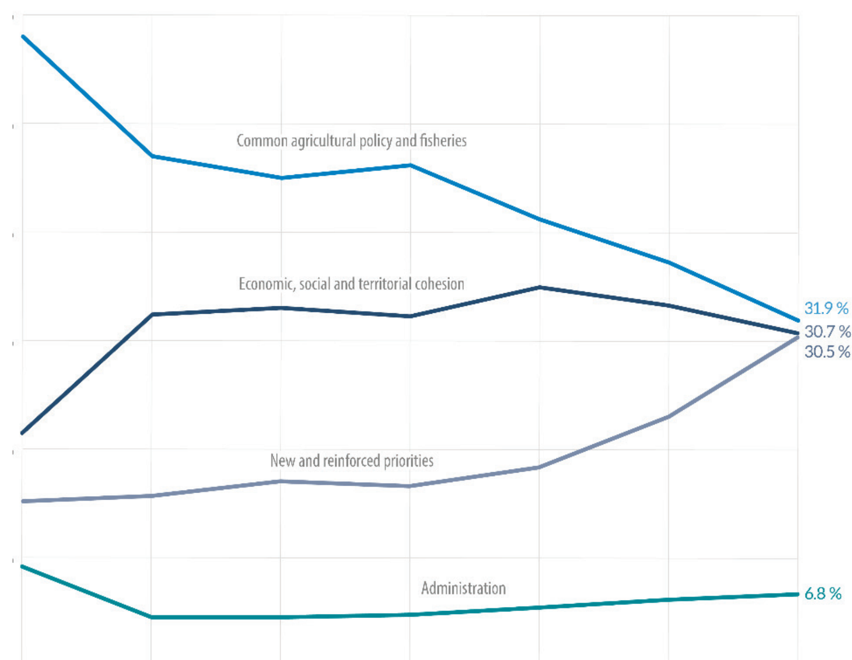
ISSN 2600-2779

Economic and Budgetary Outlook for the European Union 2021



STUDY

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Members' Research Service
PE 679.062 – January 2021

EN

Economic and Budgetary Outlook for the European Union 2021

This study, the fifth in an annual series, provides an overview of the economic and budgetary situation in the EU and beyond, and summarises the main economic indicators in the EU and euro area and their two-year trends. It also explains the annual EU budget, provides an overview of its headings for 2021, and sets out the wider budgetary framework – the post-2020 multiannual financial framework (MFF) and the Next Generation EU recovery instrument. This year's special 'economic focus' puts the spotlight on EU social and employment policies in the context of the coronavirus outbreak.

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The authors wish to thank Benjamin Nielsen, trainee in the Budgetary Policies Unit, for his research assistance.

This paper has been drawn up by the Members' Research Service, within the Directorate-General for Parliamentary Research Services (EPRS) of the Secretariat of the European Parliament.

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LINGUISTIC VERSIONS

Original: EN

Translations: DE, FR

Manuscript completed in January 2021.

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PE 679.062
ISBN: 978-92-846-7722-1
ISSN: 2600-2779
DOI:10.2861/597358
CAT: QA-CH-21-001-EN-N

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Executive summary

Growth in gross domestic product (GDP) in Europe collapsed in 2020 as a result of the economic crisis caused by the coronavirus pandemic. Moreover, in contrast with previous recessions, the uncertainty caused by the pandemic also caused a shift in consumption and investment patterns. In great part thanks to the discovery of effective vaccines against the virus, GDP growth is expected to rebound in the coming two years. This forecast depends on several variables, however, including the length and size of the support programmes put in place by governments and central banks, geopolitical tensions, and the future relationship between the European Union and the United Kingdom.

When it comes to employment, the positive trends observed in previous years were reversed in 2020 as a result of the economic crisis. The picture would have been bleaker had it not been for various support schemes and policy measures at national level, supported by a number of measures at EU level, and the EU's new SURE instrument for temporary support to unemployment schemes. Nevertheless, interpretation of the numbers must be nuanced, given that many unemployed people were pushed out of the labour force in 2020, hiding the full effect of the economic crisis. Moreover, future unemployment figures will depend on the timing and pace of the withdrawal of policy support schemes and on whether the economic recovery has materialised by then. Taking these factors into consideration, unemployment is expected to increase in 2021, and then decrease slightly in 2022.

General government deficits are expected to have increased significantly, as a result of the various fiscal measures put in place to counter the economic crisis. Deficits are expected to decrease from those highs in the next two years, but still remain over the 3 % limit set by the Maastricht Treaty. Similarly, the debt-to-GDP ratio is expected to increase significantly in 2020, both for the euro area and for the EU as a whole, and to continue increasing slightly in 2021 and 2022.

Lastly, in 2020, inflation for the euro area was slightly above zero and, despite picking up in the next two years, is still expected to remain below the target of 2 % set by the European Central Bank. In this context, but also to support the Member States, the ECB maintained its asset purchase programme (APP), launched a new one for the duration of the pandemic, and extended its accommodative measures.

The coronavirus pandemic influenced the negotiations on the medium-term architecture of EU finances, which resulted in the adoption of an unprecedented budgetary package in December 2020. This combines the €1 074.3 billion multiannual financial framework (MFF) for the years 2021 to 2027 with the €750 billion Next Generation EU (NGEU) instrument. The agreement brought new momentum to the EU budget, assigning it a major role in the Union's strategy to relaunch the economy. The launch of NGEU, a temporary recovery instrument (2021-2023), to be financed through resources borrowed on the markets by the European Commission on behalf of the Union, is a major innovation.

The 2021 budget is of a transitional nature. As the first under the new MFF, it shows the amounts needed to launch the new generation of EU actions and programmes, but also provides the payment appropriations needed for the closure of the programmes relating to the 2014-2020 MFF. Furthermore, NGEU will significantly increase the resources channelled through the 2021 EU budget, adding an estimated €285.15 billion in commitments and €75.93 billion in payments to selected programmes. As a result, in 2021, total commitments will almost triple the usual annual expenditure of the EU budget. While investment in recovery and resilience measures is the overarching priority of EU spending in 2021, the EU budget will continue contributing to the achievement of other objectives, in such areas as the green and digital transition, cohesion and agriculture, security and defence, migration and border management, and the EU's role in the world.

Social and employment policies are strongly interlinked with other major policy fields, most importantly the economy, the public health system and education. Social considerations are also part and parcel of all policy fields – also set out in Article 9 of the Treaty on the Functioning of the European Union – and are woven into the fabric of society, directly affecting people's everyday lives. The coronavirus outbreak and lockdown measures have caused major disruption, and exacerbated existing social risks and challenges, such as: an ageing population; rising inequalities between socio-economic groups, generations, genders and regions; new forms of work; and greater polarisation of wages between higher and lower paid workers. This situation is threatening to increase the divergence between Member States, and regions, making achievement of one of the main EU objectives, (upward) social and economic convergence, more difficult. Moreover, it again raises issues around the sustainability of public finances. Therefore, there is an even greater need than before to update the EU's welfare states and labour markets, which implies structural changes in many instances.

Given the complexity of the issues that social and employment policies have to tackle, the EU has a broad range of tools available to design and support the implementation of policies in the Member States. These range from setting minimum standards and targets, and providing policy guidance and funding, to the EU's economic governance mechanism. Beyond the immediate response to the crisis, the EU intends to contribute to nurturing more systemic resilience across the board, to enable Member States to bounce back, or even forward, from shocks in a sustainable way, to preserve the well-being of all of the EU's population.

Close to three quarters of the funding programmes within the multiannual financial framework (MFF) for 2021-2027 and most of the investments through the new instrument, NGEU, can be used to support the implementation of policies that could contribute to the update of welfare states and labour markets. However, due to the relatively small size of the MFF compared to national budgets, its main function is to incentivise transformation and innovation on the ground that – in the longer term – can lead to systemic change. For that reason, the way the MFF, combined with other EU policy tools, shapes both the quantity and quality of spending (i.e. governance mechanisms and institutions on the ground) matters equally. This time, NGEU is designed to give an additional boost to the resources channelled through EU budgetary instruments and strengthen their pull for investment into relevant fields. Both new and old instruments seek to open avenues for increased solidarity among Member States based on common borrowing, and to promote a social investment approach to financing. In addition, through its other policy tools, including setting objectives and targets, the EU can help Member States to develop the necessary structures and institutions that in turn can help them absorb the increased funds more efficiently.

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1. Introduction

According to preliminary results for 2020, gross domestic product (GDP) is projected to drop significantly in all Member States. GDP in the euro area is expected to drop by 7.8 %, while the figure for the EU-27 is expected to be -7.4 %. The European Commission then expects euro-area and EU GDP growth to rebound in the next two years (by 4.2 % and 4.1 % in 2021, and by 3.0 % for both the euro area and the EU in 2022). Most major economies are experiencing the same thing, with significant drops in GDP as a result of the pandemic. Similarly, after several years of positive results, unemployment levels in the euro area and the EU as a whole are projected to increase, before decreasing again in 2022.

To protect the Member States' economies from the economic crisis caused by the pandemic, Member States, the EU institutions and central banks in the EU have engaged in significant support measures. Fiscal measures are reflected in an increased deficit in the forecast, while government debt is on a similar path. Projections for the coming years will depend on a number of variables, including the probability of a third wave of the virus in Member States and of further lockdown measures, the speed of deployment of vaccines (and their acceptance by the population), the presence or absence of geopolitical tensions and, last but not least, the terms of the future relationship between the EU and the United Kingdom.

The main figures reflecting the economic situation in the EU and the euro area, as well as the two-year projections for the main economic indicators are further developed in Section 2.

As in last year's edition, the study goes on to present the EU budget, its nature and its role (Section 3), before providing an overview of the budget for 2021 (Section 4) and the design of EU finances after 2021 (Section 5).

The 2021 budget represents 1.19 % of EU gross national income (GNI) – the €166.06 billion of total payments agreed represents less than half the annual public expenditure of the Netherlands. The commitments adopted for 2021 amount to €164.25 billion. However, Next Generation EU (NGEU), the temporary recovery instrument agreed in the wake of the coronavirus pandemic, will significantly increase the resources channelled through the 2021 EU budget, adding an estimated €285.15 billion in commitments and €75.93 billion in payments. NGEU, part of a broader agreement on EU finances for the 2021-2027 period, will play a major role in addressing the overarching priority of EU spending in 2021: investment in recovery and resilience measures. At the same time, the EU budget will continue contributing to the achievement of other objectives, both traditional and new, in such areas as the green and digital transition, cohesion and agriculture, security and defence, migration and border management, and EU's role in the world.

This year's edition of the study includes a focus on EU social and employment policies in the context of the pandemic (Section 6). First, it explains the impact of the pandemic on EU welfare states and labour markets. Second, it explores existing policy tools, including the EU budget, to design and implement social and employment policies in the EU, and to strengthen the wider social dimension of the EU, as a whole. Finally, it delves into current discussions on whether and how EU social and employment policies combined with the new budget can support the necessary structural changes in the Member States and possible (upward) convergence as opposed to divergence between them.

2. The EU economy

2.1. Overview

Geopolitical tensions and uncertainty regarding the future relationship between the UK and the EU notwithstanding, the defining element influencing the global and EU economy in 2020 was the coronavirus pandemic and the measures taken by Member States to protect their populations.

While the pandemic presented itself as a symmetric shock, affecting the health of individuals across all EU Member States, the magnitude of the economic contractions was uneven across countries. While this was mainly due to structural features of the Member States' economies,[1] differences in the measures adopted to contain the pandemic also played a major role.[2]

While in November 2020 there was finally some good news regarding vaccines, economic recovery is still dependent on several variables, including whether another wave of the virus will force a third lockdown, the time it takes to roll out the vaccine and/or medical treatment, and the willingness of the vast majority of the population to be vaccinated.

In this context, the Commission is projecting negative growth for the European Union (EU) and euro-area economies in 2020, with year-end gross domestic product (GDP) estimations at -7.8 % for the euro area and -7.4 % for the EU-27. The economies should then experience a significant rebound in 2021 (4.2 % for the euro area and 4.1 % for the EU), which will be slightly muted in 2022 (3.0 % for both the euro area and the EU).[3]

The coronavirus crisis put an end to a multi-year streak of positive employment trends: the European Commission estimates that in 2020 unemployment for the euro area will increase to 8.3 % from 7.5 % last year, while the rate for the EU as a whole is marginally better at 7.7 % compared with 6.7 % a year ago. Unemployment is expected to peak in 2021 at 9.4 % in the euro area and 8.6 % in the EU, before retreating to 8.9 % and 8.0 % respectively in 2022.

Another major consequence of the pandemic-induced economic crisis is the extraordinary fiscal interventions at national (and EU) level, with the result that all Member States except Bulgaria are projected to breach the 3 % deficit criterion for 2020: the average general government deficit is expected to reach -8.8 % in the euro area and -8.4 % in the EU for the year. It is expected to decrease progressively over the next two years, the projections being -6.4 % in the euro area and -6.1 % in the EU for 2021; and -4.7 % and -4.5 % respectively for 2022.

The debt-to-GDP ratio is, meanwhile, expected to jump in 2020 from 85.9 % of GDP to 101.7 % for the euro area and from 79.2 % of GDP to 93.9 % for the EU. It is then expected to further increase (albeit very slowly) to 102.3 % and 94.6 % respectively in 2021, and 102.6 % and 94.9 % respectively in 2022.

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[1] For instance, those with economies relying heavily on tourism were more heavily impacted than others.

[2] See, for example the policy contribution 'Why has COVID-19 hit different European Union economies so differently?' by Andre Sapir (Bruegel, September 2020). The author finds that the strictness of lockdown measures, the share of tourism in the economy and the quality of governance all play a significant role in explaining differences in economic losses in different EU countries, while public indebtedness did not.

[3] European Commission European Economic Forecast Autumn 2020, European Economy Institutional Papers, November 2020, pp. 35-46. In the autumn there were also projections published by the International Monetary Fund and the OECD. The projections by the three institutions vary: for example, the OECD estimates that the euro area will rebound by 3.5 % in 2021 and 3.25 % in 2022, while the International Monetary Fund (IMF) respective estimates are 5.2 % and 3.1 %. This can be explained by the fact that their data differ (differing sources and selection at different moments in time) and that their scenarios include different elements and hypotheses.

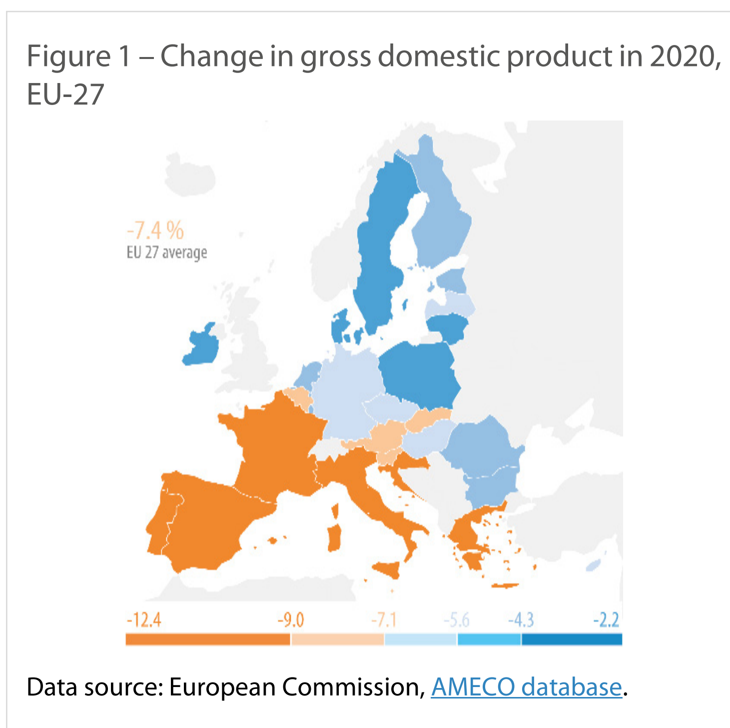
Lastly, inflation for the euro area is projected to reach 0.3 % for 2020, before increasing slightly to 1.1 % in 2021 and 1.3 % in 2022. Similarly, for the EU inflation should hover around 0.7 % for 2020, before increasing to 1.3 % in 2021 and 1.5 % in 2022. To boost inflation, but also to support the economies of the Member States, the European Central Bank continued its asset purchase programme (APP) in 2020, adopted a pandemic emergency purchase programme, and took further accommodative measures (see Section 2.3.2. for more detail).

2.2. Main indicators

2.2.1. Gross domestic product

Europe was among the first world regions to experience a severe outbreak of Covid-19. The escalation of cases during the first wave of the pandemic in February and March led the governments of many Member States to introduce stringent lockdown measures in order to slow the spread of the virus and avoid overwhelming the health sector. By the end of the spring, the outbreak appeared to be under control in most EU countries, leading them to reopen their economies (with varying timing,[4] pace,[5] and sequencing of sectoral reopening),[6] so as to alleviate the unprecedented economic shock generated by the lockdown. With economies reopening, however, the virus started to spread anew, (albeit at a varying pace and intensity in each country), leading to a new round of containment measures, which were relaxed – for some Member States – as of December 2020. As a result, GDP is projected to drop by 7.8 % in the euro area and by 7.4 % in the EU for 2020.[7]

Figure 1 – Change in gross domestic product in 2020, EU-27



Data source: European Commission, AMECO database.

[4] Using the evolution of daily fatalities as an indication of the pandemic's stage, the IMF found that some countries (e.g. Belgium and France) started opening only when the number of daily deaths had declined substantially with respect to the peak. Other countries opened at about the time that fatalities started to decline (e.g. Austria, Germany), or even when they were still on the rise (e.g. Poland). See International Monetary Fund, 'Whatever it takes: Europe's response to COVID-19', Regional Economic Outlook, October 2020.

[5] The authors of the IMF report note that one way of capturing the difference in speed is to compute, for a given sector and at a given date after reopening, the ratio of effective days of reopening to total days of reopening, where effective days are adjusted to take into account the extent of the reopening. As of mid-July, this metric ranged from about 30 % (e.g. Italy and Spain) to above 50 % (e.g. France).

[6] For example, many countries spaced sectoral reopening measures over several weeks, while others chose to open several sectors simultaneously. For example, retail was among the first sectors, with the median country reopening it in the second phase of its overall plan. There has been more variability in the case of schools. In many countries, reopening steps were accompanied by additional health-related measures, such as recommended or mandated use of face masks in some public places, the launch of contact tracing applications, and an expansion of testing.

[7] European Commission 'European Economic Forecast Autumn 2020', European Economy Institutional Papers, November 2020, pp. 35-46.

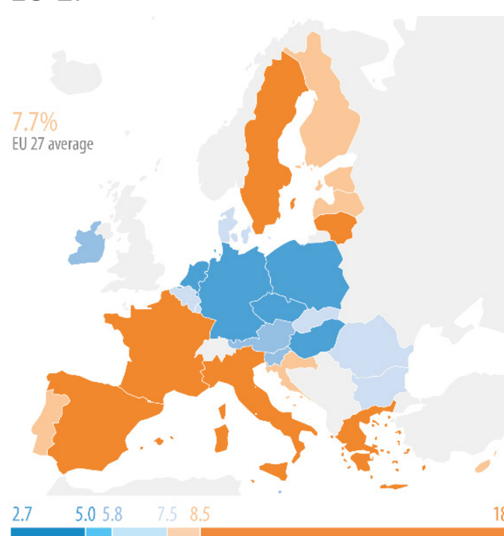
The decline in euro-area real GDP was driven by a decline in private consumption (-8.7 % compared with the year before)[8] and investment (-11.2 %)[9] as well as by a negative contribution from net exports (-11.5 %).[10] The figures for the EU as a whole were a bit less pronounced, with -8.2 % for private consumption, -10.3 % for investment and -11.3 % for exports.[11]

Going forward, private consumption is set to rebound by 4.3 % in 2021 and 3.3 % in 2022 in the euro area. Investment is projected to grow by 6.1 % in 2021 (5.6 % in the EU) and a further 4.2 % in 2022, supported by the accommodative monetary policy of the European Central Bank (ECB), low interest rates and the InvestEU programme[12] (successor to the Investment Plan for Europe).[13] Lastly, exports in the euro area and the EU are forecast to increase by 6.2 % in 2021 and 4.7 % in 2022.

2.2.2. Labour market

A combination of government interventions and limited mobility, but also changing behaviour out of fear of infection, put the brakes on several types of economic activity. This has placed the labour market under strain. The latest projections for the 2020 unemployment rate were 8.3 % for the euro area and 7.7 % for the EU. The various furlough schemes and other supportive policy measures were instrumental in keeping the rise in the unemployment rate moderate (in comparison with the drop in economic activity). These policy measures were supported by the new EU instrument for temporary support to mitigate unemployment risks in an emergency (SURE).[14] Nevertheless, the picture is nuanced: mobility restrictions during the lock-down pushed many unemployed people out of the labour force, as they no longer complied with the requirements necessary to be defined as unemployed.[15] The Commission notes that this change in labour participation affects the relationship between employment and the unemployment rate (the decline in the labour participation rate masks

Figure 2 – Unemployment rate, forecast for 2020, EU-27



Data source: European Commission, AMECO database.

[8] The Commission notes that the uncertainty created by the pandemic affected the behaviour of economic agents and resulted in a collapse of private consumption, which did not match previous recessions, as usually private consumption remains stable.

[9] Companies were prevented from going through with existing spending plans in light of the sudden halt in activity. Moreover, in a similar way to what happened with private consumption, uncertainty led to a 'wait-and-see' approach.

[10] The fall in exports hit some countries much harder than others, as a result of the varying sectoral specialisation of each Member State (e.g. the contribution of services such as tourism to economic growth).

[11] European Commission, ibid.

[12] For more information on InvestEU, see the relevant Commission webpage 'What's next? The InvestEU Programme (2021-2027)'.

[13] For more information on the Investment Plan for Europe, also known as the 'Juncker Plan', see the relevant Council webpage 'Investment Plan for Europe'.

[14] SURE has a support fund of up to €100 billion. At the time of writing, the Council has approved a total of €90.3 billion in financial support for 18 Member States.

[15] Many were not looking for a job during this period as they could not take up a position within two weeks, but were willing to work.

employment losses in the unemployment statistics). Going forward, the Commission notes that the slower reaction of labour markets to a potential economic rebound, the expiry of work schemes, the extent of the use of telework and the speed of reallocation of employees from severely hit sectors to more resilient ones, are all factors expected to contribute to an increase in the unemployment rate, which is expected to peak at 9.4 % in the euro area and 8.6 % in the EU in 2021, before slowly dropping to 8.9 % and 8.0 % respectively in 2022.[16]

Despite being protected by government measures, aggregate labour income is set to decrease in 2020 as many companies defer decisions about employing new staff, or reduce working hours or staff numbers. Some segments of the workforce are likely to be affected more than others, with the incomes of lower-wage earners and younger cohorts showing greater vulnerability to downturns.

Moreover, many workers and firms are still reliant on policy support schemes. As these schemes are withdrawn, many jobs may be put at risk if the economic recovery does not take firm hold. Short-time work schemes have been already extended in a number of countries, though often under stricter conditionality or less generous terms. In view of the latest developments in the pandemic, a further extension of these policies into 2021 is under discussion in most Member States. However, it is expected that these schemes will be discontinued in 2021.

2.2.3. Public finances

National authorities have deployed unprecedented fiscal support to protect workers and businesses from the crisis caused by the pandemic. Measures taken to protect employment and support workers have included expanding health spending, providing direct income assistance, expanding job-retention programmes and strengthening unemployment insurance. To support corporations, governments approved tax deferrals, loan guarantees and direct equity injections. These measures were taken following the activation – for the first time – of the general escape clause of the stability and growth pact in March 2020.[17] As a result, in 2020, fiscal deficits are projected to increase significantly (-8.8 % for the euro area and -8.4 % for the EU). Going forward, deficits are expected to decrease to -6.4 % and -4.7 % for the euro area and -6.1 % and -4.5 % for the EU. This decrease in projected deficits reflects the resumption of economic activity, the winding down of pandemic-related emergency measures, and measures that are expected to be financed under Next Generation EU and its Recovery and Resilience Facility.[18]

The aggregate general government debt-to-GDP ratio was on a declining path between 2014 and 2019, when it reached 85.9 % of GDP in the euro area and 79.2 % in the EU. As a result of the significant measures taken to counter the pandemic in 2020, the debt-to-GDP ratio is projected to rise significantly and reach 101.7 % in the euro area and 93.9 % in the EU. The debt ratio is forecast to grow further (albeit at a slower pace) in 2021 and 2022. For 2021, the figures are forecast to be 102.3 % in the euro area and 94.6 % in the EU as a whole, while the respective numbers for 2022 are forecast at 102.6 % and 94.9 %. Moreover, in 2022, the ratio is forecast to remain above 100 % in seven Member States,[19] while nine more Member States[20] will have debt exceeding the Maastricht debt criterion of 60 % of GDP.[21]

[16] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 46-49.

