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European Economic and Social Committee

ECO/473

European Investment Stabilisation Function

OPINION

European Economic and Social Committee

**Proposal for a Regulation of the European Parliament and of the Council on the establishment of a
European Investment Stabilisation Function**

[COM(2018) 387 final – 2018/0212 (COD)]

Rapporteur: **Philip VON BROCKDORFF**

Co-rapporteur: **Michael SMYTH**

Referrals	European Parliament, 11/06/2018 Council, 25/06/2018
Legal basis	Articles 175(3) and 304 of the Treaty on the Functioning of the European Union
Section responsible	Economic and Monetary Union and Economic and Social Cohesion
Adopted in section	03/10/2018
Adopted at plenary	17/10/2018
Plenary session No	538
Outcome of vote (for/against/abstentions)	196/2/4

1. Conclusions and recommendations

- 1.1 The EESC notes that at the current level of political and societal integration, a large federal budget in the euro area is unrealistic. This notwithstanding, the proposed EISF aims to make national fiscal policies more stabilising with respect to asymmetric shocks. The EESC considers this as a step towards closer euro area integration, and possibly an attempt to encourage non-euro Member States to join the single currency.
- 1.2 The EESC understands that the EISF differs from the **European Stability Mechanism (ESM)**, which evolved as a backstop fund during the financial crisis. However, a clear distinction needs to be made between the two funds. The EISF is much more limited in scope and the EESC has concerns about the size of the fund in the event that asymmetric shocks affect two or more Member States.
- 1.3 The loans provided through the EISF would provide some boost to public investment at times of asymmetric shocks. The EESC cautions that the impact is unlikely to be immediate. Economic recovery will take time and any positive effects are likely to be felt in the medium and long term.
- 1.4 The EESC notes that having unemployment as the sole criterion to activate support may lead to some deficiencies with regard to the timeliness of the stabilisation function. The EESC therefore suggests other complementary indicators which normally precede unemployment in terms of predicting an impending large shock, in a way that an initial level of support can be triggered before the "large" shock is fully transmitted to the unemployment indicator.
- 1.5 Given that the EISF is not considered as "additional" to the other financial instruments, namely the Balance of Payments Facility and the European Financial Stabilisation Mechanism (EFSM), the EESC is of the view that utilising the EISF would reduce the overall borrowing capacity. It is therefore incumbent on the European Commission to balance on an on-going basis outstanding re-payments on the part of concerned Member States and contingent liabilities.
- 1.6 The EESC is not against oversight by the Commission of public investment financed loans provided through the EISF. However, the Member State concerned should be allowed sufficient leeway in determining the type of investment required. The EESC therefore advocates that a balance be struck between the Commission's oversight on one side and, on the other hand, the concerned Member State's discretion on public spending.
- 1.7 The EESC urges the Commission to investigate how an insurance mechanism to cater for macroeconomic stabilisation could operate across the EU. The EESC is of the view that a well-crafted union-wide insurance scheme that acts as an automatic stabiliser amidst macroeconomic shocks would be more effective than the proposed EISF. Should another financial and economic

crisis hit the EU in the meantime, the EESC advocates a coordinated approach to deploy all relevant financial instruments including the EISF.

2. Background

- 2.1 For the forthcoming Multiannual Financial Framework, the European Commission is proposing a European Investment Stabilisation Function (EISF), the overall aim of which is to strengthen the Economic and Monetary Union by anchoring the euro area into the Union's long-term budget. The EISF would take the form of back-to-back loans of up to EUR 30 billion guaranteed by the EU budget, together with an interest rate subsidy to cover the cost of the loan.
- 2.2 The subsidy would be funded from contributions from Member States equivalent to a percentage of the monetary income allocated to their national central banks by the ECB (commonly known as "seigniorage") and collected through a Stabilisation Support Fund (SSF). An intergovernmental agreement would be concluded to determine the calculation of the Member States' financial contributions and the rules regarding their transfer.
- 2.3 The amount of loan that an eligible Member State would be allowed to borrow would be determined by a formula based on a number of criteria, including:
- i) the maximum level of eligible public investment that the EISF may support;
 - ii) the increase in unemployment; and
 - iii) a threshold level defined as the quarterly national unemployment rate increased above one percentage point in comparison to the unemployment rate observed in the same quarter in the previous year.

