Submission to the European Commission on the Economic Governance Review

December 30 2021

Note: This is a PDF version of our responses to the Commission’s survey.

Question 1: How can the framework be improved to ensure sustainable public finances in all Member States and to help eliminate existing macroeconomic imbalances and avoid new ones arising?

Given the severe environmental and social challenges we are facing, we believe the core task of the fiscal framework should be to help render the EU’s financial system far more equitable and less dependent on debt than at present.

Two factors need to be taken into account:

1. Public finance must adapt to a future economy that will have a radically different relationship to resource use, and to energy use in particular

2. The fiscal framework needs to address overall societal needs in the most equitable and balanced manner possible, both within the EU and in relation to other economies[2]

Concerning point 1 above, public finances can never become truly ‘sustainable’ in the financial sense of the word unless they play a highly active - and judicious - role in achieving sustainability in the broader, environmental sense. The risks posed to finance - both public and private - by environmental threats are real and urgently need to be addressed[3]. This will have strong implications for public spending, and more generally for the ways in which the money supply is created, distributed and managed.

Energy’s role in the economy is often downplayed or even ignored in financial analyses. Nonetheless, the energy supply is central to all economic activity[4]. Renewable energy, while useful and indeed vital, does not provide anywhere near the same ‘energy return on investment’ as fossil fuel energy did during its most productive period in the mid-twentieth century[5], and also poses specific challenges stemming from its intermittency and the related extensive need for energy storage[6,7]. It is therefore very likely that the future EU economy will have access to a considerably smaller and more intermittent energy supply. Other resources, from rare metals to topsoil to clean water, will also need to be conserved far more carefully. Regulations to promote the circular economy will help the transition, but as long as the overall economy is under pressure to expand, any progress in the efficiency of resource use in one sector risks being undermined by increased resource use elsewhere (the ‘Jevons effect’).

Policymakers need to be able to make lucid decisions based on a level-headed assessment of risks, including risks arising from an over-dependency on GDP growth in EU public finance - whether at present or in future projections.

Given the empirical evidence referred to above, we believe it would be extremely risky to base the EU’s fiscal framework design on the assumption that aggregate sustainable (or ‘green’) growth will be feasible in the EU in the future[8]. A far more clear-eyed and sensible stance would be a ‘growth-agnostic’ one, as advocated by ecological economist Kate Raworth, among others.
So the framework will need to help to ensure that public finance can be sustainable whether or not GDP expansion is taking place.

This brings us on to the second point from above: the meeting of societal needs.

Much criticism has been levelled at the framework over the past decade for requiring painful spending cutbacks in member states which are already suffering from the effects of a chaotic economic slowdown. In the near future, faced with an economy that is continually hitting against ecological limits that will very likely impact aggregate GDP growth, there is a clear danger that policymakers may once again attempt to stabilise the public sector’s finances by recommending cuts in essential public services that are deeply harmful to societal wellbeing. Such cuts may perhaps achieve greater debt sustainability and a more balanced budget on paper, at least in the short term, but at an unfathomable human cost which, apart from raising obvious moral concerns, would also be likely to trigger dangerous social instability[9].

We will therefore need to consider other approaches to debt stabilisation - approaches that do not require either an increase in GDP or reductions in public spending.

There are many useful lessons to draw from in this area by exploring and reflecting, both on the general history of debt as a widespread human phenomenon, and also on the specific experiences of other jurisdictions that are faced with the challenge of meeting the fiscal needs of a highly diverse set of member states. Two key insights are:

- Both debtors and creditors need protection. Or, to put this another way: power inequalities, which of course include financial inequalities, need to be considerably reduced both within and outside the EU if we are to achieve a stable and sustainable future economy. Among other things, this implies that there is a need for a permanent central fiscal capacity in the EU with the ability to take on and manage common spending. This is particularly important in the Eurozone, but will also be useful elsewhere in the EU.

- Increased economic production (or indeed increased ‘economic activity’, however defined) should no longer be assumed to be an end in itself.