[17] See Commission press release 'Coronavirus: Commission proposes to activate fiscal framework's general escape clause to respond to pandemic' 20 March 2020.

[18] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 54-56.

[19] Belgium, Greece, Spain, France, Italy, Cyprus and Portugal.

[20] Germany, Ireland, Croatia, Hungary, the Netherlands, Austria, Slovenia, Slovakia and Finland.

[21] European Commission, ibid.

2.2.4. Trade and developments at global level

Following a slowdown in growth at the end of 2019, global trade contracted sharply in the first half of 2020 as a result of measures taken around the world to contain the pandemic. World merchandise trade volumes (excluding the EU) decreased by 0.5 % in 2019, in contrast with increases of 4.2 % in 2018 and 5.9 % in 2017. It is projected to drop by 10.3 % in 2020, before rebounding by 6.3 % in 2021 and 4.1 % in 2022. This relatively muted rebound is likely to be due to persisting disruptions in (and reconfiguration of) global supply chains, rising corporate insolvencies and heightened uncertainty. In Europe, an extra factor weighing on trade developments has been the uncertainty surrounding the UK's exit from the EU and the shape of the future relationship between them, which has resulted in considerable trade volatility and contributed to weak trade data. Already in 2019, the Organisation for Economic Co-operation and Development (OECD) expressed the view that if trade between the UK and the EU were to revert to World Trade Organization terms after 2020, the outlook would be significantly weaker and more volatile than otherwise, particularly in the short term. Such effects could be stronger still if preparations for border arrangements failed to prevent significant delays, or if financial market conditions and consumer confidence were to deteriorate considerably.[22] Such fears were partially assuaged after the Trade and Cooperation Agreement between the EU and the UK was signed on 30 December 2020.[23] However, despite this positive development, the effect on trade between the EU and the UK in the future is still unknown.

The Commission expects global GDP growth (excluding the EU) to contract by around -3.8 % in 2020 as a result of the pandemic shock. Containment measures and increased uncertainty are set to lower private consumption, investment and foreign trade. Going forward, the recovery in private demand and accommodative macroeconomic policies should support the global economic rebound. However, the Commission estimates that elevated unemployment, the possibility of a significant number of insolvencies and the reconfiguration of global supply chains are all likely to moderate growth in the medium term. Thus, the global economy (excluding the EU) is expected to grow by 4.7 % in 2021 and by 3.7 % in 2022.[24]

In **China**, the economic recovery is progressing faster than expected, especially in exports and industrial production, benefitting from an early emergence from the lockdown phase and targeted stimulus. The growth of retail sales and services has also entered positive territory lately together with a sharp rebound in imports, suggesting that the recovery has become broader and more sustainable. At the same time, uncertainty relating to a lasting recovery of external demand and global supply chains looms large, in particular if the US is set to remain committed to trade and technological decoupling.[25] China's GDP is forecast to increase by 2.1 % in 2020 (the only major economy growing) and by 7.3 % in 2021 before growth moderates to 5.6 % in 2022 – reflecting a combination of factors, including China's structural slowdown and softer domestic demand, but also the ongoing effort to render the financial sector less risky.[26]

In contrast to China, GDP growth in **India** is expected to drop by 8.3 % for 2020, as the country was placed under one of the most stringent lockdowns in the world. Unfavourable health and economic

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[22] The OECD estimates suggested that the gross domestic product of the United Kingdom could be 2.0 to 2.5 % lower than otherwise in the first two years if trade shifted to WTO terms and over 0.5 % lower than otherwise in the first two years following trade becoming subject to WTO most-favoured nation terms.

[23] Trade and cooperation agreement between the European Union and the European Atomic Energy Community of the one part, and the United Kingdom of Great Britain and Northern Ireland of the other part, OJ L 444, 31.12.2020.

[24] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 27-32.

[25] See, in this context, Alicia García-Herrero and Junyun Tan, 'Deglobalisation in the context of United States-China decoupling', Bruegel contribution, 21 December, 2020.

[26] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 160-162.

developments and the fact that monetary and fiscal space remains constrained mean that the rebound in real GDP in 2021 and 2022 is likely to be moderate (7.6 % and 5.2 % respectively).[27]

In **Japan**, real GDP growth is forecast to fall by -5.5 % in 2020, reflecting a deep contraction in private consumption in the last three quarters following an increase in the consumption tax and pandemic-related restrictions. At the same time, exports and private investment are expected to decline more moderately, as a result of demand from China and rising spending on information technologies and automation. In 2021, the economy is forecast to grow by 2.7 % but this growth is projected to decelerate to 0.9 % in 2022, as changes in global supply chains are expected to hamper the already weak potential growth outlook.[28]

In **Russia**, growth is expected to drop by -4.2 % in 2020 as a result of the relatively closed and static nature of the economy. Going forward, the Commission notes that a weak investment climate and limited scope for strong consumption growth limit a sharp recovery going forward (current projections hover around 2.0 % for 2021 and 1.9 % for 2022).[29]

In **Brazil**, GDP growth is projected to drop by 6.1 % in 2020, before it gradually recovers to 3.0 % in 2021 and 2.0 % in 2022.[30]

Lastly, after a record-long expansion of more than 10 years, the **United States** economy contracted sharply in the first half of 2020. Overall, real GDP in the US is forecast to decline by 4.6 % in 2020 and to rebound by 3.7 % in 2021 before growth slows to 2.5 % in 2022. Growth is expected to be sustained by fiscal stimulus measures, and by an accommodative monetary policy from the Federal Reserve, which should continue to ensure the provision of favourable financing conditions, but also by household spending, enhanced by precautionary savings accumulated in 2020.[31]

2.3. Inflation and monetary policy

2.3.1. Inflation

Inflation has remained very low, due to the fall in HICP energy prices,[32] the effect of certain tax cuts, and lower services inflation. In the euro area, inflation is expected to have reached 0.3 % in 2020, and to reach 1.1 % in 2021 and 1.3 % in 2022. In the EU as a whole, inflation will be a bit higher, hovering around 0.7 % in 2020, 1.3 % in 2021 and 1.5 % in 2022.[33] Going forward, the Commission projects that inflation should slowly increase, but remain below the objective of 2 %.[34]

2.3.2. Monetary policy

By the end of 2019, preliminary results for the year and two-year projections pointed towards muted growth for the euro area and the EU as a whole. This worsened considerably with the spread of the coronavirus. The ECB's initial decision to tackle the crisis by adding only €120 billion of net purchases in the public sector purchase programme (PSPP) to be concluded in 2020, and some unfortunate

[27] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 28-29.

[28] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 158-160.

[29] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 165-167.

[30] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 28-32.

[31] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 156-158.

[32] According to Eurostat, the harmonised index of consumer prices, abbreviated as HICP, is 'the consumer price index as it is calculated in the European Union (EU), according to a harmonised approach and a single set of definitions. It is mainly used to measure inflation'.

[33] Aggregate rates continue to conceal significant disparities between Member States, with Hungary, Poland and Romania showing the highest inflation for the forecast period (2.5 % to 3.3 % in 2021, 2.4 % to 3.1 % in 2022), and southern European countries showing the lowest.

[34] European Commission 'European Economic Forecast Autumn 2020', op. cit., pp. 50-53.

comments during the press conference in March that the financial markets initially read as a sign of reluctance on the part of the ECB to fully engage in mitigating the unfolding crisis, led to divergences between the sovereign bonds yields of euro-area countries not seen since 2012. This induced the ECB to intervene further by establishing the temporary pandemic emergency purchase programme (PEPP) as separate from – and in addition to – the abovementioned net purchases under the APP, with an envelope of €750 billion, later increased to a total of €1 850 billion.[35]

Alongside the PEPP, on 12 March 2020,[36] the Governing Council also decided to conduct additional longer-term refinancing operations on a temporary basis, under a fixed-rate full allotment procedure, to provide immediate liquidity support for banks and act as a backstop to possible deterioration of money market conditions. On the same date, targeted longer-term refinancing operations (TLTRO) III conditions were further eased, along with a temporary reduction of applicable interest rates (as low as -0.75 %) for all operations outstanding during the period between June 2020 and June 2021. On 30 April 2020, the Governing Council decided to ease TLTRO III conditions for operations further, and to conduct a series of seven pandemic emergency longer-term refinancing operations (PELTROs)[37] to provide liquidity support for the euro area financial system and ensure smooth money market conditions during the pandemic period. At its June TLTRO III operation, banks took up €1.31 trillion of funding, an unprecedentedly high amount.

According to the latest available data,[38] Eurosystem holdings under the programme[39] amount to €2 309 billion for the public sector purchase programme (up from €2 097 billion the year before), €285.8 billion for the covered bond purchase programme (up from €263.2 billion), €243.3 billion for the corporate sector purchase programme (up from €183 billion) and €29.4 billion for the asset-backed securities purchase programme (up from €28.2 billion), for total holdings of €2 867 billion.

Holdings under the PEPP[40] reached €565.6 billion in September 2020. At its September 2020 meeting,[41] the ECB confirmed that it would continue its asset purchases under the pandemic emergency purchase programme (PEPP), until at least the end of June 2021 and, in any case, until the Governing Council judged that the coronavirus crisis phase was over.

In addition to the above, the swift implementation of macroprudential policies has provided capital and liquidity relief for banks to strengthen their conditions. The ECB banking supervision allowed banks to operate temporarily below both the level and quality of capital required under 'Pillar 2'. The ECB also allowed flexibility in the classification and provisioning of loans backed by public support measures. These temporary measures were enhanced by the appropriate relaxation of macroprudential requirements, with national authorities either releasing countercyclical capital buffers or revoking previously announced increases. Together with the restrictions on dividend

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[35] The eligibility criteria for the PEPP are the same as under the corresponding programmes that constitute the asset purchase programme (APP). In addition to the asset categories eligible under the APP, the programme includes a waiver of the eligibility requirements for securities issued by the Greek government. It further shortens the minimum eligible remaining maturity to 70 days (the maximum eligible remaining maturity remains at 30 years and 364 days). Non-financial commercial paper is also now eligible for purchases under both this programme and the corporate sector purchase programme (CSPP).

[36] European Central Bank, press release, 'ECB announces measures to support bank liquidity conditions and money market activity', 12 March 2020.

[37] European Central Bank, press release, 'ECB announces new pandemic emergency longer-term refinancing operations', 30 April 2020.

[38] October 2020 data.

[39] See the dedicated webpage of the European Central Bank.

[40] European Central Bank 'Pandemic emergency purchase programme (PEPP)' webpage.

[41] European Central Bank 'Meeting of 9-10 September 2020' webpage.

distribution and share buybacks, this has helped to reduce the impact of the crisis on banks and has supported lending to the real economy.[42]

Under these conditions, bank lending to the real economy continued in 2020, despite the pandemic. More specifically, credit to households in the euro area increased by 1.5 % in 2020 (1.2 % in the EU) and its increase is projected to be stronger in 2021 (3.0 % and 2.4 % respectively) and 2022 (3.2 % and 2.7 %). As for loans to non-financial corporations, they are expected to have increased by 4.1 % for the euro area and 3.5 % for the EU in 2020, and to increase by 2.4 % in 2021 and 3.7 % in 2022 for both the euro area and the EU as a whole.

Lastly, the euro appreciated versus safe-haven currencies such as the Japanese yen, the US dollar and the British pound,[43] as well as against emerging currencies.

2.4. Going forward

2.4.1. Potential risks

Among the several factors that may influence the economies of the EU Member States over the forecast period, four stand out:

1 The *timing and phasing out* of current support measures. On one hand, fiscal policy support was meant to be provided temporarily, so as not to lead to the zombification of the economy (unviable firms kept alive).[44] On the other, given the significant development and logistical challenges inherent in deploying a vaccine, many Member States will probably have to face another wave of infections and therefore another lockdown. In this context, a premature scaling back of fiscal support could drag companies back into recession, damaging economies and undoing much of what has been achieved so far.[45]

2 *Mass insolvencies* in Member States, despite governments' support measures. While large-scale bankruptcies have not yet materialised, because of the significant support afforded to the private sector, the longer-than-previously expected duration of containment measures is most probably going to impact negatively on companies' balance sheets. A wave of corporate bankruptcies would generate a loss of wealth, productive capacity and firm-specific human capital. Furthermore, the link between SMEs and banks in Europe means that a wave of bankruptcies could lead to one or several banking crises.

3 Ongoing *weak bank profitability* and increasing non-performing loans. This may hamper banks' capacity to support lending to the real economy in the months ahead; coupled with increased risk-taking, potentially undermining financial stability.[46]

4 The *relationship between the United Kingdom and the EU* following the UK's exit from the EU. While the EU-UK Trade and Cooperation Agreement cannot match the level of economic integration that existed while the UK was an EU Member State, it goes beyond a traditional

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42 International Monetary Fund 'Whatever it takes: Europe's response to COVID-19' Regional Economic Outlook, October 2020.

43 The Commission notes that the appreciation of the euro versus the dollar and the yen is due to three main factors: the increase in market confidence in the recovery of the euro area economy, the broad weakening of the US dollar in the context of the accommodative measures by the Federal Reserve, and the improved global climate, which reduced the safe-haven demand for the dollar and the yen. As for the appreciation versus the pound, it seems to be attributable to the uncertainty about the future trading relationship between the EU and the UK.

44 See Luc Laeven, Glenn Schepens and Isabel Schnabel, 'Zombification in Europe in times of pandemic', VoxEU, 11 October 2020.

45 The IMF notes, for example, that abruptly ending job-retention programmes would be highly damaging for the millions of workers and families that have benefited from them.

46 European Central Bank 'Financial Stability Review', November 2020. See also the contributions by Nicolas Veron 'Banks in pandemic turmoil' and by Alexander Lehmann 'The impact of the crisis on smaller companies and new mechanisms for non-performing loans' Bruegel, March and July 2020 respectively.

free trade agreement. Given that last year's forecasts were prudent and, as such, based their projections on most-favoured-nation rules, the economic activity between the EU and the UK from 2021 onwards might be higher than projected.

5 The time it takes to *implement Next Generation EU* and, in particular, its centrepiece – the Recovery and Resilience Facility. An ambitious and swift implementation of Next Generation EU over the forecast years could provide a significant boost to economic recovery.

2.4.2. Potential ways to mitigate the impact of the above risks

Both the International Monetary Fund (IMF) and the OECD are in favour of central banks keeping their accommodative monetary policies in place to support the recovery, and possibly enhancing them if the economic weakness deepens, or appears likely to persist for longer than expected.[47]

Similarly, banking supervision authorities should continue applying regulatory flexibility so as to allow banks to continue providing the real economy with credit. On the other hand, the authorities should address the increasing fragility of bank balance sheets and adjust the pace at which banks' capital relief measures are wound down.

To support workers, alongside job retention schemes, in its outlook the OECD proposes substantial additional investments in active labour market programmes, including employment services to help jobseekers find jobs, and enhanced vocational education and training, so as to create new opportunities for displaced workers, lower-skilled workers, and those on reduced working hours. In addition to those investments, enhanced childcare provision and adequate income protection for vulnerable groups should be built into policies in order to enhance participation, and make the labour market more inclusive.[48]

To avoid a wave of corporate bankruptcies, the IMF suggests in its outlook,[49] that Member States provide further support for 'systemic' firms, through equity injections or junior claims, with appropriate conditionality and safeguards to limit moral hazard.[50] The OECD reflects on the possibility of extending the maturity of loan guarantees, or converting pandemic-related public support into public equity stakes, at the same time ensuring conditional exit strategies for such investments. Furthermore, they are of the view that some assistance could also be made state-contingent, with repayments (or deferred payments) beginning only once profits are returned. To meet the funding needs of SMEs, the OECD is of the view that it might be worth exploring the option of converting government (crisis-related) loans into grants, conditional on the funding being used to cover operating expenses.

Exceptional crisis-related policies need to be accompanied by the structural reforms most likely to boost opportunities for displaced workers and improve economic dynamism, fostering the reallocation of labour and capital resources towards sectors and activities that strengthen growth, enhance resilience and contribute to environmental sustainability. In addition to national efforts, the OECD is of the view that stronger international cooperation remains necessary to help end the pandemic more quickly and speed up the global economic recovery.

[47] OECD Economic Outlook, Vol. 2020(2): Preliminary version, OECD Publishing, December 2020.

[48] OECD Economic Outlook, ibid.

[49] International Monetary Fund, 'Whatever it takes: Europe's response to COVID-19', op. cit. pp. 24-27.

[50] The authors of the forecast note that 'In the case of SMEs, taking equity stakes by the government is more challenging because of the large number of SMEs, and the difficulties related to implementation and governance. Consideration could be given to strengthen SMEs' capital structure with the use of hybrid capital (i.e. preferred capital, subordinated loans) and debt restructuring (including the conversion of an amount of guaranteed loans)'.

2.5. In-focus: the coronavirus pandemic

The coronavirus pandemic has caused a global collapse in activity and loss of jobs that is probably unprecedented in its scale and speed. Small and large businesses across most countries in the world have had to close their doors to customers and employees. The sharp accompanying fall in firms' revenues and households' incomes will result in the first global recession since 2009. It will also present the global financial system with its largest stress event at least since the global financial crisis.[51] Contrary to the global financial crisis, however, the EU's response has been quick and multi-pronged.

To limit the economic damage during confinement, Member States' governments put broad programmes in place to support companies (to avoid bankruptcies), and workers (to dampen income losses and avoid a surge in unemployment), as well as measures to avoid a financial meltdown. In total, more than €3.3 trillion had been mobilised at national and EU level by the end of April 2020[52] to respond to the economic consequences of the coronavirus pandemic.

Member States' measures have been complemented by action at EU level. This includes the following: the activation of the stability and growth pact's general escape clause so as (temporarily) to give national governments greater flexibility to adopt counter-cyclical budgetary measures for their economies; the related simplification of information requirements for the 2020 cycle of the European Semester; the adoption of a temporary framework for State aid measures to accelerate public support for companies; a banking package (targeted amendments to the prudential rules and an interpretative communication) to facilitate lending to households and businesses.

Three additional 'safety nets' were put in place in April 2020. The first, SURE, was a new €100 billion initiative aimed at protecting employment in the EU by supporting efforts to mitigate unemployment risks during the pandemic emergency period. The aim was to cover some of the costs of national public programmes allowing firms to reduce working hours, while at the same time providing income support.[53] The second safety net was the creation by the European Investment Bank of a €25 billion pan-European guarantee fund to protect companies in the EU. The fund is expected to generate up to €200 billion in loans throughout the EU, primarily for SMEs. Lastly, in the euro area, the Eurogroup established that assistance under a precautionary credit line of the European Stability Mechanism (ESM) (based on the enhanced conditions credit line) would be available to any euro area Member State,[54] to be used for covering costs relating to direct and indirect healthcare, and cure and prevention relating to the pandemic crisis. The precautionary credit line allows precautionary financial assistance of up to 2 % of 2019 GDP to be granted to a requesting Member State, as a benchmark. To obtain access to the credit line, Member States must remain committed to strengthening their economic and financial fundamentals, once the crisis subsides.[55]

Another difference with the global financial crisis is that, this time, in contrast, the financial system has remained (at the time of writing) strong and stable and has played a key role in providing

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[51] On the economic aspect, see Charles Wyplosz, 'The Euro Area After COVID-19', in-depth analysis requested by the ECON committee of the European Parliament, November 2020.

[52] See, for example, Luke Hurst, 'EU agrees massive aid package of immediate support for member states', Euronews, 24 April 2020.

[53] For more information, see Alessandro D'Alfonso 'Temporary support to mitigate unemployment risks in an emergency (SURE)' EPRS, European Parliament, 15 April 2020.

[54] Non-euro area Member States can access the Balance of Payments Facility.

[55] For more information on ESM pandemic crisis support, including the instrument's features, eligibility, pricing and financial conditions and surveillance, see the briefing by Alice Zoppè and Cristina Dias, 'The ESM Pandemic Crisis Support' Economic Governance Support Unit of the European Parliament, August 2020.

companies and households with credit during the pandemic. This is due in great part to the regulatory initiatives as well as to the actions taken by financial institutions in the key areas of capital, liquidity and leverage. Nevertheless, it will be important once the crisis abates to focus research and potentially regulation on examining whether there are areas not covered by regulation where risk has increased. In specific areas, looking for 'fault lines' can include monitoring market-based finance,[56] conducting wider stress tests, and carefully assessing the potential and challenges of financial innovation.[57]

The pandemic may shape Member States' economies for long after it is over. By way of example, it may affect the structure of the economy by increasing the time spent working from home. Indeed, researchers have estimated that approximately a third of jobs in the United States, accounting for 44 % of all wages, could plausibly be performed from home.[58] This in turn will probably affect the commercial and residential property markets.

The economic downturn caused by the current pandemic has substantial implications for gender equality. In contrast with 'normal' recessions, which tend to affect men's employment more severely than women's employment, the drop in employment relating to social distancing measures has had a major impact on sectors with high female employment shares.[59] In addition, closures of schools and day-care centres have massively increased childcare needs, with a particularly large impact on working mothers.[60]

In addition, there appear to be important age inequalities, too: the International Labour Organisation,[61] for instance, argues that young people have been 'disproportionately affected' by the pandemic, which has disrupted their education and training, and forced them out of work.[62]

For this reason, there will be a need to reflect on what labour policies are necessary to help those people who were worst affected.

Given that the pandemic affected not just one sector but many, there have been calls[63] to extend stress testing from the financial sector to the wider business sectors, to assess the health of the economy, estimate the duration and time it will take to exit support programmes and prevent a wave of bankruptcies and major bailouts.[64]

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56 Including asset managers, hedge, investment and money market funds.

57 J. Giese and A. Haldane, 'COVID-19 and the Financial System: A Tale of Two Crises', *Oxford Review of Economic Policy*, 2020, pp. 200-214.

58 J. Dingel and B. Neiman, 'How many jobs can be done at home?', *Journal of Public Economics*, September 2020. The authors note, however, that there is significant variation in this percentage across cities and industries, '…whereas most jobs in finance, corporate management, and professional and scientific services could plausibly be performed at home, very few jobs in agriculture, hotels and restaurants, or retail could be'.

59 Relatively more men work in industries heavily affected by a 'standard' downturn (such as manufacturing and construction), while women's employment is concentrated in less cyclical sectors such as health care and education. In contrast, the current crisis is having a major impact on service occupations with high female employment shares, such as restaurants and hospitality.

60 See T. Alon, M. Doepke, J. Olmstead-Rumsey and M. Tertilt, 'The impact of Covid-19 on gender equality', NBER working papers, April 2020. Also, A. Sevilla and S. Smith, 'Baby steps: the gender division of childcare during the COVID-19 pandemic', *Oxford Review of Economic Policy*, Vol. 36 (Supplement), 2020, pp. 169-186.

61 ILO, 'ILO Monitor: Covid-19 and the World of Work', International Labour Organization, published online, regularly updated.

62 At the time of the ILO survey (May 2020), one in six young people surveyed had stopped working since the start of the pandemic crisis.

63 J. Giese and A. Haldane, 'COVID-19 and the Financial System: A Tale of Two Crises', op. cit., pp. 200–214.

64 M. Johnstone-Louis, B. Kustin, C. Mayer, J. Stroehle and B. Wang, 'Business in Times of Crisis', *Oxford Review of Economic Policy*, Vol. 36 (Supplement), 2020, pp.242–255.

Some have pointed to the fact that, despite the fact that the pandemic has created a global medical crisis and that many of the tasks involved in controlling an infectious disease like Covid-19 are global public goods, there has been no effective global cooperation to tackle the crisis,[65] in contrast to what happened during the global financial crisis of 2007-2008. There have been calls for the G-20 to take the lead in this and future pandemics.

