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Growth, Jobs and Migrations: the Real Challenges

Alberto Majocchi

1. Two documents proposed by the Italian Government[1] put the right emphasis on the main problems faced by the EU and, particularly, the euro area: the low rate of growth, the large number of unemployed and the unmanageable question of migrants. I largely agree with the content of these papers, but there is a weak point regarding the financing of the policy proposals that could risk ending in the failure of the actions suggested.

The first document, after recognizing the challenge of the current fragile recovery, suggests a comprehensive policy mix based on the three pillars outlined in the recent Annual Growth Survey[2]: re-launching investment, pursuing structural reforms and promoting fiscal responsibility. On the last two pillars there is now broad agreement, even though it appears difficult for many Member States to achieve the proposed goals. Strengthening the recovery through a substantial boost to new investment is accepted in principle, but difficult to implement.

The adoption of the Juncker Plan has been a turning point, showing that the prevailing view within the Commission is that the efforts of the ECB need to be complemented by a fiscal shock for supporting investment demand. This would take the form of an agreement of the Commission with the European Investment Bank (EIB) to establish a European Fund for Strategic Investments (EFSI), with the Union providing €16 billion to the

EIB to conduct its financing and investment operations. The financial resources required will be found by reducing other appropriations within the existing European budget. Given the political difficulties facing the Union, this seems realistic, but it shows two main flaws: firstly, there is no additional public money on the table and, secondly, there is a problem of governance since selecting investments and distributing benefits among Member States is not just a technical issue but requires a political choice that cannot be delegated to the EIB.

According to the Italian document, the potentially catalyzing role of the Plan should be exploited in full – exploiting the synergy between resources from the EU budget and from the national budgets, including resources from National Promotional Banks – for genuine European investment initiatives aimed at financing European common goods such as trans-European networks or the Energy Union. Knowledge-intensive initiatives focusing on human capital, research, innovation and high-level education are investments with the highest growth potential and should be adequately supported. A strong effort in structural reform would help boost profit and strengthen investment opportunities.

In this context the document suggests that "countries should fully use their fiscal space, where available, to expand investment. The governance framework should provide for further incentives for investments in European public goods also at national level. Further common European initiatives should be explored: projects to enhance EU growth potential could be financed by joint debt issuances". Two principles emerge from this paragraph: first, the so called investment clause that has been included in the Commission document on flexibility[3] and, second, the possibility to support growth through the emission of Eurobonds. We will come back on this later.

2. Since the outbreak of the crisis, public and private investment has been in decline. Different estimates quantify the current

gap as ranging between €190 billion for the Eurozone and €300 billion for the EU as a whole per year[4], and present initiatives are insufficient to bring current investment levels up to potential levels. In this context, a recent paper[5] has examined the state of play of the Juncker Plan and has put forward an interesting proposal to improve its results.

According to what has been published by the Commission (April 2016) a total of 222 projects have been approved: based on €11.2 billion provided under the EFSI, they will receive additional funding of €82.1 billion. The main beneficiaries are Italy, France, Germany and United Kingdom. From these data it could be noted that "the size of the mobilized resources is not enough to compensate the EZ investment gap. Hence a more systemic way to mobilize resources has to be introduced"[6]. And from this the need follows to substantially increase the amount of QE asset purchases by the ECB from the EIB in order to finance supranational investments.

The proposal in a nutshell is to substantially increase the amount of QE asset purchases by the ECB from the EIB in order to finance supranational investments. The EIB issues new bonds ("Investment Bonds") and sells them on the markets. At present, the EIB issues additional bonds to the extent of three times the guarantee of the EFSI (from €21 to €60 billion), while the remainder (up to €315 billion) is collected through private financing. The "internal multiplier" has to be increased. The ECB should be ready to buy "Investment Bonds" on the secondary market within the framework of a renewed QE through an increase of base money on the liabilities side of ECB's balance sheet. Funds made available are then passed on to the EFSI which could expand grants to Member States according to some equity criteria. In the proposal it is explicitly stated that Member States will continue to be responsible for their level of earlier debt and will bear debt service on grants received.

In order to be of significant magnitude, but remaining compatible with existing rules, the purchasing of EIB bonds which are part of the investment program should be increased within the 20% risk-sharing regime of the Juncker Plan, given the amount of monthly asset purchases, through a corresponding decrease in the share of other European institutions' securities and government and agencies bodies. In a second phase the EFSI should become a sort of Euro Treasury under the control of the European Parliament, like the one proposed by Bibow[7], the French and German Governors of their respective Central Banks[8] and the Italian Minister of Economy and Finance[9].

