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What budget for the EU? Principles, spending priorities and the impact of Brexit

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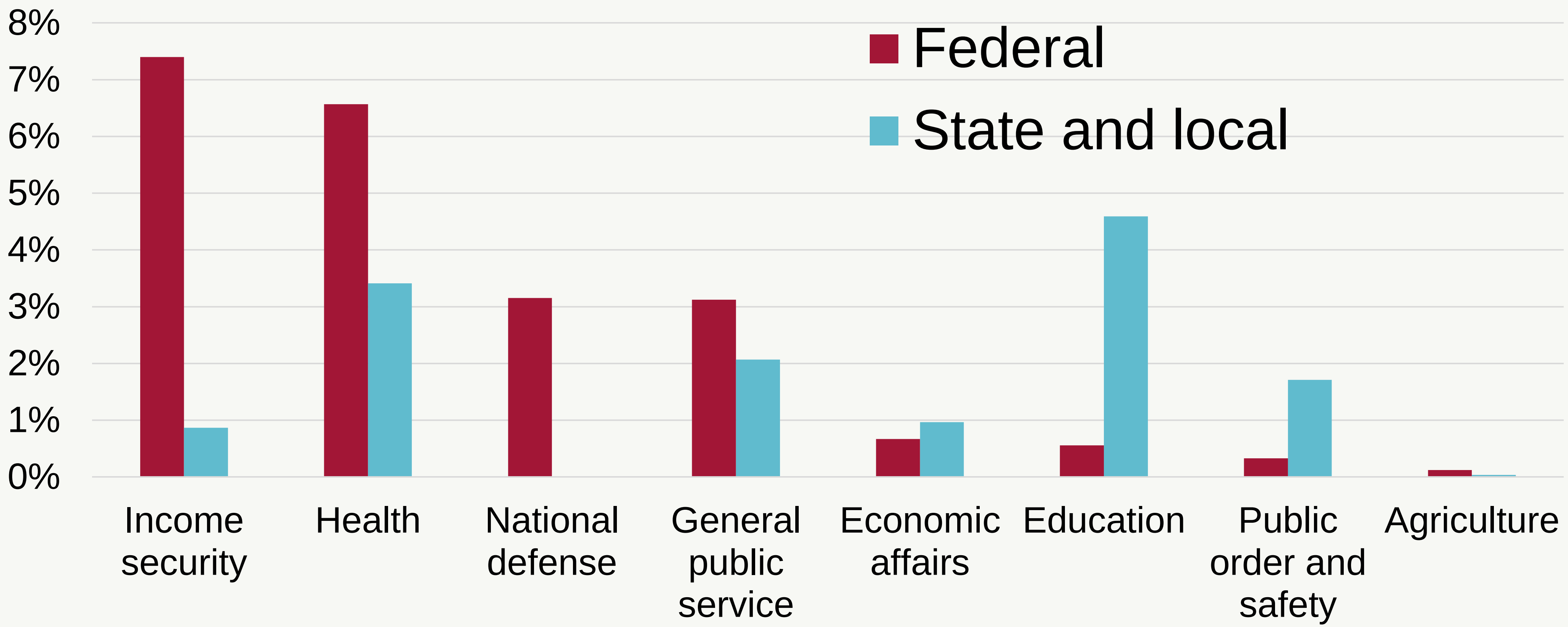
Outline