The pandemic could also become an opportunity to tackle other emergencies that are in some ways similar, such as **climate change**,[66] provided there is clear public support. This is already the case at EU level with the European Green Deal and the discussion on how to finance it, but it is a good moment to reflect on whether more can and should be done at national level too. The discussion should not be reduced to fiscal measures but be comprehensive and take into consideration what changes to human habits and behaviours could help with reaching this goal.[67]

The pandemic has increased public awareness of the extent to which the economy relies on a low-wage workforce.[68] Given that many of these occupations are also heavily dependent on migrant workers, this is likely to have substantial implications for **immigration** policies.[69]

Lastly, the pandemic has had an impact on **international trade**. There have therefore been calls[70] to reinvigorate and strengthen existing trade institutions.

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[65] See, among others, G. Brown and D Susskind, 'International Cooperation during the COVID-19 Pandemic', *Oxford Review of Economic Policy*, 2020, pp. 64–76.

[66] See C. Hepburn, B. O'Callaghan, N. Stern, J. Stiglitz and D. Zenghelis, 'Will COVID-19 Fiscal Recovery Packages Accelerate or Retard Progress on Climate Change?', *Oxford Review of Economic Policy*, Vol. 36 (Supplement), 2020, pp. 359–381. The authors note the pandemic and climate change are in a way similar, in that they 'Both involve market failures, externalities, international cooperation, complex science, questions of system resilience, political leadership, and action that hinges on public support. Decisive state interventions are also required to stabilize the climate, by tipping energy and industrial systems towards newer, cleaner, and ultimately cheaper modes of production that become impossible to outcompete'.

[67] Mention could be made in this context of the creation of several bike paths in major cities, enabling people to avoid having to use public transport.

[68] For instance, delivery drivers, food producers and supermarket staff have been recognised as 'essential' workers in the current context.

[69] M. Fernández-Reino, M. Sumption and C. Vargas-Silva, 'From Low-skilled to Key Workers: The Implications of Emergencies for Immigration Policy', *Oxford Review of Economic Policy*, 2020, pp. 382–396.

[70] See, for example, B. Demir and B. Javorcik, 'Trade Finance Matters: Evidence from the COVID-19 Crisis', *Oxford Review of Economic Policy*, 2020, pp. 397–408.

3. The EU budget in perspective

The EU budget represents a limited share of public spending in the European Union, but it has features that can increase its impact. The challenges emerging in recent years have widened the debate on the budget's role and its possible reform.

3.1. Size and role of the EU budget

Amounting to €163.9 billion in 2019,[71] the EU budget accounted for around 1 % of EU-28 gross national income (GNI).[72] The same year, Member States' public spending represented, on average, 46 % of their GNI, a share that is expected to increase in the wake of the coronavirus pandemic, owing to the resulting recession and increased public spending to mitigate its impact.

Before the outbreak of the pandemic, the EU budget represented some 2 % of total public spending in the European Union (see Figure 3), reflecting the fact that spending competences and resources in most policy areas lie mainly at national and/or local levels. These data show a situation very different from that of federal entities, where federal spending usually represents some 50 % at least of final public spending (or 15 to 20 % of gross domestic product) in decentralised models, such as the United States (US).[73]

Figure 3 – EU budget and general government expenditure in the EU (2019, € billion)

Data source: European Commission (DG Budget and Eurostat) data. Eurostat data are provisional.

Analysts[74] note that, to date, the EU budget has played two of the three functions that economic theory traditionally attributes to public finance: the provision of public goods (e.g. promotion of research and innovation activities), and some redistribution of resources to reduce disparities,[75] in line with the objectives of economic, social and territorial cohesion between EU regions enshrined in the Treaty on the Functioning of the European Union (TFEU).[76] These two functions are not mutually exclusive, since a policy area with redistributive objectives, such as cohesion, can also provide public goods.

Studies often draw attention to the relatively small size of the EU budget, concluding that this and other features limit its overall capacity to provide public goods and to play a redistributive role. For

[71] The consolidated annual accounts of the EU for financial year 2020 are expected to be made available in June 2021.

[72] As of 2021, this percentage is expected to increase above 1 % of EU-27 gross national income (GNI), following the adoption of a new multiannual framework and a temporary recovery instrument as well as the withdrawal of the UK from the Union. In 2021, the authorised EU budget (payments) represents 1.19 % of EU GNI (See Chapter 4), excluding expenditure financed by the Next Generation EU recovery instrument.

[73] C. Cottarelli and M. Guerguil (eds.), *Designing a European Fiscal Union. Lessons from the experience of existing federations*, Routledge, 2015. The authors examine the budgetary arrangements between the central and subnational levels of government in a sample of 13 federations (all those with a nominal gross domestic product higher than US$400 billion in 2011).

[74] A. Bénassy-Quéré, X. Ragot and G. B. Wolff, Which Fiscal Union for the Euro Area?, Les notes du conseil d'analyse économique, No 29, February 2016.

[75] The third function, which has not been covered so far by the EU budget on account of its size and limited flexibility in the context of multiannual planning, is macroeconomic stabilisation. A new temporary recovery instrument, Next Generation EU, is to play this function to a certain extent as of 2021.

[76] Part Three, Title XVIII, TFEU.

example, one paper[77] estimates that the annual redistribution of resources operated by the EU budget over the last 15 years corresponds to 0.2 % of the area's GNI,[78] as compared with 1.5 % for the federal budget in the US. In other words, in the EU 80 % of resources are returned to the Member State that provided them.

In December 2020, the adoption of an unprecedented budgetary package for the years 2021 to 2027 brought new momentum to the EU budget. A major innovation will be the launch of a temporary recovery instrument, Next Generation EU (NGEU), to be financed through resources borrowed on the markets by the Commission on behalf of the EU (see Sections 3.2 and 5.2). This collective borrowing represents more than 5 % of EU GNI.[79]

Therefore, NGEU will increase significantly the resources channelled through EU budgetary instruments in the first part of the programming period, with a view to helping the EU and national economies recover and become more resilient. In this respect, the EU budget will for the first time contribute to a certain extent to macroeconomic stabilisation, although this role mainly remains with the monetary policy of the European Central Bank and national budgets.[80]

In any case, even without considering the temporary recovery instrument, the role that the EU budget can play in the economy, and the achievement of EU policy objectives on account of a number of its characteristics, should not be underestimated. Examples include the share of the EU budget devoted to investment (as compared with national budgets, where most resources are usually allocated for consumption and transfers), and its capacity to leverage complementary sources of financing (e.g. through innovative financial instruments) and to achieve advantages such as economies of scale in policy areas where the pooling of resources at EU level may help to meet objectives more effectively (e.g. in the field of development cooperation with third countries).

In some countries, the EU budget may represent a significant source of resources for investment.[81] For example, in 15 Member States, mainly among those that joined the European Union after April 2004, the EU budget, as a share of total public spending, is significantly higher than 2 %, with figures ranging between 4.47 % for Slovenia and 11.75 % in Latvia (Figure 4).[82]

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[77] P. Pasimeni and S. Riso, The redistributive function of the EU budget, IMK – Hans-Böckler-Stiftung, Working Paper No 174, November 2016.

[78] In recent years, the figure has reached 0.3 % as a result of increasing diversity in the EU, determined on the one hand by the accession of 13 Member States with lower per capita income as of 2004, and on the other by growing divergence in economic performance and unemployment rates following the financial and economic crisis.

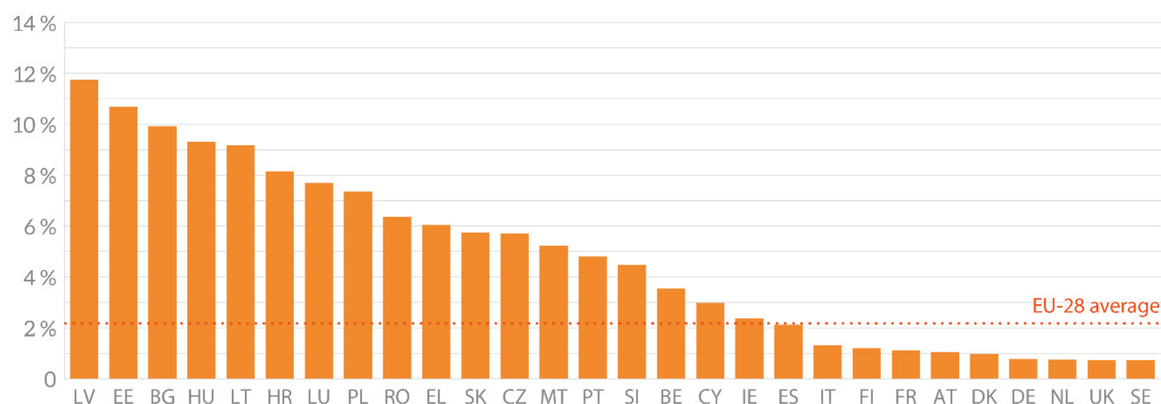
[79] A. D'Alfonso, Next Generation EU: A European instrument to counter the impact of the coronavirus pandemic, EPRS, European Parliament, July 2020.

[80] L. Codogno and P. van den Noord, Assessing Next Generation EU, Luiss School of European Political Economy, Working Paper 9/2020, 30 November 2020.

[81] While the European Commission publishes the allocation of expenditure to Member States, it underlines that this is only an accounting exercise, which does not provide a complete overview of the benefits that each Member State derives from EU membership: Annex 1 recapitulates this allocation for each major category of EU spending in 2019.

[82] The group also includes some pre-2004 Member States. For example, the case of Luxembourg (7.69 %) is mainly explained by the size of the country, its role as host to a number of EU institutions, and the administrative expenditure attributed to the country on this basis. As for the EU budget, the graph does not include either spending in countries outside the EU or spending that could not be attributed to individual Member States. In 2019, this figure amounted to €24.5 billion.

Figure 4 – EU budget as a share of public spending in individual Member States (2019)



Source: EPRS, based on European Commission (DG Budget and Eurostat) data. Eurostat data are provisional.

In addition, when focusing on investment only, the contribution of the EU budget to public investment in the Union is higher: according to the European Commission, for the 2015-2017 period, cohesion policy alone represented 8.5 % of government capital investment in the EU. On average, this share was estimated at 41 % in the 13 Member States that joined the Union after April 2004.[83] As regards investment in research and innovation, Horizon 2020 (2014-2020) was the world's largest transnational programme devoted to such activities: in 2019, the largest recipients were Germany, France, the United Kingdom (at the time still part of the EU), the Netherlands, and Belgium (in decreasing order according to the total amount beneficiaries located in their territories received from the programme).

From this perspective, the European Commission and the European Parliament stress[84] that the EU budget is different in nature and function from national budgets, since it is mainly an investment budget with a focus on measures with European added value. The new multiannual financial framework (MFF), which defines the EU's budgetary structure for the 2021 to 2027 period, seeks to further concentrate resources on such measures, in line with the debate that characterised the preparation of relevant proposals and brought about their adoption.

Co-financing is a characteristic of the EU budget that can increase its impact on job creation and growth. This means that EU spending is normally used in conjunction with funding from other public and/or private sources, thus resulting in total investments higher than the EU contribution proper. To some extent, this is already the case for traditional grants. In addition, with a view to maximising the 'multiplier effect' of the EU budget, innovative financial instruments (triggering equity, quasi-equity, debt or guarantee funding) have been developed to support economically viable investments in line with EU objectives.

While innovative financial instruments are not appropriate for all kinds of public spending, they have features that make them attractive for some policy areas and objectives, notably by: attracting additional funding from other sources (leverage effect); and generating income through amounts repaid by beneficiaries of funding that can be used for new operations in line with the same policy objectives (revolving nature of the instruments). The leverage effect can vary significantly from one instrument to another.

[83] Seventh report on economic, social and territorial cohesion, European Commission, 9 October 2017, p. xxii.

[84] The added value of the EU budget, (SEC(2011) 0867), staff working paper, European Commission 29 June 2011; European Parliament, Resolution on the multiannual financial framework and own resources, 13 June 2012; Reflection paper on the future of EU finances, (COM(2017) 358), European Commission, 28 June 2017.

As regards the 23 financial instruments covering internal policies, the European Commission reports that, by the end of 2019, EU contributions worth over €10 billion had triggered just under €100 billion in total financing provided by financial intermediaries for final recipients. These data suggest average leverage close to a factor of more than 9, i.e. each euro invested by the EU has generated on average more than €9 of financial support for final beneficiaries. Over the 2014-2019 period, more than 600 000 small and medium-sized enterprises (SMEs) are reported to have received funding thanks to these 23 financial instruments.[85]

The High-Level Group on Own Resources notes that, based on a study[86] it commissioned, wealthier Member States have a comparative advantage when it comes to attracting resources linked to the main financial instruments.[87] Therefore, the distribution of such resources differs from that in traditional EU spending areas (e.g. cohesion and agriculture). The leverage effect and evolving nature of these instruments mean that the standard representation of the allocation of EU expenditure to Member States (see Annex 1) provides only a partial picture of the overall benefits deriving from the EU budget and EU membership.

In some policy areas, the pooling of resources at EU level may bring advantages such as economies of scale and elimination of duplication, generating EU added value and enabling a more effective achievement of results. An EPRS study analysed budgetary benefits and cost savings (such as the additional provision of public goods, efficiency gains, and lower administrative costs) that Member States can realise by means of funding policies and programmes with EU added value at EU rather than national level. Applying a new methodology for assessing the 'waste rate' in overlapping national spending to four case studies (on health, climate change, social insurance and defence), the study concludes that €180 billion per year could be saved by Member States through improved allocation of budgetary resources in these policy areas.[88] Another example is development cooperation, in which the OECD deems EU programmes to have comparative advantages thanks to their geographic reach, scale and scope.[89] The EU, with its Member States, is the world's biggest development aid donor. However, in addition to EU programmes, Member States channel development assistance by means of other schemes. According to the mapping the cost of non-Europe exercise carried out for the European Parliament, improved coordination of EU donors could bring economic benefits worth between €3.6 billion and €14.5 billion per year – with a mid-point estimate of €9 billion – including both direct savings and better results in recipient countries.[90] Other policy areas often deemed to have great potential for enhanced joint action include: digital infrastructure and its protection, external borders and asylum management.[91]

In conclusion, the EU budget is relatively small in size, but has features that can reinforce its overall impact. It has changed over time, but its reform has advanced rather slowly due to the procedures for the adoption of its financing system and multiannual planning tool, which require unanimity in

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[85] Draft General Budget of the European Union for the financial year 2021: Working Document X (COM(2020) 300), European Commission, June 2020. For more detail on the advantages and challenges of financial instruments, see: Implementing the EU budget through financial instruments – lessons to be learnt from the 2007-2013 programme period, European Court of Auditors, (Special Report No 19/2016); and J. Núñez Ferrer et al., Financial instruments: defining the rationale for triggering their use, Policy Department for Budgetary Affairs, European Parliament, October 2017.

[86] J. Núñez Ferrer, J. Le Cacheux, G. Benedetto and M. Saunier, Study on the potential and limitations of reforming the financing of the EU Budget, 3 June 2016, CEPS, Université de Pau et des Pays de l'Adour, LSE Enterprise and Deloitte.

[87] Future financing of the EU: final report and recommendations, High-Level Group on Own Resources, December 2016.

[88] J. Saulnier, Improving the quality of public spending in Europe: Budgetary 'waste rates' in EU Member States, EPRS, European Parliament, 2020.

[89] European Union – DAC Peer Review of Development Cooperation, Organisation for Economic Co-operation and Development, 2012.

[90] Europe's two trillion euro dividend: Mapping the Cost of Non-Europe, 2019-24, EPRS, European Parliament, 2019.

[91] J. Pisany-Ferry, 'Europe can take a bigger role in providing public goods', *Financial Times*, 3 December 2019.

the Council (see Section 3.3). The outbreak of the coronavirus pandemic and its severe socio-economic consequences across the EU led to a change of pace in the negotiations on EU finances for 2021-2027 (see Section 3.4). The result was the adoption of a package dubbed unprecedented by various analysts, who nevertheless see room for further reform.[92]

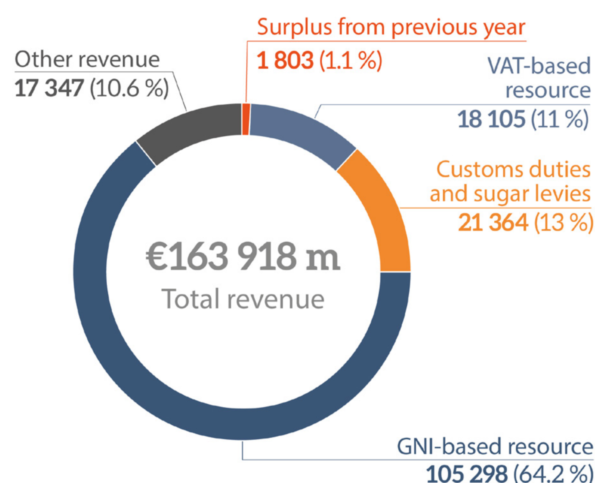
3.2. Structure of the EU budget: Revenue, multiannual planning and recovery instrument

The 'own resources' system sets out how the EU budget is financed, while the structure of the expenditure side of the budget is determined, for a period of at least five years, by a multiannual planning tool – the multiannual financial framework (MFF).

Unlike national budgets, the EU budget cannot run a deficit. Its financing has so far been ensured[93] by three main sources of revenue: traditional own resources (customs duties and sugar levies); an own resource based on a harmonised base of value added tax (VAT); and an own resource linked to Member States' GNI, which plays the role of balancing the budget.[94] The maximum level of resources available for the EU budget is set at 1.20 % of EU GNI (the 'own resources ceiling', which has remained virtually unchanged since the 1990s).

Adopted by the Council in December 2020, the new own resources decision[95] will introduce a series of important changes to the system to be applied retroactively as of 1 January 2021 once the decision is ratified by all Member States. In particular, the own resources ceiling will rise permanently from 1.20 % to 1.40 % of EU GNI to take account of developments such as the smaller total GNI of the post-Brexit EU and the uncertain economic outlook owing to the pandemic. In addition, the Commission will be allowed to borrow on the markets at favourable interest rates on behalf of the EU to finance Next Generation EU (NGEU). The sole purpose of the temporary recovery instrument will be to address the consequences of the pandemic crisis. A temporary increase in the own resources ceiling, worth a further 0.60 % of EU GNI, will be devoted exclusively to guaranteeing borrowing operations for NGEU and apply until December 2058 at the latest. A new own resource based on non-recycled plastic waste will be introduced as of 2021.

Figure 5 – EU revenue in 2019



Data source: European Commission, see Annex 2.

Currently, the bulk of revenue is provided by a GNI-based resource and a VAT-based resource, which Member States perceive as national contributions rather than EU own resources. In 2019, these two resources jointly accounted for around three quarters of EU financing (see Figure 5). According to a number of analysts and stakeholders, including the European Parliament, the predominant role of

[92] See for, example, F. Jones, Financing the European Union, EPRS Ideas Papers, European Parliament, December 2020; and J. Núñez Ferrer, Reading between the lines of Council agreement on the MFF and Next Generation EU, CEPS, Policy Insights 2020/18, July 2020.

[93] Council Decision of 26 May 2014 on the system of own resources of the European Union (2014/335/EU, Euratom).

[94] Other revenue, which is not classified as own resources, includes tax on EU staff salaries, contributions from non-EU countries to certain programmes, and fines on companies for breaching competition law.

[95] Council Decision (EU, Euratom) 2020/2053 of 14 December 2020 on the system of own resources of the European Union and repealing Decision 2014/335/EU, Euratom.

national contributions promotes a focus in budgetary negotiations on Member State net balances and programmes with geographically pre-allocated expenditure. In the MFF negotiations, Parliament managed to obtain a roadmap for the introduction of other new own resources in addition to the one linked to non-recycled plastic waste that has already been agreed (see Section 5.3).

With the withdrawal of the United Kingdom from the EU, the permanent correction mechanism (the UK 'rebate')[96] that reduced its contributions to the EU budget has been eliminated. For the 2021-2027 period, five Member States (Austria, Denmark, Germany, the Netherlands and Sweden) will enjoy temporary lump-sum corrections reducing their contributions, once the new own resources decision is ratified and starts to apply retroactively. Annex 2 recapitulates national contributions by Member State and traditional own resources collected on behalf of the EU in 2019.

As for the expenditure side of the budget, the 2021-2027 MFF[97] sets the maximum level of resources ('ceiling') for each major category ('heading') of EU spending for a period of seven years. The MFF resources for commitments over the entire 2021 to 2027 period amount to €1 074.3 billion in 2018 prices. Negotiated between 2018 and 2020, the new MFF is complemented by the NGEU recovery instrument to address the consequences of the coronavirus pandemic (see Sections 3.4 and 5.2). Worth €750 billion in 2018 prices, this major innovation in EU finances will provide a mix of grants (€390 billion) and loans (€360 billion) over the 2021-2023 period: grants will increase the size of the EU budget as external assigned revenue (see Chapter 4), while resources borrowed to finance loans are transferred directly to Member States through a EU budgetary instrument.

Figure 6 shows the distribution of MFF and NGEU resources among the seven major categories of EU spending.[98] The MFF details the annual ceilings for new commitments in each spending category and an overall ceiling for annual payments. In addition, it contains some special instruments outside the MFF ceilings (the European Globalisation Adjustment Fund, the Solidarity and Emergency Aid Reserve, the Brexit Adjustment Reserve, and the Flexibility Instrument) and flexibility provisions, to give some room for manoeuvre in case of unexpected events (see Section 5.1.4). The challenge is to strike the right balance between predictability of investments and the capacity to address the unforeseen events and new priorities that can emerge during a rather long programming period.[99]

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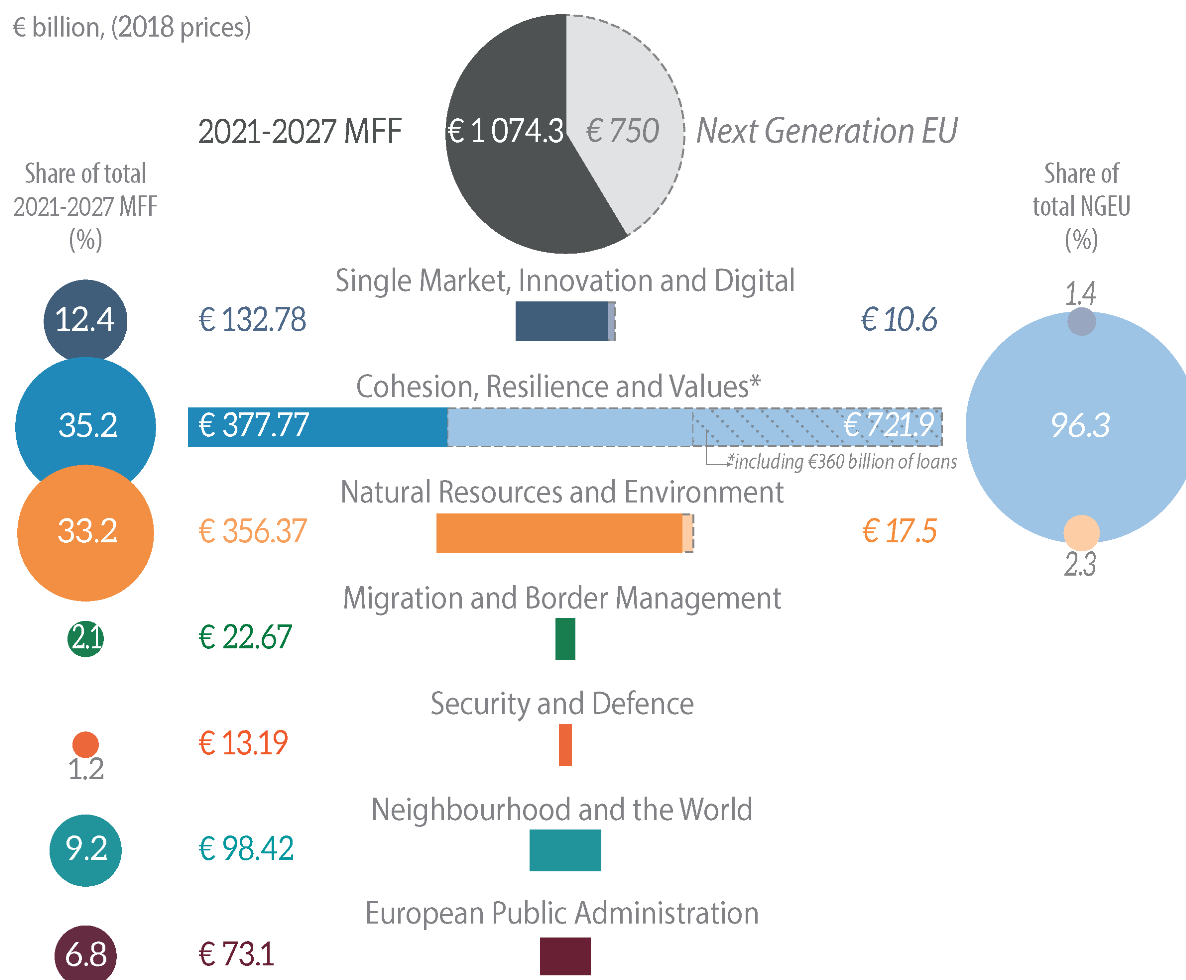
96 A. D'Alfonso, The UK 'rebate' on the EU budget: An explanation of the abatement and other correction mechanisms, EPRS, European Parliament, 2016.

