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**Speech by the President of the European Council
Herman Van Rompuy
at the KU Leuven**

“Building a more social Europe one step at a time”

It is always a pleasure to be back here in Leuven, my Alma Mater, and especially today to discuss Europe's social dimension with you. I gather you had a full afternoon of fruitful exchanges, and judging by the participants, these discussions must have been the occasion to collect thoughts and insights from scholars and practitioners who have been working for years, if not an entire lifetime, on these issues. I've carefully listened to Loukas Tsoukalis whom I know and respect very much.

This discussion is all the more relevant since the Belgian Commissioner, Marianne Thyssen, will be responsible for social affairs and employment. My ties to this subject are also long-standing and deeply rooted in my personal political commitment — to finding a workable compromise between the 'market economy principle' and fairness; to achieve a social market economy that respects and promotes human dignity. This has been the work of my entire political career and it is precisely this approach that I see at the heart of the European project.

Cohesion and social justice are always a quest, a work in progress that is social, economic and political, but even more so at a time when many things can no longer be taken for granted. National politics, prosperity, the multicultural society, geopolitical stability, the European idea: all have come under pressure the last fifteen years – even before the financial crisis. And at such times, what we need most is courage, resolve, and a sense of social fairness to confront the challenges-at-hand truly as a society.

The financial and economic crisis since 2008 has taken a deeper toll than we would like to acknowledge. In too many parts of our continent, unemployment is becoming deep-seated; vulnerabilities that were simmering before the crisis have resurfaced with a vengeance; inequalities are on the rise, affecting the very fabric of society. In turn, this situation has also undermined the trust of people also in the European idea, and in the promises it holds. This deep and partly new disenchantment, with Europe, with politics at all levels, is a reason for great concern – and it looms over any possible discussion on social matters, such as the one we are having today.

There are many differences – important differences – between countries and the performances of social policies differ greatly (*interestingly, not always proportionally to the resources spent on welfare states*). National policies matter. Some countries had similar levels of unemployment in 2008, whereas today the difference is double! But there are many aspects that concern all our countries and the Union as a whole.

Before coming to Europe's social dimension in a strict sense, I should like to sketch the broader economic context – that of the immediate economic policy debate this fall.

There is a growing consensus on where we are currently standing. The recovery on which we were placing much hope is anaemic. This is the result of both a major cyclical shock (to which we need to respond) and of a structural one (which requires a different but equally determined response).

The difficulty comes precisely from the fact these two dimensions are linked; that when you are facing a cyclical shock, if you don't manage to overcome its effects, it can permanently hurt your structural prospects for growth, it can leave permanent scars on the employment situation, scars in the work lives of people.

To rekindle growth and above all employment we need to be – and are – working on both: the cyclical and the structural, demand and supply. And we are right now in a better position to do more on both, simultaneously, than at any point previously these past years.

At the height of the financial crisis, the worst-hit countries had no choice: with default looming, and the risk of being cut out from the financial markets, difficult decisions on budgets had to be taken right there and then. “Frontloading” the adjustment as economists call it. It was a matter of economic and financial survival – indispensable to stay afloat financially in the immediate term, and essential to restore healthier economic fundamentals and resilience for the future. But in the short term, the pain and the sacrifices were real; and those measures did take a cost on growth. But of course we pay of huge price for the *'malgoverno'* before 2008, when growth in too many countries was based on high private and public debt – a situation against which rather few people raised their voices at the time.

The situation is more stabilised now, for all the eurozone; this gives each country somewhat more breathing space. We overcame the existential threat to the eurozone; we won that battle also against the Cassandras and the speculators. The structural efforts to put our economies on the right footing with sound budgets and sustainable debt are still vitally important. It is still a matter of individual and collective credibility, of economic sustainability. We cannot throw away the efforts and sacrifices that we made.

It is more widely accepted that for the eurozone in particular, where national economies are so tightly knit, we need to look at fiscal policy in a much more comprehensive, coordinated way, also looking at a growth-friendly aggregate fiscal stance, meaning: for the eurozone as a whole.

The second avenue to explore, beyond a more effective coordination of national budgetary policies, is tackling together the so-called “investment gap”. A significant investment programme could have a big impact on overall demand in Europe. Mobilising the Union's coordination capacity and the resources we share in common would help maximise impact of such investments in areas that are so important to our potential growth, such as digital infrastructures, energy transition and interconnections... The incoming Commission President has committed to put forward proposals on this over the next few months, amounting to 3 pct. of GDP over three years from public and private sources. It is critically important.

But if these policies are necessary to manage the here and now, they need to be accompanied by policies that deal with our structural challenges – and these are not small. Indeed, yes, fiscal policy can support demand but it works best when companies are competitive and innovate. This is the role of structural policies. Because if companies aren't competitive enough, the risk is that more public spending simply leads to higher public debt and higher trade deficits, because the extra money will largely be spent abroad...! So measures on the "demand" side have to go hand in hand with measures on the "supply" side. For the latter, think for instance of the internal market or all the work to create a climate of job creation and entrepreneurship. I've pushed within the European Council for an Energy Union, for closer defence industry cooperation, and for the digital market. These are some of the areas where "more Europe" is also needed.

