

# Public Investment for the EU Recovery

*Forum on Macroeconomics and Macroeconomic Policies*

*Berlin, October 28th, 2020*

# Outline

- Public investment and the Recovery Plan
- A state of the art: The European Public Investment Outlook
- How to Spend it? A truly European investment program
- When to spend it?
- Conclusion: Fiscal rules and industrial policy

# Next Generation EU

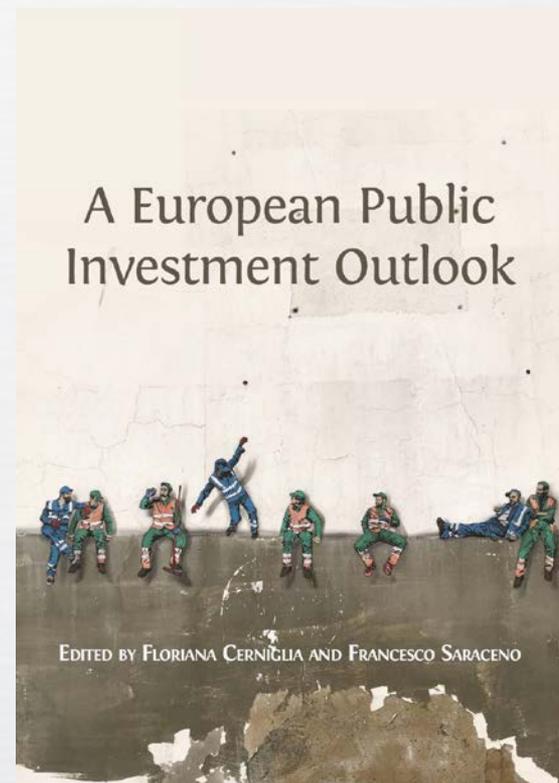
- The *European Recovery and Resilience Facility* factsheet
  - “consists of large-scale financial support to both **public investments** and reforms, notably in green and digital, which make EU countries’ economies more resilient and better prepared for the future”
  - “The support will take the form of up to €310 billion in grants and up to €250 billion in loans. The Facility will be demand-driven and powered by an emergency European Recovery Instrument, ‘Next Generation EU’, amounting to €750 billion”
- Features of the RRF:
  - Centered on Investment
  - Medium term perspective (not really aimed at facing the short run challenge)
  - Nested in the Commission 5 years work plan (digital, environmental transition)

# The newfound centrality of Public Investment

- Low interest rates + deteriorated capital stock →
- Public investment has
  - High returns
  - High multipliers
- *Public investment is a free lunch* (IMF WEO Fall 2014)

# The Need for Public Investment in Europe

- *European Public Investment Outlook*
  - 30 authors from different backgrounds and nationalities
  - Possibly the first of a series
- Two parts
  - Outlook
  - Challenges
- The report was finalized before the pandemic
- Since then, the discussion on public investment has been focused on a wide range of sectors (ecological transition, value chains, welfare)
- The report had already adopted, as its common theme, the very same ***broad definition of “investment” as whatever increases human as well as physical capital***



# Part I - Outlook

- Europe (Bubbico – Brutscher – Kappeler - Revoltella)
  - Public Investment in EU declined from 2008. in 2018 still 15% lower than in 2008 (2.9% vs 3.4%). Infrastructure were particularly hit (-25%)
  - Fiscal consolidation identified as the main driver of the drop
- France (Plane - Saraceno)
  - France is decumulating capital since 2015 → Debt increase has not increased assets but mostly financed current expenditure
- Germany (Dullien – Jürgens – Watzka)
  - Severe deterioration of public capital stock since 2 decades. Sector by sector analysis leads to the estimation of €450bn over the next decade.
- Italy (Cerniglia – Rossi)
  - Public investment the main victim of fiscal consolidation since 2010. Important territorial inequality and public administration inefficiencies
- Spain (Villaverde – Maza)
  - Strong decline since 2009 Public investment still see preponderant share of infrastructures → Need to rebalance towards other sectors (e.g. ICT)

