Opinion of the European Economic and Social Committee on the recommendation for a Council recommendation on the economic policy of the euro area

(COM(2015) 692 final)

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On 22 December 2015, the European Commission decided to consult the European Economic and Social Committee, under Article 304 of the Treaty on the Functioning of the European Union, on the:

Recommendation for a Council recommendation on the economic policy of the euro area

(COM(2015) 692 final).

The Section for Economic and Monetary Union and Economic and Social Cohesion, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 3 March 2016.

At its 515th plenary session held on 16 and 17 March 2016 (meeting of 17 March 2016), the European Economic and Social Committee adopted the following opinion by 201 votes to 3 with 6 abstentions.

1. **Conclusions and recommendations**

1.1. The EESC welcomes in principle the establishment of economic priority programmes to stimulate growth in euro area countries at the start of the European Semester. However, the Committee regrets that civil society, and the social partners in particular, were not consulted on the design and national processes of the European Semester.

1.2. The EESC believes that by means of these recommendations, the existing gap between the countries of the euro area and the other Member States must under no circumstances be extended but reduced. In particular, the aim is to keep an eye on the long term to develop the euro so it becomes the common currency of all Member States.

1.3. The EESC recognises the importance of the Commission document for the deepening of Economic and Monetary Union (EMU). As already pointed out in previous opinions ([1]), the Committee is strongly in favour of further strengthening and completion of EMU. The Member States, acting both individually and collectively, should take all necessary measures to ensure more convergence and integration, especially in the economic field. This should go in parallel with progress towards establishing a euro area fiscal union (including a dedicated budget), social union, and a unified external representation in international financial institutions.

1.4. The EESC recognises the political need to provide the euro area with a solid political and institutional foundation, which is something that has so far not been provided for since the establishment of monetary union ([2]). Individual initiatives such as the creation of a banking union or a Capital Markets Union are to be welcomed, but do not replace the solid architecture that is required.

1.5. It is further noticeable that the recent investment programmes in job offensives have not sufficiently achieved their aims. To achieve a recovery of growth and employment a mix of financial, taxation, budgetary, economic and social policies is needed. In contrast to the recommendation of the Commission, the focus of fiscal policy should be designed to be more expansionist than neutral.

([1]) See EESC opinions on 'Completing EMU — The proposals of the European Economic and Social Committee for the next European legislature' (OJ C 451, 16.12.2014, p. 10) and opinion on 'Completing EMU: The political pillar' (OJ C 332, 8.10.2015, p. 8).

([2]) Idem.

1.6. The EESC believes that a neutral fiscal stance, although preferable to continued fiscal austerity, is not appropriate under the current circumstances. Given that recession leads to lower growth potential, fiscal policies in the euro area have to do more than usual to stimulate the euro area economy as a whole. At this point, the risks from overheating economies are much lower than the risks from continued low inflation or deflation. Therefore, the EESC recommends a fiscal stimulus focusing on public investment: this would deliver stronger demand in the short term but also expand growth potential in the long term.

1.7. Furthermore, the EESC advocates the reduction of taxation on labour insofar as it does not threaten the financial sustainability of already fragile social protection systems. The EESC recalls that modern social protection systems should be based on the principles of solidarity and equality of opportunity and not just on the promotion of employability. Furthermore, the effect of robotics and digitalisation, which will disrupt jobs and have a likely impact on tax revenues, will have to be taken into account at a fiscal level.

1.8. The EESC welcomes that the 'flexicurity' concept has been reconsidered, but temporary contracts should ideally enable transitions to permanent contracts, not precarious jobs. In order to fight against growing social inequalities, it is necessary to create jobs and to focus on the quality of work. At the same time, the potential of the sharing economy should be used and must not be undermined; new forms of employment and work should be introduced for the benefit of society, without jeopardising workers' rights and social protection systems.

1.9. During the last eight years growth in the euro area has been suffering due to weak demand and not due to weak supply. Labour market adjustment has been unbalanced and asymmetric, having taken place mostly through lower nominal and real wages and unit labour costs in the Member States worst affected by the crisis. Therefore, the EESC concludes that structural reforms *alone*, aiming at improving the supply side of economies and thereby stimulating investment and growth, cannot be the answer to the problem of weak recovery. At the very least, structural reforms that may have positive effects on demand in the short term and even under credit constraints for households and firms should be prioritised.

1.10. The EESC also calls for a coordinated effort to create a more business-friendly environment for small and medium enterprises (99 % of EU companies and about 60 % of workers, or about 65 million people) through better regulation and consistent reduction of bureaucracy, and ensuring sufficient and adequate financing ('Access to Finance') ([3]) as well as a systematic facilitation of exports to markets outside the European Union. This generates business scope for investment in growth and jobs.