References


2. These two factors map onto the outer and inner edges, respectively, of economist Kate Raworth’s Economic Doughnut which consists of two concentric rings: a social foundation, to ensure that no one is left falling short on life’s essentials, and an ecological ceiling, to ensure that humanity does not collectively overshoot the planetary boundaries that protect Earth’s life-supporting systems. Between these two sets of boundaries lies a doughnut-shaped space that is both ecologically safe and socially just; a space in which humanity can thrive: https://doughnuteconomics.org/about-doughnut-economics

3. Among many other important institutions, the European Central Bank now views climate-related and environmental risks as key risk drivers: https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202111guideonclimate-relatedandenvironnementalrisks-4b23454055.en.pdf


6. ‘The real lesson of the Energiewende is that the German economy uses too much energy to be sustainable and needs to degrow’, Brian Davey, January 2018: https://www.feasta.org/2018/01/28/the-real-lesson-of-the-energiewende-is-that-the-german-economy-uses-too-much-energy-to-be-sustainable-and-needs-to-degrow/


Question 2: How to ensure responsible and sustainable fiscal policies that safeguard long-term sustainability, while allowing for short-term stabilisation?

The environmental crisis is an emergency. Many commentators, including European Council President Michel, have compared climate disruption to a war situation[1,2]. The first priority in any war is obviously to win the war if at all possible.

So - as has happened with the COVID crisis - considerable flexibility needs to be granted to governments to rapidly invest in measures to green the economy, even if this entails the generation of more public debt in the short term.

Given the likely impact of the much-needed climate mitigation measures - and probably also of resource depletion - on the overall economy (discussed above), it seems entirely appropriate for EU’s governance bodies to extend or re-activate the SGP’s General Escape Clause for at least 2-3 years in order to provide member states with sufficient short-term liquidity to initiate the types of highly front-loaded green investments which are necessary for the transition. These include renewable energy infrastructure, low-carbon transport infrastructure and the retrofitting of buildings.

However, the General Escape Clause should not be made permanent, as this could exacerbate harmful inflation and arguably could also weaken the economy by damaging investor confidence[3]. We believe that a reformed framework should be introduced that would encourage creditors to spend rather than lend their surpluses, that would explicitly aim to reduce overall income and wealth inequality, and that would work towards a system of balanced, fair trade, both within the EU and between the EU and the rest of the world.

Moreover, in order to ensure that any future investment actually has the needed effects on the environment - i.e., in order to achieve truly sustainable finance - it is absolutely vital that a reform in the EU-wide fiscal stability measures be accompanied by equally strong reforms in environmental regulations, in monetary policy, in taxation within member states, in trade regulations, and in the Fit for 55 package. While none of these types of reform are within the direct remit of fiscal framework policywork, we will describe them briefly in the discussion on the European Semester below (question 9).
References


3. Some analysts believe that investor confidence plays a less important role in the economy than is often assumed, arguing that governments with sovereign power over the creation of their currencies can simply spend money into the economy as needed (see for example The Deficit Myth by Stephanie Kelton). In this author’s opinion, this spending-money-into-existence power of governments does exist but varies enormously from jurisdiction to jurisdiction, and is influenced (among other things) by the extent to which the economy in question is dependent on accessing foreign currency in order to secure a sufficiently stable energy supply. (Japan is the exception that proves the rule, as it has a high-added-value, export-based economy.) The geopolitics governing the ability to access energy are likely to shift in interesting ways during the energy transition, and these changing dynamics will be vital to monitor and factor into economic planning.

Question 3: What is the appropriate role for the EU surveillance framework in incentivising Member States to undertake key reforms and investments needed to help tackle today and tomorrow’s economic, social, and environmental challenges while preserving safeguards against risks to debt sustainability?

The framework can help to achieve ‘dynamic balance’ in the economy - to borrow another phrase from Kate Raworth - if it recognises that financial surpluses are better spent into the productive economy than lent out, invested in the ‘FIRE’ (finance, insurance and real estate) economy, or hoarded.

In the shorter term, given the environmental emergency, it may be worth considering the introduction of incentives or penalties to encourage creditor nations to spend, rather than lend, any surplus they may have. For example, they could face a financial penalty if they retain a surplus that is considered to be a drain on the economy. This may not be necessary, however, if the taxation and commons-based revenue distribution described under question 9 below, which will also have a strongly redistributive effect, is carried out.

