, i.e. the lack of clear targets for its "social" pillar seems to have been addressed in the design of Europe 2020 as the objective of lifting 20 million people out of the risk of poverty has been declared. All together the main set of targets appears representative of the three priority areas and may reflect a more balanced approach to the three components of the strategy than it was the case within the Lisbon agenda.

The seven “flagship initiatives” selected to drive progress under Europe 2020’s priority themes also seem to aim at making the overall strategy clearer and more visible; with the most relevant exception of the “European Platform Against Poverty”, they are, however, largely based on already ongoing initiatives that have now been brought under the strategy's umbrella.

2. "SMART GROWTH": INVESTING IN KNOWLEDGE AND INNOVATION

Already within the Lisbon strategy a consensus had been reached that the most valuable asset the EU and the Member States can rely on in facing globalisation and increased international competition is their human capital, whose potential needs to be further enhanced and developed through appropriate policies and investment supporting competitiveness, growth and job creation.

On the international economic arena Europe possesses a clear comparative advantage in high value-added activities with knowledge-intensive products and services and is expected to attain its best growth performances in a dynamic environment where innovation can boost productivity and employment.

However, Europe seems to be as a whole less proficient than its main direct competitors in managing to turn knowledge into innovative business opportunities and new jobs: major efforts have been made to get an understanding of the reasons for this, which has been blamed for being one main cause of the difficulties experienced in implementing the Lisbon agenda, and to identify the levers on which policy-makers should act to reverse such trend.

In this context great emphasis needs to be placed on the proper working of the so-called "knowledge triangle" based on education, research and innovation as a vehicle to growth and employment in Europe. Europe 2020 has the potential to highlight this link more consistently by including among its main targets a reference to both levels of investment in research and the need to improve educational attainments while reducing early school leaving and increasing the rate of students with tertiary education.

From a theoretical point of view, the conceptual background for this discussion is the so-called *endogenous growth theories* that have pointed to the indirect impact of human capital acquisition on per capita income growth. These theories also suggest that the availability of human capital supports the creation of innovation and facilitates the adaptation to technological change, as well as the implementation of innovations at the workplace.

Within a knowledge-centred agenda, European cooperation in the field of education and training clearly gains great momentum; reforms needed to fulfil the potential of the sector for contributing to the attainment of major EU targets have been identified in the "Education and training 2010" work programme and updated within the "Strategic framework for European cooperation in education and training" ("ET 2020").

On the one hand, innovation itself is a skill-intensive activity, thus the success of innovation policies may depend on the success of skill building policies providing adequately qualified human capital; on the other hand, innovation may change the pathways and pace of technological progress, which impacts on a changing pattern of labour demand, and require new or higher skills and qualifications to be provided through the education system.

Available data supports the assertion that good education offers, in most cases, an easy pathway to quality employment and there is growing evidence that the demand for skills and qualifications is being driven upwards in most occupations. A modern economy based on innovation-led development also typically requires employees and workers to continuously update their existing skills and/or to acquire completely new skills at several stages in their working life, with a major stress on lifelong learning.

Innovation-, knowledge-based growth both require specific skills and competences and can create needs for new or different skills. It demands a capacity to identify and develop new technologies, applications or organisational solutions and proper management skills for the implementation of new products and processes. As a result of innovation being introduced in a specific field, some existing skills may become outdated and a need for different ones may arise.

Strategies aimed at redeploying the European economy to new activities with more value-added and new and better jobs are deemed to failure if labour market skills demand and supply do not match adequately.

Research and empirical evidence indeed suggest that investment in research, innovation and education clearly pays off and dedicated public budget appropriations should never be reduced even in times of economic or financial crisis.

3. "SUSTAINABLE GROWTH": USING RESOURCES EFFICIENTLY IN A GREENER ECONOMY

In recent years there has been an evolving political consensus at EU level that a switch to a low-carbon economy is required both to combat climate change and for European industries to remain competitive in the long term. The current challenge is to maintain that long term objective in the face of short term difficulties.

At the wake of the financial crisis and the economic slowdown numerous observers suggested that the crisis could undermine the efforts and resources committed towards combating climate change. Fears have in particular been raised that the current financial situation could slow down the development of new 'clean' technologies which are seen as part of a more sustainable development and also key for the implementation of the EU's Climate and Energy package adopted in December 2008.

In fact, the crisis can also be seen as a unique opportunity to tackle both challenges at once by targeting investment and fiscal stimulus towards low-carbon infrastructure. In any case, the needs of the 'industrial age economy' and the 'environment' are currently clashing. The economic policy design of the next 5-10 years will have no other chance than to irreversibly integrate issues around environmental and social sustainability in its very core objectives.

Numerous initiatives which attempt to stimulate the declining demand and growth through "greener" demand management have been recently brought forward, which can be seen as steps towards a change in the concept of what stimulates economic growth and investment.

In practical policy terms this requires bold moves towards indicators of well-being 'beyond GDP'. GDP growth is enshrined in all economic policies and objectives both on EU level as well as on national and regional levels. However, GDP is a questionable measure of our well-being, for several reasons, including most notably that GDP does not properly account for social and environmental costs and benefits.[1] Measuring the quality of economic performance and well-being by GDP resembles a firm that never looks at its assets and liabilities, but merely at maximizing its turnover. However, this should not be understood as a call to get rid of GDP. GDP growth effectively determines levels of employment, tax revenues and subsidies paid even to the greenest of technologies. Our economies and our welfare systems are heavily dependent on GDP growth.

GDP growth, through consumption and investment, bears positive feedback mechanisms that make more of it always necessary. However, while not getting rid of GDP, it would certainly be desirable to reduce some of this dependency on it. The problem with the opposite of growth, de-growth, is that it is most likely unstable. Declining consumption would certainly lead to rising unemployment, falling competitiveness and a spiral of recession. This turns out to be a real dilemma - modern economies are simply driven towards growth, as less of it is unstable, but more of it is increasingly unsustainable2.

In its resolution on developing the job potential of a new sustainable economy[3], the European Parliament draws attention to the potential represented by the creation of "green jobs": the current global economic and social crisis should not deter Member States from making the transition towards a competitive, more sustainable, low-carbon, resource-efficient economy, given that this will make them more resilient, less dependent on increasingly expensive imports and more competitive.

[1] For a review of the pros and cons of GDP, see e.g. European Parliament (2007): Alternative Progress Indicators to GDP as a Means to Sustainable Development, Study.

[2] See e.g. Booth, Douglas (2004) Hooked on Growth – economic addictions and the environment. New York: Rowman and Littlefield.

[3] European Parliament resolution of 7 September 2010 on developing the job potential of a new sustainable economy.

Considering the post-crisis economy to be a strong opportunity for sustainable growth based on social justice and eco-efficiency, the Parliament notes that the transformation of European economies from polluting to eco-efficient economies will lead to profound changes in production, distribution and consumption, which should be used as a chance to move towards true sustainability without endangering prosperity or jobs. The Parliament believes that the transition to an economy based on non-polluting energy sources needs to be seen as an opportunity for investment in sustainable development and not merely as a burden on public and private budgets.

The European Parliament believes that market-economy based environmental policy can become the engine of growth and employment in all branches of the economy, and stresses that predictable, investment-friendly framework conditions are the basis that will allow innovative businesses to make the best possible use of these opportunities for the benefit of the environment and of employees.

4. "INCLUSIVE GROWTH": SUPPORTING EMPLOYMENT AND IMPROVING SOCIAL COHESION

The concept of "inclusive growth", which is the third basic definition of what Europe 2020 aims to achieve, has a considerable tradition in economic and social sciences literature.

Inclusive growth refers both to the pace and pattern of growth, which are considered interlinked, and therefore in need to be addressed together. The idea that both the pace and pattern of growth are critical for achieving a high, sustainable growth record, as well as poverty reduction, is consistent with the findings in the *Growth Report: Strategies for Sustained Growth and Inclusive Development* (Commission on Growth and Development, 2008). The commission notes that inclusiveness – a concept that encompasses equity, equality of opportunity, and protection in market and employment transitions – is an essential ingredient of any successful growth strategy.

The idea of equality of opportunity in terms of access to markets, resources, and unbiased regulatory environment for businesses and individuals needs be emphasized. The Commission on Growth and Development (2008) considers systematic inequality of opportunity "toxic" as it will derail the growth process through political channels or conflict.

The inclusive growth approach focuses on productive employment rather than on direct income redistribution as a means of increasing incomes for excluded groups. In the short run, governments could use income distribution schemes to attenuate negative impacts on the poor of policies intended to jump start growth, but transfer schemes cannot be an answer in the long run and can be problematic also in the short run.

Sustained, high growth rates and poverty reduction, however, can be realized only when the sources of growth are expanding, and an increasing share of the labour force is included in the growth process in an efficient way. From a static point of view, growth associated with progressive distributional changes will have a greater impact in reducing poverty than growth which leaves distribution unchanged. Evidence suggests that in a significant number of cases (around a quarter) distribution has been as important as growth in explaining the income growth of the poor.

The main instrument for a sustainable and inclusive growth is assumed to be productive employment. Employment growth generates new jobs and income for the individual - from wages in all types of firms, or from self-employment, usually in micro-firms - while productivity growth has the potential to lift the wages of those employed and the returns to the self-employed. Hence, inclusive growth is not only about employment growth, but also about productivity growth.

The inclusive growth approach takes a longer term perspective. This is necessary because of the emphasis on improving the productive capacity of individuals and creating

a conducive environment for employment, rather than on income redistribution as a means of increasing incomes for excluded groups. Due to this longer term perspective, the inclusive growth analytics framework focuses explicitly on structural transformation and internal migration.

5. THE "FULL EMPLOYMENT" OBJECTIVE: CREATING INCLUSIVE LABOUR MARKETS

"Full employment" was already mentioned by EU policy-makers as the main objective of the European Employment Strategy (EES). The new legal framework provided by the Treaties as amended by the Lisbon Treaty, and especially the new article 3 of the Treaty on the European Union that aims "for the sustainable development of Europe based on (...) a highly competitive social market economy, aiming at full employment and social progress" now enshrines this objective in the basic text of European law.

Indeed, in the perspective of population ageing, opening up the labour market to all those who wish and can work will be a precondition for ensuring a steady growth path. This basically means easing access to work for all the target groups who are currently underrepresented in the labour market: the EU needs to dramatically raise the employment levels of groups that are currently under-represented in the labour market, which means raising the employment rate of older workers and women, as well as achieving a significant reduction in the unemployment gaps for people at a disadvantage, such as people with disabilities, ethnic minorities and migrants.

This approach, however, could be misleading in that it might entail an underestimation of the danger of in-work poverty and of the difficulties experienced by the most disadvantaged groups, who need targeted additional measures.

Contrary to the assumption that having a job is the most effective way to secure oneself against the risk of poverty, a significant minority of the employed population of the EU, around 8%, live in a household whose income is situated below the national poverty line. The European Parliament has continuously been underlining the urgency to face the problem of an increasing number of working-poor by promoting the concept of "decent work" to guide any growth and job creation strategies implemented at EU and national level.