1.11. The EESC welcomes the initiatives for SME financing within the Capital Markets Union. Nevertheless, there is a particular need to open up new funding opportunities for micro-enterprises and start-ups such as seed capital, venture capital, crowd investing and financing, and innovative forms such as private equity. In this context, the EESC stresses the need for the planned creation of an EU venture capital fund. An evaluation is urgently required to discover the opportunities that the new models of banking ([4]) might offer for corporate financing in the EU.

2. **Background**

2.1. Following the Five Presidents' Report on Completing Europe's Economic and Monetary Union, there is a renewed approach within the European Semester to strengthen the integration between the euro area and the national levels. For the first time, the Commission is publishing a recommendation for the euro area in November, together with the 2016 Annual Growth Survey, in order to integrate better the euro area and national dimensions of EU economic governance.

([3]) See the EESC opinion on 'Action plan on building a capital markets union' (OJ C 133, 14.4.2016, p. 17).

([4]) See for example comments in previous EESC opinions on 'Financing structures for SMEs in the context of the current financial situation' (OJ C 48, 15.2.2011, p. 33) and opinion on 'An action plan to improve access to finance for SMEs' (OJ C 351, 15.11.2012, p. 45) regarding Islamic finance.

2.2. The aim is to offer opportunity for discussions and recommendations about the euro area, ahead of country-specific discussions, so that common challenges are fully reflected in country-specific actions. This is an important change from the previous semester cycles where the euro area recommendations came towards the end of the semester, at the same time as the country-specific recommendations.

2.3. The Commission presented four recommendations on the economic policy of the euro area:

— pursue policies that support the recovery, foster convergence, facilitate the correction of macroeconomic imbalances and improve adjustment capacity,

— implement reforms that combine flexible and reliable labour contracts, comprehensive life-long learning strategies, effective policies to help the unemployed re-enter the labour market, modern social protection systems and open and competitive product and services markets. Reduce the tax wedge on labour, particularly on low-earners, in a budgetary-neutral way to foster job creation,

— maintain the planned broadly neutral fiscal stance in 2016. With a view to 2017, reduce public debt to restore fiscal buffers while avoiding pro-cyclicality, in full respect of the Stability and Growth Pact, and

— facilitate the gradual reduction of banks' non-performing loans and improve insolvency proceedings for businesses and households.

3. General comments

3.1. For the first time, the draft euro area recommendations are published at the start of the European semester cycle alongside the Annual Growth Survey (AGS), the Alert Mechanism Report (AMR) and the draft Joint Employment Report. The EESC agrees that this new process can help to better take into account euro area wide considerations in the design of national policies presented in stability programmes and national reform programmes.

3.2. The EESC regrets that the social partners and civil society at large were not consulted on the design of the draft euro area economic recommendations and that national processes are not yet adjusted to this new semester process. In the framework of the EU Semester, social dialogue can be a driving force for successful, sustainable and inclusive economic, employment and social reforms. Social partners at all levels should agree with the relevant public authorities on a real, timely and meaningful involvement in the EU Semester. In addition, the EESC strongly recommends a continuous and close cooperation between the ECO section of the EESC and the ECON Committee of the EP in the future.

3.3. The EESC supports the focus on a coordinated approach by all Member States of the euro area but also across monetary, fiscal and structural/supply-side policies. Further, the EESC suggests that the focus of structural reforms should be put on political measures, so that the economic recovery can be supported in the short term. As far as the flexibility of labour markets is concerned, this should not result, as in previous years, in a loss of purchasing power in the workforce, so that domestic demand will not be compromised as a key growth driver. This means that the competition is to be led through increased quality and productivity growth through innovation and not through low prices and wages.

3.4. Although the EESC recognises the enormous challenges of further strengthening and developing the euro that are required at this time and will be required in the near future to provide lasting protection for the euro and for the euro area, it believes the following objectives are desirable:

— establishment of a unified external representation of the euro area in international fora (International Monetary Fund, OECD, etc.) ([5]),

([5]) See EESC opinion on 'Euro area external representation' (see page 16 of this Official Journal).

— establishment of a euro fiscal union,

— establishment of a social union, meaning that the social partners need to be included even more by the Commission, the Council and Parliament in all legislative initiatives.

3.5. In view of the EU Multiannual Financial Framework (MFF) 2014-2020 mid-term review and in preparing the reflection on the MFF post-2020, the EESC suggests that the euro area must have a dedicated budget that should: (i) provide a temporary but significant transfer of resources in case of regional shocks; (ii) counteract severe recessions in the area as a whole; (iii) ensure financial stability. In the same vein, the euro area must have — as a first step towards an economic government — its own finance minister with a dedicated own-resources system guided by the principle of simplicity, transparency, equity and democratic accountability.