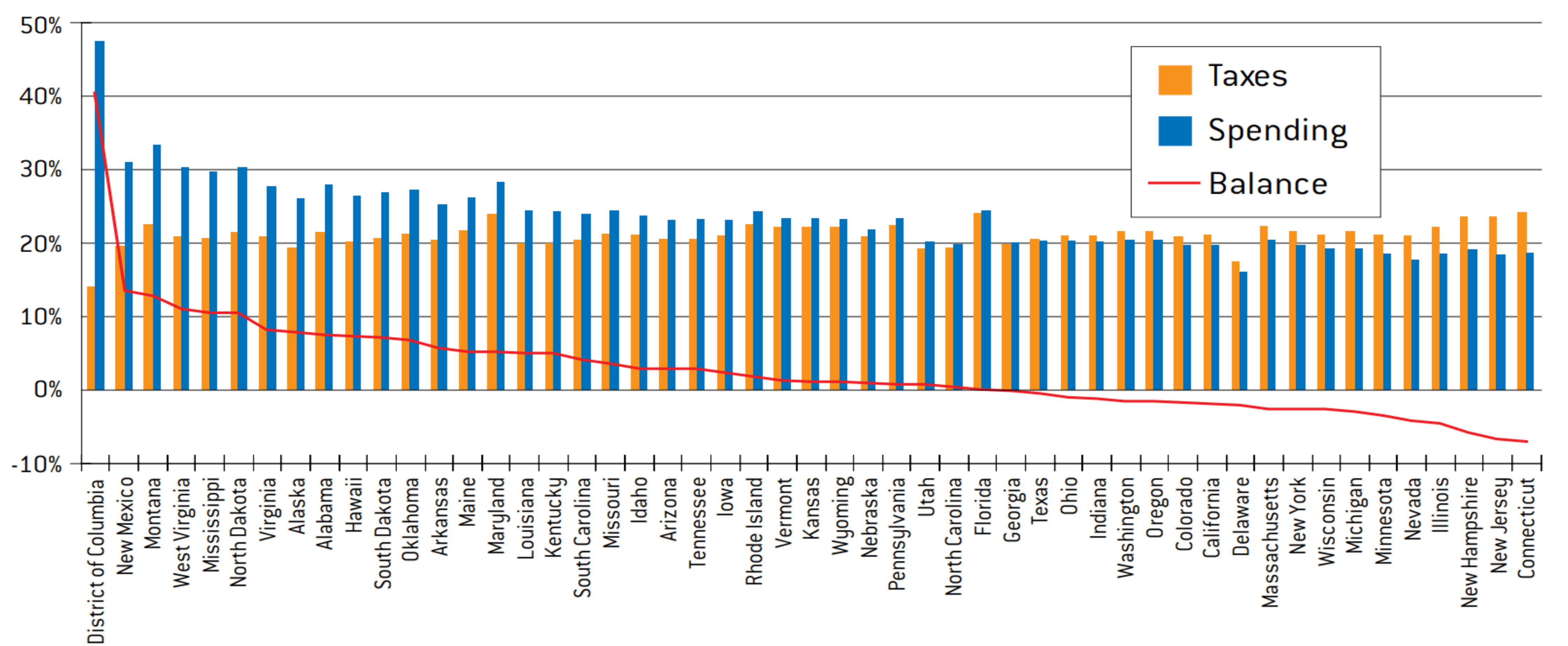
1. Lessons from the United States
2. The current EU budget:
   - Structure
   - Effectiveness of agricultural and cohesion policies
3. The new MFF
   - Fundamental rethink of EU spending
   - Impact of Brexit