97 Council Regulation (EU, Euratom) 2020/2093 of 17 December 2020 laying down the multiannual financial framework for the years 2021 to 2027.

98 Heading 2 'Cohesion, Resilience and Values' has two subcategories or 'subheadings': 2a 'Economic, social and territorial cohesion' and 2b 'Resilience and values'.

99 For more information on flexibility, see: M. Sapala, How flexible is the EU budget? Flexibility instruments and mechanisms in the multiannual financial framework, EPRS, European Parliament, January 2020.

Figure 6 – 2021-2027 multiannual financial framework and Next Generation EU (NGEU) by heading (€ million, current prices)



Data source: EPRS, based on European Commission data.

3.3. Main institutional actors in two key phases of the budgetary cycle

The European Parliament and the Council of the European Union are the two arms of the EU budgetary authority. Their tasks include intervening at the authorisation stage, and establishing the annual EU budget and its amendments, which they negotiate on the basis of a proposal from the European Commission and within the requirements set out by the own resources system and the MFF Regulation (see Section 3.2 above).

The powers of the European Parliament and the Council differ depending on the issue at stake. For the annual budgetary procedure they enjoy an equal footing. The decision on the design of the own resources system requires unanimity among the Member States in Council, while the European Parliament is consulted. The Council also adopts the regulation establishing the MFF unanimously, but in this case needs to obtain the European Parliament's consent beforehand.

This asymmetry in the powers of the two arms of the budgetary authority is said to sharpen the differences in their perspectives on budgetary issues.[100] In addition, the unanimity requirement in Council for the adoption of own resources and the MFF is often seen as an obstacle to major EU budget reform. While the budget has been modified over the years, the veto power enshrined in the procedures is deemed to favour the continuation of the status quo, which has generally ensured an equilibrium between Member States that join forces in subgroups sharing the same interests. For instance, debates on budgetary negotiations often refer to groups such as net contributors and net beneficiaries; and 'friends of cohesion', 'friends of better spending or correction mechanisms', and 'friends of agriculture'. The European Parliament has long pushed for EU budgetary reform, including in areas where its powers are more limited, such as own resources and the MFF, with the aim of shifting the focus of budgetary discussions to measures with EU added value.[101] The impact of the coronavirus pandemic brought a new dynamic to the MFF negotiations, resulting in an unprecedented package with the launch of a temporary recovery instrument, Next Generation EU (NGEU). Involvement of both arms of the budgetary authority in the governance of NGEU was part of the relevant negotiations (see Section 5.2.1).

As regards the implementation stage, the European Commission is ultimately responsible for the execution of the EU budget. However, implementation involves a wide range of actors under the three different management modes set out by the EU Financial Regulation. In practice, Member States currently implement 74 % of the MFF in 'shared management' with the European Commission, which in the 2021-2027 period applies to most expenditure under subheading 2a 'Economic, social and territorial cohesion' and heading 3 'Natural Resources and Environment'. As for the remaining MFF expenditure, 18 % is currently implemented under 'direct management' (European Commission and EU executive agencies), while 8 % is carried out under 'indirect management' (other entities such as third-country authorities, international organisations, EU decentralised agencies and the European Investment Bank).[102]

With the aim of ensuring correct and effective use of EU resources, the Financial Regulation applicable to the EU budget details key principles that the entities entrusted with budget implementation must respect. These include control and audit obligations for the various types of implementing methods. At political level, oversight of EU budget implementation is a key responsibility of the European Parliament (see Section 4.3).

3.4. The long road to the 2021-2027 MFF

The EU budget 2021 is the first to be implemented under the 2021-2027 MFF, which applies to the 27-Member State EU, given the withdrawal of the United Kingdom. The new MFF was adopted by the Council in December 2020 after an intense debate and a long process.[103]

The preparations for the post-2020 MFF and possible reform of the EU budget began at the very beginning of the 2014-2020 programming period. Unsatisfied with the limited changes to the EU's financing system agreed by the European Council in 2013, the European Parliament included the creation of an interinstitutional High-Level Group on Own Resources (HLG) among its conditions to give consent to the 2014 to 2020 MFF Regulation. The HLG, which was created by Parliament, Council and the Commission back in 2014, reviewed not only the revenue side of the budget, but

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[100] See for example: B. Patterson, *Understanding the EU Budget*, 2011; S. Becker, M. W. Bauer and A. De Feo [eds.], *The New Politics of the European Union Budget*, 2017.

[101] See for example: on the preparation of the post-electoral revision of the 2014-2020 MFF: Parliament's input ahead of the European Commission's proposal (P8_TA(2016)0309); and its reflection paper on the future of EU finances (P8_TA-PROV(2017)0401).

[102] European Commission, Integrated financial and accountability reporting. Overview: financial year 2019.

[103] For more details on proposals, legislative process and agreement, see: A. D'Alfonso, Multiannual financial framework for the years 2021 to 2027: The future of EU finances, EPRS, European Parliament, January 2021.

also EU expenditure, stressing how closely related the two aspects are. Presenting its final report in January 2017, the HLG recommended in-depth reform of both revenue and expenditure to increase the ability of the EU budget to respond to priorities.[104]

Confirming its importance, preparations on the next MFF soon became part of the broader debate on the future of the EU, kick-started by the Bratislava Declaration agreed by 27 EU Heads of State and Government in the wake of the UK referendum,[105] a Commission white paper and the Rome Declaration adopted on the 60th anniversary of the Treaties of Rome.[106] This development reflects the deeply political nature of the MFF, which translates agreed EU policy priorities into budgetary figures.

EU institutions and numerous stakeholders have contributed ideas and views to the discussion on various occasions. Examples include a Commission reflection paper on the future of EU finances,[107] mid-term evaluations on a number of EU sectoral policies and spending programmes,[108] European Parliament resolutions[109] on both the expenditure and revenue sides of the EU budget and European Court of Auditors' recommendations.[110] EU leaders held a debate on political priorities for the new MFF at an informal European Council meeting on 23 February 2018.

On 2 May 2018, following an extensive consultation of stakeholders, the European Commission put forward proposals for a 2021-2027 MFF worth €1 134.5 billion (2018 prices), including a reform of the own resources system. Taking into account lessons learnt from the 2014-2020 MFF, the package[111] included, to a varying extent, changes relating to the main issues for consideration to have emerged from the debate, such as: the own resources system; the size, structure and priorities of the MFF; its flexibility provisions; the unity of the budget (following the recent proliferation of instruments at least partially outside the budget); the streamlining of financial instruments; the possible role of the budget in EU economic governance; and respect for the rule of law.

Negotiations in the Council and European Council proved lengthy, despite the efforts of successive presidencies (Bulgarian, Austrian, Romanian, Finnish and Croatian), and several opportunities for EU leaders to exchange views on the topic at European Council meetings (June, October and December 2019). On 20-21 February 2020, President Charles Michel organised a special European Council meeting, in which EU leaders discussed the package in detail for the first time, but failed to find an agreement almost two years after the initial proposals.

Soon after that special European Council meeting, the outbreak of the coronavirus and its severe socio-economic consequences brought new momentum to the debate on the future of EU finances. On 23 April 2020, the European Council agreed on the urgent need to establish a common recovery fund and tasked the Commission with preparing a proposal and clarifying its link to the MFF.[112] On

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104 Future financing of the EU: Final report and recommendations, High Level Group on Own Resources, December 2016.

105 The expected withdrawal of the UK from the EU meant that the preparation of the proposal for the next MFF took place against a different backdrop, which a number of analysts identified as an opportunity for broader reform of the EU budget. See for example: H. Enderlein, What should happen? What is likely to happen? Notes on Brexit, Jacques Delors Institut – Berlin, 30 June 2016.

106 Bratislava Declaration and Roadmap, European Council, 16 September 2016; White paper on the future of Europe, COM(2017) 2025, European Commission, 1 March 2017; and Rome Declaration, European Council, 25 March 2017.

107 Reflection paper on the future of EU finances, COM(2017) 358, European Commission, 28 June 2017.

108 Seventh report on economic, social and territorial cohesion, European Commission, 9 October 2017.

109 See for example: European Parliament, Resolution on the next MFF: Preparing the Parliament's position on the MFF post-2020, Strasbourg, 14 March 2018; and Resolution on reform of the European Union's system of own resources, Strasbourg, 14 March 2018.

110 European Court of Auditors, EU budget: time to reform? A briefing on the mid-term review of the Multiannual Financial Framework 2014-2020, Luxembourg, 2016.

111 European Commission, EU budget for the future, May 2018 proposals, website.

112 Conclusions of the President of the European Council following the video conference of the members of the European Council, 23 April 2020.

15 May 2020, the European Parliament demanded an ambitious recovery package worth €2 trillion, linked to the next MFF, and built on the EU budget.[113] On 27 May 2020, the Commission tabled revised proposals for a lower MFF worth €1 100 billion (2018 prices) and its financing, together with a proposal for a €750 billion recovery instrument (NGEU).[114]

Less than two months after the revised proposals, the second longest European Council meeting ever (17-21 July 2020) reached political agreement[115] on a package worth €1 824.3 billion (see Figure 6) combining the new MFF (€1 074.3 billion) with the recovery instrument, NGEU (€750 billion). The allocation of resources between policy areas implies various changes as compared with the 2014-2020 MFF (see Sections 5.1 and 5.2). As regards the protection of the EU's financial interests and respect for the rule of law, the introduction of a conditionality regime was announced.

Parliament, a strong advocate of a robust MFF, had been ready to negotiate with the Council since November 2018. It confirmed and updated its negotiating mandate in October 2019. Following the July 2020 European Council meeting, Parliament welcomed the creation of a recovery instrument to kick-start the economy. However, expressing its readiness to enter negotiations immediately, Parliament criticised various aspects of the political agreement on the MFF, such as cuts to the core MFF (long-term investments) and insufficient modernisation of the own resources system.[116]

On that basis, Parliament fast-tracked its legislative opinion on the own resources decision, adopted in September 2020,[117] to enable the Council to ensure the timely launch of NGEU, while engaging in 10 weeks of intense negotiations with the Council, with a view to improving the European Council's settlement on the MFF. On 10 November 2020, Parliament's negotiating team and the Council Presidency reached a compromise on the next MFF. The compromise includes various changes strongly advocated by Parliament, such as reinforcements for a number of flagship programmes, additional flexibility, increased involvement of the budgetary authority in the governance of NGEU, and a roadmap for further reform of the own resources system (see Chapter 5).

However, the Council delayed the referral of the MFF Regulation because Hungary and Poland decided to withhold their support for the new framework, being unhappy with the result of the parallel negotiations on a mechanism protecting the EU budget in the event of deficiencies regarding the rule of law in Member States.[118] The European Council of 10-11 December 2020 solved the deadlock in the Council and the unmodified MFF Regulation was referred to Parliament.[119]

On 16 December 2020, Parliament gave its consent to the new MFF Regulation, with a large majority. The following day, the Council adopted the MFF Regulation for the years 2021-2027, which was published in the Official Journal on 22 December 2020. As for the programmes and instruments that will implement the new MFF, the adoption of a number of them is still being finalised at the time of writing.

[113] European Parliament, Resolution on the new multiannual financial framework, own resources and the recovery plan, 15 May 2020.

[114] Commission, May 2020 proposal, website.

[115] Special European Council, 17-21 July 2020.

[116] European Parliament, Resolution on the multiannual financial framework 2021-2027 – Parliament's position with a view to an agreement, 14 November 2018; and Resolution on the 2021-2027 multiannual financial framework and own resources: time to meet citizens' expectations, 10 October 2019; and Resolution on the conclusions of the extraordinary European Council meeting of 17-21 July 2020, 23 July 2020.

[117] European Parliament, Legislative resolution on the draft Council decision on the system of own resources of the European Union, 16 September 2020.

[118] Regulation (EU, Euratom) 2020/2092 of the European Parliament and of the Council of 16 December 2020 on a general regime of conditionality for the protection of the Union budget.

[119] European Council meeting (10 and 11 December 2020) – Conclusions, EUCO 22/20.

4. EU budget for 2021

The EU budget for the year 2021 is an unprecedented budget in unprecedented times. It is the first budget proposed by President Ursula von der Leyen's Commission and, at the same time, the first under the new 2021-2027 multiannual financial framework (MFF). It is a budget for a smaller EU, as in 2021 the United Kingdom will, for the first time, be treated as a third country.[120] Moreover, the EU 2021 budget was prepared and negotiated under the exceptionally difficult conditions surrounding the pandemic and the decision-making process was further complicated by the prolonged negotiations on the EU's next multiannual budget. Last but not least, much is expected of the 2021 budget in terms of its role in the implementation of the EU's landmark 'Next Generation EU' recovery instrument (see Chapter 5).

The process leading to the agreement on the 2021 budget was complicated and delayed in particular by the lack of agreement on the 2021-2027 MFF in the European Council (see Section 3.4). According to the Treaty on the Functioning of the EU (Article 312(1)), the annual budget must comply with a multiannual financial framework. Therefore, as long as there was no agreement on the new MFF, the budget for the year 2021 could not be adopted. At the beginning of December 2020, when the tension around the MFF negotiations was growing and the Treaty deadline for the adoption of the annual budget was approaching, the option of having to resort to an emergency solution, known as 'provisional twelfths',[121] was given serious consideration.[122] The annual budget procedure was unblocked only when the Member States agreed unanimously on the MFF package on 10 December 2020. However, as, in the meantime, the Treaty deadlines for the formal agreement in the Conciliation Committee had expired, the Commission had to table a second draft budget (see Section 4.1 below), which was approved without adjustments at the last plenary session of the year and signed into law by David Sassoli, the President of the Parliament, on 18 December 2020.[123]

When delving into the details of the EU 2021 budget, it is important to remember the deep changes brought by the new MFF and the recovery instrument. First, they concern the way the budget is structured and presented. The structure of the 2021-2027 MFF differs significantly from the 2014-2020 MFF. It is divided into seven headings and two subheadings. All continued and new programmes and funds under the headings are grouped into 16 clusters, corresponding to different EU policy areas. The policy clusters are reflected in the titles of the annual budget.[124] This

[120] According to Article 140 of the Withdrawal Agreement, the United Kingdom is liable for its share of the budgetary commitments of the Union budget and the budgets of the Union decentralised agencies outstanding on 31 December 2020, and for its share of the commitments made in 2021 on the carry-over of commitment appropriations from the budget for 2020, without prejudice to other components of the financial settlement. The broad parameters of the United Kingdom's future access to EU programmes under the MFF are outlined in the 'EU-UK Joint Declaration on Participation in Union Programmes and Access to Programme Services'. See also Section 5.1.5.

[121] On the basis of Article 315 TFEU and Article 16 of the Financial Regulation, in the absence of agreement on the annual budget, the system of provisional twelfths is introduced. Commitments may be made per chapter up to a maximum of one quarter of the total appropriations authorised in the relevant chapter of the previous financial year plus one twelfth for each month that has elapsed. Payments may be made monthly per chapter up to a maximum of one twelfth of the appropriations authorised in the relevant chapter of the preceding financial year. However, since with the end of the 20214-2020 MFF, the legal basis for many EU programmes and instruments expired, adoption of a budget under 2020 ceilings would also have required prolongation of the spending rules. See: European Commission, EU Public Finance, fifth edition, 2014.

[122] S. Fleming and J. Shotter, 'Brussels warns Poland and Hungary they cannot stop EU recovery fund', *Financial Times*, 4 December 2020.

[123] The approved budget for 2021 awaits final publication in the Official Journal of the European Union. For details on the procedure and the documents please see: European Parliament, Legislative Observatory, 2021 general budget: all sections, 2020/1998(BUD); New General Budget of the European Union for the financial year 2021, 2020/0371(BUD).

[124] As announced in the proposal for the 2021-2027 MFF, as of 2021 the Commission has broken with past practice and has reproduced the MFF structure when presenting the proposal for the annual budgets. For more detail on the structure of the budgets before 2021, see European Commission, European Union public finance, fifth edition, 2014.

presentation, according the Commission, is more informative and clearer, and the synergies between the programmes are more apparent. In this study, for comparison purposes, EU 2020 expenditure is also presented according to the headings of the 2021-2027 MFF.[125]

Furthermore, the EU's temporary recovery instrument, Next Generation EU (NGEU), will have a profound impact on the size, structure and organisation of the annual budget[126] (see Section 5.2.). As provided for in the regulation establishing NGEU,[127] the amount to be used for expenditure constitutes external assigned revenue (see Box 1) and will be counted over and above the MFF ceilings. In the 2021 budget, the Commission presents information on the expected external assigned revenue from NGEU, together with expenditure from the budget 2021. Specific amounts of legal commitments estimated for 2021 in relation to the given programme are indicated in the budget remarks of the relevant budget lines.[128]

Box 1 – External assigned revenue

Universality is one of the budgetary principles underpinning the EU budget, on the basis of the Financial Regulation (**FR**). It means that revenue finances all expenditure without distinction. External assigned revenue represents one exception to this principle, since it finances specific items of expenditure. The FR identifies various types of external assigned revenue, such as contributions from third countries to certain EU activities, and gives the legislative authority the possibility to establish other assigned revenue – internal or external – through a basic act. The Commission proposal for Next Generation EU is based on the latter option. The allocations for external assigned revenue are not decided by the budgetary authority in the annual budgetary procedure, but stem automatically from the implementation of related acts and are detailed in the reporting phase at the closure of the annual accounts and with the presentation of the next draft budget. Next Generation EU is expected to generate an unprecedented volume of external assigned revenue for the EU budget. While under the 2014-2020 MFF external assigned revenue has been used to finance on average 10-11 % of the total annual budget (with the biggest impact on heading 1b – Economic, social and territorial cohesion), the external assigned revenue based on the NGEU will more than double the size of the 2021 budget. Given the sums involved, there have been **suggestions** for the budgetary treatment of external assigned revenue to be reconsidered. This approach would require an amendment to the FR, to be adopted by Parliament and Council under the ordinary legislative procedure.

As a result of the MFF negotiations, the EU institutions agreed that the role of the budgetary authority needs to be enhanced in relation to external assigned revenue under NGEU. A special procedure for the oversight of the revenue was stipulated in the **Interinstitutional Agreement** of 16 December 2020, linked to the 2021-2027 MFF.

Sources: A. D'Alfonso, Next Generation EU, **EPRS**, European Parliament, July 2020 and A. Mathis, Next Generation EU. Where are assigned revenue? Which impact in 2021?, Directorate-General for Internal Policies, European Parliament**, July 2020**.

Last but not least, it should be noted that, owing to the delayed adoption of the 2021-2027 MFF, the underlying sectoral acts for the spending programmes and funds could not be adopted on time to launch their implementation on 1 January 2021. Progress on the legislative procedures to agree the

[125] This approach is based on the European Commission's presentation of the proposal for the 2021 budget. See Draft General budget of the European Union for the financial year 2021, General introduction, 27 July 2020; Second draft general budget of the European Union for the financial year 2021, European Commission, COM(2020) 836 final, Brussels, 10 December 2020.

[126] The European Recovery Instrument (EURI) is the official name of the instrument used in the draft general budget. However, the other name – Next Generation EU (NGEU) – was introduced by the Commission in the documents published with the proposal establishing the instrument. For the purposes of this study, reference will be made to the latter, commonly used, name of the recovery instrument.

[127] Article 3 of Council Regulation (EU) 2020/2094 of 14 December 2020.

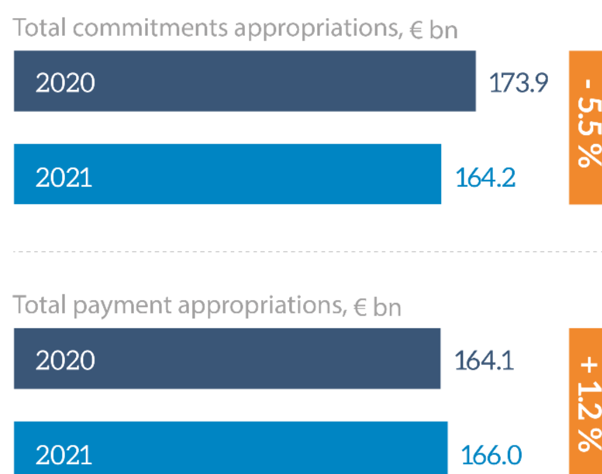
[128] Draft General budget of the European Union for the financial year 2021, General introduction, 27 July 2020.

sectoral regulations can be followed and consulted via the European Parliament's Legislative Observatory and the Legislative Train.[129]

4.1. Result of the 2021 budgetary procedure

The first annual budget prepared under the 2021-2027 MFF and for the Union of 27 Member States, i.e. without the UK, was set at €164.25 billion[130] in commitments (1.17 % of EU-27 GNI) and at €166.06 billion in payments (1.19 % EU-27 GNI).[131] In absolute numbers, by comparison with the 2020 budget this represents a decrease of 5.5 % in commitments and an increase of 1.2 % in payments (Figure 7). The changes reflect the transitional nature of the 2021 budget. While the decrease in commitments is, at least partly, a consequence of the reduced size of the EU, the increase in payments can be attributed to the accelerating implementation of many spending programmes launched under the 2014-2020 MFF, including pandemic-related measures introduced in 2020.[132] The margin below the 2021-2027 multiannual financial framework ceilings available for unexpected needs in 2021 amounts to €778.8 million in commitment appropriations and €2.0 billion in payment appropriations (for detailed figures, see Annex 3).

Figure 7 – Total commitment and payment appropriations, EU budgets for 2020 and 2021.



Data source: European Commission, see Annex 3.

The procedure, in accordance with Article 314 of the TFEU, began with the Commission presenting a draft budget on 27 July 2020 (see Box 2). On account of the exceptional circumstances linked to the pandemic, the proposal was submitted about a month later than usual. Already in May 2020,

[129] Legislative Observatory and Legislative Train Schedule of the European Parliament.

[130] Unless otherwise stated, all amounts are expressed in current prices.

[131] On 22 January 2021, the European Commission proposed its first draft amending budget to the 2021 general budget (DAB 1/2021) to incorporate funds from the Brexit Adjustment Reserve (BAR). It increases both commitments and payments for the 2021 budget by €4.24 billion. If adopted, DAB 1/2021 will increase the 2021 budget to €168.5 billion in commitments and €170.3 billion in payments. The BAR is one of the thematic special instruments based on Article 10 of the 2021-2027 MFF regulation (2020/2093). The related appropriations will be entered into the budget over and above the expenditure ceiling of the MFF 2021-2027. See: European Commission, Draft amending budget No 1 to the general budget 2021. Brexit Adjustment Reserve, COM(2021) 30 final, 22 January 2021.

[132] In addition to the reduced number of Member States, the other element that has to be taken into account when comparing the last annual budget of the 2014-2020 MFF and the first annual budget of the 2021-2027 MFF is the budgetisation of the European Development Fund (EDF) (see Section 4.2).

Parliament, Council and the Commission agreed to a pragmatic calendar[133] for the 2021 budgetary procedure to allow for the emergency conditions.[134] Since at the time there was not yet an agreement on the new MFF,[135] the Commission based the draft budget on its own proposal for the 2021-2027 MFF, revised after the outbreak of the pandemic in May 2020.[136] The draft budget for 2021 amounted to €166.7 billion in commitments and €163.5 billion in payments. On top of this, in line with the proposal to create the recovery instrument 'Next Generation EU', the Commission envisaged that selected programmes in the 2021 budget would be reinforced through external assigned revenue for a total amount of €211 billion in commitments.

The overarching priority of the proposed spending in 2021 was investment in crisis preparedness and recovery. At the same time, according to the Commission, the budget has been designed to contribute to the achievement of the political priorities[137] set out by Commission President Ursula von der Leyen at the beginning of her term, in particular the green transition (and support for implementation of the Green Deal), the digital transition and an economy that works for all, increased resilience, security and focus on defence, reinforced migration and border management, and a stronger Europe in the world.

