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POLICY BRIEF

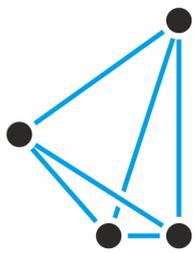
2018/January

Think Visegrad in Brussels

Preparations for the EU Multiannual Financial Framework 2021-2027 – chances and challenges for Central Europe¹

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¹ This policy brief is partly based on interviews with officials and experts in Brussels, conducted by the author in November 2017 thanks to the Fellowship Program of the Think Visegrad – V4 Think Tank Platform, financed by the International Visegrad Fund.



Introduction

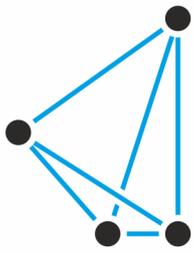
The negotiations of the 2021-2027 financial framework are about to begin in the European Union. Although the EU budget is of a relatively small size – around 1% of the combined Gross National Income of the EU member states – the Multiannual Financial Framework (MFF) sets the long-term limits of its revenues and expenditures and therefore bears a high importance to all the member states. The MFF is thus, for one to two years preceding its entry into force, the subject of heated negotiations, bargaining and trade-offs. The informal discussion has already begun with several reports and non-papers already put forward by various stakeholders, while the formal talks will start after the European Commission presents its proposal, expected for May 2018. The negotiations between the member states and among the EU institutions will last for several months with an agreement expected to be reached in 2019.

At first glance, reaching an agreement on the next MFF could seem easier than for its previous iterations. The MFF 2014-2020 was negotiated against the backdrop of a financial crisis which put significant strains on the member states, particularly those in the Eurozone. Currently, economic growth has returned to the European Union and the economic sentiments have reached their highest levels since 2000s². Nevertheless, some key political developments will affect and complicate the process of finding a consensus on the next MFF. Firstly, the negotiations on the post 2020- MFF will coincide with two major processes underpinning the future of European integration: the withdrawal of the United Kingdom from the European Union and the debate on the reform of the Eurozone. Secondly, some stakeholders see Brexit as an opportunity to substantially reform the MFF and the EU budget, which in turn widened the debate to the future of main EU policies, and could breach the fragile balance between the various interests of the member states that functioned in this sphere until now.

MFF and Central Europe

For the Central European member states, the main issue at stake is to preserve the adequate level for the EU budget and to ensure the financing of the EU policies that are essential for meeting key economic or social challenges. It applies mainly to the key pillars of the European Union and the single market that are cohesion policy and the Common Agricultural Policy (CAP). Cohesion policy has played an instrumental role in narrowing the gap between the more and less developed member states and regions. In the 12 poorest EU member states, the level of GDP per capita increased

² In November 2017, the Economic Sentiment Indicator reached the highest level in the EU since June 2007 and in the Eurozone since November 2000. Source: https://ec.europa.eu/info/sites/info/files/esi_2017_11_en.pdf.



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from 54% of the EU average in 2006 to 67% in 2015³. However, important disparities persist and further catching up with the wealthier states – especially at the regional level - will depend on continuous and adequate funding for economic, social and territorial cohesion, one of the goals stipulated by the Treaty on the European Union. All the regions of Central European member states – except for some surrounding the capital cities – fall into the category of less developed regions (below 75% of the EU average). Cohesion policy also allows the less developed countries to mitigate the negative effects of the single market, a role played by the CAP as well. It helps to create a level playing field for farmers across the EU and avoids creating a race to national subsidies in which the poorer member states would inevitably lose. Furthermore, both cohesion funds and the CAP support the member states in reaching EU-wide goals such as climate and energy policy objectives.

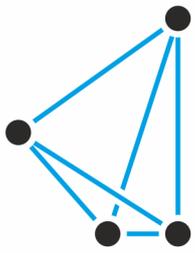
Impact of Brexit

The most immediate and visible challenge for the future of EU, including for the next EU budgets and the negotiations of the MFF, is the management of Brexit. First of all, the United Kingdom's withdrawal from the European Union means losing the third biggest contributor to its budget. Although the UK contribution has been, since the 1980s, reduced due to the agreed-upon rebate, it nevertheless amounted to approximately 12% of the EU budget. According to estimates by the Jacques Delors Institute, the gap in the EU budget after the UK's withdrawal will be around 10 billion euro per year⁴. Even if this loss might be mitigated by a possible UK contribution after March 2019, the uncertain result of the UK-EU negotiations makes it hazardous to assume any British contribution in the talks about the next MFF. The consequences for the Central European countries are manifold. First, the gap in the budget opens a debate on the general amount of the budget and may be taken by the net payers as an excuse to decrease its level. However, it may also provide a positive impulse towards getting rid of **correction mechanisms** or even increasing the budget, due to the fact that the UK was one of the biggest proponents of the budget cuts. As for the dynamics of the negotiations themselves, the withdrawal of the UK will weaken the position of net contributors, which advocate a smaller EU budget and for decreasing the amount spent on the main EU policies. Likewise, the countries that benefit the least from the Common Agricultural Policy and demand cuts in this area, will due to Brexit lose an important ally. Regarding other headings of the budget, the UK was a prominent supporter of strengthening the EU's external actions and it may therefore be more difficult to