US Budget Structure, 2016, % GDP



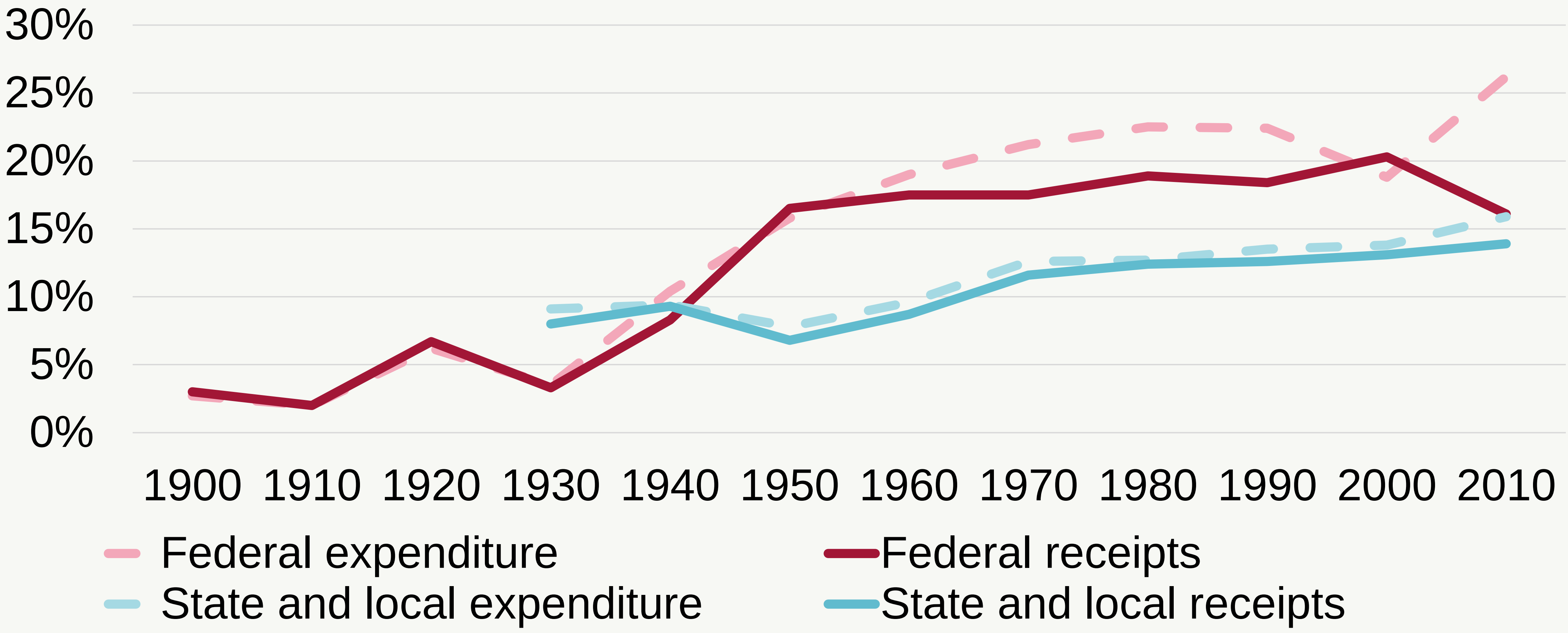
Source: Bureau of Economic Analysis

US federal budget: taxes from, spending in, and balance with states, 1999, % state GDP



Source: Figure 2 of Darvas (2010), which is based on data from http://www.hks.harvard.edu/taubmancenter/publications/fisc/ (fiscal data) and OECD regional database (GDP).