On 29 September 2020, in the next step in the procedure, the Council adopted its reading of the draft budget.[138] It was based on the political agreement on the 2021-2027 MFF reached by the Member States earlier in July and announced as a 'technical translation' of the figures included in the European Council conclusions. Overall, the Council proposed to reduce the Commission's proposal by 2.3 % in commitment appropriations and increase payment appropriations by 0.8 %. The biggest reductions in the needs estimated by the Commission concerned heading 4 'Migration and border management' (-23.5 %) and heading 5 'Security and defence' (-23.2 %).

While waiting for the result of the negotiations on the MFF, the European Parliament adopted its reading of the draft 2021 budget on 12 November 2020. It reflected both the priorities included in its resolution of 19 June 2020 on general guidelines for the preparation of the 2021 budget,[139] and Parliament's negotiating position on the long-term financial package, updated after the European Council meeting, on 23 July 2020.[140] Parliament decided to restore all cuts to the draft budget included in the Council position, with the exception of heading 7 'European public administration'. It also increased the Commission's original proposal by €16.7 billion (+10 %), bringing the difference between the positions of the two arms of the budgetary authority to €20.5 billion (Figure 8).

[133] For more on the role of the pragmatic calendar in the EU budgetary procedure, see S. Mazur, Annual EU budgetary procedure. An introduction to the steps in the EP, Briefing, EPRS, European Parliament, July 2019.

[134] Council of the EU, Joint statement on the dates for the budgetary procedure and modalities for the functioning of the Conciliation Committee in 2020, Brussels, 27 May 2020.

[135] A week before the Commission tabled the proposal, on 17-21 July 2020, the Member States reached a political agreement on all elements of the next multiannual financial package and on creation of the recovery instrument (see Chapter 5).

[136] European Commission, MFF legislation, May 2020.

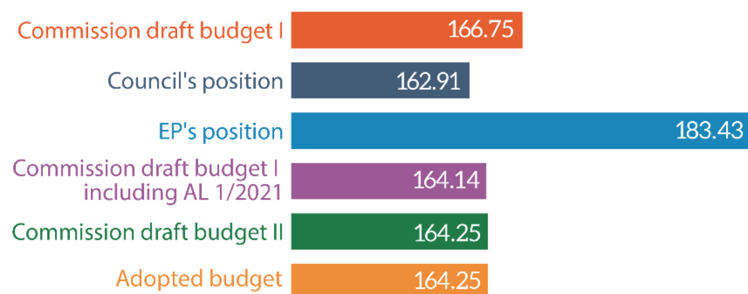
[137] E. Bassot, The von der Leyen Commission's six priorities: State of play in autumn 2020, Briefing, EPRS, European Parliament, September 2020.

[138] Council of the EU, Draft general budget of the European Union for the financial year 2021: Council position of 29 September 2020.

[139] European Parliament resolution of 19 June 2020 on general guidelines for the preparation of the 2021 budget, Section III – Commission (2019/2213(BUD).

[140] European Parliament resolution of 23 July 2020 on the conclusion of the extraordinary European Council meeting of 17-21 July 2020 (2020/2732(RSP)).

Figure 8 – 2021 EU budget (commitments, € billion, current prices)



Data source: European Commission, see Annex 3.

Parliament emphasised that the primary focus of the 2021 budget should be to mitigate the effects of the pandemic and that the recovery should be built on the European Green Deal and digital transformation. In line with its negotiating position on the MFF, Parliament decided to reinforce the EU's 15 flagship programmes[141] in such areas as climate change, research, energy, digital and transport interconnectivity, health, youth, culture, border management and external action.

On 13 November 2020, the Commission adopted Amending Letter 1/2021 (AL 1/2021) to the draft general budget for 2021.[142] It took account of the progress in the negotiations on the next long-term financial package since the annual budget proposal had been put forward, and integrated the results of the political agreements reached by the European Council on 17-21 July 2020, and between the European Parliament and German Council Presidency on 10 November 2020.[143] This had an impact on a number of spending programmes, financing of some decentralised agencies, the size of the special instruments, but also on the structure of headings and budgetary nomenclature. Moreover, the amending letter included updated estimates for expenditure on the common agricultural policy (CAP), increased payments needed for the European structural and investment funds, and made other adjustments and technical updates. In addition, as the European Council's conclusions changed the spending modalities of the EU recovery instrument, this was also taken into account in the AL 1/2021. Overall, the AL 1/2021 decreased the draft budget by €2.6 billion (-1.6 %) in commitment appropriations and increased it in payment appropriations by €2.6 billion (+1.6 %).[144]

The 21-day conciliation period began on 17 November 2020. On 4 December 2020, the negotiating parties succeeded in reaching a common understanding on the substance of the budget for 2021. In this preliminary agreement the negotiators set total commitments at €164.25 billion and total payments at €166.06 billion.[145] However, owing to the lack of clarity on the adoption of the 2021-

[141] 15 EU flagship programmes supported by the European Parliament in the MFF negotiations, EPRS, European Parliament, 24 September 2020.

[142] Amending letter No 1 to the draft general budget 2021, European Commission, COM(2020) 748 final), Brussels 13 November 2020.

[143] Compromise on long-term EU budget: EP obtains €16 billion more for key programmes, press release, European Parliament, 10 November 2020. For details of the agreement see: European Parliament recommendation on the draft Council regulation laying down the multiannual financial framework for the years 2021 to 2027, 2018/0166(APP), 14 December 2020.

[144] For more see: S. Mazur, Amending letter No 1 to the EU draft general budget 2021, 'At a glance' note, EPRS, European Parliament, November 2020.

[145] Common understanding reached in the conciliation committee, Council of the European Union, Brussels, 4 December 2020.

2027 MFF, the Conciliation Committee could not sign a formal agreement on a joint text and the conciliation had to fail 'technically'.

On 10 December 2020, when the European Council finally found the necessary unanimity on the MFF package, the Commission put forward the second draft budget for 2021.[146] The agreement reached by the Conciliation Committee on 4 December 2020 was fully integrated into this new proposal. The adoption of the 2021 budget was finalised without amendments and in a fast-track procedure applied by both institutions involved: on 14 December 2020, Council adopted its position; the next day the European Parliament's Committee on Budgets adopted its report on the Council position;[147] and on 18 December 2020 the European Parliament voted the adoption at its plenary sitting (540 to 77, with 70 abstentions).[148] On the same day the EU 2021 budget was signed into law by President David Sassoli. Thanks to the positive finalisation of these unusual budgetary negotiations, on 1 January 2021 the EU began the new seven-year MFF and the regular annual budget, and was able to avoid resorting to emergency solutions.

Box 2 – 2021 budgetary procedure milestones

27 July 2020: The European Commission tables the draft 2021 EU budget.

27 September 2020: Council adopts its position on the draft 2021 EU budget.

12 November 2020: The European Parliament amends Council's position on the draft 2021 EU budget.

13 November 2020: The European Commission tables modifications to its 2021 EU budget proposal by means of Amending Letter (AL) 1/2021, which took account of the political agreement on the 2021-2027 MFF reached between the European Parliament and the Council Presidency on 10 November 2020.

17 November – 7 December, 2020: Conciliation Committee.

4 December 2020: The Conciliation Committee reaches a common understanding on the 2021 EU budget but, in the absence of the new MFF, fails to sign a joint text.

10 December 2020: The European Commission tables its second draft 2021 EU budget.

14 December 2020: Council adopts its reading of the second draft 2021 EU budget.

18 December 2020: The European Parliament approves without amendments the Council position. On the same day the 2021 EU budget is signed into law by European Parliament President, David Sassoli.

The final agreement is €1.49 billion lower than proposed by the Commission in the first draft budget and €1.34 billion higher than stipulated in the Council reading (Figure 8). A number of increases introduced at different stages of the procedure correspond to Parliament's priorities and are the result of the simultaneous nature of negotiations on the 2021-2027 MFF and on the 2021 budget. In particular, Parliament welcomed the first reinforcements to the EU flagship and future-oriented programmes, which are part of the €15 billion MFF top-up.[149] In 2021, these reinforcements are

[146] Second draft general budget of the European Union for the financial year 2021, European Commission, COM(2020) 836 final, Brussels, 10 December 2020.

[147] Report on the Council position on the second draft general budget of the European Union for the financial year 2021, Committee on Budgets, European Parliament, 2020/0371(BUD).

[148] European Parliament resolution of 18 December 2020 on the Council position on the second draft general budget of the European Union for the financial year 2021, 2020/0371(BUD).

[149] During the negotiations on the 2021-2027 MFF, the European Parliament obtained €15 billion to reinforce 10 EU flagship programmes on top of the amounts agreed by the European Council in July 2020. The top-up will be financed through different mechanisms: based on Article 5 of the MFF regulation (Council regulation (EU, Euratom) 2020/2093), €11 billion will be financed from a new mechanism linked to the proceeds from competition fines collected by the EU. The mechanism will be implemented in the annual budgets for 2022 to 2027 and will result in an increase of the MFF ceilings on a yearly basis; €2.5 billion will be financed from margins left unallocated within the ceilings set by the European Council in July 2020; €1 billion from reflows from the ACP Investment Facility (European Development Fund); €0.5 billion from de-committed appropriations in the area of research (based on Article 15(3) of the Financial

allocated to Erasmus+ (+€175.1 million from unallocated margins), EU4Health (+€74.3 million from unallocated margins), and Horizon Europe (+€20 million from unspent commitment appropriations in line with Article 15.3 of the Financial Regulation).[150] Furthermore, on top of the amounts proposed in Council's position, additional resources were allocated for the Connecting Europe Facility Transport (+€60.3 million), LIFE (+€42 million), Digital Europe (+€25.7 million), humanitarian aid (+€25 million), UNRWA under NDICI (+€10.2 million), Rights and Values (+€6.6 million, of which €4.8 million for a renewed Daphne programme),[151] and the Justice programme (+€2.7 million). Moreover, as a result of the negotiations, additional funding will support several decentralised agencies, including +€7.3 million for European Public Prosecutor's Office, mainly for staff reinforcements. The 2021 budget also includes the package of pilot projects and preparatory actions proposed by Parliament, for a total amount of €71.8 million.

As in all years of the 2014-2020 MFF, part of the reinforcements agreed by the budgetary authority will be financed from the flexibility tools (see Section 5.1.4). In the 2021 budget it concerns sub-heading 2b Resilience and values (Table 1).

Table 1 – Flexibility tools mobilised with the adoption of the 2021 EU budget

Instrument	Amount mobilised	Goal
Flexibility Instrument	€76.4 million	To reinforce allocations of the EU4Health and Erasmus+ programmes under sub-heading 2b Resilience and values (as envisaged by the political agreement on the 2021-2027 MFF of 10 November 2020).

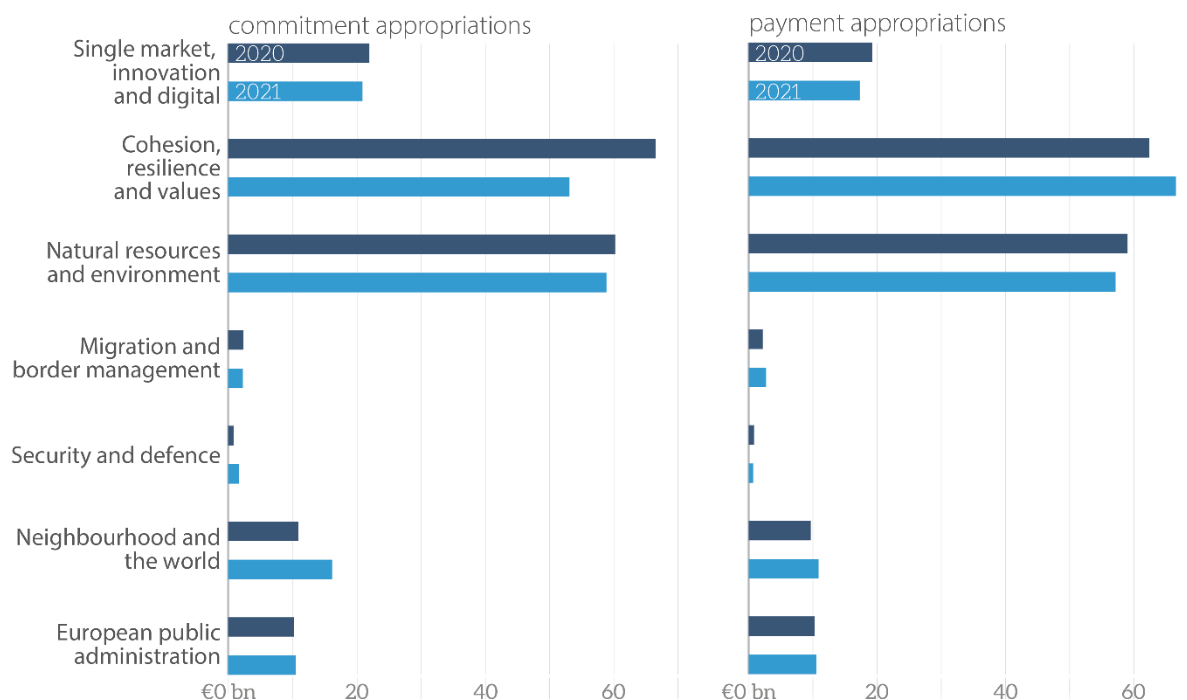
As far as payments are concerned, in 2021 their level is 1.2 % higher than in 2020. Unusually, it is also 1.1 % higher than the level of commitment appropriations. This reflects the particular transitional nature of the financial year 2021, which includes the amounts needed to start and pre-finance programmes under the new MFF, but also has to provide payments to meet needs linked to the closure of the 2014-2020 period. It had the biggest effect on spending under subheading 2a Economic, social and territorial cohesion (see Figure 9). As in recent years, in the joint declarations attached to the budgetary agreement, the budgetary authority recalled the need for close monitoring of the implementation of the 2014-2020 programmes and assessment of the progression of payments. It concerns, in particular, spending under sub-heading 2a Economic, social and territorial cohesion, and spending on rural development under heading 3 Natural resources and environment. Should the payment appropriations entered in the 2021 budget be insufficient to cover the estimated needs, the Commission is expected to present an appropriate solution as a matter of urgency to allow the budgetary authority to take the necessary decisions.

Regulation). See: M. Sapala. M. Pari and N. Kresnichka-Nikolchova, EU financing for 2021-2027, Briefing, EPRS, December 2020.

[150] The additional commitments for Horizon Europe would be made available in accordance with Article 15(3) of the Financial Regulation. Since 2018 use of this article has been an important moot point in the annual budgetary negotiations. See A. D'Alfonso, A. Delivorias, M. Sapała and C. Stamegna, Economic and budgetary outlook for the European Union 2020, EPRS, European Parliament, January 2020, p. 25.

[151] Daphne is part of the strand of the rights and values programme dedicated to the fight against all forms of violence.

Figure 9 – A comparison of EU budgets in 2020* and 2021 (commitment and payment appropriations, € billion)



* The figure presents 2020 spending according to the headings of the 2021-2027 MFF.

Data source: European Commission, see Annex 3.

The final agreement on the 2021 EU budget includes five statements. In one of them, the European Commission underlined the problem of child poverty, which is important especially in the context of the pandemic crisis. In order to improve financial support in this area, the Commission proposed to include a specific thematic concentration for addressing child poverty in the spending rules of the European Social Fund+ (see Box 4). In another statement, also in the context of the crisis, the European Parliament, Council and the European Commission agree to take 'the necessary measures to rapidly deploy full potential of the new generation of EU programmes'. Particular attention is given to the sectors and people the worst hit by the crisis, such as the tourism sector, small and medium-sized enterprises, children and young people. Furthermore, the European Parliament and the Council expressed their intention to make available appropriations under the Brexit Adjustment Reserve (BAR) as soon as possible in the financial year 2021.[152]

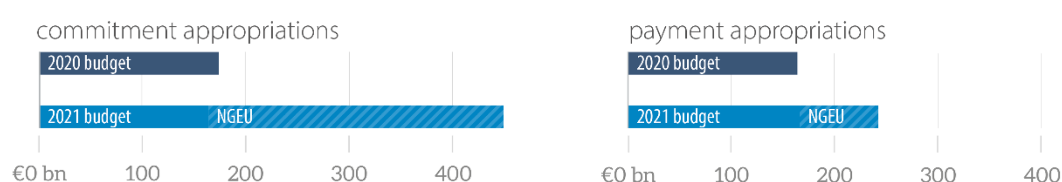
A number of EU programmes and funds under the annual budget provide financing for EU social investment and actions relating to social policy, the area that is the focus of this year's economic section of the Outlook (see Chapter 6). Broadly understood EU social policy is a horizontal topic, present to some extent in majority of the EU programmes and actions under headings 1 Single market, innovation and digital, 2 Cohesion, resilience and values, and 3 Natural resources and environment. Examples of relevant programmes and initiatives available in the 2021 budget are presented in Section 4.3.

[152] On 22 January 2020 the European Commission proposed draft amending budget No 1 to the 2021 budget in order to enter the budget resources necessary to start implementation of the Brexit Adjustment Reserve. See footnote 132.

4.2. The impact of Next Generation EU on the 2021 budget

As soon as the formal procedures in the Member States approving the new own resources decision are finalised and the borrowing process is launched (see Section 3.2), the additional resources will be introduced to the 2021 budget as external assigned revenue. According to the indicative data, the 2021 tranche of NGEU will reinforce the annual budget with €285.15 billion of legal commitments (grants component). This represents about one third of the total NGEU for the years 2021 to 2023 (€809 billion, current prices). Figure 10 shows accumulated amounts under the 2021 budget and the NGEU (commitments and payments). In 2021, commitments based on both components can reach almost €450 billion, this is two and a half times EU expenditure in 2020. This significant injection of resources will be channelled to the Member States under the relevant programmes in the 2021 budget (Table 2). However, it should be stressed that the level of payments planned for 2021 under NGEU is significantly lower

Figure 10 – Comparison between the 2020 budget and the 2021 budget + NGEU



Data source: European Commission see Annex 3.

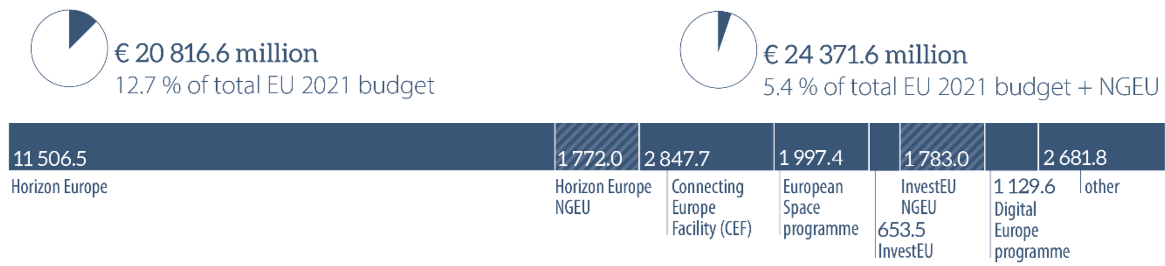
Table 2 – Planned indicative contribution from Next Generation EU to the 2021 budget (per programme)

EU programme / budget line	Contribution from Next Generation EU (€ million)	
	Commitment appropriations	Payment appropriations
Heading 1 Single market, innovation and digital		
Horizon Europe	1 772.0	177.9
Invest EU Fund	1 783.0	174.0
Heading 2 Cohesion, resilience and values		
REACT-EU European Regional Development Fund (ERDF)	27 856.5	4 983.5
European Recovery and Resilience Facility (incl. Technical Support Instrument) – grants	236 607.0	67 607.0
Union civil protection mechanism (RescEU)	682.5	197.0
REACT-EU European Social Fund (ESF)	11 938.5	2 135.8
Heading 3 Natural resources and environment		
European Agricultural Fund for Rural Development (EAFRD)	2 387.7	596.9
Just Transition Fund	2 122.0	55.0
TOTAL	**285 149.2**	**75 927.1**

Data source: Amending Letter 1/2021, COM(2020) 748 final, 13 November 2020.

4.3. Budget headings in detail

Figure 11 – Heading 1 Single market, innovation and digital



Data source: European Commission see Annex 3.

Heading 1 'Single market, innovation and digital' represents 12.7 % of the 2021 budget without the reinforcement from the NGEU instrument, and 5.4 % of the 2021 budget + NGEU combined.[153] It includes EU investments providing an important contribution in the area of research and innovation, EU strategic investments in trans-European networks in transport, communication and energy, digital transformation, single market and space policy. Examples of programmes and instruments supported include Horizon Europe, InvestEU, the Connecting Europe Facility (CEF), the Digital Europe programme, the Single Market programme, and the European Space programme.

As compared with 2020, the total volume of commitments under new heading 1 decreased by 4.8 %.[154] However, its share in the 2021 budget remains at almost the same level (12.6 %). Two programmes under the heading, Horizon Europe and Invest EU, will be reinforced from the resources under the NGEU for a total amount €3.5 billion.

Expenditure for some programmes marks significant decreases. This concerns for example the Euratom Research and Training programme (-33.3 %), CEF-Energy (-38.7%) and CEF-Transport (-30.8 %). The allocation for the biggest programme under heading 1, Horizon Europe, is reduced by 12.8 % (from €13.2 billion in 2020 to €11.5 billion in 2021). However, reinforced by an extra €1.8 billion from NGEU, it can slightly exceed its 2020 level.

Heading 1 includes two new instruments, introduced to the budget with the 2021-2027 MFF, the digital Europe programme and the InvestEU programme. The former, allocated €1.1 billion, is dedicated to investments in the strategic digital capacities of the EU and the wide deployment of digital technologies. Together with CEF-Digital, which in 2021 increases by 83.1 %, the digital Europe programme is part of the EU's effort to harness the digital transition. InvestEU is an investment instrument built on the European Fund for Strategic Investments (EFSI) and several other financial instruments launched under the 2014-2020 MFF. Its 2021 allocation is set at €653.6 million and a significant reinforcement of €1.8 billion is planned for it from the NGEU instrument. Part of the InvestEU programme is dedicated to social investment and skills (see Box 3).

[153] For detailed figures see Annex 3.

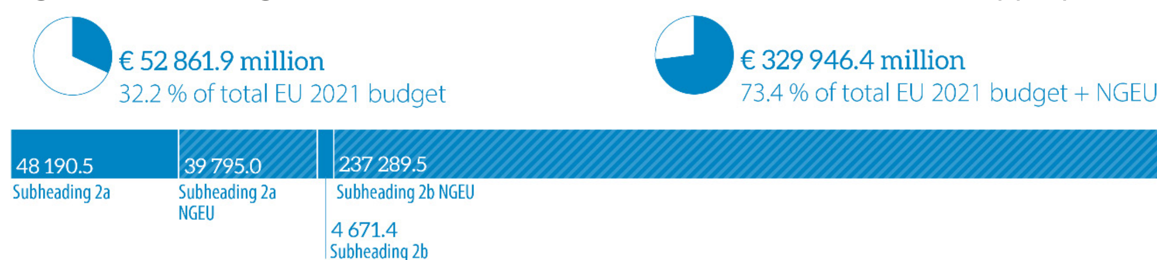
[154] All comparisons with the 2020 budget are based on the European Commission presentation of 2020 expenditure according to new headings (2021-2027 MFF). See Chapter 5 of the Second draft general budget of the European Union for the financial year 2021, COM(2020) 836 final, Brussels, 10 December 2020.

Box 3 – Social dimension of InvestEU

In the 2021-2027 programming period, the InvestEU programme will support EU investment in sustainable recovery, innovation and job creation. The main components of the programme include an EU budget guarantee, a platform providing technical advice for project development, and a database matching projects with potential investors. The InvestEU programme provides its support through four policy windows, one of which is specifically created for social investment and skills. Aimed at financing projects in areas such as social housing, education, healthcare and integration of migrants, refugees and vulnerable people, this 'social window' is allocated €2.78 billion (current prices) from the EU budget guarantee in the 2021-2027 MFF (6.7 % of the total seven-year envelope for InvestEU).

Source: Commission welcomes political agreement on InvestEU, European Commission, 8 December 2020.