# Part II- Challenges

- R&D (Daniela Palma, Alberto Silvani and Alessandra Maria Stilo)
  - Low levels and high heterogeneity. Highlights the role played by public funding and the importance of R&D for industrial policy
- Social Investment and Infrastructure (Anton Hemerijck, Mariana Mazzucato and Edoardo Reviglio)
  - Social policies to enhance competitiveness. Proposes a EU Fund for social infrastructures
- Transport Infrastructure Networks (Paolo Costa, Hercules Haralambides and Roberto Roson)
  - Highlights “Geographical obsolescence” → Reorient from internal market to linkages with emerging Asia
- Ecological Transition (D’Maris Coffman, Roberto Cardinale, Jing Meng and Zhifu Mi)
  - Focus on *financing* of environmental transition and role of multilateral institutions (development banks)
- Cohesion Policy (Francesco Prota, Gianfranco Viesti and Mauro Bux)
  - Since 2008 main source of financing of public investment in many countries. Need to enhance its role in transport and environmental transition

# How to Spend it

- Much of the debate was and still is financing *national* investment plans
- In a recent policy brief, we tried to shift the focus on a large *truly European* investment plan
  - We propose a 10-year, €2tn investment programme
  - Focus on public health, transport infrastructure, energy/decarbonisation.
  - We give a few examples along two pillars
  - In a national pillar, resources should be focused on the hardest-hit countries and front-loaded.
  - The bulk of the money would be devoted to finance *genuinely European projects*, where there is an EU value added



# How to Spend it

Covid-19 Recovery Fund: € 2 tn, 2021-30

EU pillar:  
€ 1,500 bn, 2021-30

National pillar:  
€ 500 bn, 2021-23

Health4EU:  
€ 400 bn

Ultra Rapid Train  
1<sup>st</sup> leg: € 550 bn

Relief for MS:  
€ 200 bn

100% RES e-highway  
1<sup>st</sup> leg: € 260 bn

Support to mitigate  
climate risk: € 290 bn

Relief for most  
affected MS:  
€ 300 bn

# How To Spend it

- A single European Health agency in charge of 2 objectives:
  - Extra-training and a mobility incentive to better allocate human capital and match local health demand and supply
  - Strategic supply of medicines and equipment
  - Funding equivalent to what would be appropriate for its US counterparts would have to be €20 bn p.a.
- A European Ultra Rapid Train Network
  - 18,250 kilometres would amount to about €1,100bn
  - lighthouse project in support of the European Green Deal
  - create another European champion in the transport industry
- Energy/decarbonisation – electrify the Green Deal!
  - Boost fundamental research (> foreseen expansion Horizon Europe, was €100bn weakened by frugals)
  - Accelerate construction of smart, integrated electricity grid (RES e-highway) Total cost estimated to 2050 ~€500 bn

# When to Spend it

- The RRF should be allocated and spent before 2026
- For many countries this might be a problem (Darvas, Bruegel Blog, 9/24/2020)
- The short deadline might push countries to focus on large scale projects, when diffused micro investments might be more efficient and growth enhancing
- As the agreement between European Parliament and Council has not been reached, why not reassess the timeline of the Fund?

# Conclusion: A Common Theme. Changing the Rules

- A Golden Rule
  - Formalize the preferential treatment for investment that is in the new Commission «flexibility» doctrine
  - Extensive definition of public investment (“**augmented**” golden rule)
  - Inclusion of Cohesion Policy co-financed expenditure
- Coordination of public investment choices: Public investment as one arm of industrial policy?
  - Transnational aspects of infrastructure investment
  - Joint definition (European Semester?) of what is «growth oriented expenditure»
  - Multiple instruments: EU budget - Cofinancing by EIB – Member States
- Do not waste the occasion given by the Commission!