

The European Union Is on the Brink of Historic Change

The Commission's \$825 billion rescue fund would break many taboos, possibly paving the way for EU taxes and an EU treasury.



A radical transformation. –Photographer: Vanden Wijngaert/Bloomberg

The European Union has a habit of disappointing when trying to design a joint response to an economic crisis. However, Ursula von der Leyen's speech at the European Parliament on Wednesday about a pandemic recovery fund could well be one for the history books.

The Commission president outlined a 750 billion-euro (\$825 billion) rescue program to help the bloc cope with the fallout from Covid-19. EU governments still have to agree to the plan, and some northern member states — especially the Netherlands and Austria — are likely opponents. But if the final deal looks even close to Von der Leyen's proposal, it will mark a radical transformation of Europe.

The Commission plans to borrow the hefty sum on the financial markets and then distribute it to member states between 2021 and 2024, with those who've suffered the most economically getting the bigger share. The fund is the sum of many parts. Some 560 billion euros will pay for a "Recovery and Resilience Facility" that will go directly to governments. There will also be a 31 billion-euro scheme to support solvent companies that need temporary state aid, and 9.4 billion euros to prepare for future health crises.

Italy and Spain will be the biggest beneficiaries, while Germany will receive relatively little. The EU will pay back investors via its own budget over a long period — as much as four decades.

The fund breaks a number of EU taboos. First, it raises significantly the amount the Commission can borrow on the financial markets. These are not "euro bonds" in the classic sense of the word since individual member states will still have to pay their individual contributions to the EU budget, to be calculated by the relative size of their gross domestic product. The vehicle is also expected to be a "one-off" for the pandemic. However, it will be a very useful blueprint if the eurozone ever chooses to move closer to a much-needed fiscal union.

The second big change is that two-thirds of the money would be given away as grants. This is the most controversial part of the plan, and it risks being watered down in the forthcoming negotiations between member states. There will be strings attached too since governments will have to present reform programs to receive support. The extra spending will need to comply with EU-wide priorities such as technology investments and tackling climate change. But the generous provision of grants is a step change from the European Stability Mechanism, the euro area's rescue fund, which only offers loans.

The final taboo to be possibly broken is on EU-wide taxation. The Commission has an eye on setting up new revenue streams, which could help to pay back investors, including environmental taxes and levies on multinational companies. This is the vaguest part of the plan, but potentially one of the most profound. It would create the seed of an EU Treasury, which could disburse its money where it sees fit.

Von der Leyen will have a tough time selling all of this to the so-called "frugal four," which includes Sweden and Denmark as well as Austria and the

Netherlands. They prefer loans because they fear some of this money will be misspent.

Countries in Eastern Europe have traditionally benefited from the bulk of the EU's cohesion fund, but they've have had a relatively good pandemic so they won't receive much of this new support. It will be interesting to see which way they lean. The proposal needs unanimous support, which will be hard to secure.

At least the Commission president can rely on France and Germany, the EU's biggest beasts, who struck the breakthrough deal that paved the way for Von der Leyen's proposal. Spain, Italy and other southern countries are obviously in favor since they'd get most of the money. For once, the political stars may be aligned. If so, 2020 might be remembered in Europe as more than just the year of the pandemic.

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