Figure 12 – Heading 2 Cohesion, resilience and values, 2021 commitment appropriations

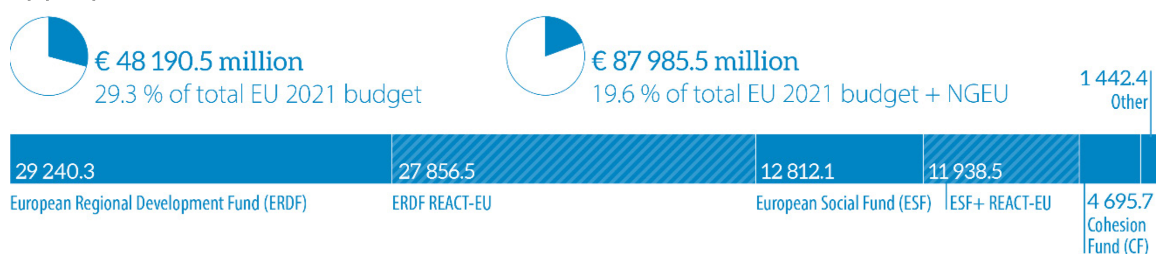


Data source: Data source: European Commission see Annex 3.

Heading 2 Cohesion, resilience and values represents 32.2 % of the 2021 budget and 73.4 % of the annual budget combined with NGEU. It covers a wide range of EU programmes, many of which were in different headings under the previous MFF. They channel EU investments in three policy areas: regional development and cohesion, recovery and resilience, and investing in people, social cohesion and values. Heading 2 is particularly important for the EU recovery following the Covid-19 outbreak. In total, 97 % of the 2021 tranche of NGEU will be implemented through four programmes under this heading.

The budget under heading 2 is divided into two subheadings: 2a Economic, social and territorial cohesion, and 2b Resilience and values. In this way the allocations for both areas are clearly ring-fenced, and appropriations and margins under one subheading cannot be used for expenditure in another subheading.

Figure 13 – Subheading 2a Economic, social and territorial cohesion, 2021 commitment appropriations



Data source: European Commission, see Annex 3.

Subheading 2a amounts to €48.2 billion in commitments and ring-fences the allocation known as the EU budget for cohesion policy. It supports the harmonious economic, social and territorial development of EU regions and cities. Most of the expenditure in this subheading is pre-allocated to the Member States and implemented through the European Regional Development Fund (ERDF), the European Social Fund+ (ESF+) and the Cohesion Fund. As far as the ESF+ is concerned, its allocation is divided between the two subheadings. The majority of the fund (€12.8 billion) is implemented under 'shared management' (see Section 3.3.) and calculated as part of subheading 2a; a relatively small part, known as the employment and innovation strand (€102.5 million), is included in subheading 2b (see Box 4).

Box 4 – European Social Fund+ in the 2021 budget

The European Social Fund+ aims to encourage a high level of employment and the creation of more and better jobs. In the 2021-2027 the ESF+ becomes the main EU budgetary instrument supporting implementation of the European pillar of social rights (see Chapter 6). It will integrate the current European Social Fund, **the youth employment initiative**, the Fund for **European Aid to the Most Deprived** and the **employment and social Innovation** programme, to enhance synergies and reduce red tape. The ESF+ is designed to provide targeted support for youth employment, up-skilling and re-skilling of workers, social inclusion and poverty reduction, especially among children.

In the EU 2021 budget the ESF+ will amount to €12.8 billion (shared management strand), representing a share of about 27 % of cohesion expenditure (subheading 2a). The commitments planned for 2021 are reduced as compared to the 2020 budget (-11.8 %). However, in line with the other EU structural funds, the level of payment appropriations in the ESF+ increases (+11.1 %) and in absolute terms exceeds the level of the commitments. Furthermore, as part of the EU Recovery Instrument, the REACT-EU initiative will provide ESF+ with an additional €11.9 billion in 2021.

Tackling child poverty with the ESF+

The revised proposal for the European Social Fund+ (**COM(2020) 447**) includes a specific thematic concentration for addressing child poverty. It requires that each Member State shall allocate at least 5 % of their ESF+ resources under shared management to support targeted actions and structural reforms to tackle child poverty (Article 7(3)a). Given the currently forecast national allocations, this represents almost €5 billion in current prices for the 2021-27 programming period. The European Parliament has long fought to establish an instrument of this kind in the EU and strongly supports the **initiative**.

Source: General budget of the European Union for the financial year 2021 – all sections, European Parliament, **18 December 2020**.

See also: M. Lecerf, European Social Fund Plus (ESF+) 2021-2027, **Briefing**, EPRS, European Parliament, March 2019.

While the level of commitments approved for the subheading is 17.7 % lower than in 2020, payments increase by 12.1 %. It reflects the accelerating implementation of the funds under the 2014-2020 MFF. On average, at the beginning of 2021, the level of executed payments reached 55 % of the total allocation.[155] In addition, the increasing need for payment appropriations is a consequence of specific flexibility measures introduced to the use of cohesion funds at the beginning of the pandemic.[156] The financial implementation of the programmes initiated under the previous MFF will continue until the end of 2023 (N+3 rule) and may also put pressure on payments in the following years of the 2021-2027 programming period.

[155] Based on the European Commission's webpage on the European structural and investment funds and cohesion data (accessed on 12 January 2021).

[156] V. Margaras, Specific flexibility measures for ESI funds in response to the coronavirus outbreak, 'At a glance' note, EPRS, European Parliament, April 2020.

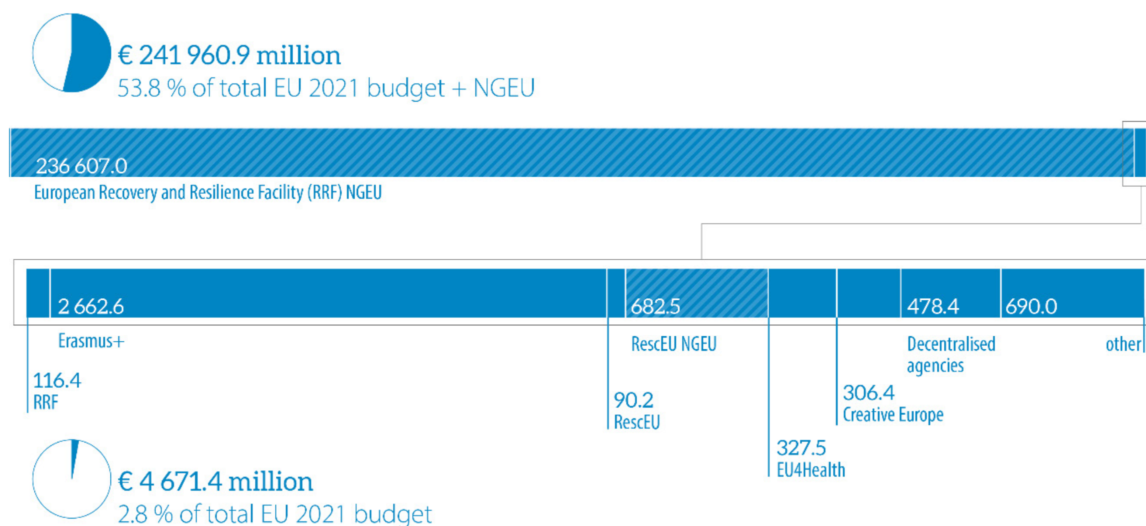
As part of the recovery plan for 2021, the ERDF and the ESF+ will be reinforced with an additional €27.8 billion for crisis repair measures in the regions (REACT-EU programme), financed by NGEU (see Box 5).

Box 5 – REACT-EU programme

REACT-EU is the EU's pandemic recovery package aimed at facilitating a more symmetric and socially cohesive recovery in Europe by offering financial support to those regions in which the negative impact of the crisis has been particularly severe. The REACT-EU budget is set at €47.5 billion (2018 prices) for the 2021-2022 period and will be implemented through the ERDF and ESF+. The additional resources from REACT-EU to ESF+ are intended to help Member States in providing access to the labour market and social support systems. Furthermore, these resources may be used to support those particularly affected by the crisis such as the self-employed, entrepreneurs, freelancers, artists and creative workers. In addition, youth employment measures, social services of general interest, and education, training and skills development are all eligible for funds. Finally, the REACT-EU funds can also be allocated to social inclusion and poverty eradication measures and to schemes supporting geographically and socio-economically peripheral regions. When distributing the additional funds from REACT-EU, the Commission will take into account the Member States' relative prosperity and the impact of the crisis on GDP and unemployment levels.

Source: A. Widuto, REACT-EU recovery assistance, 'At a glance' note, EPRS, European Parliament, **December 2020**.

Figure 14 – Subheading 2b Resilience and values, 2021 commitment appropriations



Data source: Data source: European Commission see Annex 3.

Subheading 2b includes two main policy clusters: recovery and resilience, and investing in people, social cohesion and values. The former is relatively small part of the 2021 budget, but it will increase significantly once the external assigned revenue based on the NGEU instrument is introduced to the Recovery and Resilience Facility (RRF). The RRF is the Union's main tool in support of economic and social recovery from the consequences of the pandemic (see Section 5.2.2). The 2021 allocation for the RRF financed from NGEU will amount to €236.7 billion (grant component). This represents 83 % of the total NGEU tranche planned for 2021.

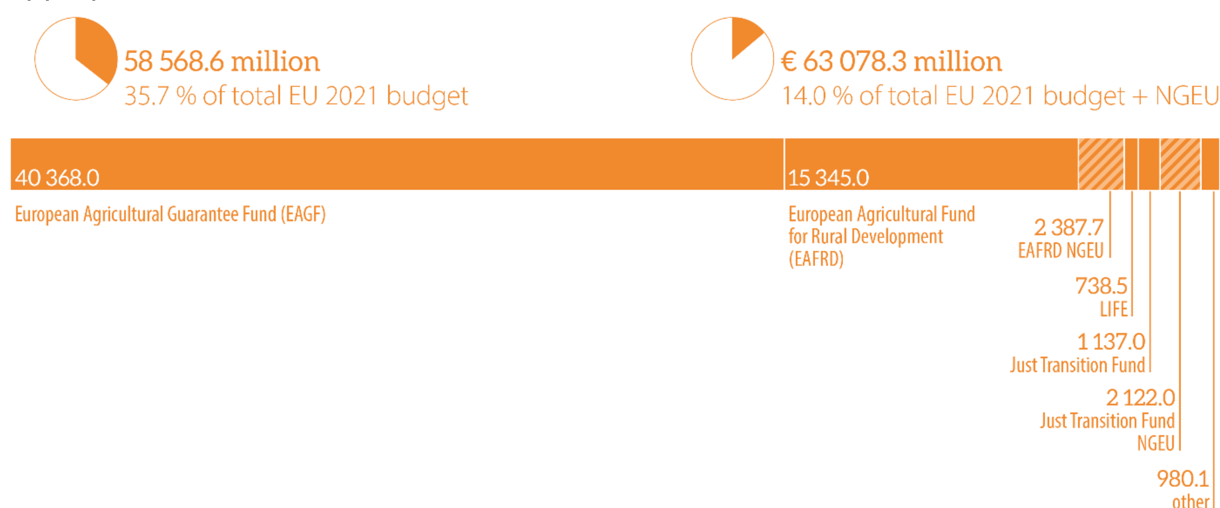
The Union civil protection mechanism (RescEU) is another programme under subheading 2b whose allocation will be based largely on the NGEU contribution. It will comprise of €90.2 million from the regular budget and a €682.5 million contribution from NGEU. The cost of financing NGEU, €39.6 million in 2021, is also shown as part of subheading 2b.

The most spectacular increase in comparison with its 2020 allocation is in the EU4Health programme. Aimed at improving EU's capacity to react effectively to major health threats such as a pandemic, it will be endowed with a budget of €327.5 million (+370 %). This includes €74.3 million added to the programme in 2021 following the political agreement between the European Parliament and Council on the 2021-2027 MFF reached on 10 November 2020 (see Section 4.1. above).

Among EU programmes investing in people, social cohesion and values, some will increase and some will decrease. For instance, as compared with the 2020 budget, there has been a significant increase in allocations for Creative Europe (+37 %), the Justice programme (+6.8 %) and the decentralised agencies (+28.1 %)[157]. Whereas a considerable decrease in funding will affect the European Solidarity Corps (-27.3 %) and Erasmus+ (-7.7 %). The decrease in the Erasmus+ allocation would have been even bigger without €175.1 million reinforcement introduced to the budget to reflect the agreement on the 2021-2027 MFF reached between Parliament and Council (see Section 4.1. above).

Last but not least, the limited margin envisaged under the MFF ceilings for subheading 2b was used to reinforce EU4Health and Erasmus+ (€249.4 million). As a result, the total appropriations requested for subheading 2b exceeded the ceiling agreed, and the Flexibility Instrument had to be mobilised for an amount of €76.4 million in the 2021 budget.

Figure 15 – Heading 3 Natural resources and environment, 2020 commitment appropriations



Data source: European Commission see Annex 3.

In terms of funding, heading 3 is the biggest in the 2021 budget (35.7 %). It is dedicated to programmes supporting two main policy areas: agriculture and maritime policy (97 % of the allocation under heading), and environment and climate action (3 %). However, the latter are also integrated under other headings through climate mainstreaming (see Section 5.1.2).[158]

The European Agricultural Guarantee Fund (EAGF) finances market-related expenditure and direct payments. Even though in comparison with the 2021 budget the EAGF decreases by 7.1 %, it remains the biggest fund under heading 3 and the whole 2021 budget. The decrease, as explained

[157] In particular the European Labour Authority and the European Public Prosecutor's Office.

[158] A. D'Alfonso, Mainstreaming of climate action in the EU budget: Impact of a political objective, EPRS, European Parliament, 2019.

by the Commission, is partly related to the withdrawal of the United Kingdom.[159] The next biggest fund under the heading, the European Agricultural Fund for Rural Development (EAFRD), supports structural changes in rural areas. In 2021 the EAFRD envelope totals €14.7 billion. As compared with 2020, it represents an increase in both commitment (+4.4 %) and payment appropriations (+8.3 %). In addition, the EAFRD will be reinforced by €2.4 billion from NGEU (+16.3 %).

According to the agreement reached in December 2020 on transitional provisions for support by the EAFRD and the EAGF, in the financial years 2021 and 2022 both measures will continue to be spent under the 2014-2020 rules, but with financial envelopes and ceilings adjusted to the new MFF. This 'old rules-new money' principle has been decided owing to the delays in the legislative processes for setting up the EU's long-term budget and for the new spending rules for the CAP.[160]

In addition, heading 3 covers EU expenditure on the common fisheries policy. The implementation of the European Maritime and Fisheries Fund (EMFF) accelerated in the last two years of the 2014-2020 MFF but was only at the half way point in January 2021.[161] Therefore, a significant share of payments for EMFF projects will fall in the first years of the new MFF. Owing to this, the level of payment appropriations for the fund increases by 7.7 % in 2021.

Furthermore, in 2020, the rules for spending under the EMFF as well as the EAFRD and the EAGF were adapted in order to mitigate the impact of the pandemic on the agricultural and fisheries sectors. The implementation of different derogations and flexibility measures continues in 2021 and has an impact on the level of approved commitments and payments for these funds.

While only 3.3 % of the allocation in heading 3 accounts for the policy cluster 'Environment and climate action', spending in this area has been significantly boosted in comparison with 2020 (+196.7 %). This is a result of the 2021-2027 MFF negotiations and reflects the EU's commitment to reinforce actions related to climate policy and to promote a green transition. The Just Transition Fund (JFT) is a new instrument contributing to the EU efforts in this area. Aimed at supporting the EU regions worst affected by the transition to a low carbon economy, the JFT is part of the overall EU growth strategy known as the Green Deal. The European Parliament strongly supported the creation of the fund.[162] Similarly to the cohesion funds, the JTF will be governed by the new Common Provisions Regulation[163] and implemented under shared management by the Member States and the Commission. The JTF allocation in the 2021 budget amounts to €1.1 billion. The reinforcement from the NGEU instrument means that it will triple, reaching a total value of €3.2 billion (see Box 6).

The LIFE programme for environment and climate measures continues to support EU projects linked to the circular economy, biodiversity, protecting and improving the quality of air and water, implementation of the 2030 energy and climate policy framework, and the achievement of the goals of the Paris Agreement. In addition, the programme will contribute to the realisation of the

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[159] Draft general budget of the European Union for the financial year 2021. General introduction, 27 July 2020, p. 56.

[160] For more see: R. Rossi, Transitional provisions for the CAP post 2020, Briefing, EPRS, European Parliament, October 2020.

[161] European Commission, webpage on the European structural and investment funds and cohesion data (accessed on 12 January 2021).

[162] Parliament called for the establishment of such a fund back in March 2018 and supported the idea throughout the process of negotiating the 2021-2027 MFF. A provisional political agreement on the JTF regulation was reached in trilogue on 9 December 2020 and its implementation should begin in 2021. For more, see the Legislative Train schedule on the regulation establishing the Just Transition Fund, European Parliament.

[163] Common provisions on European Regional Development Fund, European Social Fund Plus, Cohesion Fund, and European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the 2021–2027 Border Management and Visa Instrument, European Parliament Legislative Observatory, 2018/0196(COD).

European Green Deal.[164] In comparison with 2020, the commitments budgeted for the LIFE programme increase considerably (+25.3 %), reflecting the EU's commitment to these goals.

Box 6 – Social dimension of the Just Transition Fund

Underpinning the social dimension of the JTF is the allocation method of the JTF budget which ensures that 50 % of the distribution to Member States is determined by social indicators. More specifically, this means that 25 % of the JTF budget is allocated on the basis of relative levels of industrial employment in regions with carbon-intensive industry. The other 25 % is distributed on the basis of relative levels of employment in coal and lignite mining. Those Member States with the highest levels of employment in these areas will be compensated the most.

In addition, the JTF investments are aimed specifically at alleviating the social and economic costs of the climate transition for the territories identified. They will support, primarily through grants, economic diversification in the selected regions, reskilling, job search assistance and inclusion in the labour market for the workers concerned.

Source: S. Ionescu, G. Sabbati and F. Scholaert, A Just Transition Fund for climate-neutral EU regions, Infographic, EPRS, October 2020; Draft general budget of the European Union for the financial year 2021. General introduction, 27 July 2020.

Figure 16 – Heading 4 Migration and border management, 2021 commitment appropriations

Data source: European Commission see Annex 3.

Heading 4 is one of the smallest in the 2021 budget, but finances EU actions of high and growing importance in the area of migration and border management. Two main funds under this heading are the Asylum and Migration Fund (AMF), and the Integrated Border Management Fund (IBMF). An important share of heading 4 is allocated to the EU decentralised agencies, the European Border and Coast Guard Agency (Frontex) and the European Asylum Support Office (EASO).

The AMF supports national authorities in providing reception services for asylum seekers and migrants in the period immediately following their arrival on EU territory. It also aims to develop a common asylum and migration policy and ensure effective returns. In 2021 AMF expenditure will be mostly linked to the implementation of actions that began in the final years of the 2014-2020 MFF. Therefore, while in comparison with the 2020 authorised budget in 2021 the commitments decrease by almost one third, the payment appropriations increase by more than a third. In addition, the Member States are assisted by the European Asylum Support Office (EASO) in the performance of the tasks relating to asylum procedures. The allocation for the EASO in 2021 is €19.5 million higher than in 2020.

In the area of border management, the level of support is higher than in 2020 (+24.2 % in commitments). More financial means will go to implementation of the IBMF. Moreover, as of 2021

[164] In December 2020, The European Parliament and the Council reached a political agreement on the 2021-2027 LIFE programme. For details see: European Parliament, Legislative Observatory, 2018/0209(COD).

the allocation for the fund is split between the instrument for border management and visas (€398 million), and the new instrument for customs control (€135.5 million).

The allocation for Frontex continues to grow. Between 2019 and 2020 the increase amounted to 30 % and between 2020 and 2021 it is 20 %). In support of the agency's mandate to gradually establish a standing corps and provide Member States with enhanced support with returning third-country nationals, the budgetary authority approved an allocation amounting to €505.9 million in 2021 (+20 %).[165]

Under heading 4, €188.2 million (8.3 %) remains unallocated and can be used to cover unexpected expenditure. In relative terms, it is the biggest margin left under the MFF ceiling among all the headings in the 2021 budget.

Figure 17 – Heading 5 Security and defence, 2021 commitment appropriations

Data source: European Commission see Annex 3.

Heading 5 covers EU programmes in the area of security and defence, and represents 1 % of the total 2021 budget. It is a new element in the structure of the EU budget, introduced with the 2021-2027 MFF, and reflects mounting pressure for EU action in this area. It brings together already existing instruments addressing internal security challenges, and entirely new instruments in the area of EU defence, such as the European Defence Fund (EDF) and military mobility.

The allocation for the programmes in the area of EU defence is lower than it was proposed by the European Commission and requested by the European Parliament (-8 % and -28 % respectively). Most of the approved €1.172 billion will be implemented through the European Defence Fund (€945.7 million). The remaining €227.1 million has been ring-fenced for projects supporting military mobility. They will help to develop EU strategic transport infrastructure fit for dual civil-military use and will be implemented through the Connecting Europe Facility.[166]

Almost 33 % of the total €536.5 million allocation in the area of security will be spent through the Internal Security Fund (ISF). Created under the previous financial programming period, when it also supported actions relating to border control and visa policy now under heading 4, in the 2021-2027 period it will focus on common actions tackling terrorism and radicalisation, organised crime and cybercrime. In 2021, the ISF allocation decreases both in commitments (-10 %) and payments (-6.7 %). On the contrary, the allocation for the decentralised agencies acting in the area of EU security increases by 10.2 %. Among them, the European Union Agency for Law Reinforcement Cooperation (Europol) will be reinforced with an allocation 11.5 % higher than in 2020.

[165] In the draft budget the Commission proposed to allocate €566.9 million to Frontex. The amount finally agreed for the year 2021 is reduced by €61 million. However, as clarified in Parliament's resolution of 18 December 2020, the reduction does not affect the overall top-up of €500 million (2018 prices) agreed in the negotiations on the 2021-2027 MFF and it will be compensated for in later years. European Parliament, Resolution of 18 December 2020, 2020/0371(BUD).

[166] M. Pape, Connecting Europe Facility 2021-2027, Briefing, EPRS, European Parliament, June 2020.

A relatively high margin, amounting to 5.6 % of the allocation under heading 5, can be used for unexpected events.

Figure 18 – Heading 6 Neighbourhood and the world, 2021 commitment appropriations

Data source: European Commission see Annex 3.

Heading 6 covers two policy clusters, external action and pre-accession assistance. The instruments under the heading focus on development assistance, humanitarian aid, the EU's common foreign and security policy, and support for EU candidate countries. In the new programming period, within these policy areas, the programmes under heading 6 will tackle such issues as climate change, migration, human rights, democracy and rule of law, and security. In addition, since the outbreak of the pandemic, spending under heading 6 contributes to the implementation of the global EU response to Covid-19.[167]

In comparison with the 2014-2020 MFF, programmes and funds under heading 6 have been significantly reorganised.[168] In the 2021 budget, 75 % of the total allocation for heading 6 goes to the new Neighbourhood, Development and International Cooperation Instrument (NDICI).[169] The instrument brings together several instruments existing already in the previous programming period, and the European Development Fund (EDF), which until the end of 2020 was an intergovernmental fund, outside the EU budget.[170] As a result, the NDICI is essentially a new instrument, covering EU actions with very broad geographical and thematic scope, and, thus, difficult to compare with the 2020 budget.

The other area included in the external action policy cluster is humanitarian aid (HUMA). With the allocation amounting to €1.5 billion it delivers EU assistance to save and preserve lives, prevent and alleviate human suffering, and safeguard the integrity and dignity of populations affected by natural disasters or man-made crises. The payment appropriations under HUMA increase by 49 %, in order to cover the growing needs linked to progress in implementation of the actions that began in the 2014-2020 financial period.

The Instrument for Pre-accession Assistance (IPA III) continues to support reform in candidate and potential candidate countries. In addition, the instrument will contribute to action mitigating the consequences of Covid-19 in these countries. To fulfil these tasks, the budgetary authority set aside €1.9 billion in the 2021 budget. This represents an 8 % increase as compared with 2020.

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[167] General introduction to the draft general budget of the European Union for the financial year 2021, 27 July 2020.

[168] For details see: V. Lilyanova, Financing EU external action in the new MFF, 2021-2027, Briefing, EPRS, European Parliament, November 2019.

[169] For details see: B. Immenkamp, A new neighbourhood, development and international cooperation instrument, Briefing, EPRS, February 2020.

[170] A. D'Alfonso, European Development Fund – Joint development cooperation and the EU budget: out or in?, In-depth Analysis, EPRS, European Parliament, November 2014.