In several recent resolutions[4] the European Parliament has voiced its particular concern over youth unemployment. The European Parliament has also underlined the need to support people requiring particular support "increase the employability of legal migrants with appropriate programmes. Continued efforts and innovative programmes are also required to reintegrate people with disabilities into the labour market, including through subsidised jobs. Member States should remove the barriers which make it more difficult for people to enter the labour market for the first time, support the creation of jobs, foster social innovation and increase the quality and effectiveness of job placement services, including public employment services. Job centres must provide training and mentoring programmes particularly in the field of information and communication technologies, as well as access to high-speed internet to job seekers, especially older people, legal migrants, ethnic minorities and people with disabilities, in order to optimally facilitate the job search"[5].

Considerations around job quality and productivity are obviously highly relevant in this context. The growth model designed by Europe 2020 implies high qualified, sustainable and productive jobs. The Lisbon strategy had already set itself the goal of creating not only *more*, but also *better* jobs, although concerns about the quantitative dimension of employment had appeared later on to prevail over the qualitative dimension.

[4] See, i.a., European Parliament resolution of 6 July 2010 on promoting youth access to the labour market, strengthening trainee, internship and apprenticeship status and European Parliament resolution of 10 March 2010 on EU 2020

[5] European Parliament legislative resolution of 8 September 2010 on the proposal for a Council decision on guidelines for the employment policies of the Member States: Part II of the Europe 2020 Integrated Guidelines

In its Resolution on the guidelines for the employment policies of the Member States, the European Parliament has recently reaffirmed the principle that "it is of the utmost importance to create high-quality jobs which are also needed in the long term and which possess high added value".

Discussions on how securing for all a decent living standard guaranteeing participation in society and access to basic goods and services without creating additional barriers to employment have been high on the political agenda in many EU Member States for several years.

The flagship initiative "An agenda to create new skills and jobs" within Europe 2020 stresses the need to improve the match between employment policies, education and training systems and key sectors for job creation. The initiative also highlights the need to overcome structural rigidities in the labour market in order to prevent skills shortages, by enhancing mobility and reducing administrative and gender barriers, with the ultimate goal to improve the matching of vacancies and job-seekers' qualifications.

The initiative stresses on active labour market policies (ALMP) to improve the employability of job-seekers. While this kind of measures, however, have proved effective in the medium and long term, their suitability to help in a recession can be questioned based on evidence provided by recent experiences. As it is foreseen that cyclical moves will become more frequent and more pronounced, lessons from the current crisis should not be underestimated.

The main phenomenon to be seen as regards the impact of the crisis on employment is that dismissals have started from the periphery of temporary workers and reached the core of permanent workers, thus generating employment insecurity among the previously "stable" workforce.

In the European Union all the Member States adopted extra-ordinary measures to limit the social consequences of the crisis and mitigate their impact: fiscal stimulus packages were budgeted and employment support schemes were put in place to avoid massive redundancies. The use of temporary lay-off schemes or short-time working arrangements in firms with substantial fall of production is by far the most popular instrument, followed by rebates on social-security contributions and hiring subsidies. Efforts to train both employed and unemployed workers and to intensify job search assistance and overall public employment services capacities were also deployed. Some countries implemented other types of measures, such as increasing incentives for entrepreneurship.

The OECD Employment Outlook 2010 estimates suggest that short-time programmes alone have preserved more than 200,000 jobs in Germany and about 120,000 in Italy. These schemes, however, do not help temporary workers. Activating measures, on the contrary, have a more equitable set-up, but poor effectiveness when job openings are rare. Workers on fixed-term contracts or with a short employment record, labour market entrants, employees with low monthly earnings due to low hourly pay or part-time work and the self-employed normally also have limited or no access to substantial insurance benefits.

These observations can suggest that a reflection should be opened on the tools employment policies should have at their disposal in the future European economy to guarantee inclusive labour markets, avoiding segmentation and inequality. If, on the one hand, higher employment rates and longer professional lives appear to be a pre-condition for ensuring the long-term sustainability of welfare systems, on the other side a strategy aimed at supporting the productivity and competitiveness of the European economy through flexible and inclusive labour markets will have to be accompanied by active labour market measures, without neglecting, anyway, a comprehensive social security net based on modernised benefits schemes.

6. STRUCTURAL AND COHESION POLICIES' CONTRIBUTION TO GROWTH AND JOBS IN THE CONTEXT OF THE FINANCIAL AND ECONOMIC CRISIS AND EUROPE 2020

Assessing the crisis' impact on structural and cohesion policies[6] is not easy due to the overall lack of accurate and complete data. Presenting the general situation and the likely impact of the crisis, however, the following overview provides quantitative references where available.

Common agricultural policy: For EU27 the decrease in factor income in 2009 compared to 2008 was 13.6% in real terms - mainly due to a sharp fall (−10.5%) in output value at basic prices. Income per annual work unit decreased in 21 Member States. Hungary (−32%) was hit the most, followed by Luxembourg (−25%), Ireland (−24%) and Germany (−21%). Between 2000 and 2009 EU27 employment in the agricultural sector decreased by 25% with the loss of the equivalent of 3.7 million full-time jobs. It fell by 17% in the EU15 and by 31% in the 12 new Member States.

Common fisheries Policy: The intrinsic problems of the fisheries sector date back to before the current crisis, including combined effects of overcapacity and the low level of many stocks, reflected by poor economic returns in the catching sector and low profitability in many fleets. The market has also been suffering from concentrated distribution, rising costs due to increasing fuel prices and the reduced demand. Over 2005- 2007 the value of the fresh products covered by the Common Market Organisation (CMO) fell by 50% and the quantities marketed by 60%. After 2007, the economic and financial crises aggravated these problems, however its impact on business units, fishery segments and regions is unlikely to be homogeneous; information currently available does not allow for a thorough analyse of the crisis' impact.

Culture, education and youth: The crisis intensified the long-term trend of a drop in demand for unskilled labour, which has implications for education policies. Unemployment rates of workers not finishing school in the EU27 jumped by 3.6% between 2007 and 2009; whilst those of medium and high-skilled workers only increased by 1.1% and 0.9% respectively. The crisis resulted in a steep rise in the unemployment rate for the under 25s, which was 20.2% in the EU27 in August 2010. On the expenditure side, Lithuania was expected to cut the education budget by 8% in 2009.

Regional cohesion policy: The existence of regional disparities is at the very origin of the policy itself and is illustrated by the division into 'convergence' and 'competitiveness' regions on grounds of GDP/capita. Considered with caution, evidence tends to confirm that before the crisis a convergence process has been going on at EU 27 level, but divergence may have occurred within the group of new Member States. Moreover, there is some albeit very limited evidence that inter-personal inequality within regions outweighs inequality between regions and that overall personal-income inequality is positively correlated with regional disparities. Against this background - and in the presence of a lack of a coherent regional data set - it is highly likely that the crisis has had an asymmetric effect. Indeed at the beginning of 2010 a Committee of the Regions' survey among a group of regions and cities finds the impact of the crisis to be 'unevenly distributed among sectors and regions' and also that unemployment is rising, that regional and local public finances are under pressure and that enterprises suffer from reduced turnover and credit and liquidity constraints.

[6] For the purpose of this section the term 'Structural and Cohesion Policies' covers the Common Agricultural Policy, Common Fisheries Policy, Culture and Education, Regional Policy and Transport and Tourism Policy.

Transport and tourism: In both the road and rail sector the crisis hit the freight transport harder than the passenger sector: in 2009 road freight transport output has decreased, driver employment has decreased by more than 10% and new truck registrations were down by at least 30%. In road passenger transport some decreasing trends have been observed especially in tourism linked sectors.

The maritime and inland waterways transport and port activities contracted: World container traffic (TEUs) fell by 26% in 2009. Inland waterway SMEs were particularly concerned. In the aviation sector in 2009 air freight ton-km fell 10%, while the crisis also induced a reduction in the frequency of services and a deterioration of the financial situation of undertakings. There are however some signs of recovery in rail passenger, maritime and aviation sectors (e.g. demand in aviation, but passenger growth is at 7.8% compared to 15.5% in Asia-Pacific).

Structural and cohesion policies have played an important part in the European economic recovery package. Already before the crisis, Cohesion policy programmes of the 2007 - 2013 funding period had a strong strategic focus on jobs, infrastructure and energy, as well as research and innovation. In fact, according to the rules, at least 60 % of the funding available for the "Convergence" objective and 75 % of the "Regional competitiveness and employment" objectives were earmarked for investments related to these EU 2020 priorities. This alignment enabled Cohesion projects to quickly address the challenges of the crisis by the following measures:

First, Cohesion policy has helped overcoming the liquidity constraints in many Member States and regions by increasing direct cash flow and advance payments significantly: in 2009, the entire advances paid rose to 11, 5 billion EUR. Also, resources like JASPERS, which provides technical assistance to Members States for major projects, have been increased by 25%. By the end of 2009, 93 billion EUR were allocated to specific projects, representing 27% of the total financial volume for the period 2007-2013. The major injections of funds and highest rates of absorption - up to 90% of the total public investment - were observed in the countries which were particularly hit by the economic downturn, such as the Baltic States, Hungary and Poland, but also some regions of Spain, Italy and Germany received more than 20 % of the public investment.

Second, the regulations on Structural Funds were modified in order to facilitate and accelerate investments in Member States and regions. More flexibility was introduced to encourage investments, for example by

- extending the deadline for approval of projects under the funding period 2000-2006 (to July 2009 for the European Regional Development Fund and to 2010 for project under the Cohesion Fund),
- simplifying the financial management of the Structural funding, and reducing administrative burden, e.g. by introducing lump sums or flat-rate payments for reimbursement and by facilitating cooperation with the European Investment Bank (EIB) and the European Investment Fund (EIF),
- simplifying the rules governing state aid schemes which are co-financed by Cohesion policy allowing to make advances to state aid schemes eligible up to 100 %.

Both actions have contributed to inject purchasing power into the economy in order to stimulate growth and stabilize employment. By allowing quicker implementation of programmes, these measures have improved productive capacity and competitiveness.

An important strategic lesson of the anti-crisis efforts identifies Cohesion policies as a model for a renewed economic governance system corresponding to the challenges of the EU 2020 strategy: its multi-level architecture and integrated approach respond to the increasing need of a more effective coordination and integration of different levels of government as well as policy areas. Based on the strategic guidelines - binding for Member States and regions - Cohesion policy provides a delivery system shaped for the pursuit of European economic development and cohesion in the 21st century.

At first sight the structural and cohesion policies' structural vocation and long-term orientation might cast doubt as to their employability against the crisis being a classical task of economic and business cycle stabilisation policies. On the other hand, their long-term focus might render them particularly suited for combating the crisis by facilitating the required adjustments and smoothing transition in society and territories.