US federal and state/local government expenditure, % of GDP

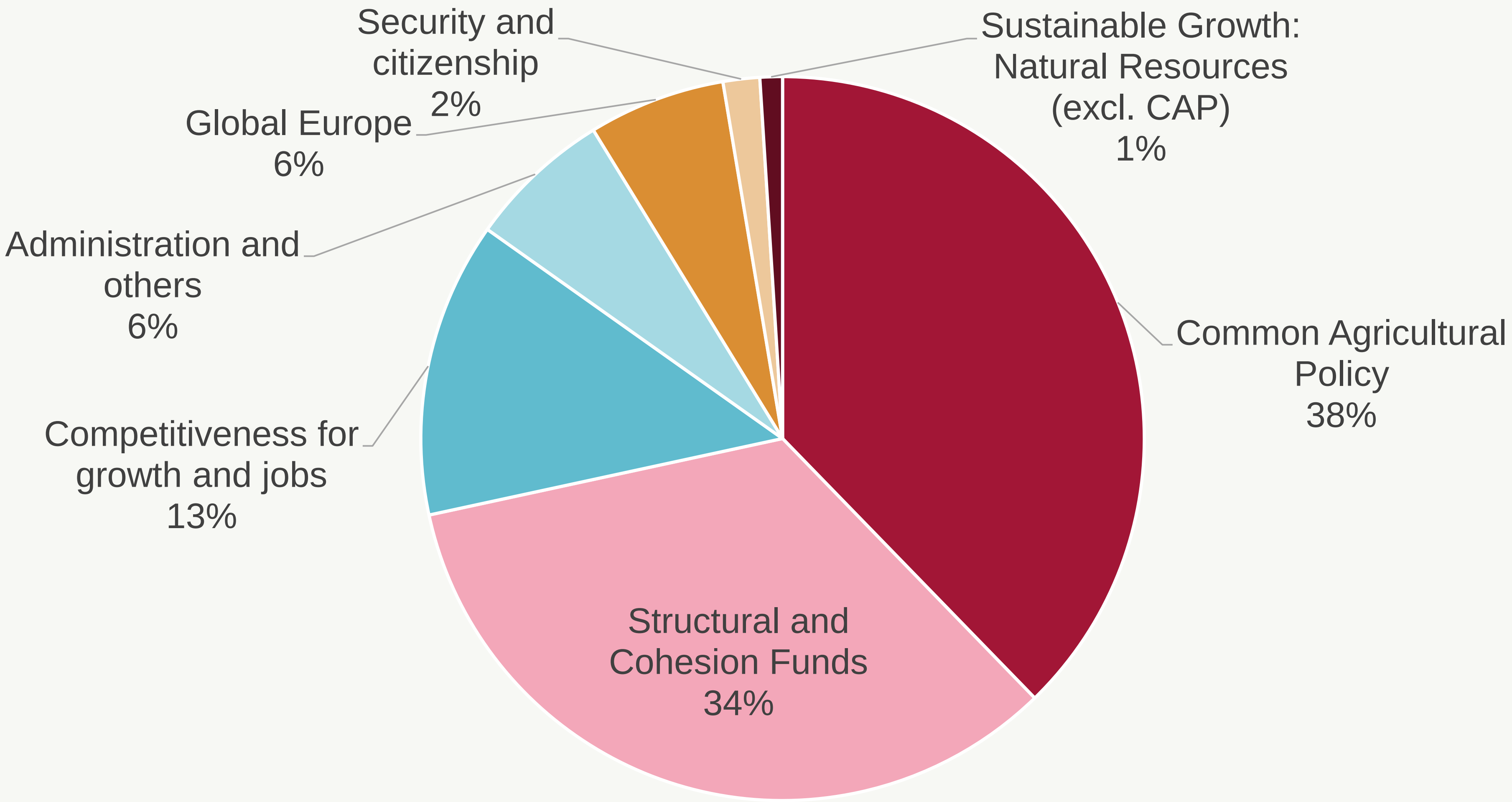


Note: Some expenditures and receipts, notably federal grants-in-aid, are counted in both the federal and S&L series. The NIPA accounts net them out in the series for the total government sector. Source: Schuyler (2014)

Lessons from US

- Federal spending did not develop at the expense of state spending but rather grew in 20^{th} centry as government took on new functions
- EU is union of well developed nation states, it is not a state nor federation. Essential government functions are difficult to move.
- Instead, EU budget plays supporting role to national functions. Even when talking of new priorities, the key is the interplay with national policies. What is the value added of the EU budget?
- Fiscal stabilisation function is national. Re-insurance models can be considered for EA as part of EU budget.

