20 November 2014

Background Policy Paper: A progressive European Investment Plan for fostering economic growth and Employment

Financial and Economic Network

Six years ago the European Union was hit by an unprecedented financial and economic crisis. Today, Europe is confronted with sluggish economic growth, with the risk of deflation, with accumulating high government debt and with unacceptably high unemployment rates especially amongst the youth. The Party of European Socialists has, since the beginning of the crisis, criticised the implementation of harsh austerity measures and challenged the austerity-only approach. Instead, the PES has been calling for the stimulation of both public and private investment via the implementation of a concrete and ambitious Investment Plan for Europe.

As our family grew bigger, our influence in Europe grew stronger. It is thanks to our constant political pressure that today we are experiencing a shift in policy orientation, and an acceptance that only through a vigorous Investment Strategy will the European Union be able to foster economic growth and create new and decent jobs. Our calls are reflected in the new Commission working plan, Jean-Claude Juncker as European Commission President is now committing to deliver a €300 billion Investment Plan for Europe. We must remain vigilant as Juncker's commitment is turning into a mere statement with no assurances. So far, there is no clear description of a concrete investment strategy, and no clear indication for using new funds.

Time is running out! Concrete steps to deliver a better future to 25 million unemployed women and men, and in particular for the 5 million unemployed youth, must be taken. We need to ensure that new funds are allocated for both private and public investments that can stimulate economic growth.

The PES would like to take the opportunity of its Financial and Economic Network to exchange constructively on the proposals that are on the table, and deepen the discussions on the measures that are available. Some of the key proposal being debated at EU and national level, and their rationale, are summarised below, to help frame the discussion.

Progressive fiscal policies that incentivize investments:

- Making full use of the flexibility clause provided in the Stability and Growth Pact. Member States can no longer undergo structural reforms that shrink public finances and block the activation of automatic stabilizers. Today more than ever governments struggle to reach the narrow interpretation of the fiscal targets set out in Stability and Growth Pact. Europe must engage into greater coordination of fiscal policies in order to effectively address the issue of macroeconomic imbalances, build a concrete framework for countering asymmetric shocks and mitigate the risk of deflation.

- Implementing the 'investment clause', whereby productive investments carried out by Member States are excluded from the calculation of their budgets deficits. This progressive rule can effectively allow for the intensification of public investment without pressuring public budgets.

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This measure can effectively boost internal demand while effectively promoting economic recovery and creating new employment opportunities.

- Shifting taxation from labour to capital as a counter cyclical fiscal policy that encourage fair redistribution of wealth and promote equality in our societies. Labour taxation has been consistently high in Europe reaching 51% of revenue in 2012, the second revenue pool is consumption taxation at 28.5% in 2012, while taxation on capital remains comparatively very low providing a mere 20.8% in revenue in 2012[1]. This trend must be reversed, we have to shift the burden from labour to capital, and in effect increase the levels of available disposable income allowing for a greater consumption propensity. Moreover we need to introduce fair corporate tax systems that put an end to unfair corporate competition between Member States.

- Pursuing environmental taxation. Engaging the Horizon 2020 goals can be achieved through the use of taxes designed to provide appropriate incentives to reduce emissions over time and improve resource efficiency, including through environmentally consistent tax rates across various energy carriers and emissions as well as through the phasing out of environmentally harmful subsidies harnessing the potential to raise revenue. In the current fiscal context, and while taking into account the serious challenge of climate change, it becomes crucial to use energy taxes to their full extent in climate and energy policy in order to mitigate the overall cost of the policy.

- Tackling tax fraud and evasion. Studies[2] have shown that every year Europe loses up to €1trillion due to these illicit practices, funds that are much needed for strengthening fiscal conditions. We welcome the efforts that have been undertaken at European and International level to tackle this issue, the agreement to automatically exchange tax related information between member states and international partners is a great step toward the eradication of tax evasion. But more can be done, we must create a legal framework for eradicating tax havens as well as for countering shadow banking activities.

- Implementation of the Financial Transaction Tax as a tool for increasing the EU's investing capacity. So far eleven Member States have agreed to implement the tax on January 1st 2016, which will provide €30 to €35 billion in additional revenue. In addition to creating new financial resources, the tax can actively contribute to tackling financial speculation and encourage financial institution to invest in the long term. The PES will continue advocating for the implementation of the tax by all Member States and favour a wide scope with ambitious rates.