Moreover, out of all European policies structural and cohesion policies represent the biggest share of the EU budget (some 62%); although small in absolute terms (87 billion EUR a year for EU27, some 54% are market related and direct payments)[7] it might be able to contribute to the stabilisation of short-term demand and provide enough guarantees to trigger private co-financing as for the time being public authorities face budgetary constraints. Also, due to the multilevel governance of the funds and participation of civil society in EU programmes, structural and cohesion policies offer direct access to those affected by the crisis, thereby speeding up trust building and offering a forum for debate for several open questions.

[7] Very rough calculations made on grounds of information on the commitment appropriations of the Financial Framework 2007-2013 at http://ec.europa.eu/budget/prior_future/fin_framework_en.htm; commitment headings are not completely congruent with the definition of SCP used in this section.

7. WHAT ROLE FOR THE EUROPEAN PARLIAMENT AND NATIONAL PARLIAMENTS IN EUROPE 2020

Scarce inclusiveness, with a failure to involve relevant stakeholders at both European and national level, was considered as one of the weaknesses of the Lisbon strategy. Such an ambitious political project could not have been viable without wide support and consensus over its main objectives within the society it aimed to transform.

Partnership between the European Commission and the Member States served as the central pillar of the whole process. Even in the Member States' institutional and administrative structures, however, the Lisbon strategy was in most cases only familiar to small groups of civil servants.

In its recent Resolution on employment guidelines[8], the European Parliament has taken the view that "ultimately, the strategy's basic goals could not be achieved, because Member States also failed to assume ownership" of its guidelines.

Collignon e.a.[9] have underlined the "*depolicitisation*" of decision-making deriving from this: the open method of coordination and the implementation process had evolved into a primarily bureaucratic exercise "with experts cooperating in obscure networks shielding decisions from electoral cycles", at least in the eyes of the public, thus undermining the political legitimacy of the strategy.

The European Parliament's influence on the Lisbon process was also considered to be weak, notwithstanding the Assembly's Treaty-based right to be consulted over the employment guidelines, as time restrictions imposed by the strategy's management cycle have often resulted in a shortening of the timeframe available for Parliament to deliver its opinion. The European Parliament had therefore been insisting on being given an opportunity for real involvement in the post-Lisbon strategy long before Europe 2020 was adopted.

Based on such considerations, efforts to endow Europe 2020 with a more efficient governance system than its predecessor have been made. The architecture of the new strategy identifies the European Parliament as the "a driving force for mobilising citizens and their national parliaments". On their turn, national parliaments should be closely associated to governments when designing and implementing national reform programmes, as well as, according to the EP, "monitoring and evaluation of those programmes, including in the definition of targets and indicators"[10]. The European Parliament "recalls that both the Commission and the European Council have underlined Parliament's crucial role in the EU 2020 strategy, and should therefore respect its prerogatives by presenting annual policy recommendations to Parliament before the European Council takes a decision; urges the Council and the Commission to acknowledge Parliament's key role in implementing a 2020 strategy".

[8] European Parliament legislative resolution of 8 September 2010 on the proposal for a Council decision on guidelines for the employment policies of the Member States: Part II of the Europe 2020 Integrated Guidelines

[9] Collignon S. e.a. (2005), The Lisbon Strategy and the Open Method of Coordination, Policy paper nr. 12, Notre Europe, Paris.

[10] European Parliament resolution of 10 March 2010 on EU 2020.

8. EXTERNAL ASPECTS OF THE EU COMPETITIVENESS

8.1. A long decline to be quickly addressed

In 2007, the Commission published a document entitled *"Global Europe, EU performance in the global economy"*[11]. The Commission's report analyses the recent changes in the international trade performance of the EU in the context of the rise of China and other emerging countries. The report also looked at the changes in specialisation and market shares of the EU on external markets over a 10 year period.

The conclusions of the reports are rather interesting and deserved to be fully mentioned:

The last fifteen years have seen a major redistribution of market share between emerging and developed countries and among developed countries themselves. In this context, the EU was able to substantially maintain its world market share for manufactured goods by containing the lost of market share. In the same period, the relative fall of the US and Japan was more serious. The recent economic crisis has accentuated the decline of industrialised countries and sealed the rise of China and other emerging economies.

A limited number of industrial sectors such as chemicals, pharmacy products, motor vehicles and non-electrical machinery have allowed the European Union to keep its foreign trade balance positive. This increase in manufactured goods exports only partly matched an even more substantial energy bill which rose to unprecedented levels during the years 2007/2008 and, despite the decrease of energy prices triggered by the economic slowdown, it is still substantially impacting on the EU's trade balance.

In the meanwhile, developing and emerging countries have generally reinforced their position as global trade players. China has been by far the most remarkable performer. In fact it more than doubled its overall market share since 1995 and become the biggest producer of manufactured goods, the world's second economic power and largest exporter.

The EU's relatively good performance (when compared to the United States or Japan) is due to an improvement in the quality of its products, combined with the ability of EU companies to sell products at premium price due to good quality, branding and related services. These *"upmarket"* products account for a third of world demand and represent half of EU exports, not only in luxury consumer goods, but across the whole range of products, including intermediary goods, machinery and transport equipment. According to the Commission, *"building on this ability to sell products at premium price is the only way to uphold EU levels of social protection, employment and wages"*.

EU's export performance is much stronger in industrialised markets while it appears that the EU was unable to reinforce its presence in emerging countries. The Commission stressed that *"worrying signs come from the fact that the EU has lost significant market share on some of the fast-growing emerging markets, particularly in Asia"* and concluded that *"in the long run, this underperformance on some of the most promising markets could undermine overall the EU's position in international trade"*.

[11] see at http://trade.ec.europa.eu/doclib/docs/2008/october/tradoc_141196.pdf

8.2. External trade aspects of the Europe 2020 communication

The core of the Europe 2020 communication is the creation of a European economy more efficient and inclusive. It mainly focuses on internal initiatives and does not (as the US has done in its similar initiatives) foresee a radical transformation of the EU into an export-oriented economy. However, the Europe 2020 communication acknowledges the importance of external trade for the future growth of the EU's economy.

The communication foresees a number of *"flagship initiatives"*; one of them entitled *"an industrial policy for the globalisation era"* aims at launching a more coherent and successful industrial strategy at EU and national level.

After having acknowledged that industry and especially SMEs are facing increasing competition and cannot harness the advantages offered by the Globalisation process, the Commission tries to fix some priorities which should inspire its future industrial policy.

The Commission in particular commits itself to actively support restructuring of sectors in difficulty by means, inter alia, of the Globalisation adjustment fund. It also stresses the need (already included in the *"Small business act"* launched in 2008 [12] and in other related initiatives) to promote the internationalisation of SMEs and, at national level, to *"improve conditions for enforcing intellectual property rights"*.

Chapter 3.3 *"Deploying our external policy instruments"* is expressly dedicated to external policy instruments. The Commission confirms its commitment towards an open and liberalised international trade and stresses that future global growth will offer new opportunities for European companies.

It pledges to ensure *that "all instruments of external policy need to be deployed to foster European growth through our participation in open and fair markets worldwide"*. In this respect the Commission proposes a two-folded initiative: improving the external aspects of EU's internal policies (such as energy, transport, agriculture, R&D) and ensuring that trade and international macroeconomic policies work well and in a more coordinated manner.

Commitment to assert the EU *"more effectively on the world stage"* appears to be rather ambitious and difficult to achieve. As noted before, the EU was, so far, able to limit the losses of its market share at global scale but it certainly has not improved its capacity to shape "*the future global economic order"* and pursue *"the European interest"* worldwide. The rise of new and powerful economies has, in fact, undermined the economic control that the EU, but also the US, enjoyed for decades and made international economy more democratic but also less predictable and more difficult to govern. This scenario has certainly worsen since the entry into force of the Uruguay Round Agreements and the capacity of the EU to play a key role in world trade has not disappeared but it has certainly declined over the last fifteen years.

According to the Commission, a serious effort has to be made to ensure that goods and services in which the EU has a comparative advantage enjoy free and fair access to emerging countries' markets (where the economic growth and internal demand is expected to be more sustained than the one of industrialised countries).

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[12] see at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0394:FIN:en:PDF, and http://ec.europa.eu/enterprise/newsroom/cf/document.cfm?action=display&doc_id=3454&userservice_id=1&request.id=0

Not surprisingly, the core of the Commission's strategy is securing a better market access to EU companies and in particular to SMEs. Among the other main goals, there are the pursuit of more successful *regulatory dialogues* (especially in areas such as climate and green growth) and whether possible the achievement of mutual standards recognition and convergence on key regulatory issues. The Communication also sets the objective of *"building strategic relations with emerging economies"* and enhancing cooperation with candidate and neighbouring countries.

To reach these wide-ranging objectives, the Commission proposes to draw up, during the current year, a new trade strategy for Europe 2020 which would encompass the following elements:

- a new impetus to multilateral and bilateral negotiations especially with countries having the *"strongest economic potential"*;
- a better enforcement of existing trade agreements in particular as far as behind-the-border barriers are concerned;
- the promotion of new initiatives at international level for key sectors such as "green " and high-tech products as well as for services;
- the introduction of high-level strategic dialogues with key partners on key issues such as market access, regulatory framework, global imbalances, energy and climate change, access to raw materials, fight to poverty, development and education [13];
- the publication of an annual *"trade and investment barrier report"* identifying sectors where improvements on market access and regulatory issues is needed;

The Commission also confirms its commitment to developing a real partnership with developing countries with the view to eradicating poverty, promoting growth and fulfilling the *Millennium Development Goals* (MDGs). Particular relevance is given to relationships with Africa for which a revised set of policies is foreseen (more and better development aid, better coordination with Member States).

Only by being able to produce innovative and high-quality products the EU would be able to escape the relative decline which is experiencing in the world trade. The reform will be successful if it is able to stimulate the EU's external trade performance. There is in fact no other way to sustain economic growth and create jobs in Europe. In fact, bearing in mind that the EU economies are still recovering from the financial and economic crisis and that the traditional markets of our products (other industrialised countries and in particular the US) are also experiencing a severe decline in their demand and increased conditions of competition from third countries, the only option available to the European products is to find new outlets in emerging countries.

Unfortunately, as acknowledged by the Commission itself, the EU has, in these very markets, lost important positions and is still fighting to ensure an adequate level playing field for its products and services. Reversing this negative trend will therefore be difficult, also because the EU is probably one of the most open economies in the world and it often has little to offer in return to emerging countries which are already enjoying (almost) free access to the Single Market. Internationalisation of SMEs would also be difficult to achieve without a serious economic and political coordinated effort by both the EU and Member States.

[13] In particular as far as the United States (i.e. the Transatlantic Economic Council), Japan, Russia and China are concerned.

The announced new EU trade Strategy will perhaps clarify some doubts but at the moment it is not clear in which way the EU expects to secure such important objectives which (unlike the internal ones) do not entirely depend on its-own goodwill but are instead subject to the appreciation and the approval of third countries' governments.