The Commission, however, may increase the amount of the EISF loan up to the maximum level of eligible public investment that the EISF may support, in the event of particular severity of the large asymmetric shock experienced by the Member States concerned.

- 2.4 The proposed regulation is essentially based on the key principles of solidarity at EU level and responsibility on the part of individual Member States. Reference to the EISF was made by the President of the European Commission in the State of the Union Address 2017¹, the Five

¹ [Letter of Intent to President Antonio Tajani and to Prime Minister Jüri Ratas](#), Jean-Claude Juncker, State of the Union, 13 September 2017.

Presidents' Report of June 2015², the Reflection Paper on the Deepening of EMU of May 2017³, and the Commission's position on the further deepening of the Economic and Monetary Union as outlined in December 2017⁴.

- 2.5 In conjunction with the EISF, the Commission is also proposing a Reform Support Programme (RSP) aimed at providing support, where necessary, for economic reforms in all Member States. The RSP would consist of three components: a reform-driven mechanism, technical support and a convergence facility to assist non-euro area Member States to join the euro. The EESC is delivering a separate opinion on this.
- 2.6 The EISF has two primary objectives:
- i) to help stabilise public investment at times of asymmetric shocks caused by a change in economic conditions that may affect Member States differently. As the financial crisis has shown, maintaining stability in public investment at a time of crisis is a huge challenge for countries that share a common currency, such as the euro area; and
 - ii) to support economic recovery at times of economic shocks in the euro area and for Member States participating in the European Exchange Rate Mechanism (ERM II) and which can no longer use their monetary policy as a lever for adjustment to shocks.
- 2.7 It should be remembered that the current euro area economic policy framework remains incomplete. While monetary policy is centralised, national fiscal policies remain decentralised and this dichotomy can put a heavy burden on a Member State impacted by an asymmetric shock, as the aftermath of the financial crisis has shown.
- 2.8 The EISF is intended, therefore, to complement national automatic stabilisers when such national automatic stabilisers – designed to offset fluctuations in a Member State's economic activity and automatically triggered without explicit government action – may be deemed ineffective. In theory, the EISF could have the effect of cushioning the economy from mainly domestic economic shocks and thereby helping it to recover. The EISF could also help reduce the risk of spill-over to other Member States.
- 2.9 When faced with a crisis, Member States can lose access to financial markets. In that case, the available toolbox for the Member State affected includes the European Stability Mechanism (ESM) or the Balance of Payments (BOP) programme. Currently, however, there is no mechanism to support a Member State if it experiences an asymmetric shock without

² [The Five Presidents' Report: Completing Europe's Economic and Monetary Union](#), 22 June 2015.

³ [COM\(2017\) 291 final](#).

⁴ [COM\(2017\) 821 final](#).

necessarily losing access to capital markets. The EISF, therefore, aims to fill this gap by providing loans to the Member State concerned.

- 2.10 To enhance the effectiveness of the proposed mechanism, the European Commission is proposing measuring asymmetric shocks using a "double unemployment trigger". This comes into effect when the national unemployment rates go beyond what could be considered as "normal" and are deemed to be a relevant indicator of the impact of a large asymmetric shock in a specific Member State.
- 2.11 In providing loans to Member States affected by economic shocks, the mechanism presupposes that macroeconomic and fiscal policies have been applied in line with the Stability and Growth Pact (SGP), which is a set of rules designed to ensure that countries in the European Union pursue sound public finances and coordinate their fiscal policies, as well as the Macroeconomic Imbalances Procedure. The latter aims to identify, prevent and address the emergence of potentially harmful macroeconomic imbalances that could adversely affect economic stability in a particular Member State, the euro area, or the EU as a whole.
- 2.12 Over time the EISF can be complemented (via the SSF) by additional financing resources, outside the EU budget, possibly from these sources: the ESM (the future European Monetary Fund) and a voluntary insurance scheme to be set up by Member States.