In the longer run, it seems advisable to establish a clear symmetry between the penalties and incentives faced by debtors and creditors, along the lines of Keynes’ bancor proposal[1] or of existing demurrage currencies[2]. (The bancor proposal was intended for countries with their own sovereign currencies, so it could not be applied within the Eurozone, but a bancor-inspired EU Clearing system could be applied between the Eurozone and other EU members.)

References


Question 4: How can one simplify the EU framework and improve the transparency of its implementation?

As many have pointed out[1], taking a ‘one-size-fits-all’ approach to public finance sustainability that is based on fixed percentages with a strong focus on debt and deficit, and applying it to a group of widely varying economies, is extremely unwise. In this sense, the framework is actually oversimplistic at present, failing to reflect the complexity of economic reality.
The current choice of indicators of ‘microeconomic imbalances’ is based on many questionable economic premises and appears to lack a broader vision of the type of economy that we are trying to achieve. Indeed, the ‘Macroeconomic Balance Procedure Scoreboard’ is laden with assumptions that combine a kind of (presumably unconscious) mercantilism with a blinkered productivism, along with disturbing overtones of ‘punching down’.

For example, within the MIP criteria, if there is a rather modest rise in the percentage of a member state’s population that chooses not to seek out employment - which might be, for example, because they are looking after a disabled relative or small children - this is considered inherently problematic because their time would not be spent in ‘economically active’ ways. Meanwhile, if nominal unit labour costs rise beyond a certain percentage, that is also considered to be troublesome because it ‘could potentially be a threat to an economy’s cost competitiveness’[2] - an attitude which risks encouraging a race to the bottom in labour rights and standards.

The ‘export market shares’ MIP indicator sends up a ‘red flag’ if a EU member state loses 6% of its world export market share over a period of 5 years. But why should such a change in export market share be considered problematic in itself, in a world of wildly varying levels of per-capita prosperity, and in which the EU currently has a proportionately high share (in per-capita terms) of global exports?

The existing framework appears to take a zero-sum-game approach to trade-related activity that should in fact be mutually beneficial. Surely, instead of focussing on retaining already-high export levels, we need to imagine and plan towards achieving a world economy in which everyone, both within and outside the EU, has converged to a more-or-less equal footing, and trade between nations or trading blocs is as balanced and fair as possible.

As already implied above, we believe the framework would be far clearer and more effective if it focussed on two core objectives: the need to adapt public finance to a future economy that will have a radically different relationship to resource use; and the need to address overall societal requirements in the most equitable and balanced manner possible, both within the EU and in relation to other economies.

References


Question 5: How can surveillance focus on the Member States with more pressing policy challenges and ensure quality dialogue and engagement?

By seeking to identify the fundamental needs (e.g. financial stability, economic stimulation) that can sometimes be ‘hidden’ behind irreconcilable demands (e.g. short-term debt repayment versus an increase in the supply of credit), and engaging in discussion with a focus on finding creative ways to resolve such needs.

Question 6: In what respects can the design, governance and operation of the RRF provide useful insights in terms of economic governance through improved ownership, mutual trust, enforcement and interplay

We have not answered this question.
**Question 7: Is there scope to strengthen national fiscal frameworks and improve their interaction with the EU fiscal framework**

As others have argued, a harmonisation of taxation policies between the member states, and in particular the targeting of practices that encourage tax avoidance and evasion, should be prioritised[1].

**Reference**


**Question 8: How can the framework ensure effective enforcement? What should be the role of pecuniary sanctions, reputational costs and positive incentives?**

Please refer to our responses to questions 3 and 9.

**Question 9: Within the context of the European Semester, how can the SGP and the MIP interact and work better together, so as to improve economic policy coordination among Member States?**

We are answering this question in very broad terms, as it has the widest scope.

As discussed above, there is an urgent need to acknowledge that ‘Stability and Growth’ in the current conditions is very likely to prove impossible to achieve[1], and is therefore not a coherent policy goal[2].