Finally, the Europe 2020 communication seems to be a little weak as far as industrial policy is concerned. During the last fifteen years, a notable part of the EU industry has been dismantled and delocalised. In the name of the doctrine of "competitive advantage", the EU has put forward an economic strategy which had certain merits but also involved a dramatic contraction in the EU industrial (and often agricultural) output. To be able to export more, the EU should also be able to produce more and better. This can only be done if there is a clear understanding that a modern, solid productive base has to be preserved in Europe.

9. QUESTIONS FOR DEBATE

Europe 2020 has the ambition to design a growth model for the European Union in the horizon 2010-2020: how can balance between its three priorities be maintained?

The economic crisis has revealed that many European structural problems the Lisbon strategy was meant to address are still there: what can make Europe 2020 more effective than its predecessor?

Many reforms suggested by Europe 2020 imply deep changes in national policies directly affecting citizens: how can governance of the strategy guarantee that decision-making respect basic democratic principles?

How wide is consensus over the priorities identified by Europe 2020 within European society?

Are the foundations of Europe 2020 consistent with the lessons to be learnt from the recession Europe is experiencing?

The crisis had severe human repercussions: could the EU and the Member States have reacted differently or more efficiently? Will Europe 2020 manage to avoid similar crises in the future or, in case, soften their social impact?

How will structural and cohesion policies be streamlined with the implementation of EU2020 strategy?

How will the structural and cohesion policies be considered within the upcoming negotiations on the next multiannual financial framework? How effective can an integrated framework for the structural and cohesion policies really be?

With regard to access and eligibility for financing: How to address the trade-off between flexibility and control/result orientation within the management and delivery systems of Structural Funds? How to channel the funding towards high growth and job potential and guarantee focus on SMEs?

Closely related to the previous point, how to overcome the constraints in co-financing (i.e. interaction of structural and cohesion policies and macro-economic/budgetary policies)?

Regarding the social consequences of the crisis what does the new horizontal social clause of the Lisbon Treaty (Article 9 Treaty on the Functioning of the European Union) entail?

How can the European Parliament and national parliaments mobilise European citizens around the objectives of Europe 2020 and open up ownership of the strategy to civil society?

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ANNEX 1 LIST OF EP RESOLUTIONS AND STUDIES

Recent European Parliament resolutions:

European Parliament resolution of 10 March 2010 on EU 2020

European Parliament resolution of 6 July 2010 on promoting youth access to the labour market, strengthening trainee, internship and apprenticeship status

European Parliament resolution of 7 September 2010 on developing the job potential of a new sustainable economy

European Parliament legislative resolution of 8 September 2010 on the proposal for a Council decision on guidelines for the employment policies of the Member States: Part II of the Europe 2020 Integrated Guidelines

Recent European Parliament studies and briefings:

The Situation of Youth in the European Union (2010)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=31151

The impact of climate change policies on the employment situation - Summary of evidence note (2010)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=30751

The Lisbon Strategy 2000 – 2010 - An analysis and evaluation of the methods used and results achieved (2010)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=32031

The Link between Job Creation, Innovation, Education and Training - An Assessment of Policies Pursued at EU Level (2010)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=31255

EU cooperation in the field of social inclusion (2010)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=31792

Analysis of the Social Agendas (2010)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=30151

Indicators of Job Quality in the European Union (2009)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=27929

Background note on the revision of the procedure for the IGL (2009)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=26371

The impact of new forms of labour on industrial relations and the evolution of labour law in the European Union (2008)

http://www.europarl.europa.eu/activities/committees/studies/download.do?file=23224

Demographic future of Europe (2008)

http://www.europarl.europa.eu/activities/committees/studiesCom/download.do?file=21831

Employment potential of renewable forms of energy and increased efficiency of energy use (2007)

http://www.europarl.europa.eu/activities/committees/studies/download.do?file=16451

Alternative Progress Indicators to GDP as a Means to Sustainable Development (2007)

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=19990

ANNEX 2 EP REPORTS DEALING WITH EXTERNAL EU COMPETITIVENESS ISSUES

Rapporteur: Daniel Caspary (EPP)

Title: Global Europe, external aspects of the European Competitiveness

Date of adoption: 18 April 2007

Link: http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+REPORT+A6-2007-0149+0+DOC+PDF+V0//EN&language=EN

** ** **

Rapporteur: Ignasi Guardans (ALDE)

Title: The EU's Strategy to deliver market access for European companies

Date of adoption: 7 January 2008

Link: http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+REPORT+A6-2008-0002+0+DOC+PDF+V0//EN&language=EN

** ** **

Rapporteur: Cristiana Muscardini (EPP)

Title: Enhancing the role of European SMEs in international trade

Date of adoption: 16 January 2009

Link: http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+REPORT+A6-2009-0001+0+DOC+PDF+V0//EN&language=EN

WORKING GROUP 2: WHAT KIND OF ECONOMIC GOVERNANCE?

Abstract

This briefing note briefly reviews the developments of the financial and economic crisis both in the EU27 as well as specifically in the euro area. Furthermore, the note defines the much used term "economic governance" and classifies it according to degrees of policy coordination. The main part of the note presents and reviews the central elements of the recent European Commission legal proposals to reform economic governance in the EU, which are then evaluated within an outlook to the future. The note identifies elements that may be missing within or beyond the proposals. Finally, the European Semester for policy coordination is explained, and suggestions are made as to how the European Parliament and National Parliaments could be involved in the process of economic governance in the EU in this context.

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1. A FAILURE OF ECONOMIC GOVERNANCE?

The troubles originating in a subsection of the US real estate market in the summer of 2007 quickly snow-balled into a full-scale financial crisis touching all sectors of the global economy. In the EU, the latest stage of this development is the emergence of a sovereign debt crisis with markets increasingly doubtful about states' abilities to repay their debts. Greece saw its credit supply dry up and has effectively been bailed out. Countries such as Spain, Portugal and Ireland have been on the brink of seeing similarly adverse market reactions and have had their debt downgraded. Most other countries, even if not directly affected, have pre-emptively attempted to calm markets by tightening their respective fiscal belts.

1.1. The Euro Area

At the wake of the entry into the third stage of EMU in 1999, and the introduction of the euro, there were doubts as to whether a single currency could survive without some elements of common fiscal policy, such as fiscal stabilisation mechanisms, or even common (federal-style) taxes. At least the theory of monetary union seemed to teach that it could not.[14] This debate was muted as the first ten years of the euro coincided with years of moderately high economic growth, unprecedented financial globalization and ample liquidity, which seemed to render the question obsolete. Since the spring of 2010 at the latest, this question is rising to the fore.

A (minimum) common compromise to support monetary union with fiscal policies found form in the Stability and Growth Pact (SGP). The well known criteria that states should respect were fixed at an annual budget deficit no higher than 3% of GDP and a national public debt lower than 60% of GDP, otherwise an Excessive Deficit Procedure (EDP) with sanctions could, in theory, be implemented. In the crisis, both the *preventive* and *corrective* mechanisms embedded in the SGP have failed due to a seeming lack of political will for enforcement.[15] Both these mechanisms are currently under revision (see Ch. 3).

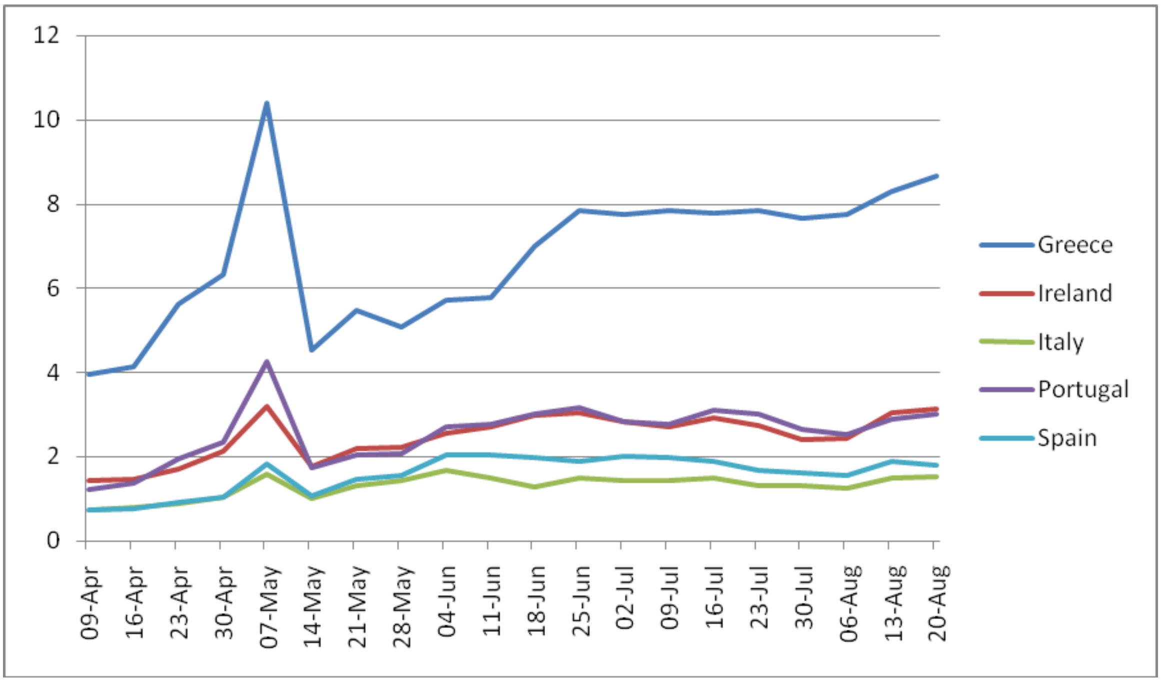
Of the euro area Member States, Greece was first to falter following the revision of its budget deficit numbers at the end of 2009. Uncertainty was further increased by the fact that the procedure of reporting national accounts had been subject to abuse. Greece quickly saw its private sector funding evaporate and it was becoming increasingly unlikely that it would be able to roll-over its debts. This put policy makers in a bind, and all the more so as investors suddenly started to take a hard look at some of the other countries' finances. Countries such as Spain, Ireland and Portugal saw their spreads increase as markets became seriously worried about contagion (see Figure 1 below). The challenges confronting the most indebted countries were indeed considerable, and continue to be so.

After some initial reluctance, in March 2010 EU Heads of State reacted first with a €110 billion intergovernmental rescue package for Greece, but soon stepped up with an unprecedentedly ambitious package. On 9 May 2010, finance ministers of EU Member States agreed a package to defend the euro, with a potential maximum of about €750 billion (incl. notably the Special Purpose Vehicle (SPV) of €440 billion). Moreover, soon after, the ECB surprised markets by announcing a hitherto unprecedented scheme to buy up government bonds on the financial markets.

[14] See e.g. Fatas, Antonio (1998): Does EMU need a Fiscal Federation? INSEAD Discussion Paper, http://faculty.insead.edu/fatas/fiscalfe.pdf for a useful discussion.
[15] The Stability and Growth Pact was originally decided in 1997 and amended in 2005. It is currently under revision, as detailed in Annex I.