3. **General comments**

- 3.1 The EESC notes that at the current level of political and societal integration, a large federal budget in the euro area is unrealistic. The EESC has consistently supported the Commission in its efforts to advance and complete Economic and Monetary Union (EMU)⁵. At the same time, the Committee has often underlined its concerns about the ongoing lack of political commitment from Member States that is key to the completion of EMU⁶. The proposals for EISF seem to reflect this and thus represent something of an interim solution. The dichotomy between a centralised monetary policy and national fiscal policies is therefore set to remain. The positive side of the proposal is that the EISF aims to make national fiscal policies more stabilising with respect to asymmetric shocks, while achieving long-term sustainability. In this regard, the proposal is seen by the EESC as a step towards a somewhat closer euro area integration, and possibly an attempt to encourage non-euro Member States to join the single currency.
- 3.2 The proposed mechanism presupposes adherence to the Stability and Growth Pact, implying sound budgeting and macroeconomic policy. This is seen by the EESC as an attempt to bring together fiscal and monetary convergence by ensuring that Member States adhere to the

⁵ See for example EESC opinion on Euro area economic policy, [OJ C 173, 31.5.2017, p. 33](#) and EESC opinion on Deepening EMU by 2025, [OJ C 81, 2.3.2018 p. 124](#).

⁶ See for example EESC opinion on Economic and Monetary Union Package, [OJ C 262, 25.7.2018, p. 28](#).

eligibility criteria implying sound budgeting and macroeconomic policy. This also implies that the EISF would be available only to Member States compliant with the Stability and Growth Pact, and therefore to Member States that have already undergone structural reforms and budgetary adjustments. This condition could serve as a motivation for Member States to fully adhere to the Stability and Growth Pact and allay fears about underwriting spending by Member States that are in the process of undergoing structural reforms and budgetary adjustments.

- 3.3 Accordingly, the EISF will result in no "permanent transfers" between euro area Member States, with governments only being eligible for support if they have met core EU budget rules for the preceding two years. The EESC notes, however, that the EISF is intended **only** for Member States with sound budgetary and macroeconomic policies, and any loan would be provided in exceptional circumstances and when asymmetric shocks manifest themselves in the form of above-normal unemployment rates. Nonetheless, whilst recognising the importance of market and fiscal discipline, the EESC agrees with the objective of a stabilisation function and acknowledges that this is a first step towards a more developed stabilisation function.
- 3.4 The EESC understands that the Commission could not provide a definitive list of asymmetric shocks which could include *inter alia* a liquidity crisis. The EESC is of the view that the appropriate response to a liquidity crisis is the Outright Monetary Transactions (OMT) programme of the European Central Bank, conditional on the participation of the Member State in the ESM programme, and not the EISF. The EESC acknowledges that an exhaustive list of asymmetric shocks would not be appropriate and is comforted by the Commission's macroeconomic simulations based on past data as to the effectiveness of a stabilisation function as a crisis prevention mechanism.
- 3.5 The EESC understands that the EISF differs from the **European Stability Mechanism (ESM)** which evolved as a backstop fund during the financial crisis. The ESM is more strictly associated with a bailout programme, which comes with more onerous conditionality and has a EUR 500 billion lending capacity and can be tapped by Member States that have lost the ability to borrow on capital markets.
- 3.6 A clear distinction, therefore, needs to be made between the two funds. The EISF is much more limited in scope, and though it is intended for any size of Member State, the EESC is of the view that the proposed EUR 30 billion fund would be more typically suitable for smaller euro area and non-euro area Member States. The EESC therefore raises concerns about the size of the fund in the event that asymmetric shocks affect two or more Member States. The proposed EISF cannot therefore be considered as the definitive solution for Member States facing one-off problems such as an ecological disaster, an energy crisis or a localised banking crisis.