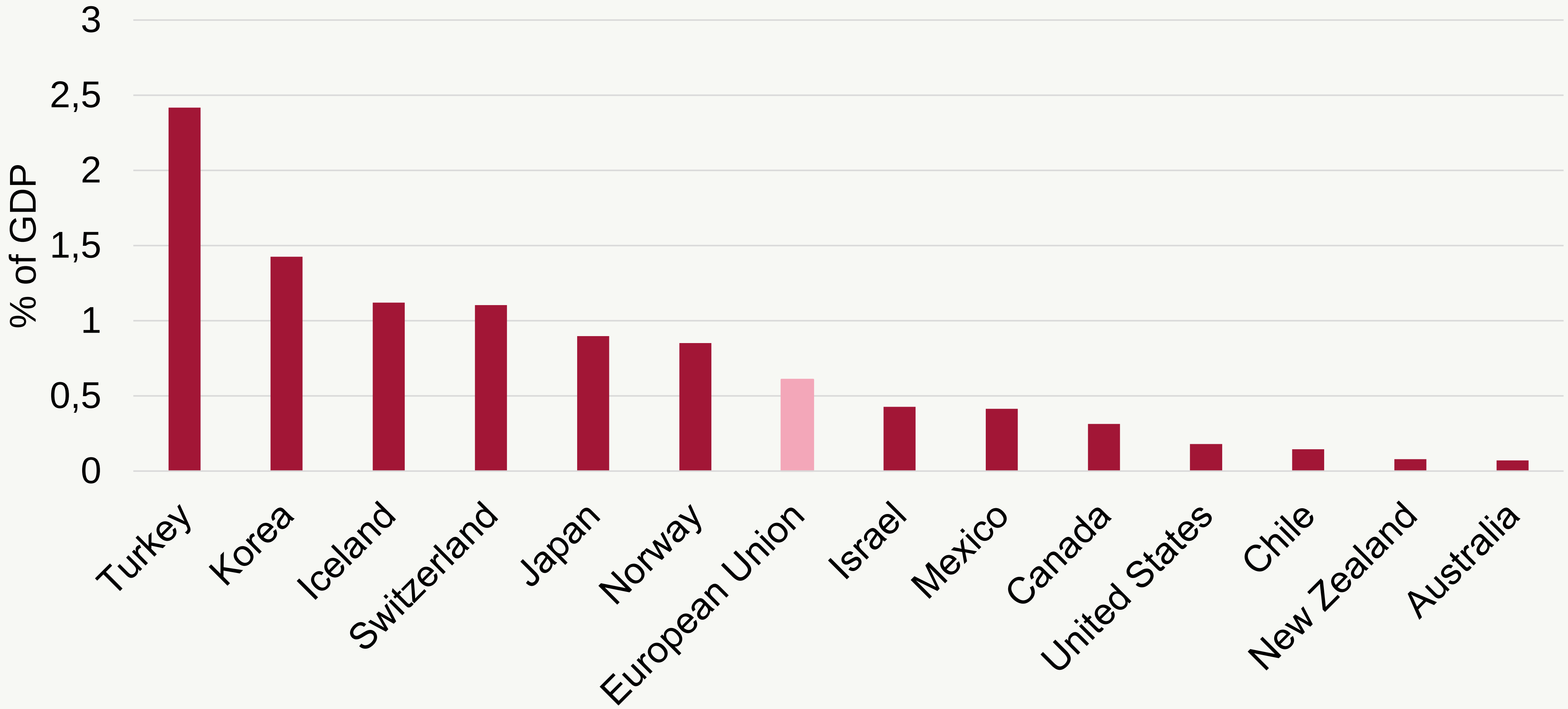
The current EU budget
The distribution of the 2014-2020 MFF ceilings



Source: European Commission, Bruegel.