Figure 1 below shows the success of these decisions, as measured by the government bond spreads. Indeed, despite an initial calming and reduction in the spreads, the difference to borrowing costs in all above mentioned countries continues to be considerably high in comparison to Germany, and no convergence to the very low levels of pre-crisis levels of spreads is in sight. This may be compelling evidence suggesting that markets do not believe that the problems are finally resolved.

Figure 1. Sovereign Interest Rate Differentials*



*10-year government bond spreads vs. Germany, source: *Financial Times*

1.2. The EU27

Different Member States were affected in a variety of ways. A full analysis of the impact of the crisis in single Member States is beyond the scope of this briefing, however some remarks appear pertinent:

The freedoms of the internal market allowed some countries to run-up large external deficits as the private sector borrowed heavily in foreign currency. Countries such as Latvia, Estonia and Bulgaria with hard currency pegs had effectively kept real interest rates too low for too long, in some cases even negative, thus distorting private sector decisions. For these countries, the currency regime proved an important factor in determining the economic impact of the crisis.

Other countries with floating exchange rates to the euro with large foreign currency denominated private sector debts inflicted serious economic pain on borrowers whose income was denominated in local currencies by allowing their currencies to depreciate. Countries hardest hit were those with the largest external imbalances through excessive reliance on foreign capital flows. Hungary, Latvia and Romania faced external funding gaps and applied for Balance-of-Payments (BoP) assistance from the EU. Moreover, the ECB played an important role in mitigating currency fluctuations for instance through widely rumoured "secret" swap lines with the Polish and Hungarian central banks. In this light, the wider macroeconomic surveillance (Ch. 3) along the lines of what is proposed by the Commission will certainly be a step forward. Whether it will be implemented effectively is a different question.

This brief description already by itself shows the challenge of designing rules for the whole of the EU27, including the euro area and countries whose currency is not or not yet the euro.

2. What is economic governance?

2.1. The need for better governance

The term "economic governance" has possibly become a "buzzword" with varying definitions. The vagueness of the term stands testimony to the fact that the EU does not have an economic '"government" (or model of economic management) in the traditional sense of the word. There is no single player, no single cabinet, responsible for economic policy in the EU. Rather, economic policy making in the EU is a complex set of interaction between the European Parliament, Commission and possibly currently most importantly, the Member States (through the Council). However, through the new Lisbon Treaty, the powers of the European Parliament have been strengthened in economic policy making, mainly through Art. 121(6) on multilateral surveillance which falls within the ordinary legislative procedure (formerly known as co-decision procedure).

National parliaments currently have an important role in EU economic governance both in implementing structural reforms and deciding on the national budgets. Joint Parliamentary meetings (JPM) or other EU level parliamentary gatherings have a role to play in this process, albeit informal. What is discussed at Joint Parliamentary meetings (JPM) or other EU level parliamentary gatherings may have a role to play in this process, yet it is all somewhat informal. The proposed European Semester, a system of early peer-review of national budgets that should detect inconsistencies and emerging imbalances, stands the chance of changing this and strengthening parliamentary roles in governance, but improvements to its design are needed (see below Ch. 4.1).

2.2. Degrees of policy coordination

One way to think about governance is in terms of "degrees of policy coordination". Policy coordination can be defined as "a significant modification of national policies in recognition of international interdependencies".[16] However, there is a wide spectrum of meanings to the term. In his briefing to the European Parliament's Economic and Monetary Affairs (ECON) Committee, Stefan Collignon[17] distinguishes at least five forms of cooperation depending on how binding a cooperation agreement is:

1. *Cooperation only by exchange of information* is the weakest form. Policy modifications result from insight and voluntary changes in the preferences of actors. The proposed "European Semester" belongs into this group.
2. *Coordination as crisis management*. An *ad hoc* reaction may prevent clearly perceived negative consequences from not cooperating. This was the logic behind the European Stabilisation Mechanism, set up on 9 May 2010.
3. *Coordination by targets*. This requires negotiations between actors who focus on specified variables as surrogate for coordination, but leave it to the discretion of coordinating partners how the targets will get achieved. This is the underlying logic of the "open method of coordination" that emerged from the Lisbon Strategy. The Commission now wants to use this approach to "develop a scoreboard of indicators to identify alert thresholds for severe imbalances" and set "more ambitious budgetary targets".

[16] P. Mooslechner and M. Schuerz 1999: International macroeconomic policy coordination; *Empirica: Journal of Applied Economics and Economic Policy*, Vol 26.3; Austrian Institute of Economic Research.

[17] The following text and classification is a slight modification of what is has been proposed by Collignon (2010): Europe's economic government or how to use the Treaty for more effective economic coordination, Briefing paper, Monetary Dialogue June 2010, European Parliament, PE 440.282.

4. *Partial coordination*. Partners agree on policy assignment to specific actors, although not all partners have to do the same thing. Under this approach, it is possible to formulate more binding constraints and even to impose sanctions. Examples are making the Stability and Growth Pact more "flexible" by giving different targets according to structural policy parameters, like aging dynamics, or having different degrees of strictness in the excessive deficit procedure depending on how far public debt exceeds the 60%-mark of GDP.

5. *Full coordination*: a bargain across *all* targets and policy instruments that binds all actors, because individual policy makers will only get substantial gains by trading off less relevant policy issues. This is the usual process in democratic legislative processes, where political parties bundle policies into programmes, which are then chosen by citizens.[18] However, in an intergovernmental context, the bargaining between governments makes the link to the citizens more distant. In the EU, bundling policy issues into a coherent programme and submitting alternative platforms for the approval by voters has not really happened yet, although Treaty negotiations between Member States do cover a broad range of policies. This could change, as the "ordinary legislative process" (Art. 294) becomes a more frequently used tool for policy coordination in the EU.

As Stefan Collignon points out, delegation to a single institution, like in the case of monetary policy with the ECB, is not coordination, because the responsibility for policy design and implementation is unified in the hand of a single agent, who is accountable to the principal. The Treaty specifically allows such policy making delegation through legislative acts.[19]

The EU economic policy, whether monetary or fiscal, operates in a stochastic environment where outcomes are uncertain, and sometimes very difficult to predict. Binding ex ante rules are not always the most suitable way to address this environment. "Hard rules" must be applied in deterministic environments, where the same rule always produces the same results. However, when policies must respond to unforeseen shocks, policy delegation and discretion is required, Monetary policy is the archetype for such discretionary policy. The euro area has already centralised monetary authority in the ECB and it has proven extremely successful in responding to the unforeseen shocks of the recent crises.

Some would argue that also in the case of fiscal policy (within the context of a monetary union), the same logic should apply. For example, ECB President Trichet has often called for a "quantum leap" in thinking about this necessary (but currently weak) link between monetary and fiscal policy. However, currently, and for the foreseeable future, fiscal policy remains a national prerogative. Others, such as Charles Wyplosz or Lars Calmfors[20], would argue that a decentralized solution is the only viable solution, since markets can effectively provide the correct incentives by punishing profligate fiscal policy, even in a monetary union. The jury on this issue is still out, it seems.

[18] The Lisbon Treaty recognises this role also for the European Union: TEU, Art. 10 says: "3. Every citizen shall have the right to participate in the democratic life of the Union. Decisions shall be taken as openly and as closely as possible to the citizen. 4. Political parties at European level contribute to forming European political awareness and to expressing the will of citizens of the Union."

[19] *Article 290:* "1. A legislative act may delegate to the Commission the power to adopt non-legislative acts of general application to supplement or amend certain non-essential elements of the legislative act."

[20] See e.g. Wyplosz, Charles (2010): The Debt Crisis and the Treaty, Briefing paper, Monetary Dialogue June 2010, European Parliament, PE 440.282; Calmfors, Lars (2010): Fiscal policy coordination in Europe, Briefing paper, European Parliament, PE 440.292.

3. Assessment of the Commission proposals September 2010

Following the sovereign debt crisis, the handling of the first support mechanism for Greece, the establishment of the stabilization mechanisms on 9 May 2010 and suggestions put forward by the Commission on 12 May and 30 June in its Communications (COM(2010) 215 and 367 final, respectively) on enhanced economic coordination and surveillance, the Commission introduced a comprehensive package of EU economic governance reform on 29 September (see Annex I for a detailed overview of the legislative proposals, their legal base and EP Rapporteurs). The Commission did so under close coordination with the Council Task Force on the Economic Governance chaired by President of the European Council Herman Van Rompuy.

The legislative package is made up of six pieces of legislation: four proposals deal with fiscal issues, including a wide-ranging reform of the Stability and Growth Pact (SGP), while two new regulations aim at detecting and addressing effectively emerging macroeconomic imbalances within the EU and the euro area. Four of the proposals are in the ordinary legislative procedure, while in two proposals the European Parliament has a consultative role (see Annex I). It is worthy to note at this stage that the ECON Committee of the European Parliament has decided to treat all six pieces of legislation as a legislative package, similarly to its dealing with the financial supervision legislation agreed in September 2010. What this could mean in practice is that the EP's leverage over the consultative files is de facto increased, as all six pieces of legislation are treated as a whole.

3.1. Reforming the Stability and Growth Pact (SGP) – Fiscal Policy

In the package, the Commission introduces a new concept of prudent fiscal policy-making (PFPM) that it hopes will ensure actual convergence towards the medium-term objectives (MTO) in Member States fiscal policy. If a Member State is not within its MTO, the Council will verify if Member States comply with PFPM principles. The Commission may issue a warning in case of significant deviation from the PFPM.

While the existing version of the Stability and Growth Pact, in practice, focused on fiscal deficits rather than debt stocks, the reform also entails a closer monitoring of sustainable debt developments, and whether excessive debt (above 60% of GDP) is sufficiently on a decreasing track. However, loopholes remain for countries with low nominal growth, special ageing related burdens or high private debt levels, in which cases an Excessive Deficit Procedure (EDP) can still be avoided.

Under the new procedure, Member States whose debt is over 60% of GDP have to commit to reducing this stock at a pace of 5% per annum, measured of the difference above the 60% threshold of the average of the previous three years. This means that this retrospective measure will only gradually be put in place in the next years.

First calculations of what this means have been conducted by Nikolaus Heinen (2010)[21], in the table below. What becomes visible is that if applied with debt levels of 2011, the reform would mean very stringent consolidation (debt reduction) efforts annually, inter alia amounting to roughly 26 billion euros for Germany, and 8.6 billion for Greece.

The success of these reformed mechanisms hinges on their effective enforcement and Member States' ability to impose these ambitious consolidation efforts. There is hope, but certainly no guarantee, that this will work.

[21] Heinen (2010), Ambitious? Yes. Effective? Perhaps. The Commission Proposals on the SGP, Deutsche Bank Research, http://www.dbresearch.com/MAIL/DBR_INTERNET_EN-PROD/PROD0000000000263157.xhtml, accessed on 12 October 2010.