- Measures to ensure that bank failure will no longer burden public finances. The creation of the Single Resolution Mechanism is a fundamental step in improving the financial system and to setup the Banking Union. Moreover, the Single Resolution Fund (SRF), with an agreed total capacity of €55 billion by 2024, ensures that potential future bank failures in the banking union are managed efficiently, with minimal costs to tax payers and the real economy. However, the results of the Asset Quality Review (AQR) by the ECB (stress tests) indicate financial gap of €9.5 billion in capitalization from the reviewed banks. It is clear that ultimately those gaps should be covered by banks, notably via the Single Resolution Fund. This mechanism will however not come into full effect immediately, but in stages over time. What mechanisms should be used to cover the financial gap in the meantime?

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[1] http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2014/pr_92-2014_en.pdf

[2] http://www.socialistsanddemocrats.eu/sites/default/files/120229_richard_murphy_eu_tax_gap_en.pdf

Use existing EU instruments to foster investment opportunities

- Strengthening the financial capacity of the European Investment Bank. In 2012 within the scope of the 'Compact for Growth and Jobs' the European Investments Bank's financial capacity was increased by €10 billion, this measure marked a great success as the EIB was able to lend €20billion in a year to the real economy. Considering the success of the measure, a further increase of the paid-in capital of the EIB should be considered. Studies[3] have demonstrated that by boosting the paid-in capital of the EIB by a further €10billion, would allow for an increase of the banks' total lending capacity of up to €160billion in the next 3 to 6 years. Growth and job creating sectors have to be identified and a larger investment portfolio should be channeled through the financial capacity of the EIB to allow for greater risk diversification.

- Project Bonds. The intensification of the use of project bonds can serve as a catalyst for relaunching big infrastructure investment in the EU. During the pilot stage project bonds were able to raise funds exceeding €700 million, demonstrating the appetite of European capital markets for straightforward refinancing of infrastructure projects. But more can be done in order to make better use of this initiative and for effectively reaching the goals of the Europe 2020 Strategy. It can for example be extended to cover areas beyond those of Connecting Europe Facility (CEF). Further diversification of funding can also be promoted by granting more flexibility on the licensing rules of the bonds and on their implementation. Such steering can unblock funding towards other infrastructure sectors such as social sectors, renewable energy, and the digital economy.

- The midterm review of the European budget also provides a great opportunity for reallocating more resources into areas with greater investment return. The use of the European Budget as a principal tool for promoting investments in Europe has to be intensified by optimizing its operation. More flexibility to use funds across the different headings and throughout the five year period needs to be granted as well as making greater use of its co-financing abilities.

Exploring new investment tools

- In order to ease the flow of investment in Member States consideration should be given to developing national development banks. Drawing from examples such as the case of the German Development Bank (KfW) which has effectively streamlined strategic investments in multiple sectors since it began operating in 1948, representing 12.7% of total bank credit in the German economy up to 2013. We advocate for the creation of national development banks that can allow for the correction of market rigidities without distorting EU competition rules, by ensuring the management of private equity or specialized funds and allowing for greater SME access to be financed by co-investing with private investors.

- Creating a long-term financial facility. We should explore the possibilities available to create a steady financial facility dedicated to promoting investment. One instrument that is often discussed is the use of the European Stability Mechanism (ESM): The ESM has a total paid in capital of €80billion which, if leveraged, could create a total subscribed capital up to €600billion[4]. The Mechanism can be used as a steady capital buffer for leveraging funds through the EIB or the MFF. Another possible instrument is to strengthen the use of the European Investment Fund by making more capital available for supporting the real economy. These potential investment tools can significantly improve market conditions, boldly contribute to the promotion of investments and effectively stimulate speedy economic recovery.

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[3] http://www.feps-europe.eu/assets/5ab4d17c-819f-47d7-9e65-3d9b4356387d/epv%234_sgj%20gc_europe%20investment.pdf

[4] http://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Topics/Europe/Articles/Stabilising_the_euro/european-stability-mechanism.html

- Bringing down debt. The European sovereign debt crisis is still a great challenge, current indicators show a 13% increase of Eurozone government debt over the past 5 years, while European public debt has also been steadily accumulating over the same time period to reach €86.6 billion in 2012. Action has to be taken through measures of shared responsibility and joint guarantees to bring the debt levels to performing levels.

It is time for Europe to act and vigorously promote investment. We need a European Investment Strategy that resources new funds and that lays down the framework for both public and private investments. Positive reforms must be undertaken by allocating to the areas which will provide the best returns. This includes pursuing investments for greening our economies and bringing down energy costs. As well as creating solid digital infrastructures and promoting innovation that can enhance the added value of our services and industrial grid. We need to invest in our labour force from the start by promoting education and lifelong learning.

Europe needs to take coordinated action and apply a well-balanced policy mix that strengthens rather than weakens our social models. Our aim is to promote sustainable economic growth by applying expansive rather than regressive measures. The PES will continue being at the forefront providing viable progressive alternatives that are aligned to our values, and we look forward to all contributions in our Financial and Economic Network.