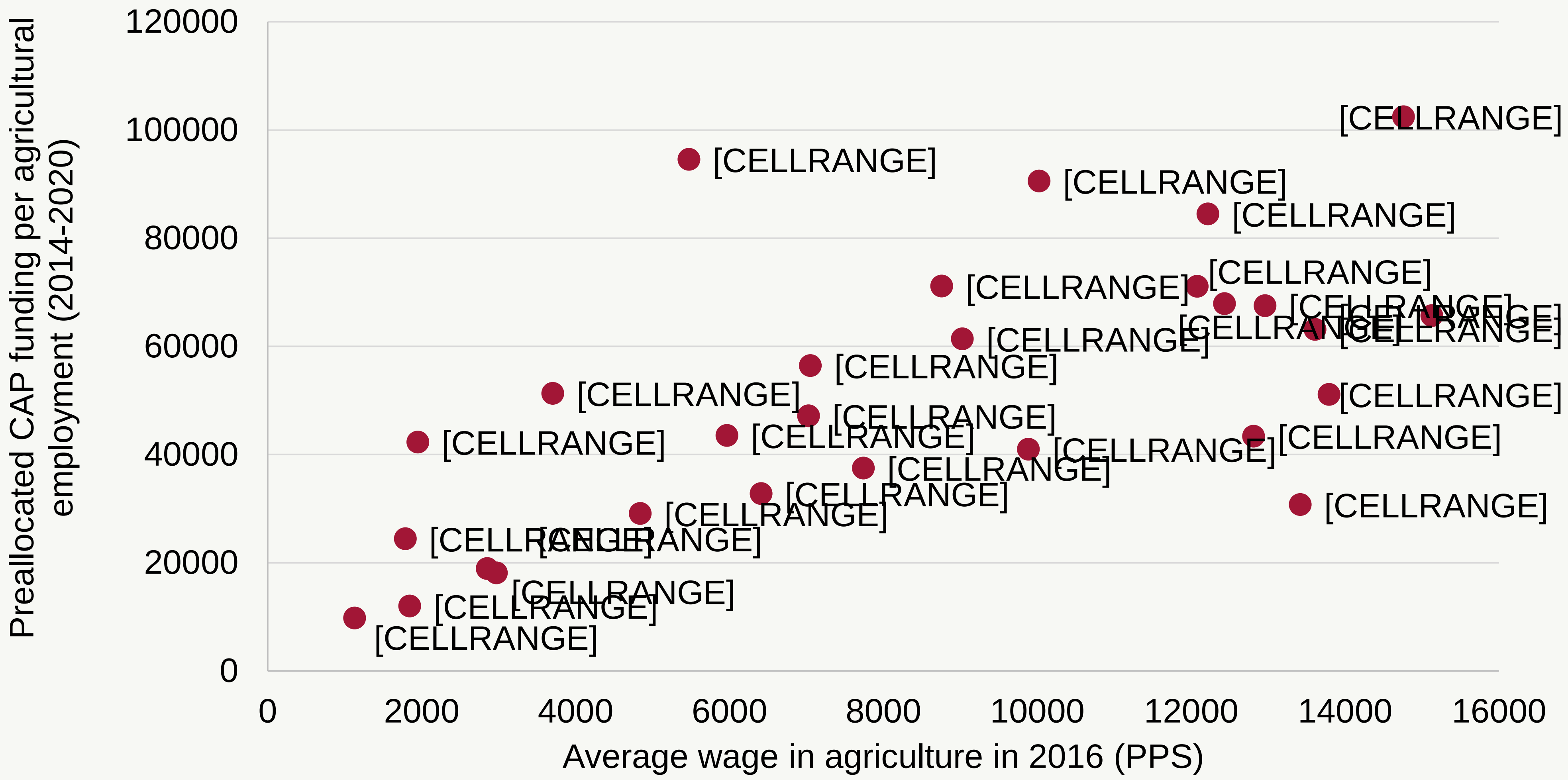
The Common Agriculture Policy (CAP)

Net support to agricultural producers OECD economies, 2016, % of GDP



Source: OECD Agricultural Policies database.

Relation between CAP funding and wages in agriculture



Source: Bruegel calculation using Eurostat data

CAP should change

- CAP is basically an income support scheme for farmers. But even there unequal: 80% of spending goes to happy 20% of farmers.
- Overall EU spending is thus highly concentrated in a very small group of people.
- There is no reason why that should be done through CAP. If social problem, use national social programmes and ESF
- CAP has not achieved its goals in terms of “greening”, biodiversity, see European Court of Auditor’s report.
- Scope for national co-finance on income support?
- Fundamental rethink is necessary

EU budget discussions

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- Empirical assessments of cohesion policy is mixed, some efficiency gains and re-orientations are in order.
- Right to strengthen public goods such as border control, immigration policy, defence cooperation, climate policy and research
- Especially on border and immigration, the larger numbers presented by EC look politically desirable. E.g. 20-25bn for Frontex etc.
- Possible euro-area stabilisation policy: key is national counter-cyclical policy, better coordination and perhaps a fiscal capacity. Reforming the EU budget is an important step to achieve some form of fiscal capacity.
- But anything put into “rainy day fund” or flexible euro area budget line limits available funds for regular programmes. Flexibility comes with a cost!

