Next Generation EU: Europe needs pan-European investment

Roe Versteeg, Laurence Castagnoli, Paul van den Noord
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Next Generation EU should not turn out to be a missed opportunity to initiate and fund genuine pan-European infrastructure projects with high impact on potential growth. Roe Versteeg, Laurence Castagnoli and Paul van den Noord argue for the automatically applicable value for such a pan-EU initiative.

Epidemiologists advocate the use of a circuit breaker lockdown to fight the pandemic. The economic policy response should become the ‘circuit maker’ to speed up the recovery since the pandemic is under control.

European leaders seem to have woken up to this need, but we are concerned that the institutional ‘circuit breaker’ will act as a drag.

Next Generation EU, the unprecedented fiscal package adopted by the European Council this summer, is a commendable endeavour. Its aim is to launch public investment with a long-term objective of ‘building Europe, not just the eurozone’ (Van den Noord 2020). It will reach a massive amount of funds, after which the member states will have to contribute actual funds for the projects.

Indeed, Next Generation EU is about much more than an attempt to return to pre-crisis conditions. It is the EU’s ‘New Deal moment’ (European Commission 2020a), aiming to not only compensate for the macro-economic downturn since the coronavirus crisis, but also to transform the post-crisis economic landscape, and to achieve strong and sustainable growth.

The bulk of the funds are channelled through the Recovery and Resilience Facility. Each country has a right to claim a fraction of the total pot for grants and loans, based on a prior agreed formula relying on a set of objective indicators. Figure 1 shows the distribution of Next Generation EU funds among the Member States. One expects the extraordinary size of the funds to put pressure on national decision making and budgets, or not undertaken at all.

So far, several studies have already concluded the projects should be guided and coordinated at a European level. The subsidiarity principle would argue for top-down rather than bottom-up in the case of large infrastructure projects.

Moreover, the scale of such investments is too large for national administrations to handle on their own. Not only do individual countries fail to internalise positive spill-overs, but they also find it inherently complicated to work together on projects with a high impact on sustainable growth (renewable energy, human capital, green mobility) that have broader spill-overs and a strong ‘common good’ characteristic and for which national governments are ill equipped.

The EU is in dire need of pan-European infrastructure projects, pan-European meaning involving two or more countries and yielding spillovers from which the entire EU can benefit. Examples are high-speed railways, power grids with sufficient capacity to transport the electricity generated by renewable energy, infrastructure for hydrogen (produced by renewable energy to replace carbon energy), digital investments, but also human capital and mobility.

Projects need to fulfil certain conditions and should be reform- and investment-related, based on guidelines provided by the Commission. As such, projects should come as a complement to structural reform plans.

This approach has a strong macroeconomic rationale. Yet, it is subject to a number of risks, common to most EU policy initiatives that rely on countries submitting their own plans (even when subject to coordination such as the European Semester), and of which some are acknowledged to have long plagued the effectiveness of EU projects:

1. The additivity of the plans turn out not selected during the process. What countries do: they focus on existing projects or projects that would have been undertaken anyway. In that case, support funding can at most limit the debt increase of countries with already high fiscal space.

2. Projects lack of long-term horizon. Countries would not fund such projects because they are already authorised or feasible. Only funding grants and market loans have strings attached. The same story can be told for the awful affected countries risk not being covered by the EU’s guarantee and the credit risk-based assumptions of the package.

3. Countries would prefer to delay the funding of large infrastructure projects on top of their priority list, because countries are unable to satisfy well-defined agreements of projects. In any case, start-up delays may cause patients to lose interest in the project, because countries are unable to satisfy well-defined agreements of projects. In any case, start-up delays may cause countries to lose interest in the project, because countries are unable to finance well-defined agreements of projects. In any case, start-up delays may cause countries to lose interest in the project.

Therefore, the EU (Commission and other European institutions), not primarily national governments, should initiate such genuine pan-European infrastructure projects that transcend national interests. The emphasis should not be on projects implemented on a top-down basis. However, not only do individual countries fail to internalise positive spill-overs, but they also find it inherently complicated to work together on projects with a high impact on sustainable growth. Awaiting is a great example of a large pan-European project that was successfully implemented on a top-down basis.

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