Table 1: Annual debt reduction under 2011 debt scenario

Ambitious Consolidation Targets

	debt level 2011 (%GDP)	debt above 60% GDP (%GDP)	consoli-dation p.a.(%GDP)	consoli-dation p.a. (m. Euro)
BE	100,9	40,9	2,0	7.139,5
DE	81,6	21,6	1,1	26.269,7
IE	87,3	23,3	1,2	1.811,5
GR	133,9	73,9	3,7	8.600,8
ES	72,5	12,5	0,6	6.579,8
FR	88,6	26,6	1,3	25.889,3
IT	118,9	58,9	2,9	45.746,2
CY	67,6	7,6	0,4	65,5
MT	72,5	12,5	0,6	37,0
NL	69,6	9,6	0,5	2.809,5
AT	72,9	12,9	0,6	1.803,5
PT	91,1	31,1	1,6	2.648,4

*Finland, Slovenia, Slovakia and Luxembourg are below the 60% threshold.

Source: European Commisison, DB Research

3.2. New Macroeconomic Surveillance Mechanism

The past failure of economic governance is not limited to fiscal policy but bears a more general macroeconomic (competitiveness) component including diverging developments in unit labour costs, productivity and savings, just to mention a few relevant variables. This is because not all problems in the run up to the crisis were fiscal. Apart from financial regulation and supervision deficiencies, countries such as Ireland and Spain recorded healthy fiscal surpluses in many years, yet the problem lied in the imbalances in private debt and savings, and or asset price developments. It is therefore sensible to keep a wider array of macroeconomic indicators in track.

The Commission now introduces an "alert mechanism" for macroeconomic imbalances. Once an alert is triggered, the Commission proposes to make a country-specific analysis and recommendations to the Council on how to tackle the imbalances, or to warn the Member State directly. As an enforcement mechanism, the Commission could place the country in an "excessive imbalances position", EIB, (equivalent of excessive deficit in SGP) triggering stricter surveillance of corrective action. The new proposals do not yet spell out which variables of competitiveness the Commission wants to use and monitor in its scoreboard.

What is interesting is that the Commission does not place the burden exclusively on current account deficit countries, such as Spain or Ireland. It seems that the approach taken is symmetric, i.e. also current account surplus countries such as Germany or the Netherlands would have to do their share to correct imbalances, if such a state is declared. However, the feasibility of this side of the coin is a much contested matter, and yet to be clarified.

In its resolution on economic governance of 16 June 2010 (see Annex I), the European Parliament had called for a consistency of macroeconomic and budgetary policies with the EU2020 strategy to foster sustainable growth and development. Indeed, the design of the macroeconomic surveillance mechanism would be the natural place to ensure such consistency.

3.3. Enforcement is critical

On both the SGP and the macroeconomic surveillance, euro area Member States are proposed to get their own more stringent enforcement rules, including non-interest bearing deposits which would be converted to fines in the event of repeated non-compliance. To reduce discretion in enforcement, a new "reverse voting mechanism" is also envisaged. Under the new voting rules, which would apply when imposing sanctions, a Commission proposal will be considered adopted unless the Council overturns it by a qualified majority.

In the corrective part of the fiscal SGO, a non-interest bearing deposit amounting to 0.2% of GDP would apply upon a decision to place a country in excessive deficit. This could be converted into a fine (of up to 0.5% of GDP) in the event of non-compliance with the recommendation to correct the excessive deficit. In the macroeconomic EIP, on the other hand, if a euro-area Member State repeatedly fails to act on Council EIP recommendations to address excessive imbalances, it will have to pay a yearly fine equal to 0.1% of its GDP. To date, the Commission has not provided the economic rationale or underlying calculations for these figures, 0,2% and 0,1%, and where they come from.

3.4. Enhancing national fiscal frameworks

The Commission also proposes to strengthen national fiscal frameworks by means of a directive. The proposal entails include harmonizing and strengthening accounting and transparency requirements in the national budget process, aligning national fiscal rules with Treaty obligations and requiring binding numerical targets (e.g. constitutional debt breaks) and switching to multi-annual budgetary planning in all Member States. In addition, Member States are encouraged to put in place budgetary institutions that help achieving these goals. These include establishing independent fiscal watchdogs (e.g. as in Sweden, Netherlands, Hungary or UK). Indeed, a number of academics who are sceptical about the feasibility of enforcement in the SGP place their hopes in this kind of decentralized accountability (see e.g. above notes on Charles Wyplosz or Lars Calmfors under 2.2).

4. An outlook on the future of EU economic governance

Within the possibilities of the Treaty, the Commission can be credited for having tabled an ambitious package. This was undoubtedly needed, as unless bold reforms are undertaken, it is not exaggerated to say that the common currency and the EMU are in existential danger.

However, are the proposed measures enough, and do they capture the right dimensions of the problems? Given that enforcement and implementation of any existing or future rules are crucial, what can realistically be expected?

One reason why it is difficult to answer this question is because the Commission did not accompany its proposal with an impact assessment. Under the Interinstitutional Agreement on better law-making[22], each legislative proposal of the Commission should be accompanied by an impact assessment of the proposed measures. This was not the case for the present package, for the lack of which the Commission refers to time pressure. Nonetheless, the absence of an impact assessment makes it more difficult to assess the impact of the measures, as well as their chances of effective enforcement.

[22]Art. 29 - European Parliament, Council and Commission, Interinstitutional agreement on better law-making, (2003/C 321/01), OJ C 321 of 31.12.2003, p. 1.

The European Commission's communications of May and June 2010 initially had four elements: compliance with the Stability and Growth Pact and deeper fiscal policy coordination; surveillance of macroeconomic imbalances and competitiveness developments; a "European Semester"; and a framework for crisis management.[23]

An enhanced framework for crisis management did not make into the concrete proposals of 29 September. The European Semester was agreed in advance but has no formal role in the proposal and is intended to be kept as an informal exercise supportive of the rules agreed under this package.

A complete system of crisis management should comprise three steps: 1) crisis prevention, 2) crisis mitigation and 3) crisis resolution.[24] The present package deals largely with crisis prevention (1), as it puts in place procedures to prevent similar events happening again. While the emergency measures decided on 9 May belong to crisis mitigation (2), there is no progress in the EU in finding suitable models of crisis resolution (3). Crisis resolution includes institutions such as European Monetary Fund (EMF), sovereign default and debt restructuring etc. In its resolution on 16 June 2010 on economic governance the European Parliament called for the creation of such an EMF (Art. 12).

Some observers have pointed out that most probably the "uncertainty over the end game", or the worst case scenario of a mechanism of debt default and restructuring, for sovereigns (but also for banks), has probably exacerbated the crisis. Still today there is no real plan beyond 2013 that is when the temporary European Stabilization Mechanisms presently run out.

Solutions to all components, namely the fiscal, the macroeconomic and the crisis resolution dimensions need to be coherent towards each other. Also, very importantly, they need to be coherent with any private sector (financial sector) solutions discussed. In the present crisis, the private and the public problems go hand in hand and therefore the "circuit-breaker" for debt needs to be strong enough to address both sectors.

Moreover, while more macroeconomic coordination and transfers of sovereignty in fiscal matters are welcomed by many, there are also justified doubts as to whether fiscal sanctions can work in practice with "sovereign" countries. Will a euro area Member State in difficulty ever effectively be subject to sanctions? At this point, the debate is no longer one of economic rationale, but of deeply political nature, including considerations of democratic accountability.

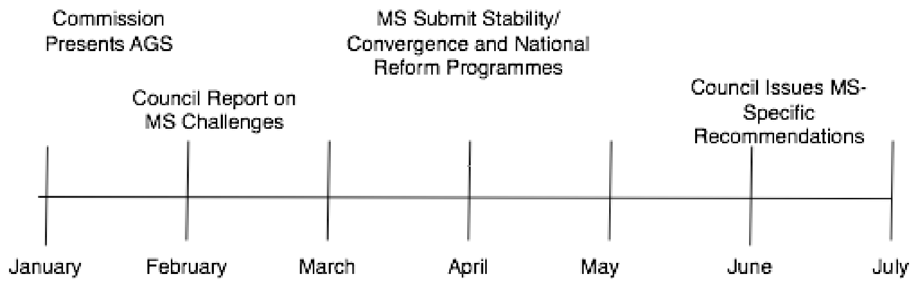
Finally, how can binding policy rules oblige democratically elected governments to do things they have not been elected to do? How can an unelected body such as the European Commission impose sanctions on elected governments? There are indeed legitimate concerns on the democratic accountability of the sanction regime. Without involving the elected representatives on both the European and national level in an adequate way, this reform may not be sustainably enforceable. In order to maximize efforts to prevent failure, parliamentary involvement in the process needs to be strong and it is probably most naturally placed within the European Semester.

[23] See COM(2010) 250 on Reinforcing economic policy coordination and COM(2010) 367/2 on Enhancing economic policy coordination for stability, growth and jobs – Tools for stronger EU economic governance.
[24] See e.g. Kapoor, Sony (2010), Building a Crisis Management Framework, in "Euro Area Governance - Ideas for Crisis Management Reform", Study compilation, European Parliament, PE 440.292, p. 23.

4.1. The European Semester: A forum for parliaments in economic governance?

The European Commission announces that the "European Semester will integrate all revised and new surveillance processes into a comprehensive and effective economic policy framework". It is proposed to start in 2011 and does not require any further legal basis. It should work in the following way:

Table 2: Proposed Timeline, European Semester



The first AGS will be presented in January 2011. As of then, the process begins every January, when the European Commission is set to present an "Annual Growth Survey (AGS)." The Council would then provide by the end of February a report on what challenges Member States face. They, in turn, would submit both Stability/Convergence Programmes (SCP) and National Reform Programmes (NRP) to the Commission in April. The Council would then issue Member State-specific recommendations in early July before the summer. Its evaluation would be based on the fiscal plans, the macro-economic scenario, and policy reforms a given government provided in April.

National parliaments could then use this information in discussions of individual budgets. In the following January, the Commission would then assess how Member States integrated the advice given to them in July. Note that it will take three years before the process is fully in place, since only in 2012 can the first year of the semester, 2011, be evaluated. In 2012, recommendations would be given for to 2013. Only in 2013 is the whole cycle therefore fully in place.

The Commission invites the European Parliament to be the place where it would present the AGS, which would represent "stronger involvement of the European Parliament."[25] However, it is a non-clarified question whether this is sufficient in terms of democratic accountability. Possibly an accountability exercise on the Commission recommendations and Council decisions later in the cycle, in May or June, would be a way to further enhance the process.

In the spirit of the increased powers of national parliaments under the Lisbon Treaty, the AGS each January could also be an appropriate moment to involve the national legislatures and to give recommendations for the European Council. This could possibly happen through an annual JPM on a high parliamentary level, e.g. on the level of Chairs of relevant parliamentary committees, in order to strengthen the message. In the EP, the responsible committee would be the Economic and Monetary Affairs (ECON) Committee, but in most national parliaments, the committee responsible for budgets would be the competent committee. Official recognition by the Commission and Council for this kind of a n enhanced parliamentary role in the process could be sought by the European Parliament in the course of the upcoming negotiations on the economic governance package.