4. **Specific comments**

4.1. ***Macroeconomic imbalances***

4.1.1. The EESC agrees with the Commission that structural reforms in the Member States should continue according to country-specific circumstances in order to foster convergence and facilitate the correction of macroeconomic imbalances. However, there must be a balance between structural reforms and investment in productive activities leading to the creation of jobs.

4.1.2. The EESC welcomes the European Commission recommendation that Member States with large current account surpluses should implement as a priority measures that help to channel excess savings towards the domestic economy and thereby boost domestic investment. However, such measures should not be limited to the supply side (for example, reforms in product markets) but also include more decisive government initiatives on the public investment front as the current Juncker plan ([6]).

4.1.3. The EESC believes state subsidies should align in particular with innovative SMEs. In order to provide this category of enterprise with easier access to finance, it is the responsibility of the state, on the one hand to grant financing that provides an impulse, and on the other hand to provide a system of public guarantees and warranties. The relevant interaction between the state, SMEs and universities and research institutions is an important element of the investment system.

4.1.4. The EESC highlights the fact that exports represent a key growth driver for the SMEs in the euro area. In addition to the favourable euro-dollar rate caused by the ECB monetary policy, Free Trade Agreements are essential in order to increase exports. Although the EESC supports the current focus on negotiating TTIP it also equally recommends concluding an agreement that will facilitate market access for European companies in their trade with high-growth emerging markets. It is important to ensure that human rights and ILO standards are respected, along with consumer rights and environmental regulations in force within the EU.

4.2. ***Labour, product and services markets***

4.2.1. The EESC notes that although, as the European Commission reports, labour markets continue to gradually improve, there is no mention of the fact that the employment rate in the euro area at 68,9 % in 2015 is still well below the Europe 2020 headline target of 75 %. The EESC notes that according to evidence provided by the European Commission services (Labref database), there does not seem to be any positive relation between the number of labour market reforms implemented at any stage (before or after the crisis) and the labour market performance of Member States ([7]).

([6]) OFCE, ECLM, IMK, AK-Wien, INE-GSEE (2015), *The Independent Annual Growth Survey 2016*, Paris.
([7]) ETUI/ETUC (2015), *Benchmarking working Europe 2015*, Brussels, ETUI, p. 26.

4.2.2. Structural reforms in the labour markets must favour social investment, that is to say measures which support the continuous training of employed and unemployed workers and ensure that their financial security — particularly of the unemployed — is promoted. Furthermore, the EESC supports the reduction of taxation on labour, provided it is compensated by other sources of public revenue. In the medium term, higher labour market participation can also contribute to this process.

4.2.3. To solve the European competitiveness and sustainability problem, the EESC recommends establishing a digital holding following the model of the very successful Airbus Group. This multinational cooperation includes several subsidiaries of different EU Member States and is a key player in the European economy and industry.

4.2.4. US digital dominance already represents a new form of global dominance. Particularly dramatic effects can be seen in the financial sector, where the big American investment banks have already created the strongest capital ties with the innovative FinTechs, which in turn threaten the European model of the classic retail banks ('boring banks') and can successfully compete against them in their core functions.

4.2.5. To design and develop the details of a comparable model of a European Digital Holding the EESC suggests the short-term creation of an interdisciplinary project group. This group should include representatives of the Commission (Commissioner Oettinger) and the EU Parliament (ITRE Committee) and be run with the involvement of the EESC. As regards the question of financing, it is important from the outset to pay attention to compatibility with the Juncker Investment Plan. Strong impetus for growth and new jobs will be opened up by close cooperation between the competence units of the digital holding with the SMEs themselves.

4.3. ***Fiscal policies***

4.3.1. The EESC welcomes the European Commission emphasis on considering the fiscal stance for the euro area as a whole when shaping guidelines for national fiscal policies. However, the EESC notes, without prejudice for the independence of the ECB, the remarkable absence of an analysis of the developments in the monetary policy developments in the euro area in assessing the appropriateness of a neutral fiscal policy stance. This is at least odd, given that members of the ECB governing council have been repeatedly and publicly referring to the fiscal policies of the euro area ([8]).

4.3.2. This is a worrying omission insofar as the euro area is currently in a situation where the capacity of the monetary policy to stimulate demand is severely limited. Demand has been weak for so long that inflation (even when not taking into account oil prices) is well below the ECB target of 2 %, while the main policy interest rates of the ECB are almost zero, not allowing any further substantial reductions. The euro area economy is in a so-called 'liquidity trap' and is at risk of falling into a 'deflation trap' should inflation not pick up soon. If that happened, then the euro area economy would remain in stagnation for many years, eventually threatening the political viability of the euro.