The margin available under the MFF ceiling is relatively small and represents less than 1 % of allocation under heading 6.

Figure 19 – Heading 7 European public administration, 2021 commitment appropriations

Data source: European Commission see Annex 3.

Heading 7 covers the administrative expenditure of all EU institutions, pensions for former staff and former Members of the institutions, and financing for the European schools. The share of the budget allocated to this heading is 6.4 %, slightly higher than the level in 2020 (6 %).

The 2021 budget for the EU administration reflects the strict measures that have been taken to ensure that this category of expenditure integrates all possibilities for rationalisation and savings. Drivers of the 2.2 % increase in appropriations in comparison to the previous year include the increase of 22 % in the pensions bill for former Members of the institutions, in particular for Members of the European Parliament retiring following the end of the eighth parliamentary term in 2019.[171]

4.4. Scrutiny of EU spending: Procedures in the European Parliament

In accordance with the cycle of scrutiny for the EU annual budget, management and execution of the 2021 budget will be evaluated during the course of 2022 and 2023 (Figure 20). The procedure will begin in the middle of 2022 after adoption of the final accounts by the European Commission (stage A), and end with a decision of the European Parliament adopted before 15 May 2023 (stage D) or in October 2023 in case of postponement (stage E).[172]

In 2021, the European Parliament is expected to take a discharge decision on the 2019 financial year. In June 2020, the European Commission launched the procedure with the publication of the annual accounts for the year 2019.[173] By the end of January 2021, the European Parliament's Budgetary Control Committee (CONT) had closed the hearings stage with respective commissioners and representatives of EU institutions and bodies (stage C).[174] In February, the members of the CONT committee will discuss the draft reports. Based on the reports, and after receiving the Council recommendation on the discharge, the European Parliament will take its decision by 15 May 2020 at the latest (stage D). According to the timetable for the procedure for the year 2019, most likely the decision will be taken at Parliament's April 2021 plenary session.[175]

[171] General introduction to the draft general budget of the European Union for the financial year 2021, 27 July 2020.

[172] The discharge procedure is based on Articles 317 to 319 of the Treaty on the Functioning of the EU. The timeframe for the procedure is determined in the Financial Regulation, in particular Articles 258 to 263. Regulation (EU, Euratom) 2018/1046 of 18 July 2018. For more see: A. D'Alfonso, Discharge procedure for the EU Budget: Political scrutiny of budgetary implementation, EPRS, European Parliament, May 2020.

[173] Integrated financial and accountability reporting 2019, European Commission, 24 June 2020.

[174] See the timetable for the discharge procedure for the financial year 2019 as of October 2020, Secretariat of the Committee on Budgetary Control.

[175] In recent years the institutions have managed to accelerate the procedures slightly. The decision on the 2017 discharge was voted in March 2019, one month earlier than usually. The decision on the discharge for the 2018 was

The European Parliament will also carry out the next discharge procedure in 2021, covering the 2020 budgetary year. The procedure will begin with the publication of the accounts and series of budgetary reports and evaluations by the European Commission. Following this stage, the European Court of Auditors (ECA) will present its annual report with the statement of assurance (DAS)[176] on the implementation of the 2020 financial year.

The possibility to accelerate the discharge procedure and close it within the year following the accounting year in question (n+1) is a longstanding demand of the CONT committee. However, the revision of the EU's Financial Regulation adopted in July 2018 did not introduce any significant changes that could shorten the time lag between the implementation of the budget and its political scrutiny.

Figure 20 – EU discharge procedure from the perspective of the European Parliament

Source: EPRS.

The European Parliament plays a crucial role in the democratic scrutiny and control of the implementation of the EU budget.[177] Within the annual discharge procedure it not only signs off the financial year, but also makes recommendations for improving the financial management and implementation of the EU budget. After receiving a recommendation from the Council, it ascertains whether the European Commission upheld the principles of sound financial management and abided by the applicable rules and regulations when implementing the budget.[178] Parliament grants separate discharge to the other EU institutions for the management of their sections of the general budget, and to the decentralised agencies and joint undertakings for their budgets.

In addition to scrutinising the regularity and legality of the budget's implementation, the discharge procedure focuses increasingly on performance culture, performance information and achievement of goals. The principles of performance orientation have gradually permeated many aspects of the management, implementation and control of the EU budget. Since 2015, the principles have been included in the Commission's 'EU budget focused on results' initiative. This wider approach to the assessment of EU spending is strongly supported by the European Parliament and the ECA. Many of the improvements introduced so far in this respect were triggered by opinions and demands expressed during the budgetary discharge procedure, for instance in the ECA's annual and special reports and the European Parliament's resolutions.[179]

tabled for the vote in the EP plenary in March 2020. However, due to the outbreak of the pandemic, it had to be postponed and was voted in May. The discharge procedure for the 2019 financial year can be followed on the European Parliament's Budgetary Control Committee website.

176 The statement of assurance (known as the DAS) is the official opinion issued by the ECA on the reliability of the accounts and on the legality and regularity of the underlying transactions (Article 287 TFEU and Article 148 Financial Regulation).

177 Please see: R. Corbett, F. Jacobs and D. Neville, The European Parliament, 9th edition, John Harper Publishing, 2016, pp. 333-337; A. D'Alfonso, Discharge procedure for the EU budget. Op. cit.

178 For the methods of implementation of the EU budget please see Section 3.3.

179 For more on performance-based budgeting in the EU's budget see: M. Sapala, Performance budgeting – A means to improve EU spending, EPRS, European Parliament, March 2018.

Box 7 – ECA publications in 2021

Employment and social affairs is one of the core areas covered in the publications of the ECA. Examples of recently published and particularly relevant reports include a special report on combating child poverty, and a special report on the Fund for European Aid to the Most Deprived.

Furthermore, in the course of 2021, the ECA will be publishing various special reports and other products on topics related to EU social and labour policy, for instance a review of the Commission's strategies and initiatives on basic digital skills for adults (25-64 years); a special report on gender equality, to assess whether the EU budget promotes equality between women and men through gender mainstreaming; and a special report to assess the effectiveness of the European Social Fund in fighting long-term unemployment.

Source: European Court of Auditors, Work plan 2021.

One of the results of these developments is a new approach to the presentation of budgetary performance in the ECA's annual report. For the first time in the report for the financial year 2019, the presentation is split into two parts: one on compliance and regularity of the EU accounts and transactions, as required by the Treaty, and the other on performance of spending programmes. Up until now the annual report has focused on legality and regularity, and the report on performance was included in one chapter of the document. A more in-depth analysis and assessment of performance and achievement of objectives was presented in other documents, such as the special reports and landscape reviews (see Box 7).[180] The new performance report assesses how much relevant performance information is available and how well EU spending programmes have actually performed. It presents detailed analyses of performance indicators, of the impact of EU spending and of progress towards targets.[181] The approach will be continued in future annual reports.

[180] For more see: Audit reports and opinions, European Court of Auditors.

[181] Report of the European Court of Auditors on the performance of the EU budget – Status at the end of 2019, Luxembourg 2020.

5. The EU budget beyond 2021

The new MFF sets out the structure for EU spending up until the end of 2027, while the Next Generation EU (NGEU) recovery instrument significantly reinforces the resources channelled through EU budgetary instruments over the years 2021 to 2023. The withdrawal of the UK from the EU on 31 January 2020 and the end of the transition period on 31 December 2020 mean that the new MFF is the first budgetary framework in which the UK will not take part. In the new programming period, further reform of the financing system is envisaged, since the European Commission is expected to table proposals for new own resources.

5.1. Overview of the 2021-2027 MFF

5.1.1. Ceilings for commitments and payments

Table 3 recapitulates the maximum level of resources available for each major category of EU spending under the traditional MFF each year until 2027. Total appropriations amount to €1 074.3 billion for commitments and €1 061.06 billion for payments (2018 prices). However, these figures will gradually increase by €11 billion each, thanks to upwards adjustments of the ceilings secured by Parliament during the MFF negotiations (see Section 5.1.3 below).

As for the year 2021, any margins left available between relevant ceilings and the appropriations authorised by the budgetary authority for the annual budget (see Chapter 4) represent resources that amending 2021 budgets could mobilise during the year to address new challenges and unexpected events.[182]

Looking at the evolution of ceilings for commitments over time, it can be noted that the structure of the EU budget financed by the traditional MFF is projected to change to a certain extent in the course of the programming period. Upwards trends characterise the following headings: '2. Cohesion, Resilience and Values'; '4. Migration and Border Management'; '5. Security and Defence'; and '7. European Public Administration'. The opposite is true for the remaining headings: '1. Single Market, Innovation and Digital'; '3. Natural Resources and Environment' (and direct payments under the common agriculture policy); and '6. Neighbourhood and the World'.

With regard to payments, the ceilings are higher in the first two years of the programming period before stabilising at €149.9 billion as from 2023 (2018 figures). This feature may help to avoid a repeat of the issue of payments backlogs that afflicted the initial years of the 2014-2020 MFF.[183] Payments needs tend to increase during the transition between programming periods, on account of the fact that many projects financed under the old generation of programmes come to completion. In addition, the European Court of Auditors reported a record level of outstanding commitments at the end of 2019, on the account of a number of factors, including delays in the implementation of the 2014-2020 European structural and investment (ESI) funds.[184]

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[182] It should be noted that the MFF Regulation presents ceilings in 2018 prices, while the annual budget is presented in current prices. For example, 2021 ceilings are set at €154 049 million for commitments and €156 557 million for payments (see Table 3). Expressed in current prices, the ceilings amount to €163 483 million for commitments and €166 140 million for payments. The adopted 2021 budget leaves margins below the ceiling of €778.8 million for commitments and €2 001.4 million for payments (current prices).

[183] For a thorough analysis of the problem see: A. D'Alfonso and M. Sapala, Payments backlog in in recent EU budgets. Lessons learnt and outlook, EPRS, European Parliament, November 2015.

[184] European Court of Auditors, Annual reports concerning the financial year 2019, November 2020. In the joint declarations attached to the 2021 budget, the budgetary authority recalled the need to monitor implementation of the 2014-2020 programmes and the progression of payments closely. Should the payment appropriations entered in the 2021 budget be insufficient to cover the estimated needs, the Commission is expected to present an appropriate solution as a matter of urgency to allow the budgetary authority to take the necessary decisions.

Table 3 – MFF for the 2021-2027 period (€ million, 2018 prices, EU-27)

Commitments	2021	2022	2023	2024	2025	2026	2027	Total 2021-2027
1. Single Market, Innovation and Digital	**19 712**	**19 666**	**19 133**	**18 633**	**18 518**	**18 646**	**18 473**	**132 781**
2. Cohesion, Resilience and Values	**49 741**	**51 101**	**52 194**	**53 954**	**55 182**	**56 787**	**58 809**	**377 768**
2a. Economic, social and territorial cohesion	45 411	45 951	46 493	47 130	47 770	48 414	49 066	330 235
2b. Resilience and values	4 330	5 150	5 701	6 824	7 412	8 373	9 743	47 533
3. Natural Resources and Environment	**55 242**	**52 214**	**51 489**	**50 617**	**49 719**	**48 932**	**48 161**	**356 374**
of which: market-related expenditure and direct payments	38 564	38 115	37 604	36 983	36 373	35 772	35 183	258 594
4. Migration and Border Management	**2 324**	**2 811**	**3 164**	**3 282**	**3 672**	**3 682**	**3 736**	**22 671**
5. Security and Defence	**1 700**	**1 725**	**1 737**	**1 754**	**1 928**	**2 078**	**2 263**	**13 185**
6. Neighbourhood and the World	**15 309**	**15 522**	**14 789**	**14 056**	**13 323**	**12 592**	**12 828**	**98 419**
7. European Public Administration	**10 021**	**10 215**	**10 342**	**10 454**	**10 554**	**10 673**	**10 843**	**73 102**
of which: administrative expenditure of the institutions	7 742	7 878	7 945	7 997	8 025	8 077	8 188	55 852
TOTAL COMMITMENTS	**154 049**	**153 254**	**152 848**	**152 750**	**152 896**	**153 390**	**155 113**	**1 074 300**
TOTAL PAYMENTS	**156 557**	**154 822**	**149 936**	**149 936**	**149 936**	**149 936**	**149 936**	**1 061 058**

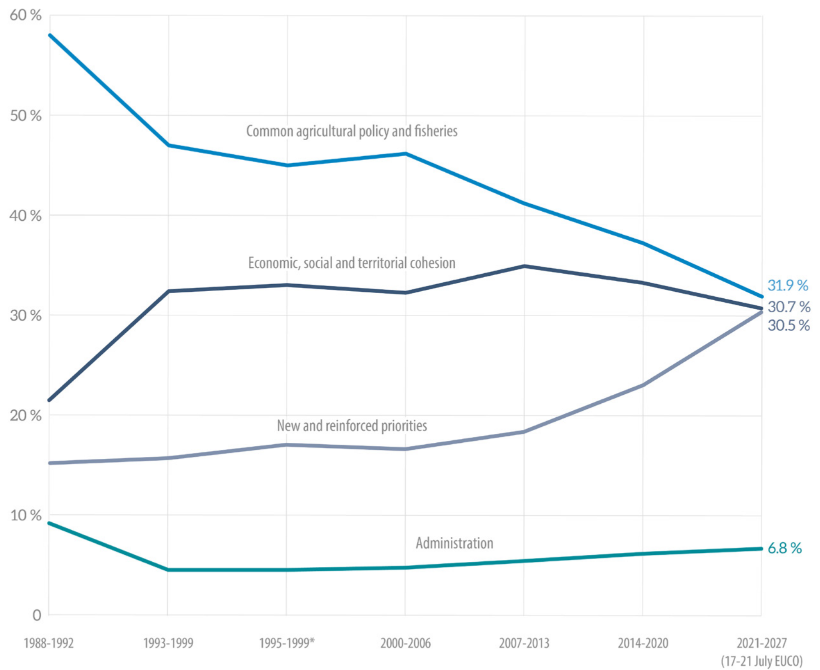
Source: Council Regulation (EU, Euratom) 2020/2093, Annex I.

For these reasons, it is appropriate for the MFF to have payments ceilings commensurate with high payments needs expected in the initial years of a new framework. In addition, as of 2022, unused resources under the payment ceiling from the previous year will be used to adjust upwards the payment ceiling of subsequent years, by means of the Single Margin Instrument, which is designed to increase the flexibility of the framework (see Section 5.1.4 below).

5.1.2. Changes to EU spending structure and priorities

The new framework implies a rebalancing of resources between broad categories of expenditure. Figure 21 shows that the shares of the MFF devoted to both traditional policies – agriculture and cohesion – decrease, while the resources for new and reinforced priorities rise. This development results in the three broad categories of expenditure having similar shares, each above 30 % of the total.

Figure 21 – Share of main policy areas in multiannual financial frameworks



Source: European Commission.

In the Commission proposals, the rebalancing was even more significant. As compared to the Commission proposal of May 2020, the European Council of July 2020 increased appropriations for cohesion policy and agriculture (by 2.2 % and 0.9 %), confirming Member States' attention to funds with geographically pre-allocated expenditure. 'Migration and Border Management' and 'Security and Defence', the two headings afflicted by the largest relative cuts, have higher allocations than in 2014-2020, but significantly lower than in the Commission proposals and in Parliament's position of November 2018. The same applies to programmes considered to be investments in EU common goods such as Horizon Europe (-6.2 % on the revised Commission proposal) and Erasmus+ (-13.8 %). Parliament criticised these cuts to the amounts proposed for programmes with high European added value and managed to obtain reinforcements for 10 flagship instruments in the MFF negotiations (see Section 5.1.3). The rebalancing of resources between traditional policies and reinforced priorities is even more significant when taking into account the resources expected to stem from NGEU (see Section 5.2).

Another feature that characterises the new MFF is the reduction in the number of its implementing programmes as part of an effort to simplify the EU budget and the rules that govern its implementation. One example of this strategy is the new InvestEU programme, a single investment support mechanism that is to bring together various EU financial instruments for internal policies, previously supported by different funds and programmes of the EU budget.[185]

In addition to the allocation of resources between headings, the new MFF and NGEU have horizontal priorities involving different headings. Climate mainstreaming[186] is the incorporation of climate considerations and objectives across all major spending programmes. The political agreement reached by Parliament and Council on the new MFF includes an increase in the climate

[185] A. D'Alfonso, InvestEU programme: The EU's new investment support scheme, EPRS, European Parliament, 2020.

[186] A. D'Alfonso, Mainstreaming of climate action in the EU budget: Impact of a political objective, EPRS, European Parliament, 2019.

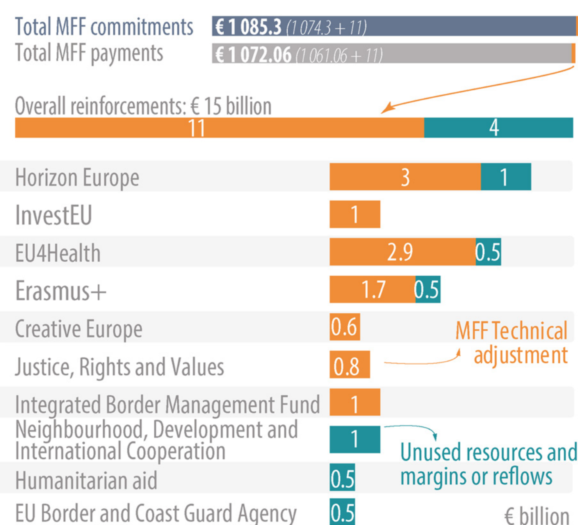
mainstreaming objective from 20 % of total resources in the past framework to 30 % in the years 2021 to 2027. This strengthened objective applies both to the new MFF and Next Generation EU, which could result in a €550 billion EU budget contribution to the broader European Green Deal Investment Plan[187] by 2027.

As advocated by Parliament, the new interinstitutional agreement on budgetary matters[188] includes provisions to strengthen climate mainstreaming methodology and to introduce corrective measures in case of insufficient progress towards the 30 % objective. In addition, Parliament managed to obtain the development of methodologies for a biodiversity spending target (7.5 % in 2024 and 10 % from 2026) and to measure the gender impact of expenditure.

5.1.3. Programme-specific reinforcements to ceilings as of 2022

During the years 2022 to 2027, the overall level of MFF resources will gradually increase to €1 085.3 billion for commitments (i.e. €2 billion more than the 2014-2020 MFF without the UK and including the EDF) and €1 072.1 billion for payments (2018 prices), thanks to a new article in the MFF Regulation negotiated by Parliament (see Section 3.4) that introduces annual upwards adjustments of the ceilings for subheading '2b. Resilience and Values' (+€6 billion in total by 2027) and headings '1. Single Market, Innovation and Digital' (€4 billion) and '4. Migration and Border Management' (+€1 billion). These adjustments will start as of 2022 and be programme-specific, focusing on instruments with high European added value that Parliament identified as deserving further resources as compared to the European Council's settlement of July 2020 (see Section 3.4). The financing of the total €11 billion reinforcement will be linked to revenue stemming from competition fines, in line with Parliament's long-standing call for such revenue to finance the EU budget. The top-ups will go to flagship programmes providing EU common goods such as research, health, Erasmus+ and border management, based on an allocation key defined in the new Annex II of the MFF Regulation.

Figure 22 – Agreed reinforcements by instrument



Source: EPRS, based on MFF Regulation, IIA and joint declarations.

In addition, some of these programmes as well as other two instruments (the Neighbourhood, Development and International Cooperation Instrument and humanitarian aid) and Frontex (the EU Border and Coast Guard agency) will receive a further €4 billion from the re-use of de-committed funds for research (another recurrent demand from Parliament), reflows from predecessor instruments and unused margins (see Figure 22 for an overview of top-ups by instrument). These resources, some of which are already included in the adopted budget for 2021, do not lead to upward revisions of the ceilings.

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[187] For more information on the investment plan, see: A. D'Alfonso, European Green Deal Investment Plan: Main elements and possible impact of the coronavirus pandemic, EPRS, European Parliament, April 2020.

[188] European Parliament, Decision on the conclusion of an Interinstitutional Agreement between the European Parliament, the Council of the European Union and the European Commission on budgetary discipline, on cooperation in budgetary matters and on sound financial management, as well as on new own resources, including a roadmap towards the introduction of new own resources, 16 December 2020.

5.1.4. Special instruments

The MFF includes five special instruments, either thematic or non-thematic, to address unexpected events with resources on top of the MFF ceilings. Four out of five have annual or total amounts available set in the MFF Regulation, including a Brexit Adjustment Reserve that aims to counter unforeseen and adverse consequences in Member States and sectors worst affected by the UK withdrawal.

Table 4 recapitulates the amounts available for these four instruments. The European Parliament is a strong advocate of flexibility tools to address new challenges, given the long timespan covered by MFFs in a world that is changing at an increasingly fast pace. In the MFF negotiations (see Section 3.4), Parliament managed to reinforce these instruments and bring the total amounts available for them up to €21.1 billion over the next seven years, by ensuring a €1 billion increase for the Flexibility Instrument and broadening the possibilities for its use.

Table 4 – Four special instruments with specific (annual or total) amounts available outside the MFF ceilings (2018 prices, € million)

Special instrument	Annual amount	Total amount	Total amounts for 2021 to 2027
European Globalisation Adjustment Fund	186		1 302
Solidarity and Emergency Aid Reserve	1 200		8 400
Brexit Adjustment Reserve		5 000	5 000
Flexibility Instrument	915		6 405
TOTAL			**21 107**

Source: EPRS, based on Council Regulation (EU, Euratom) 2020/2093.

A fifth special instrument, the Single Margin Instrument, has no pre-fixed amounts, but makes it possible to increase ceilings in a given year by resorting to unused margins from previous years or to resources to be offset in subsequent years. Its annual use is capped at 0.04 % of EU GNI for commitments and 0.03 % of EU GNI for payments. Different rules apply to unused margins from previous years for payments, which are automatically transferred to the following year (see Section 5.1.1), and for commitments, which may be mobilised by Parliament and Council in the framework of the budgetary procedure.

5.1.5. United Kingdom: Past obligations and participation in a limited number of new programmes

The 2021-2027 MFF is the first budgetary framework in which the UK will not take part following its withdrawal from the European Union. Given the multiannual nature of many expenditure items in the EU budget, a number of the commitments that the EU, still including the UK, entered into during the 2014-2020 period will only become payable after 2020. The settlement of the UK's financial obligations towards the EU was one of the three priorities identified for the first phase of the negotiations on the withdrawal agreement.[189] During the negotiations, the UK agreed to honour its

[189] The MFF and the annual EU budget are immediate examples of financial liabilities to be disentangled, but the landscape of financial obligations jointly undertaken by EU Member States is broader and more complex than that. For more details, please see A. D'Alfonso, E.-M. Poptcheva, J. McEldowney and L. Tilindyte, The Brexit negotiations: Issues for the first phase, EPRS, European Parliament, June 2017; C.-C. Cirlig, Brexit: Understanding the withdrawal agreement and political declaration, EPRS, European Parliament, March 2019; and C.-C. Cirlig, The revised Brexit deal: What has changed and next steps?, EPRS, European Parliament, October 2019.

share of the financing of all the obligations undertaken during its EU membership. The Withdrawal Agreement translates the conclusions on the financial settlement reached during the negotiations into legal provisions. In practice, this results in the UK withdrawal having no impact on the 2014-2020 MFF, the payment of related obligations and the transition to the new MFF.[190]

As for the 2021-2027 MFF, the EU-UK Trade and Cooperation Agreement,[191] announced on 24 December 2020,[192] enables the UK's continued participation in a number of EU programmes and activities. The relevant protocols, which have still to be finalised at the time of writing,[193] list four programmes in the areas of research, innovation and space, namely: Horizon Europe; the Euratom Research and Training programme; the fusion test facility ITER; and the earth monitoring system Copernicus. The UK's participation in the programmes will be that of a third country and will be subject to a financial contribution to the EU budget, based on a contribution key linked to the EU and UK's respective gross domestic product (GDP) at market prices. These provisions mean that relevant programmes will receive additional resources from the UK, on top of those stemming from the MFF and, where applicable (i.e. Horizon Europe), from NGEU. Furthermore, the UK will not participate in but will have access to the services of the EU's satellite surveillance and tracking (SST) services, based on a number of conditions. In addition, already under the Withdrawal Agreement, both the EU and the UK have committed to continued financing of peace, prosperity and reconciliation projects on the island of Ireland under the PEACE PLUS programme, which will be the subject of a separate financing agreement.