³ European Commission's estimates, "7th Report on Economic, Social and Territorial Cohesion", p.XXII.

http://ec.europa.eu/regional_policy/sources/docoffic/official/reports/cohesion7/7cr.pdf

⁴ Jörg Haas, Eulalia Rubio, "Brexit and the EU Budget: Threat or Opportunity?" Policy Paper 183, Jacques Delors Institute, 16 January 2017, <http://www.delorsinstitut.de/2015/wp-content/uploads/2017/01/BrexitEUBudget-HaasRubio-JDI-JDIB-Jan17.pdf>.



mobilise adequate funding for neighbourhood policy in times of growing needs due to the instable situation in the countries bordering the EU, in particular Ukraine.

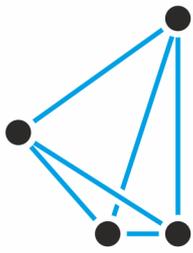
Impacts of Eurozone reform

The Economic and Monetary Union's reform will also mobilize political attention in parallel with MFF negotiations. Some proposals, put forward especially by President Macron, go as far as creating a large-scale Eurozone budget (*fiscal capacity*) or a separate parliament and minister of finance for the euro area have evoked a rather sceptical response by other Eurozone members and the European Commission. It is likely that the actual reforms will fall short of these proposals, but shall however open the door to further risk-sharing within the Eurozone. The roadmap presented by the European Commission in December 2017, goes towards anchoring existing intergovernmental mechanisms in the EU legal framework (eg. European Stabilisation Mechanism, Fiscal Pact), rather than creating instruments or institutions outside the current structures⁵. Instead of a separate budget for the Eurozone, the Commission envisages a dedicated euro-area budget line within the EU budget, including for instance a convergence instrument to assist the member states on their way to joining the euro. Nevertheless, even the incremental changes can have a significant impact on the EU budget and endanger existing policies; establishing a euro-area line in the EU budget will require a modification in the expenditure side of the budget, consequently making it a potential threat to the current amounts spent on cohesion policy and CAP. Several EU member states which have not adopted the common currency will be excluded from the planned new budgetary heading. Furthermore, the very fact that both the MFF negotiations and talks on EMU reform will take place in parallel might increase the unpredictability of both processes, for instance by opening the door for possible trade-offs between member states negotiating both issues, that could also upset the delicate balance that existed so far.

Ideas on reforming the MFF

Several ideas about reform of the MFF have been circulating throughout the years. A radical overhaul of the financial framework is rather unlikely, because the final result of the negotiations must balance the differing priorities and objectives of member states, regions and EU institutions (among others), and satisfy the obligation of being accepted unanimously by the member states. Nevertheless, several far-reaching changes may eventually be implemented. Potential directions of MFF reform have been presented by the European Commission in the reflection paper on the future of EU

⁵ "Commission sets out Roadmap for deepening Europe's Economic and Monetary Union", European Commission - Press release. Brussels, 6 December 2017. http://europa.eu/rapid/press-release_IP-17-5005_en.htm.

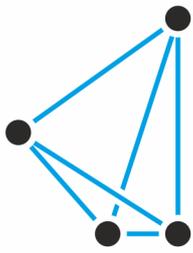


finances⁶. The Commission outlines several options and scenarios, however the prevailing assumption is that the next MFF should create a fiscal space for the “new challenges” of the EU, such as the refugee crisis, security concerns, cyberthreats, terrorism and defence. Although the Commission emphasizes the need to keep the balance between existing policies and priorities and new challenges, the need to allocate funds for the latter will create a pressure to scale down the current policies, especially cohesion policy and Common Agricultural Policy. The solutions suggested by the Commission can strongly affect the Central European states, for instance the introduction or increase of national co-financing, which would disproportionately affect poorer EU member states. Moreover, the idea of leaving more resources unallocated in order to be able to respond in a more flexible manner to future challenges may result in a more ad hoc bargaining in the yearly budgets and decrease the strategic dimension of EU investments. Another potentially problematic proposal for the beneficiaries of cohesion policy would be to increase the conditionality of the EU’s structural and investment funds, especially if it means linking the disbursement of EU budget funds with political issues, such as the implementation of the refugee relocation mechanisms or the state of rule of law, and not to the actual aims that the particular policy pursues.