Although the focus of the economic policy debate is mostly on the pace of budgetary adjustment, the quality of the budget planning, both in terms of how the money is spent and how the money is raised, also plays a central role.

What really matters is the longer-term reforms plan. Making sure that those at the bottom of the wage and pension scales and the most vulnerable people – poor families, the elderly, or disabled people – are protected, and the same for vital sectors like education and health. Fiscal policy is making choices, it is true for national budgets and we also had to make choices for Europe's multi-annual budget for 2014-2020 [the MFF], preserving spending on R&D, on competitiveness, on education.

This brings me, beyond the immediate economic policy debate, to what we can jointly do in Europe to improve social justice and cohesion. Here all the work to boost employment should get the first mention.

Of course, social policies can and should not be reduced to employment and activation policies alone, but the latter offer a firm and indispensable basis. Our best social policy is boosting employment. This is truer than ever.

In today's world, the deepest social divide is perhaps that between the insiders and outsiders on the labour market. That is a defining factor for inequality and poverty – and one of the reasons why overall unemployment was hit more heavily during this economic crisis than in previous ones. Indeed, over the years, the labour markets in some countries have become much more compartmentalised – with a growing divide between long-term protected contracts and flexible insecure jobs (often for younger, poorer or migrant workers). The wider this divide between the so-called 'ins' and so-called 'outs', the more vulnerable the latter become. In this crisis, flexible labour was hit the hardest, with a dramatic impact on the younger generations in particular. Social partners, too, must reflect on their responsibilities in this respect. Therefore, a true social agenda involves not just protecting the rights of insiders but also creating opportunities for outsiders.

To encourage new recruitment, two specific types of action matter most: eliminating this duality in the labour markets, and reducing the tax burden on labour. Because it is the unemployed (the "outs") who today pay the price of excessively high labour costs (for the "the ins"). That is why shifting taxes away from labour is potentially the single most important boost for jobs right now. Hence the European Council's and the Commission's repeated insistence on it. On average, the so-called "tax wedge on labour", is 11 percentage points higher among eurozone countries than among non-euro EU countries, and much higher than in the United States and Japan. Belgium is unfortunately the European champion in this area. If you want to explain why expanding companies do not hire more or faster, no need to search any further!

Unfortunately, when it comes to employment, there are no magic wands. Many of the key policies – on the labour market, tax incentives, pensions, education, labour costs, etc. – remain a national responsibility. But the EU institutions can advise, steer, support and coordinate. Of course they do not and cannot take over.

The member states must do most of the work individually but can do some of it jointly as a Union. But I am glad we were nonetheless able to pull off a few big initiatives these last years, in particular the specific employment policies for young Europeans, like the €8 bn Youth Guarantee Scheme, aiming to ensure quality offers of employment, continued education, apprenticeship or a traineeship to all young people, within three months after leaving school. In individual countries there is more need for specific employment policies, certainly in times of weak recovery; even wage subsidies can be envisaged.

Which brings me to the fight against inequality – one of the defining themes nowadays. It is an issue close to my heart and I am glad it is finally again in the headlines. The rise in inequality, and the feeling that the gains before the crisis and the pain after the crisis have been unfairly distributed, are at the core of people's disenchantment with politics – both national and European politics.

Ultimately, rising inequality could threaten not only social cohesion and the stability of democratic institutions, but also put a break on growth and prosperity. The key element here is to look at education and jobs. Inequality feeds on inadequate skills and long-term unemployment; these reduce opportunities and undermine social mobility.

That is why it is at the root that we must tackle inequality. Tax policy and social transfers have a role to play in correcting inequality *ex-post*, but they are not enough. Indeed, we can see with a country like France how you can have very high taxes and social transfers, yet still have high inequality for decades now.

Tackling inequality at the root means better education. That does not necessarily mean more spending; it means better spending. For example, Finland spends on education roughly the same share of its GDP as Belgium, but with much better education outcomes (as measured by the so-called Pisa tests). Of course you can never simply copy a model, but there is clearly scope to draw from best practices.

Another front in the fight for social fairness is combating tax evasion and tax fraud – a matter on which the European Council has acted decisively the two last years and where it will continue to act, especially on the automatic exchange of information on income data. The strongest shoulders should carry the heaviest burden.

Over the last few years, many of our debates about Europe's economic governance have revolved around the idea of ensuring a greater coordination and commitment of economic reforms, particularly in labour markets. This debate is picking up again.

Some meaningful progress has been made, for instance with the so-called "Macroeconomic Imbalances Procedure". But the idea of "contractual arrangements" to be concluded between the Commission and member states on structural reforms – an idea which I proposed in the December 2012 report *Towards a Genuine Economic and Monetary Union* – has not materialised yet. This road is long and tortuous and an endeavour that will keep my successor busy as much as it has kept me busy.