4.3.3. The unconventional policy of quantitative easing pursued by the ECB in earnest since early 2015 does not seem to have made a considerable difference ([9]) in stimulating demand. Under such circumstances and given the presence of 'hysteresis' phenomena mentioned above (where recession leads to lower growth potential), fiscal policies in the euro area have to do more than usual to stimulate the euro area economy as a whole ([10]). Given the fiscal policy limitations in Member States at the south of the Eurozone, fiscal policies in Member States with below target inflation, low public borrowing costs, comparatively low public debt/GDP ratios and current account surpluses should expand to push inflation above the ECB target of 2 %, so that on average inflation in the euro area can accelerate again to approach the target. At this point, the risks from overheating economies are much lower than the risks from continued low inflation or deflation.

([8]) The most prominent example was the speech 'Unemployment in the euro area' by President Draghi at Jackson Hole in August 2014 (https://www.ecb.europa.eu/press/key/date/2014/html/sp140822.en.html).

([9]) http://epthinktank.eu/2015/12/10/the-ecbs-quantitative-easing-early-results-and-possible-risks/

([10]) Theodoropoulou S. (2015), *How to avert the risk of deflation in Europe: rethinking the policy mix and European economic governance*, Brussels ETUI.

4.3.4. Given, however, concerns about public debt sustainability, against a background of demographic developments, expansionary fiscal policies, especially in Member States with large current account surpluses, can and should expand by increasing spending on public investment. A fiscal stimulus focusing on public investment would deliver stronger demand in the short term but also expand growth potential in the long term. Such public investment could focus not just on infrastructure but also on education and skills policies ('social investment').

4.4. ***The financial sector***

4.4.1. The EESC calls for the creation of a European insolvency law, on the one hand to open up the possibility of debt relief for households and on the other hand to make it easier for start-ups to deal with business failure. In this way households will have increased purchasing power and the start-ups will be encouraged.

4.4.2. A still unsolved but serious problem is the fact that there are approximately EUR 900 billion of non-performing loans in existence in the euro area banks. It is only by reducing them that the banks will be able to expand their lending to businesses and households, thereby increasing the effectiveness of the loose monetary policy of the ECB to enhance the growth outlook and strengthen market confidence. The relevant political and regulatory institutions of the euro area should be required to submit relevant concepts on this topic.

4.4.3. As one of the central aims as a consequence of the financial crises, there was a consensus to decrease significantly sovereign risks in the balance sheets of the European banks. The present situation of most of the banks shows that the sovereign risks have dramatically increased. The EESC underlines that the first priority should be to reduce these sovereign risks in the balance sheets to guarantee future stability of the banking and financial sector, also in the light of the recent EDIS proposal ([11]).

4.4.4. The EESC notes that for any positive effects on demand to materialise, households and businesses should not be liquidity constrained. Restoring positive credit flows would help stimulate demand but also help to increase the effectiveness of the monetary policy of the ECB in improving the growth outlook and strengthen market confidence. The relevant political and regulatory institutions of the euro area should be required to submit relevant concepts on this topic.

4.4.5. Furthermore, the EESC calls for the reform agenda and for the regulatory bodies to lay more emphasis on greater transparency and on the supervision of non-banks or shadow-banks in order to sustainably secure the stability of financial systems and restore their function for the real economy, in particular in the field of securitisation ([12]). It should be ensured that securities are not to be used as speculative investment instruments by hedge funds and financial institutions who have yield-maximising objectives to meet (vulture funds).

4.4.6. Since the financial crisis was in large part caused by the speculative activities of the investment banks, the speculative banking business remains a latent threat to financial market stability. It still has not been thoroughly examined how highly speculative trading activities such as high frequency trading can take place when the objective is more stable markets in the world, and it is necessary to strictly separate the low-risk investment practices and the lending business from the high-risk activities of investment banking. To this end, there are already a number of models such as the Vickers model and the Volcker-Rule. The EESC recommends the establishment of a Glass-Steagall Act in the European Union, as other financial markets (such as the USA and the BRICS countries) are discussing to reinstall it to improve the stability of the banking sector. This would avoid risks for savers and tax payers.

Brussels, 17 March 2016.

The President
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Georges DASSIS

([11]) See EESC opinion on 'European deposit insurance scheme' (see page 21 of this Official Journal).
([12]) See EESC opinion on a legal framework for securitisation (OJ C 82, 3.3.2016, p. 1).