[25] COM(2010) 367/2, p. 13.

Since the European Semester is a crucial exercise for the democratic legitimacy and ownership of economic governance rules by the European people, it would be important that each parliament is represented on a high level, and substantial recommendations are given. Only if the European Parliament and national parliaments manage to enhance their cooperation in this process and the Council allows the voice of the citizens be heard, will democratic legitimacy of economic governance in the EU stand a chance to be significantly increased.

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ANNEX I - SCHEMATIC OVERVIEW OF LEGISLATIVE PROPOSALS OF 29 SEPTEMBER 2010

Fiscal surveillance	**Macroeconomic surveillance**
1) Amendments to reg*. 1466/97* *(ordinary legislative procedure)* 2) Amendments to reg. *1467/97* *(special legislative procedure; Parliament and ECB consulted)* 3) New Directive *on national fiscal frameworks (Council Directive, EP consulted)*	5) New regulation *on prevention and correction of macroeconomic imbalances* *(ordinary legislative procedure)*
Enforcement	**Enforcement**
4) New regulation *on effective enforcement of budgetary surveillance* *(ordinary legislative procedure)*	6) New regulation *on effective enforcement of macroeconomic surveillance* *(ordinary legislative procedure)*

1) Regulation of the European Parliament and of the Council amending Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies (COM(2010)526, 2010/0280(COD)).

Legal basis: Article 121(6) (o*rdinary legislative procedure),*

EP Rapporteur: Corien WORTMANN-KOOL (EPP)

2) Council Regulation amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure (COM(2010)522, 2010/0276(CNS)).

Legal basis: Article 126(14) subparagraph 2 (consultation),

EP Rapporteur: Diogo FEIO (EPP).

3) Council Directive on requirements for budgetary frameworks of the Member States (COM(2010)523, 2010/0277(NLE)).

Legal basis: Article *126(14) subparagraph* 3*(consultation),*

EP Rapporteur: Vicky FORD (ECR).

4) Regulation of the European Parliament and of the Council on the effective enforcement of budgetary surveillance in the euro area (COM(2010)524, 2010/0278(COD))

Legal basis: Article 121(6) and Article 136 (ordinary legislative procedure),

EP Rapporteur: Sylvie GOULARD (ALDE).

5) Regulation of the European Parliament and of the Council on the prevention and correction of macroeconomic imbalances (COM(2010)527, 2010/0281(COD)).

Legal basis: Article 121(6) (ordinary legislative procedure),

EP Rapporteur: Elisa FERREIRA (S&D)

6) Regulation of the European Parliament and of the Council on enforcement measures to correct excessive macroeconomic imbalances in the euro area (COM(2010)525, 2010/0279(COD))

Legal basis: Article 121(6) and Article 136 (ordinary legislative procedure),

EP Rapporteur: Carl HAGLUND (ALDE)

ANNEX II - QUESTIONS FOR DEBATE

While the negative effects of the crisis are felt everywhere, the crisis hit different Member States differently. How can common rules be designed for the whole of the EU27, while respecting the necessity to have stricter rules in place for the euro area?

What is economic governance? Do we need economic "government" from the centre (Brussels)? If yes, who should that government be? How can the National and European Parliaments contribute?

Alternatively, is decision-making (e.g. fiscal policy objectives) better dispersed into Member States and regions? If yes, how can consistency of policies be ensured?

The Commission has proposed an extensive economic governance package on 29 September. Are the proposed measures enough, and do they capture the right dimensions of the problems?

In that proposal, the absence of an impact assessment makes it more difficult to assess the impact of the measures, as well as their chances of effective enforcement. Should such an assessment be conducted before the finalization of the process?

The success of these reformed mechanisms hinges on their effective enforcement and Member States' ability to impose these ambitious consolidation efforts. Will a euro area Member State in difficulty ever effectively be subject to sanctions, something that has never happened? Has ownership of the common rules increased enough that this will now happen?

What is missing within and beyond the proposals? By way of example, there is still no progress in finding suitable models of crisis resolution. Crisis resolution includes institutions such as European Monetary Fund (EMF), sovereign default and debt restructuring etc. (In its resolution on 16 June 2010 on economic governance the European Parliament called for the creation of such an EMF).

What the EU currently has are the emergency mechanisms created on 9 May 2010, the European Financial Stabilization Facility as well as the Mechanism (EFSF and EFSM. There is no real plan currently beyond 2013, that is when these institutions presently run out. What should be done? Should the mechanisms simply be extended?

The past failure of economic governance bears a more general macroeconomic (competitiveness) component including diverging developments in unit labour costs, productivity and savings, just to mention a few relevant variables. The Commission introduces a new macroeconomic alert mechanism. Which variables should be monitored?

Within the macroeconomic surveillance mechanism, how to ensure consistency with the EU2020 strategy to foster sustainable growth and development?

How can an unelected body such as the European Commission impose sanctions on elected governments? Do the present proposals give the Commission too much power?

The European Semester was agreed in advance but has no formal role in the proposals and is intended to be kept as an informal exercise supportive of the rules agreed under this package. Is this sufficient? How can the parliamentary input in the European Semester be made as effective as possible?

National parliaments currently have a role in EU economic governance so far as they can influence or are consulted by the national government. What is discussed at Joint Parliamentary meetings (JPM) or other EU level parliamentary gatherings may have a role to play in this process, yet it is all somewhat informal. How can this process be made more effective?

ANNEX III - LIST OF EP RESOLUTIONS AND STUDIES IN ECONOMIC GOVERNANCE

Recent European Parliament resolutions:

- European Parliament resolution of 16 June 2010 on economic governance, P7_TA(2010)0224.[26]

- Own initiative (INI) report with recommendations to the Commission on improving the economic governance and stability framework of the Union, in particular the euro area. (Rapporteur: Diogo Feio, report voted in ECON Committee, tabled in October 2010 plenary), (A7-0282/2010)

Recent European Parliament studies and briefings:

Calmfors, Lars (2010): Fiscal policy coordination in Europe, Briefing paper, European Parliament, PE 440.292.

European Parliament (2010), Ideas for the Reform of the Multilateral Surveillance Regulation, Study compilation, European Parliament, PE 447.500, various authors.

European Parliament (2010), Euro Area Governance - Ideas for Crisis Management Reform", Study compilation, European Parliament, PE 440.292.

European Parliament (2010), Euro Area Governance, Monetary Dialogue - Topic 1, Study compilation, European Parliament, PE 440.282.

Kapoor, Sony (2010), Building a Crisis Management Framework, in "Euro Area Governance - Ideas for Crisis Management Reform", Study compilation, European Parliament, PE 440.292, p. 23.

Wyplosz, Charles (2010): The Debt Crisis and the Treaty, Briefing paper, Monetary Dialogue June 2010, European Parliament, PE 440.282.

[26] http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2010-0224+0+DOC+XML+V0//EN&language=EN, accessed on 12 Oct 2010.

WORKING GROUP 3: HOW TO COMPLETE EUROPE'S SINGLE MARKET?

Abstract

This note provides a brief overview of the most important recent Commission communications and resolutions of the European Parliament on the single market and comprehensive strategies to deepen single market integration, to close remaining gaps and overcome remaining obstacles. In a second part, the note provides a brief non-exhaustive overview of policy responses: proper application and implementation of single market legislation, problem-solving tools, public procurement, consumer rights legislation, product safety, accreditation and market surveillance.

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INTRODUCTION

Article 26 of the Treaty on the Functioning of the European Union (TFEU) stipulates that "the internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties".

In the past decades, significant progress has been made to create this single market. However, the European Union is currently facing a particularly problematic time in the history of single European market integration. Surveys show that attitudes towards the single market today range from lack of interest to open rejection. The continued existence of the single market should not be taken for granted. In some cases, the economic crisis has been used as a justification for the re-emergence of economic protectionism at Member State level, which could result in re-fragmentation of the single market[27].

However, at the same time, the single market and the common currency have acted as a protective shield in Europe, reducing the negative impact of the financial crisis on businesses and citizens in Europe.

In its Communication on "Europe 2020, a strategy for smart, sustainable and inclusive growth"[28], the Commission identifies the single market as a cornerstone of the EU 2020 Strategy, with the challenges of social justice and economic growth and a focus on benefits to citizens, consumer protection and SMEs.

> *"A stronger, deeper, extended single market is vital for growth and job creation. However, current trends show signs of integration fatigue and disenchantment regarding the single market. The crisis has added temptations of economic nationalism. The Commission's vigilance and a shared sense of responsibility among Member States have prevented a drift towards disintegration. But a new momentum – a genuine political commitment - is needed to re-launch the single market, through a quick adoption of the initiatives mentioned below. Such political commitment will require a combination of measures to fill the gaps in the single market."*

This paper is structured as follows: Chapter 2 will look at the most recent important responses from both the European Parliament (Grech report) and the European Commission (Monti-report) to the current challenges for single market integration. Chapter 3 will deal in somewhat more detail with some of the identified remaining bottlenecks and possible policy responses.

2. Recent reports of European Parliament and Commission outlining policy options

2.1. European Parliament – Grech report

The European Parliament has recently adopted an important resolution on "Delivering a single market for consumers and citizens", in which it outlines the importance of the single market integration process and makes recommendations for actions to deepen the integration and close remaining gaps.

[27] Grech report, EP Resolution 3 May 2010 on Delivering a single market for consumers and citizens.
[28] Commission Communication 3rd March 2010, COM(2010)2020.

The policies to tackle the crisis should not detract from the single market integration process, but rather provide a window of opportunity for reforming, consolidating and improving the current structure of the internal market, releasing the job creation potential of a green economy and regaining the trust and confidence of citizens, especially consumers and SMEs.

However, the relaunch of the single market must not be wholly dictated by the financial downturn and the revival must go beyond the fundamental lessons learned from the crisis.

To restore the credibility of and the confidence in the single market, strong leadership from the European institutions together with political ownership of the members states are needed.

The report proposes measures to inform and empower consumers and SMEs more effectively in the single market, e.g. by:

- Developing a targeted communication strategy focusing on day-to-day problems that citizens encounter relating to the single market;
- To prioritise consumer-friendly legislation, followed by adequate information campaigns;
- To improve the capacity of problem-solving mechanisms, such as SOLVIT;
- To keep up and increase citizen's confidence in the CE mark through information campaigns and tougher checks on quality standards;

The report also stresses the importance of correct and timely implementation of European legislation.