Modelling MFF post Brexit

- If no UK contribution to next MFF and no EU spending in the UK, while spending in EU27 and revenues form EU27 grow with GNI: financing gap of €93 billion in 2021-2027
- If CAP and cohesion spending is fixed nominally at current 2014-2020 MFF level, while everything else increase with GNI: €102 billion surplus available for spending on other priorities
- Yet UK might contribute to the next MFF due to:
  1. ”EU exit fee” (around €20 billion in net terms in 2021-2027)
  2. Contribution for some form of access to EU markets, like Norway?

Modelling the next MFF after Brexit with frozen CAP and cohesion spending

(A)The current 2014-2020 MFF (28 Member States)

	Payment ceilings*	Revenues	
CAP	387	Total own resources	978
Cohesion	348	Other revenues	48
Other spending	291		
Total	**1,026**	**Total**	**1,026**
		Balance	**0**
Total % GNI	1.0	Total % GNI	1.0

*Note: * payment ceiling is available only for the total. We approximated sub-heading payment ceilings using the ratio between sub-heading and total commitment ceilings.*

Modelling the next MFF after Brexit with frozen CAP and cohesion spending

(B) The 2014-2020 MFF for 27 Member States excluding the UK from both revenues and spending

	Payment ceilings*	Revenues	
CAP	362	Total own resources	856
Cohesion	336	Other revenues	43
Other spending	275		
Total	**973**	**Total**	**900**
		Balance	**-73**
Total % GNI	1.1	Total % GNI	1.0

*Note: * payment ceiling is available only for the total. We approximated sub-heading payment ceilings using the ratio between sub-heading and total commitment ceilings.*

Modelling the next MFF after Brexit with frozen CAP and cohesion spending

(C) 2021-2027 MFF for 27 countries, no contribution by the UK and no spending in the UK)

Payment ceilings		Revenues	
CAP	362	Total own resources	1,097
Cohesion	336	Other revenues	55
Other spending	352		
Total	**1,050**	**Total**	**1,152**
		Balance	**102**
Total % GNI	0.9	Total % GNI	1.0

Our estimate for the UK’s net contribution to the EU budget after 2020 from the financial settlement of EU membership (€ billions)

	2021-27	Post-2027
Net UK contribution (if non-rebate adjusted share)	28	8
Net UK contribution (if rebate adjusted share)	17	6

Source: Authors’ calculations using the methodology of Darvas, Efstathiou and Gonçalves Raposo (2017).

Possible UK contribution to the 2021-2027 EU budget for some form of access to EU markets

	Historical contributions		Total UK net contribution in 2021-2027 if its GNI share as in the first data column (€ billion)
	% GNP	€ per capita	
Iceland	-0.05%	-25	-11
Switzerland	0.02%	12	3
Liechtenstein	0.03%	40	7
Norway	0.16%	115	31
Italy	0.26%	71	51
United Kingdom	0.33%	111	64
France	0.34%	110	67
Netherlands	0.38%	149	74
Germany	0.42%	149	82

Note: historical data is the average of 2010-2016 for EU countries and average of 2014-15 for the four non-EU countries.

Conclusions

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- Two variables to adjust: spending and revenues
- Sensible to reduce *share* of CAP & cohesion in total spending and increase spending on “new” priorities significantly, especially migration, research, climate and defence
- Worthwhile to consider increase in revenue from 1% GNI to higher but this will be a huge political fight.
- Could the EU finally take a step to agree on an EU tax on CO2 emmissions? Treaty does allow it. Would be sensible climate policy and interesting source of revenue…