Using the new elements in the existing governance framework more systematically would most probably already allow us to go much deeper and further. The European Commission will launch an important review of our governance in the winter.

Let me now turn to social policies in a stricter sense, which is the focus of interest for most of you in this audience today but, which I thought useful to place back in the broader context of economic policies.

As you know, on social policies, European institutions have a difficult role to play. There are many loud calls for a more “social Europe”, but at the same time many consider that social policies are exclusively a national competences. By the way, sometimes the same people insist on both aspects!

This discussion reminds me somewhat of the early discussions about the monetary union. The founding compromise of the Delors Committee allowed our countries to move towards monetary unification without deep integration of fiscal and economic policies. Over the last few years, we have adjusted that initial compromise, finding a new balance. And by doing so, we have also extended coordination to areas that were historically out of bound or limited to the most basic form of cooperation (“the open method of coordination”). Similarly, on social issues, I think we have made some progress over the last fifteen years.

First, with the creation of the EU2020 strategy, which we may not fulfil to our satisfaction but which still serves as an anchor in analysing our respective policy efforts and initiatives. We will have a review of our targets in 2015 and this will be the occasion for a new impetus in that area.

But already these recent years, the discussion on the social dimension of the European Monetary Union has been building up – with Member States having to confront seriously the profound interdependence of their social policies. It is now an exercise that is more firmly in the European Semester, feeding into the country-specific recommendations and informing policy debates, best practice exchanges, and peer reviews. It might not be visible and flashy, but this is the concrete and daily work that makes us day after day grow from our diversity and from our experiences.

Welfare is and remains the responsibility of national governments. But we have seen with the crisis how there can be no simple answer, no black and white division of labour, when our interdependence plays such a strong and fundamental role. What happens to one country matters for others, it can matter for the whole.

With the crisis, this has forced the Union and its institutions to take on new roles – in control, in enforcement. It has not made us popular. Europe has always been a convenient scapegoat. But there is more to this feeling of disenchantment with Europe than just scapegoating. It is about what we want the Union to do, what we want the Union to be.

For over sixty years, the focus for Europe has been mainly on opening up, bringing down borders, encouraging new movement, new opportunities. Even today – on fields as diverse as energy, telecom or the digital economy – it is still about bringing down borders, creating this big common space. But we’ve never really thought of Europe as a home, a shelter, and today we pay a price for it.

For decades it worked well. The open borders brought huge opportunities, for working, trading, studying abroad. And the impact of all the opening was mostly cushioned – by economic growth, and by the welfare states, set up in parallel.

It was a division of labour: Europe opened, and national governments protected, including as regards social protection. Nobody expected otherwise. But with the crisis, with globalisation, things have changed. And suddenly, whereas for decades Europe had been all about opening, liberating, unlocking, emancipating, empowering... today it has come to be seen as meddling, judging, prescribing, dictating, correcting, even punishing... Europe, the great 'opener' of opportunities is now perceived by many as an unwelcome 'intruder'. We need to get the balance right.

The Union must keep doing what it is good at and continue to unlock opportunities, but it must also be perceived and experienced as a source of protection. Not just benefiting businesses, but also employees; not only the "movers", but also the "stayers"; not only those with diplomas and language skills, but all citizens; and people not only as consumers, who like cheap products and a wide choice, but also as workers, who can see in others, competitors for their jobs.

How to get this balance right? When it comes to protection, people expect two things from the European Union. First, for problems that individual countries are clearly not big enough to fight on their own, that the Union steps in. On global and cross-border issues, people really want Europe to defend their interests and keep threats at bay. Second, where national authorities are best-placed to provide care, people expect that the Union does not get in the way. Indeed, there are cases, where precisely because of its scale, the Union must tread softly. Not disrupt, but respect familiar places of protection and belonging – from national welfare choices, to regional traditions and identities, all the way down to local cheese...

From this perspective, the citizen's message to the Union is clear. As the European Council summed it up in its Strategic Agenda for the next five years: "The Union must be stronger outside and be more caring inside". Doing more to unlock talent and life chances for all, to promote cohesion, while helping ensure all our societies have safety nets fit for future, to promote fairness and accompany change. My successor as European Council President Donald Tusk, just as the incoming Commission President Jean-Claude Juncker, have committed to this agenda.

For me, this task – for a Union that is both more caring and more respectful – is one of the main challenges ahead to regain people's confidence in our Union.

To me it is crystal clear: the ultimate goal of our endeavours always is a social one. Sometimes it requires taking the long-term view over the short-term (when we speak about sustainable pensions for instance); sometimes it requires helping outsiders against vested interests; and many times you know as a politician that you will not be popular...

But always it is about defending a vision of a just society, a vision which is at the heart of what we in Europe have achieved together and what we should continue to strive for.