4. Specific comments

- 4.1 The EESC acknowledges that in applying the formula to determine the loan amount for the eligible Member State (euro area members and aspiring members in the European exchange rate) the loans would provide some boost to public investment (assuming these are quality investments) at times of asymmetric shocks, but the impact is unlikely to be immediate. Economic recovery will take time and any positive effects are likely to be felt in the medium and long term. The proposal, therefore, needs to be more realistic about the intended aims and possible outcomes of the EISF.
- 4.2 The EESC notes that having unemployment as the sole criterion to activate support may lead to some deficiencies with regard to the timeliness of the stabilisation function. It is worth also considering other complementary indicators which normally precede unemployment in terms predicting an impending large shock, in a way that an initial level of support can be triggered before the "large" shock is fully transmitted to the unemployment indicator. Once unemployment has risen significantly, the economic damage may have already been done to the productive capacity of the economy. For instance, an economy experiencing a sharp drop in exports of goods and services may not necessarily experience a concurrent increase in unemployment.
- 4.3 It would therefore be valuable to have an instrument that can be activated before the symptoms are fully translated to the labour market. In other words, it is necessary to complement the unemployment criterion with a set of early warning indicators that can include the change in exports of goods and services, the change in the level of inventories and other leading indicators that clearly indicate the presence of an economic shock. In this way the proposed stabilisation function would be much more timely and effective.
- 4.4 Furthermore, the 15 year average unemployment rate which has to be exceeded for a Member State to qualify for support may work against countries that have been successful in reducing structural unemployment. A shorter time frame of perhaps five years would be more suitable.
- 4.5 The EESC notes that the EISF, as proposed, would be allowed to borrow money on capital markets and lend to Member States with interest being subsidised to cover the costs of the loans. As stated earlier, the subsidy would be financed based on what is known as "seigniorage" and collected through national contributions to an SSF. The EESC is of the view that Member States need to demonstrate their political and financial commitment *a priori*.
- 4.6 Given that the EISF is not considered as "additional" to the existing instruments, the total amount of loans available for the BOP facility, the European Financial Stabilisation Mechanism (EFSM) and the EISF itself could be constrained by a "single" limit. In theory at least, a new facility such as this would effectively reduce the EFSM's capacity to lend by EUR 30 billion as proposed for the EISF. It is incumbent on the Commission, therefore, to balance on an on-going

basis outstanding re-payments on the part of concerned Member States and contingent liabilities.

- 4.7 The EESC considers the EISF and EFSM to be somewhat similar in scope. Both funds are intended to provide financial support to Member States. However, while the EISF and EFSM have separate eligibility conditions, it is the EESC's understanding that the conditions of the EFSM would still apply, thereby restricting somewhat the effectiveness of the EISF.
- 4.8 The EESC refers to the interest subsidy that the concerned Member State would benefit from. In the event of a crisis, all things being equal, the effect of this interest rate subsidy could be to potentially increase the cost of interest payment due to the risks posed by a Member State facing a crisis. This in turn would impact negatively on the public finances of the concerned Member State. The effectiveness of quality public investment and thereby the effectiveness of the EISF itself is therefore critical to reduce any market risks affecting the Member State concerned and its cost of borrowing in the medium and long term.
- 4.9 The EESC refers to the oversight of public investment that the Member State concerned would be subject to on the part of the Commission, as required by the proposal. The EESC is not against this in principle but is of the view that the Member State concerned should be allowed sufficient leeway in determining the type of investment required and therefore advocates that a balance be struck between the Commission's oversight on one side and, on the other hand, the concerned Member State's discretion on public spending. The EESC also takes the view that public investment should also be regarded as an instrument of solidarity.
- 4.10 Finally, the EESC notes that the Commission's proposal allows for a future upgrade to the scheme – that is, a possible insurance mechanism to cater for macroeconomic stabilisation. This, in the view of the EESC, is a recognition of the limitations of the EISF itself and that the proposals in their current format will eventually need to be complemented by a full-scale stabilisation function such as a union-wide insurance scheme that acts as an automatic stabiliser amidst macroeconomic shocks. Should another financial and economic crisis hit the EU in the meantime, the EESC advocates a coordinated approach to deploy all relevant financial instruments including the EISF.

Brussels, 17 October 2018

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The president of the European Economic and Social Committee