3. The second Italian non-paper deals with the dramatic problem of migration. The first step of this "Fair Grand Bargain" strategy should concern the identification of key partner countries to cooperate with on migratory issues and the definition of the kind of cooperation to develop with each of them. The EU could offer investment projects of high social and infrastructural impact – to be identified together with the partner country – as a crucial incentive to enhance cooperation with the EU, and EU-Africa bonds to facilitate the access of African countries to capital markets. Furthermore, the EU could offer cooperation on security, legal migration opportunities and resettlement schemes as a compensation for the burden on those countries that engage in establishing national asylum systems in line with international standards.

On the part of African countries, EU could ask for commitment on effective border control and a reduction in flows towards Europe; cooperation on returns and readmissions; management of migration and refugees flows; establishment of asylum systems; strengthening the fight against human trafficking and smuggling of migrants also through joint police and judicial cooperation. To implement this approach the new European Border Guard should develop a plan for joint EU return operations to be financed by the EU budget and for supporting return operations from third countries of transit to countries of origin.

This "Migration Compact" approach should be financed through: a) reorienting the programming of external action financial instruments; b) a new financial "Instrument for the external action in the field of migration" to be established within the EU budget; c) a new EU Fund for Investments in third countries to finance sustainable investments in the region where the outflow of migrants is the largest and to attract European investors; d) common EU Migration Bonds to be issued to fund migration management in Member States and to finance the "Migration Compact" goals.

This point is the most controversial one. It is true that the costs of migration control are large. To deal with the migrant emergency, Kirkegaard and Philippon[10] propose the emission of Security and Mobility Bonds (SMB), since nowadays the management of the immigration problem should be seen more and more as a common-interest issue for all Europeans. Along the same lines Lucrezia Reichlin[11], having remarked that no country is able to face the problem of immigration and security without violating the rules of the Stability Pact, suggests that "not only is it desirable, but also unavoidable, to move along a different path and to increase the expenditure capacity of the Union by issuing federal debt". While Reichlin's suggestion that the emission of Eurobonds should finance investment expenditures which are multi-annual by nature seems totally acceptable, it must be underlined that "a residual part of the expenditures to manage the inflow of migrants and to guarantee security against terrorism has the characteristics of current expenditure and must be funded through the levy of fiscal resources"[12].

In this framework particularly significant is the position taken by the German Finance Minister Wolfgang Schäuble, stating in an interview to the *Süddeutsche Zeitung* (16 January 2016) that "if the funds in the national budgets and the European budget are not sufficient, then let us agree for instance on collecting a tax on every litre of petrol to get the financial means to face the refugees crisis". This statement is important since it links the creation of new own resources, and the strengthening of the European budget, to an issue that risks creating deep divisions within the Union, limiting the Schengen Treaty's guarantee of free movement of people – a highly important issue in European public opinion – mainly after the recent wave of terrorist attacks.

Schäuble's proposal of a tax on petrol to finance migration control and the management of security measures could be supplemented with an additional tax on the carbon content of fossil fuels in the sectors not included in the Emission Trading System, thus providing additional resources to the European budget. Using these new own resources as a guarantee, the EU could increase the financial means of the Juncker Plan by issuing Eurobonds. At the same time, the introduction of a carbon tax will help reach ambitious objectives in reducing CO_2 emissions, in line with the conclusions of the COP21 held in Paris.

4. There are major difficulties in setting a price on carbon, but something is beginning to move. The French government said recently that it would unilaterally set a carbon price floor of about €30 a tonne for electricity producers in its 2017 finance bill in the absence of a European initiative, seeking to kickstart broader European action to cut emissions. The combination of currently low carbon emission prices and coal prices in Europe is making coal-fired plants twice as profitable as gas-fired plants even though they are more polluting.

This is an important starting point, but it seems more realistic to assume that the likely agreement among the European governments will not foresee the introduction of new taxes before the round of national elections in 2017. Notwithstanding, since the problem of migration is pending and the risk of a suspension of the Schengen Treaty is real, the Commission is preparing an external leg of the Juncker Investment Plan as proposed by Vice-President Mogherini and Commissioner

Mimica. In the Commission's draft this Plan would not need any additional financial resources.

The idea is to complement the EFSI with an Investment Plan for Developing Countries, fully in line with the agenda of financing development, addressing essential sustainable development objectives as well as delivering growth and jobs for the EU. The Juncker Plan II will be based on the same pillars as the investment plan for Europe: a) mobilising finance for investment. Together with the Commission, financial institutions and private investors managed investments for infrastructure and SMEs that resulted in leveraging €2.2 billion EU grants into €44 billion of investments under the previous financial perspective (2007-2013); b) making finance reach the real beneficiaries, providing specific technical assistance embedded in project financing to boost sustainable development projects already in the pipeline; c) improving the investment environment in third countries.