The integration of the SDGs into the European Semester seems to be a clear attempt to acknowledge the need for a broader vision of the EU economy. Unfortunately, however, the current incarnation of SDG8 risks undermining the other SDGs for the same reason that the term “Stability and Growth Pact” is likely to prove to be an oxymoron [3].

We therefore urge that the European Semester, and the wider EU governance framework, take a more holistic approach. Specifically, we believe the EU should implement a set of measures that would create ‘guard rails’ to prevent the EU economy (a) from encouraging environmentally destructive behaviour, and (b) exposing vulnerable people to economic danger. These ‘guard rails’ would correspond to the outer and inner edges of ecological economist Kate Raworth’s ‘economic doughnut’, with the doughnut itself being the safe space where humanity can thrive.

Some measures will apply on EU level; some on member state level; and some require either EU- or state-level legislative backing. Additionally, the role played by the EU in the broader global economy is crucial to take into account when considering how to reconstruct the EU’s economic policy, and so we include suggestions on how this could be improved.

Finally, we wish to reiterate that the EU needs to have access to its own permanent fiscal space. Some of the measures mentioned below could help to fund this space, while others focus more on the uses that could be made of it.

The measures are as follows:

- Introduce regulations to ensure the EU-wide capping and gradual phasing out of the production and import of materials that pose an extreme danger to the environment. These should not only include frequently-discussed harmful products such as pesticides that compromise pollination, but other, widely-used, yet highly problematic resources such as fossil fuels[4].
• Emphasise commons-based revenue generation, including the introduction of an EU-wide Financial Transactions Tax, and a Site/Land Value Tax within member states. By ‘commons-based revenue’ we mean revenue that is generated from fees or taxes on the use of collectively-managed common pool resources[5]. These types of revenue generation, which are hard to evade, discourage overconsumption and emphasise collective responsibility, should be privileged over taxation on labour or the improvement of property, both of which can have the unintentional side-effect of penalising economic ‘good’ behaviour.

• To ensure that the effects of the revenue generation described above are progressive rather than regressive, it is very important that such revenue be distributed in as clear and fair a way as possible. For this reason - among others - we recommend that a Universal Basic Income and Social Wage (Universal Basic Services) be provided for all EU residents, and funded, at least in part, with commons-generated revenue[6]. It is noteworthy that 71% of Europeans support a UBI[7].

• In order to simultaneously promote decarbonisation and climate justice, we propose that the EU form a ‘carbon club’ with a group of Global South countries of a roughly equal (total) population to the EU, implementing a joint phase-out of all fossil fuel production and imports and sharing the revenue from production and import permits with residents of the partner countries ('CapGlobalCarbon'). This would reflect their rights and responsibilities with regard to the global atmospheric commons. Other non-EU countries would be subject to a CBAM until they meet the conditions required to join the ‘carbon club’[8]

• Housing and property value inflation need special attention in the EU, as the housing supply has reached crisis point in many member states[9]. A compelling argument can be made that housing should be a constitutional right. Many analysts believe that the current overheated housing situation has been exacerbated by the ECB’s quantitative easing measures that were introduced in response to financial crises[10]. We strongly recommend that the Commission and ECB consider the reforms that are being proposed by Positive Money Europe in this regard[11].

• Legislative changes are needed both to the EU’s core legal documents so as to prioritise well-being and sustainability rather than economic growth and price stability, and to international trade agreements, to ensure that (1) any environmental and social protections introduced by the EU are automatically mirrored by equally strong protections in partner countries, and that (2) access to justice is not effectively limited to those individuals or companies who have the means to engage costly legal support.