2.2. European Commission: Europe 2020 and Monti report

In its Communication on "Europe 2020" published 3 March 2010, the Commission announced that it will propose action to tackle bottlenecks in the single market by:

– Reinforcing structures to implement single market measures on time and correctly, including network regulation, the Services Directive and the financial markets legislative and supervision package, enforce them effectively and when problems arise, resolve them speedily;

– Pressing ahead with the Smart Regulation agenda, including considering the wider use of regulations rather than directives, launching ex-post evaluation of existing legislation, pursuing market monitoring, reducing administrative burdens, removing tax obstacles, improving the business environment, particularly for SMEs, and supporting entrepreneurship;

– Adapting EU and national legislation to the digital era so as to promote the circulation of content with high level of trust for consumers and companies. This requires updating rules on liability, warranties, delivery and dispute resolution;

– Making it easier and less costly for businesses and consumers to conclude contracts with partners in other EU countries, notably by offering harmonised solutions for consumer contracts, EU model contract clauses and by making progress towards an optional European Contract Law;

– Making it easier and less costly for businesses and consumers to enforce contracts and to recognise court judgments and documents in other EU countries

The Report of Professor Mario Monti to the Commission on ”A new strategy for the single market at the service of Europe’s economy and society”, presented on 9 May 2010, tries to develop a new comprehensive strategy for the single market, deploying all policies: competition, consumer, industrial, energy, transport, digital, social, environment, climate change, trade, tax and regional policies.

Three broad sets of initiatives are proposed:

1. Initiatives to build a stronger single market
2. Initiatives to build consensus on a stronger single market;
3. Initiatives to deliver a stronger single market.

The report presents several initiatives to build a stronger single market, aiming at removing the remaining bottlenecks and plugging the gaps and missing links that hamper innovation and dampen growth potential in the single market. The initiatives are grouped in clusters of recommendations concerning:

- Ensuring better functioning of the single market in the perspective of citizens, consumers and SMEs;
- Creating a digital single market;
- Exploiting the potential of the single market to support green growth and Europe’s transition to a low-carbon, resource efficient economy;
- Reaping the full benefits of the single market for goods;
- Fully exploiting the potential of the single market for services;
- Ensuring geographical labour mobility in the single market;
- Establishing the “physical” infrastructure for the single market;

An important aim of the Commission is to “put back at the heart of the internal market those who live in it and use it daily”, i.e. to put the citizens, consumers and SMEs at the centre of single market policy.

3. Remaining obstacles and possible policy responses

3.1. Remaining obstacles

Consumers are important beneficiaries of the single market. However, in some areas, there is still insufficient competition, access to the single market is difficult or precluded, or consumers are not adequately protected.

Obstacles that stand in the way of citizens, consumers and SMEs wishing to move, shop, sell or trade across borders with the same sense of security and confidence they enjoy in their own Member States, result from:

- A lack of information about rights and opportunities;
- Fragmented regulation
- A lack of legislative initiatives in a number of key areas;
- Inadequate transposition of single market legislation;
- Inadequate application and enforcement of rules;
- A lack of administrative coordination and cooperation
- Language barriers

As a result, some obvious problems encountered by consumers, especially in the services sector, are that their access to reliable, comparative and objective information, including price comparisons is hampered, as well as their access to a variety of high quality goods. Consumers feel that they have still greater legal security and clarity in contractual relations, greater payment security, access to adequate, affordable and effective systems of redress when buying goods or services in their own Member State. It is of crucial importance to increase consumers' knowledge of, and greater confidence in, the single market.

3.2. Implementation of single market legislation

The internal market scoreboard reveals that in September 2010, 85 single market directives had not yet produced their full effect in the EU due to lack of national implementation measures in one or more Member States. On average, Member States grant themselves an extra 7 months to adopt the legislation after the deadline expires.

Services Directive

The Services Directive is of crucial importance in completing the single market, since it has a huge potential for delivering benefits for consumers and SMEs. An open single market for services must be created on the basis of the Services Directive, whilst at the same time ensuring the quality of services provided to consumers. The full implementation of the Services Directive could increase trade in commercial services by 45% and Foreign Direct investment by 25%, bringing an increase of between 0.5% and 1.5% increase in GDP[29].

The successful implementation of this Directive requires sustained political commitment and support from all actors at European, national, regional and local level. The Directive requires Member States to adopt new legislation, to screen and adapt existing legislation, to set up single points of contact and to organise administrative cooperation between Member States.

The deadline for implementation of the Directive has expired on 28 December 2009. However, the implementation is significantly delayed in a number of Member States.

Directive on Recognition of professional qualifications

[29] Commission Communication on « Europe 2020 ».

Directive 2005/36/EC on the Recognition of Professional Qualifications has come into effect on 20 October 2007. It replaces and modernises 15 directives, providing for a more automatic recognition of qualifications. The aim is to make labour markets more flexible and liberalise the provision of services. The Directive is crucial to the functioning of the single market.

The Monti report recommends to "extend automatic recognition of qualifications" and to "strengthen the transparency and recognition of qualifications and skills". The European Commission is currently working on the preparations for the mandatory review of Directive 2005/36/EC in 2012.

3.3. Informal dispute settlement – SOLVIT

SOLVIT was established by the Commission in July 2002 as a network of national administrations using an online inter-active database as a tool solving problems caused by misapplication of internal market law, without going into formal legal proceedings. It has proven to be a successful tool, it has enhanced transparency and has created peer pressure to speed up problem solving.

Over the past years, the SOLVIT network has developed significantly. Yet, it is still underused, handling only 1600 cases per year. As it relies on centres managed by the national administrations, it struggles with some shortcomings, such as lack of adequate staff, insufficient oversight from the Commission and a wide variety of procedures and quality standards used[30].

It could be strengthened by providing for a clearer legal basis, minimum rules on staffing and some EU co-funding. Many citizens and businesses are not (sufficiently) aware of the work of SOLVIT.

3.4. Product safety, accreditation and market surveillance

In order to promote safety of goods and confidence in the CE mark, the application of Regulation (EC) No 765/2008 of the European Parliament and of the Council of 9 July 2008 setting out the requirements for accreditation and market surveillance in relation to the marketing of products is of crucial importance. It entered into force 1 January 2010, and the Commission and European Parliament are following the enforcement of the Regulation in the Member States closely. The Commission is furthermore obliged to present a report in 2013 on the application of the Regulation and other relevant legislation addressing market surveillance.

The Commission is also working on a revision of the General Product Safety Directive (Dir. 2001/95/EC). In order to influence the revision the European Parliament is right now working on an own-initiative report on the revision on the General Product Safety Directive and Market Surveillance. It will be adopted in the Parliament early 2011 which will be in due time before Commission presents its revision.

3.5.Consumer rights legislation

On 8 October 2008, the European Commission published the proposal for a Directive on Consumer Rights. The proposal merges four existing directives in the area of consumer law:

- Directive 97/7/EC on distance contracts
- Directive 85/577/EEC on contracts negotiated away from business premises "doorstep selling"
- Directive 93/13/EEC on unfair terms in consumer contracts

[30] EP Resolution 9 March 2010 on SOLVIT.

- Directive 1999/44/EC on the sale of consumer goods and associated guarantees

The aim of the Commission is to establish a real retail internal market while preserving a high level of consumer protection. It updates the four existing directives.

3.6. Public procurement

In 2008, EU public procurement amounted to around 17-18% of EU GDP[31]. EU public procurement law plays a key role in the creation and maintenance of the single market. The Monti report proposes to re-think public procurement policy to make it simpler, more effective and less onerous for national and local authorities; and to strengthen the participation of SMEs by applying the Small Business Act Code of Conduct.

3.7. A future new Single Market Act

The Commission is preparing a new Single Market Act designed to boost job creation and stimulate growth. The proposal is planned for October 2010 and will be inspired by the Monti report.

It will contain approximately 50 proposals, including new legislation in areas like taxation, counterfeiting and helping small businesses.

The EP has called on the Commission[32] to incorporate in this Single Market Act specific measures aimed at, but not limited to:

- Putting the consumer interests referred to in Article 12 TFEU and social policy based on Article 9 TFEU at the heart of the single market;
- Making the single market fit for the future by improving consumer and SME access to e-commerce and digital markets;
- Supporting the creation of a sustainable single market based on Article 11 TFEU through the development of an inclusive, low-carbon, green, knowledge-based economy, including measures to further any innovation in cleaner technologies;
- Ensuring the protection of services of general economic interest on the basis of Article 14 TFEU and Protocol 26;
- Creating a strategy for better communication of the social benefits of the single market.

[31] Monti Report p. 76.
[32] Grech report, EP resolution of 3rd May 2010 on Delivering a single market to consumers and citizens.

QUESTIONS FOR DEBATE

Below we provide a non-exhaustive list of questions that could be discussed during the Joint Parliamentary Meeting.

- How could the European Parliament and the National Parliaments contribute to setting up and developing a targeted communication strategy focusing on the day-to-day problems that citizens encounter when undertaking cross-border transactions, shopping or selling cross-borders, and the standards (e.g. consumer protection, safety) they can rely on?
- The Monti report suggests that the European Parliament and National Parliaments could participate in the review of how EU rules are transposed and implemented. It proposes that every year the EP and national parliaments could select one piece of legislation or an area of single market law and conduct a review of its implementation at national level, to spot inadequate implementation and unanticipated negative effects. What do participants think of this suggestion?
- How can the European Parliament and the National Parliaments contribute to the promotion of the SOLVIT network?
- How could administrative cooperation between Member State authorities responsible for the single market be improved?
- How can the access of SMEs to the single market be facilitated and administrative burdens reduced?
- In the long term: does the single market need full harmonisation measures or do we opt for minimum harmonisation (e.g. for consumer legislation)?
- Does the single market need a coordination of tax policies?

LIST OF EP RESOLUTIONS AND STUDIES

Recent European Parliament resolutions:

EP resolution of 04 September 2007 on The Single Market Review: tackling barriers and inefficiencies through better implementation and enforcement; T6-O367/2007

Resolution of the European Parliament of 20 May 2008 on the "EU consumer policy strategy 2007-2013",

Resolution of the European Parliament of 23 September 2008 on the Internal market scoreboard, T6-0421/2008

Resolution of the European Parliament of 9 March 2010 on consumer protection, P7_TA-PROV(2010)0046;

Resolution of the European Parliament of 9 March 2010 on SOLVIT, P7_TA-PROV(2010)0047;

Resolution of the European Parliament of 9 March 2010 on the internal market scoreboard, P7_TA-PROV(2010)051

EP resolution of 20 May 2010 on Delivering a Single Market to Consumers and Citizens, T7-0186/2010.

EP resolution of 07 September 2010 on EEA-Switzerland: obstacles with regard to the full implementation of the internal market,T7-0300/2010

EP resolution of 21 September 2010 on Completing the Internal Market for E-Commerce; T7-0320/2010

Recent European Parliament studies and briefings:

- Recognition of Professional Qualifications

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=es&file=27071

- Internal Market beyond the EU: EEA and Switzerland

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=29109

- Market Surveillance and revision of General Product Safety Directive

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=es&file=32451

- Implementation of the Services Directive

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=es&file=32455

- Briefing Paper on the Proposed Consumer Rights Directive: Chapter I - Definitions

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=es&file=32515

- Briefing Paper on the Proposed Consumer Rights Directive: Consumer Rights concerning Contract Terms: Chapter V

http://www.europarl.europa.eu/activities/committees/studies/download.do?language=es&file=32511

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