Conclusion

- All the Central European EU members support the position that the EU budget should be maintained at an adequate level. They also agree on the importance of keeping an effective cohesion policy and CAP, but often differ on details due to the particularities of their economies. Therefore, achieving overall priorities will depend on the determination to maintain this common position as long as possible despite existing differences on specific items. For instance, the Czech Republic (and Slovakia to a lesser extent) is particularly opposed to introducing a ceiling of CAP payments for large farms; Hungary most firmly defends cohesion policy due to the high reliance of its economic growth on EU funds; Poland is particularly concerned with introducing national co-financing in CAP, while Romania and Bulgaria focus most distinctively on securing financing for infrastructure development. Therefore, if each country enters negotiations with the aim of achieving one particular goal, the overriding priorities can fall short from being achieved and make everyone lose.
- Central European countries should use the variety of different regional formats to discuss their standpoints and articulate common interests. The Visegrad Group (V4) has experience in coordinating the positions in the previous negotiations and proved to be an effective basis for consultations with other like-minded states from the region (eg. Bulgaria, Romania, Croatia, Slovenia). Moreover, a more recently

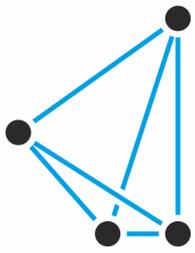
⁶ One of the six documents about the future of EU-27, presented by the European Commission in 2017: “Reflection Paper on the Future of EU Finances”, 29.06.2017, https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-eu-finances_en.pdf.



established presidential format of regional cooperation – the Three Sea Initiative (TSI) - might serve this purpose as well, particularly as its main goal is the interlinking of Central European infrastructure (energy, transport etc.), which fits the EU's objectives and relies mostly on EU funding.

- A robust EU budget and adequate financing of the existing policies are a vital issue vital for many other EU member states outside of Central Europe. Cohesion policy is of high importance for the Southern European states still affected by the economic crisis. Preservation of the Common Agricultural Policy is supported by a majority of EU member states, including some of the biggest countries, such as France even if President Macron has opened to door to a certain flexibility regarding CAP reform. The success of the negotiations will rely upon effective coalition-building and lessons should be learned from previous negotiations, such as the experience of the so-called friends of cohesion group. It is also useful to look not only for like-minded states, but also other actors, such as EU institutions and civil society or business associations, for instance the Committee of Regions in the case of cohesion policy.
- It is equally important to demonstrate the benefits of cohesion policy for the entire EU-27, including the so-called net contributor states, since EU budget funds allocated to the less developed states have spillover benefits to the wealthier countries, through investments and trade. To put it simply, money spent on cohesion by wealthier countries to a large extent eventually comes back to them⁷. This is especially true for countries such as Germany and Austria, which maintain significant economic links with the biggest beneficiaries of the EU funds in Central Europe. Moreover, the more developed economies in the EU should be aware of the competitive advantage their companies have in a single market over the companies from less developed member states. Cohesion policy contributes to moderate the negative effects of the single market for the less developed economies. Likewise, the CAP helps to diminish the disparities between the farmers from regions of different levels of economic development.
- Central European countries should also emphasize that an ambitious budget is in the interest of the whole European Union and that they are ready for a bigger commitment. One of the possible solutions is to advocate increasing their contribution to the EU budget. This postulate coincides with European Commission's position and has been already endorsed by Hungary and Poland. Another option is to start the debate by agreeing first on the goals that needs to be achieved by the EU during the next budgetary period and then assure the adequate funding.

⁷ "How do EU-15 Member States Benefit from the Cohesion Policy in the V4?" Report prepared within the Ex post evaluation and forecast of benefits to EU-15 countries as a result of Cohesion Policy implementation in V4 countries, commissioned by Polish Ministry of Economic Development. Warsaw 2017, https://www.ewaluacja.gov.pl/media/32979/EU-15_report_final_EN.pdf.



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- Cohesion policy is not only a prime investment policy and a mean to diminish the economic, social and territorial disparities in the EU, but also a policy with high European added value. The ready examples are listed in the EU documents, such as the extension of the metro in Sofia or Szeged's electric public transport which was not only beneficial in terms of economy, but also contributed to reducing toxic emission, by extension bringing it closer to completing the EU's environmental goals⁸. Moreover, support for more transparency and control over the use of EU funds may help the beneficiary countries ensure net contributors that EU projects are free of corruption and abuse.
- Finally, a strong EU budget will cement the EU in times of uncertainty about the block's future due to Brexit and the growth of Eurosceptic sentiment across the continent. It is therefore important for Central European leaders to emphasize that it contributes to the unity of the block. Furthermore, the key EU policies – such as cohesion and CAP – are visible to people on a daily basis and show direct benefits of the EU membership to citizens, thus increasing support for the European integration.

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⁸ 7th Report on Economic, Social and Territorial Cohesion, pp. 198-199.

http://ec.europa.eu/regional_policy/sources/docoffic/official/reports/cohesion7/7cr.pdf