References


2. We would echo the point made by the EEB in their submission to this consultation that ‘ultimately, there is a need to amend the Treaty on the Functioning of the EU (FTEU) and to design and implement new flexibility rules and guidelines within a Sustainability and Wellbeing Pact as a replacement of the SGP.’ ‘EEB submission on the review of the EU Economic Governance Framework’, EEB, Dec 2021: https://eeb.org/library/eebs-submission-on-the-review-of-the-eu-economic-governance-framework/

4. The phasing out of fossil fuels at the supply end is an objective of the newly-launched Beyond Oil and Gas Alliance, which has undertaken to eliminate fossil fuel production in its members in line with the Paris Agreement. The Alliance includes several EU member states: https://beyondoilandgasalliance.com

5. Such resources have been extensively researched and documented worldwide by the economist Elinor Ostrom. See also the proposals of Peter Barnes on ‘universal property’: https://universal-property.org, and ‘Common Wealth Dividends: History and Theory’ by Brent Ranalli, Palgrave Macmillan 2021.

6. Concerns are sometimes raised that a UBI could encourage environmentally harmful resource use, and in this regard, it is very important to note that the hard caps and phase-out of dangerous materials that are mentioned above would go a considerable way towards ensuring that recipients of this revenue spend the money in socially and environmentally beneficial ways.


11. ‘Concerned about housing costs? Don’t put your faith in the ECB”, Positive Money Europe 2021: https://www.positivemoney.eu/2021/12/housing-costs-ecb/

Question 10: How should the framework take into consideration the euro area dimension and the agenda towards deepening the Economic and Monetary Union?

If the framework is intended to further the goal of deepening the Economic and Monetary Union, then there will clearly need to be a permanent central fiscal capacity in the EU. Most crucially, the EU will need to have the power to rapidly introduce strongly countercyclical financial measures, so as to effectively support vulnerable member states in times of economic difficulty.

Given the urgent need to address the environmental crisis, the natural disaster clause of Article 122 of the TFEU could be invoked, thus enabling a centralised fiscal fund to be established while avoiding an immediate need to change the Treaty on the European Union[1].

While the two jurisdictions have many important historical differences, useful lessons with regard to centralised fiscal policy can be learnt by the EU from the USA’s experience as a fiscal union - both its successes and its failures[2]. Wherever there is a single currency for a very widely varied group of economies, there need to also be built-in measures to promote balance between them.

References


Question 11: Considering how the COVID-19 crisis has reshaped our economies, are there any other challenges that the economic governance framework should factor in beyond those identified so far?

The COVID crisis has strongly reinforced the already-existing need for a fiscal framework that steadily reduces, and aims to minimise, inequalities of power - including financial inequality - between EU residents, EU member states, and between the EU and the wider world.

COVID, and the resulting lockdowns, have exacerbated inequality along race and gender lines[1], have exacerbated the housing crisis by rendering tenants - who are more likely to hold unstable jobs that are vulnerable to lockdowns - still more financially fragile than before[2], and have increased the already worrying trend towards economic dominance by a small group of very large companies. To take just one example, Amazon, which has greatly benefited from COVID in financial terms, has been accused of dubious labour standards[3] and tax practices[4], and takes a questionable approach to competition with fellow retailers[5].

Many of the measures listed under question 9 above would help to reduce inequality, but further measures are needed on EU level to help break up the near-monopoly power of some companies.

It is noteworthy that the introduction of a Universal Basic Income, which we suggest in our response to question 9, would provide some relief to those affected economically by lockdowns, and would likely also help to prevent people who are infected with COVID19 - or indeed, any highly-contagious disease - from being obliged to go to work and potentially spread the infection in order to meet their immediate financial needs.

Note: This version of the submission differs slightly from the one that was uploaded to the Commission website. The sentence ‘The measures listed under question 9 above would all help to reduce inequality’ has been corrected to ‘Many of the measures listed under question 9 above would help to reduce inequality’.

References


Feasta (the Foundation for the Economics of Sustainability) is an ecological economics think tank, based in Ireland and with international membership. ‘Feasta’ is the Irish word for ‘in the future’. Our aims are to identify the characteristics (economic, cultural and environmental) of a truly sustainable society, articulate how the necessary transition can be effected and promote the implementation of the measures required for this purpose.

Feasta is a member of the Irish Environmental Network, the Environmental Pillar, Stop Climate Chaos and the global Wellbeing Economy Alliance, and a partner of the International Movement for Monetary Reform.

Further information can be found at http://www.feasta.org.

Point of contact: Caroline Whyte, caroline.whyte@feasta.org, +33642278918.