Under the current Multiannual Financial Framework, €4.8 billion in grants has been allocated in the various programs. It is expected that this can leverage at least €66 billion investments from financial institutions and private investors in EU partner countries. At the moment, 200 projects are in the pipeline already worth about €300 billion.

The Plan is now being discussed by the Juncker Cabinet and will presumably be approved by the Commission on June 7 and presented to the European Council on 28-29 June. It is a positive development of the Italian proposal of a Migration Compact and, from the point of view of finding the needed financial resources, represents a compromise between the Italian suggestion of issuing Eurobonds and the German idea of a tax on petrol: as in the case of the original Juncker Plan, limited resources will be found within the current European budget.

In para. 2 a proposal was discussed to enlarge the amount of resources that could be used for financing the Investment Plan. The EIB issues new bonds and sells them on the markets. The ECB should be ready to buy "investment bonds" on the secondary market within the framework of a renewed QE through an increase of base money on the liabilities side of ECB's balance sheet. The funds made available are then passed on to the EFSI which could expand grants to Member States according to some equity criteria. Something analogous could be envisaged for Juncker II. But keeping in mind the idea that, in the future, something must be done to increase the amount of European own resources if Europe really wants to boost investment for providing growth and jobs to its citizens and to efficiently manage the dramatic problem of migration.

5. "No taxation without representation" is a fundamental principle of democracy. If collecting enlarged own resources is envisaged, the management of the budget should be entrusted to a Finance Minister within the Commission under the control of the European Parliament. The road towards a Treasury managing a Eurozone budget - additional to the EU budget – is long and difficult. But an essential requirement should be complied with: as was asserted in the 1993 Report of an independent group of economists[13], "in the early years following the introduction of a single currency a small EC budget of about 2% of Community GDP is capable of sustaining economic and monetary union, including the discharge of the Community's growing external responsibilities".

Notes

1 Ministero dell'Economia e delle Finanze, *A Shared European Policy Strategy for Growth, Jobs and Stability*, February 2016; Italian Non-Paper, *Migration Compact, Contribution to an EU strategy for external action on migration*, April 2016

2 European Commission, *Annual Growth Survey 2016: Strengthening the recovery and fostering convergence*, Brussels, November 2015

3 European Commission, *Making the best use of the flexibility within the existing rules of the stability and growth pact*, COM/2015/012 final

4 Rubio, E., Rinaldi, D., Pellerin-Carlin, T., *Investment in Europe: making the best of the Juncker Plan. With case studies on digital infrastructure and energy efficiency*, Notre Europe Studies and Report, No. 109, March 2016

5 Fontana, O., Vannuccini, S., *Conventional Direction to Unconventional Measures: Using Quantitative Easing to Shape Eurozone Fiscal Capacity*, Centro Studi sul Federalismo, Research Paper, Turin, May 2016. In the same perspective a previous contribution is: Watt, A., *Quantitative easing with bite: a proposal for conditional overt monetary financing of public investment*, IMK WP 148, March 2015

6 Fontana, O., Vannuccini, S., *ibidem*, p. 16

7 Bibow, J., *Making the Euro Viable*: The Euro Treasury Plan, Levy Institute WP No. 84, July 2015

8 Weidmann, J., Villeroy de Galhau, F., *L'Europe à la croisée des chemins*, Banque de France, February 2016

9 Padoan, P.C., *Il faut un ministre unique des Finances de la zone euro*, Le Figaro, 30 March 2016

10 Kirkegaard, J., Philippon, T., *How To Pay for Europe's Border Control*, Bloomberg View, Nov 18, 2015

11 Reichlin, L., *Un'Europa più stabile è possibile*, Corriere della Sera, 28 November 2015

12 Majocchi, A., *Migrations, security, environment: the contribution of a Carbon Tax*, Centro Studi sul Federalismo, Comments, no. 75, Turin, February 4, 2016

13 *Stable Money - Sound Finances*, Community public finance in the perspective of EMU, "European Economy", No 53, 1993

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The **Centre for Studies on Federalism (CSF)** was established in November 2000 under the auspices of the Compagnia di San Paolo and the Universities of Turin, Pavia and Milan. It is presently a foundation.

The activities of the CSF are focused on interdisciplinary research, documentation and information on internal and supranational federalism, the developments of regional and continental integration (notably, of the European Union), the issues related to the world order and the democratization process of the international system.

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