5.2. Next Generation EU: Temporary recovery instrument

5.2.1. Main features

A major innovation of the new programming period is the launch of Next Generation EU, the common instrument that will provide resources for the economic recovery on top of MFF resources. Its financing is to be ensured by borrowing operations that the Commission will carry out on behalf of the Union. Borrowing operations for NGEU activities can start once the new own resources decision has been ratified by all Member States (see Section 3.2).

The Commission has already borrowed resources on the markets to provide Member States with financial support. The relevant instruments have been built on the use of the margin available under the own resources ceiling as a guarantee and/or on guarantees from Member States. One recent example is SURE, a €100 billion instrument for temporary support for unemployment schemes, which the EU created as part of its response to the pandemic.[194]

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[190] Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community, OJ L 29, 31.1.2020, p. 7–187. See in particular: Part Five, Chapter 2.

[191] Trade and Cooperation Agreement between the European Union and the European Atomic Energy Community, of the one part, and the United Kingdom of Great Britain and Northern Ireland, of the other part, OJ L 444, 31.12.2020, pp. 14–1462.

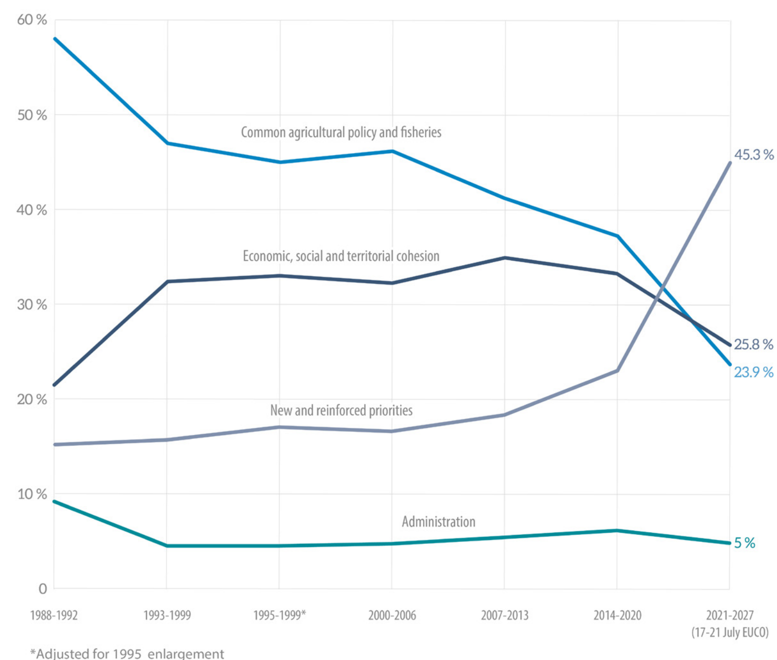
[192] The agreement began to apply, on a provisional basis, on 1 January 2021, but it has not yet been approved by the European Parliament at the time of writing.

[193] Declarations referred to in the Council Decision on the signing on behalf of the Union, and on a provisional application of the Trade and Cooperation Agreement and of the Agreement concerning security procedures for exchanging and protecting classified information, OJ L 444, 31.12.2020, p. 1475–1485.

[194] A. D'Alfonso, Temporary support to mitigate unemployment risks in an emergency (SURE), EPRS, European Parliament, April 2020.

However, NGEU is unprecedented in scale, involving collective borrowing that represents some 5 % of EU GNI (although spread over a number of years).[195] For the first time, it will enable the EU budget to contribute directly to macroeconomic stabilisation (see Section 3.1). Amounting to €750 billion (2018 prices), NGEU means that the Commission will become a major emitter of bonds. Commission President, Ursula von der Leyen announced that 30 % of borrowing will be through green bonds,[196] which gives the EU an opportunity to establish itself as a standard-setter in this area worldwide.

Figure 23 – Share of main policy areas in the MFFs, including NGEU



Source: European Commission.

NGEU aims specifically to address the socio-economic consequences of the coronavirus pandemic and make the EU economy more resilient and sustainable through investment and reforms. Combined with the new MFF, it represents the largest stimulus package ever financed through the EU budget and further modifies the structure of EU spending as compared with the 2014-2020 period (see Figure 23 and Section 5.1.2). Commentators have dubbed the agreement momentous.[197]

Various analysts have identified the absorption capacity of the unprecedented level of resources channelled through the EU budget as an important challenge for the recovery package.[198] The CEPS think tank has estimated that NGEU support for individual southern and eastern European Member States may be worth as much as 3 % to 5 % of domestic GDP each year.[199]

Given its close link to the recovery from the impact of the pandemic, NGEU has been designed as a temporary instrument, with a shorter timespan than the new MFF. Commitments under NGEU must be carried out over the 2021-2023 period, while payments must be finalised by 2026. However, implementing rules enable the instrument to finance retroactively expenditure that Member States already incurred as from 2020 in the wake of the pandemic, with a view to countering its consequences.

NGEU resources are composed of grants (€390 billion) and loans (€360 billion). The former will provide additional resources for the EU budget and increase its size in the form of external assigned revenue (see Chapter 4), while the latter will be transferred, through a EU budgetary instrument but

[195] A. D'Alfonso, Next Generation EU: A European instrument to counter the impact of the coronavirus pandemic, EPRS, European Parliament, July 2020.

[196] U. von der Leyen, State of the Union Address at the European Parliament Plenary, 16 September 2020.

[197] Recovery fund is a huge breakthrough for the EU, Editorial Board, Financial Times, 21 July 2020.

[198] Z. Darvas, Will European Union countries be able to absorb and spend well the bloc's recovery funding?, Bruegel Blog, 24 September 2020.

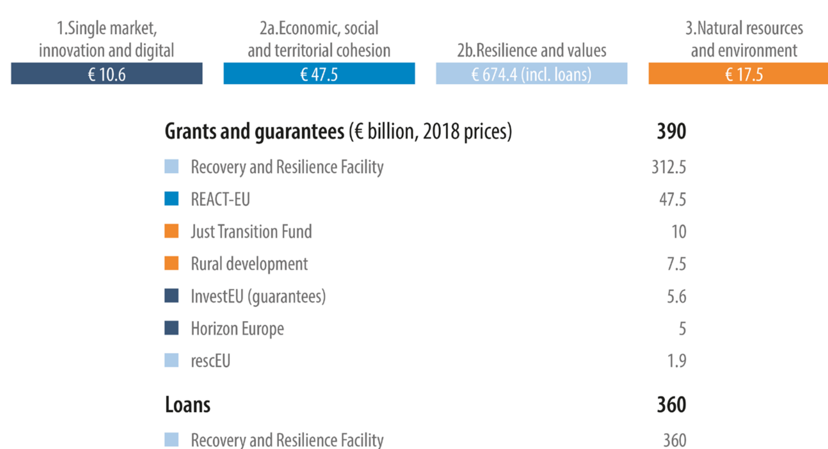
[199] C. Alcidi, D. Gros and F. Corti, Who will really benefit from the Next Generation EU funds?, CEPS, Policy Insight 2020-25, October 2020.

outside the EU budget, to the Member States that have requested them. Repayments are spread over a long timeframe (by 2058 at the latest). The EU budget will repay the grants and their borrowing costs, while Member States that have resorted to loans will be in charge of their repayment.

Another significant feature of NGEU is that resources will be spent in line with commonly agreed EU objectives, such as the green transition and digital transformation, with a view to increasing the resilience and sustainability of economies and societies. The idea is to ensure not only an economic rebound, but also a quality recovery. This approach is consistent with calls for stimulus packages to invest in activities contributing to the fight against climate change, an opportunity that fiscal spending left largely untapped in the wake of the 2007-2008 financial crisis.[200]

NGEU will provide resources for seven EU budgetary instruments under headings 1, 2 and 3 of the MFF, including in the area of cohesion (through the €47.5 billion REACT-EU programme, which will extend the crisis response and repair measures delivered under two Coronavirus Response Investment Initiative packages in 2020). Figure 24 presents the 2021-2023 allocation of resources between the seven instruments, showing that the bulk of funding will go to the Recovery and Resilience Facility (RRF).

Figure 24– Allocation of NGEU resources



Source: EPRS, based on Commission data.

Both in the interinstitutional agreement on budgetary matters[201] and the political agreement on the RRF,[202] Parliament managed to strengthen the involvement of the budgetary authority in the governance of NGEU and its largest implementing instrument, including through a regular recovery and resilience dialogue.

[200] See: McKinsey & Company, How a post-pandemic stimulus can both create jobs and help the climate, 27 May 2020.; and A. Bailey et al. The world must seize this opportunity to meet the climate challenge, *The Guardian*, 5 June 2020.

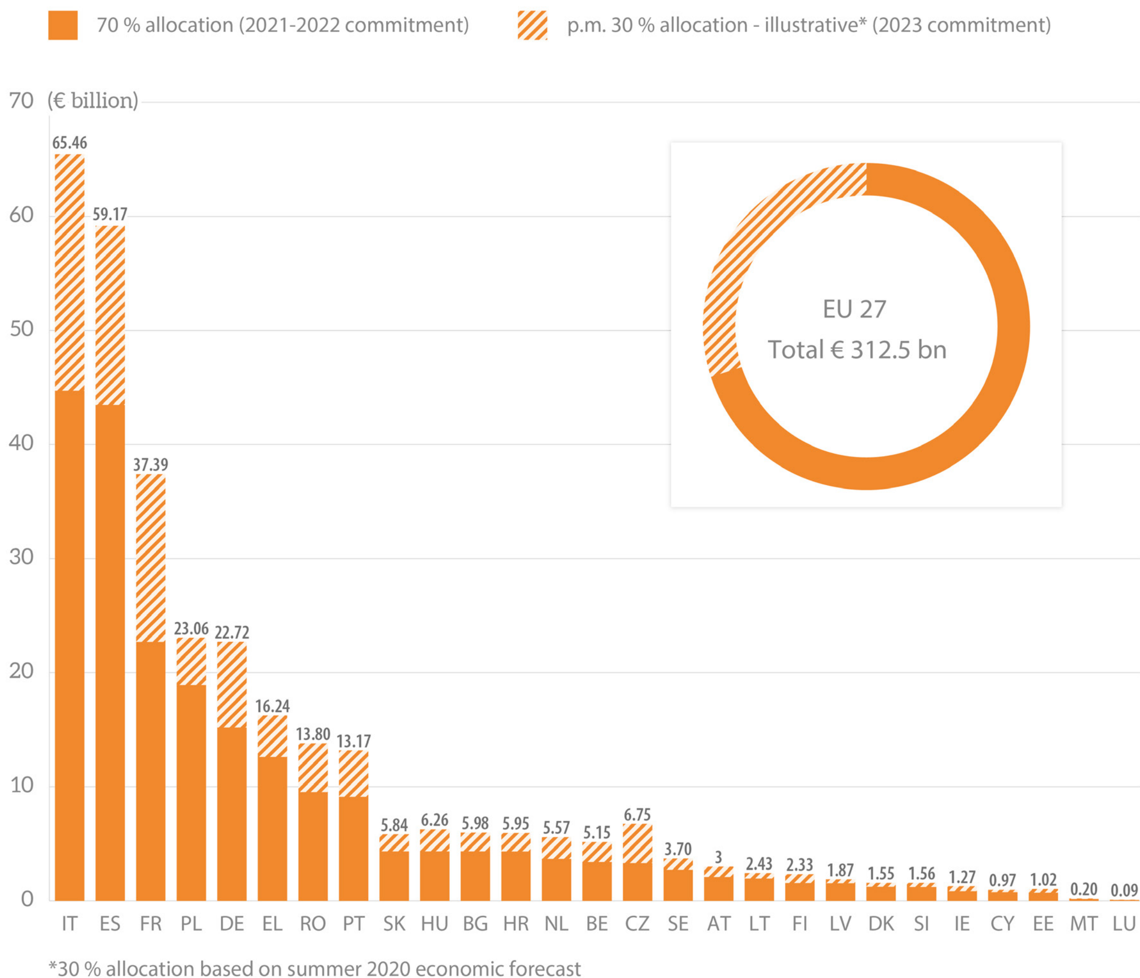
[201] European Parliament, Decision on the conclusion of an Interinstitutional Agreement between the European Parliament, the Council of the European Union and the European Commission on budgetary discipline, on cooperation in budgetary matters and on sound financial management, as well as on new own resources, including a roadmap towards the introduction of new own resources, 16 December 2020.

[202] Commission welcomes political agreement on Recovery and Resilience Facility, press release, 18 December 2020.

5.2.2. Recovery and Resilience Facility

The RRF will be the main implementing tool for the recovery instrument, channelling 80 % of NGEU grants and all NGEU loans. RRF spending will total €672.5 billion over the 2021-2023 period if Member States decide to use the loan component fully. To use these resources, Member States are to prepare national recovery and resilience plans with a coherent package of investments and reforms, taking into account the country-specific recommendations of the European Semester. Each plan should address issues that require significant investment to create jobs and growth, and earmark at least 37 % of the resources for the green transition and at least 20 % for the digital transformation. The Commission has encouraged national authorities to focus their plans on seven flagship areas: clean technologies and renewables; energy efficiency of buildings; sustainable transport and charging stations; rapid broadband services; digitalisation of public administration; data cloud capacities and sustainable processors; and education and training to support digital skills. Once the plans are approved by the Council, Member States will receive 13 % of the amount in pre-financing, with a view to ensuring that the flow of resources for the recovery start immediately. Subsequent payments will be linked to the achievement of milestones and targets.

Figure 25 – Recovery and Resilience Facility: National allocations for grants



Source: EPRS, based on Commission data.

One element under the spotlight is the allocation of resources among Member States, since one objective of NGEU is to focus support on the areas where the impact of the pandemic has been most

severe. Figure 25 shows the geographical distribution of RRF grants, with final allocations already known for 2021-2022 and estimated for 2023. The formula for the calculation is based on population, inverse of GDP per capita and the 2015-2019 unemployment rate compared with the EU average. The fall in real GDP in 2020-2021 replaces the last indicator for the allocation of resources for 2023. A series of safeguards avoid excessive concentration of resources. As for loans under the same facility, the maximum amount for each Member State is capped at 6.8 % of its GNI in 2019.

5.2.3. The debate on a permanent fiscal capacity

Following the euro crisis, one challenge in relation to which the possible role and contribution of the EU budget have been debated concerns efforts to strengthen economic and monetary union (EMU). In this respect, one idea that has long been on the table is the creation of a specific 'fiscal capacity' for the euro area, either inside or outside the EU budget.[203] Proving politically sensitive, the debate on this idea has advanced slowly, but it is possible that it will stay on the agenda and be broadened to the entire EU after the launch of NGEU.

In 2017, four months after being elected, French President Emmanuel Macron revived the idea, calling for the creation of a common budget for the euro area,[204] while Jean-Claude Juncker, Commission President at the time, supported the establishment of a dedicated euro-area budget line as a subsection of the EU budget itself.[205] In May 2018, the European Commission put forward[206] proposals for the establishment of two new budgetary instruments to deepen EMU under the post-2020 MFF. In the Meseberg Declaration of June 2018, France and Germany jointly proposed creating a euro-area budget within the EU framework as of 2021, identifying the promotion of competitiveness, convergence and stabilisation in the currency area as its objective.[207] In this respect, the two countries presented a proposal on the architecture of such an instrument to the Eurogroup in November 2018. In 2019, discussions advanced on the design of a – rather limited – budgetary instrument for convergence and competitiveness (BICC), but references to a stabilisation function were not included.[208]

In 2020, the outbreak of the coronavirus pandemic and its severe impact changed the debate on this instrument dramatically, as the European Council and Parliament asked the Commission to put forward proposals for an appropriate recovery instrument (see Section 3.4). On 18 May 2020, a Franco-German initiative backed the idea of an ambitious recovery fund at EU level for solidarity and growth. A few days later, the Commission presented the proposal for NGEU and the amended proposals for the 2021-2027 MFF, withdrawing the proposal for the BICC.

The subsequent agreement on NGEU has led to the establishment of a recovery instrument that is much bigger in size and scope than the BICC would have been. Another important difference concerns the geographic coverage, since NGEU is not limited to the euro area but is an EU-wide instrument, contrary to ideas that were explored in the wake of the euro crisis.

NGEU being a temporary tool, the debate on the need to create a permanent fiscal capacity has been relaunched. In October 2020, Christine Lagarde, President of the ECB, deemed NGEU a turning

[203] A. D'Alfonso and A. Stuchlik, A fiscal capacity for the euro area?, EPRS, European Parliament, September 2016.

[204] E. Macron, Initiative for Europe, Sorbonne speech, 26 September 2017.

[205] J.-C. Juncker, State of the Union address 2017, 13 September 2017.

[206] EU budget: A reform support programme and an investment stabilisation function to strengthen Europe's economic and monetary union, press release, European Commission, Brussels, 31 May 2018.

[207] Meseberg Declaration. Renewing Europe's promises of security and prosperity, Presse- und Informationsamt der Bundesregierung, 19 June 2018.

[208] Eurogroup, Term sheet on the budgetary instrument for convergence and competitiveness (BICC), press release, 10 October 2019.

point for the EU, arguing that its possible transformation into a permanent instrument should be discussed as well as the creation of a common budgetary tool for the euro area.[209] Some analysts consider that transforming the recovery instrument into a permanent facility is a key priority for reinforcement of EMU.[210] However, views on this idea continue to differ, requiring further political debate.

5.3. Roadmap for further reform of the financing system

At the European Council meeting of July 2020 (see Section 3.4), EU leaders agreed on the introduction of a new own resource as of 2021, a national contribution based on non-recycled plastic waste, and invited the Commission to make proposals for other new own resources (a border carbon adjustment mechanism and a digital levy, and a revised proposal linked to the EU's emissions trading system – ETS).

Parliament, which has long pushed for a thorough reform of the own resources system, deemed the agreed modernisation insufficient and included additional progress on this aspect as an essential element in its negotiations with Council on the 2021-2027 MFF.[211] The launch of NGEU is an additional reason for this position. In the absence of new own resources, there would be two main options for the repayment of the costs of NGEU grants when they become due: either an increase in national contributions to the EU budget or cuts to MFF expenditure in the post-2027 framework. Parliament has repeatedly stressed that new own resources should cover at least the repayment costs of the recovery instrument.[212]

On this basis, Parliament fast-tracked its legislative opinion on the own resources decision, to make it possible for Council to ensure the timely launch of NGEU, but managed to obtain the inclusion of a roadmap for the introduction of new own resources in the interinstitutional agreement on budgetary matters with Council and the Commission.[213] Under the agreed guiding principles for the reform set by the roadmap, new own resources should: raise enough revenue to repay the grant component of NGEU and its borrowing costs; be linked to EU policies and objectives,[214] such as the fight against climate change, the circular economy, and 'Europe fit for the digital age'; and contribute to fair taxation and to the strengthening of the fight against tax fraud and tax evasion. In addition to these and other guiding principles, the interinstitutional agreement includes a detailed roadmap for the introduction of new own resources, on top of the contribution based on plastic waste, by 2026 (see Figure 26). Envisaged own resources are linked to: a carbon border adjustment mechanism; a digital levy; a revised ETS; a financial transaction tax; and a financial contribution linked to the corporate sector or a new common corporate tax base.

The fact that the EU budget is currently financed mainly by national contributions is often deemed to hinder budgetary reform and exacerbate the focus of negotiations on budgetary balances (see

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[209] *Le Monde* Interview with Christine Lagarde, President of the ECB, conducted by M. Charrel and E. Albert, 19 October 2020.

[210] See for example: Á. Ubide, Memo to the European Commission on reforming Europe's economic policy to handle pandemic shock, Peterson Institute for International Economics (PIIE), 9 December 2021.

[211] European Parliament, Resolution on the conclusions of the extraordinary European Council meeting of 17-21 July 2020, 23 July 2020.

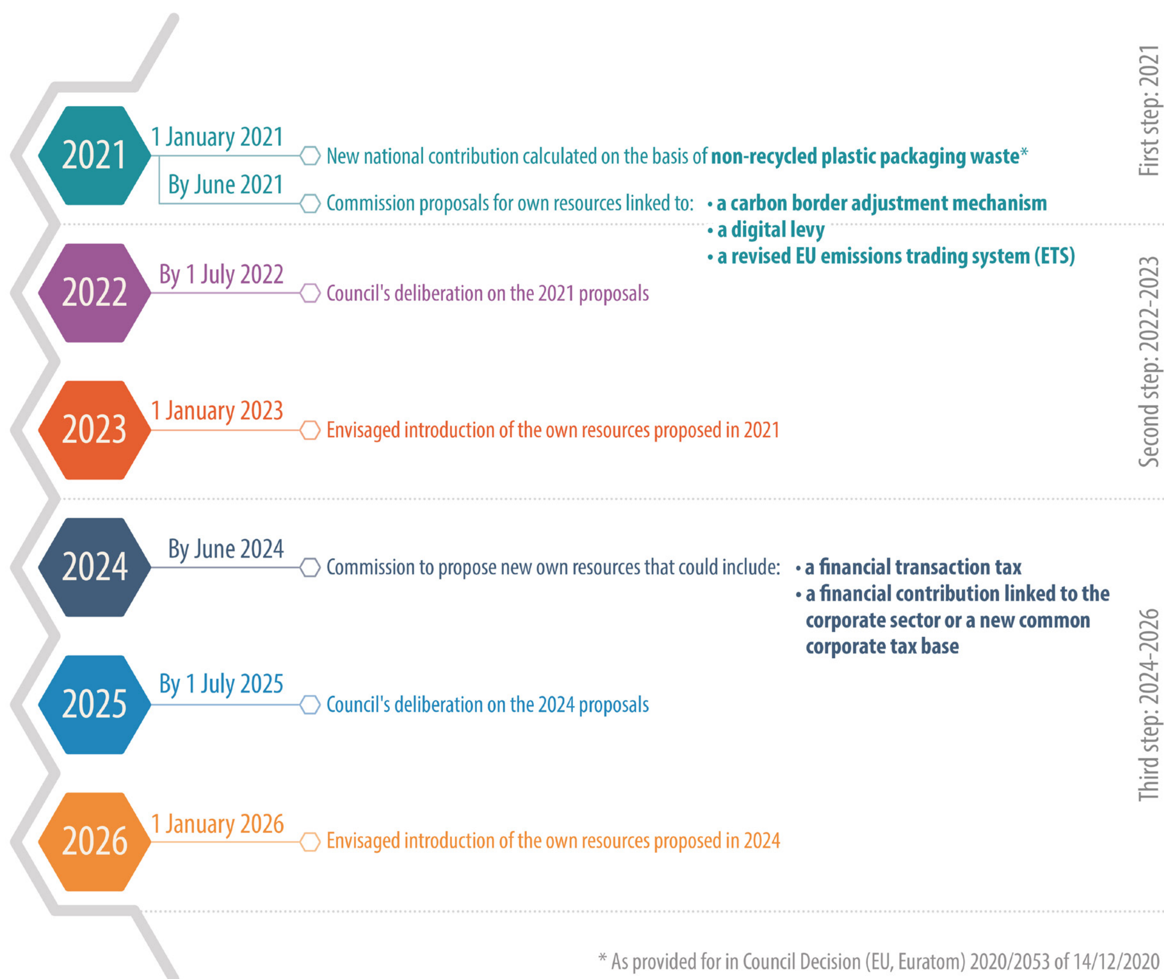
[212] A. D'Alfonso, Own resources of the European Union: Reforming the EU's financing system, EPRS, European Parliament, 2020.

[213] European Parliament, Decision on the conclusion of an Interinstitutional Agreement between the European Parliament, the Council of the European Union and the European Commission on budgetary discipline, on cooperation in budgetary matters and on sound financial management, as well as on new own resources, including a roadmap towards the introduction of new own resources, 16 December 2020.

[214] In line with High-Level Group on Own Resources' recommendations that the revenue side of the budget should contribute to achieving EU policy objectives.

Section 3.2). The adoption of new own resources could lead the way to considering avenues for broader reform of the EU budget.[215]

Figure 26 – Roadmap for the introduction of new own resources



Source: EPRS, based on the interinstitutional agreement on budgetary matters.

[215] F. Jones, Financing the European Union, EPRS Ideas Papers, European Parliament, December 2020.

6. Impact of the pandemic on European society

6.1. Society, labour markets and the pandemic

This chapter has been written in the middle of the second wave of the coronavirus pandemic. While economic output picked up swiftly following the easing of confinement measures and the initial re-opening of businesses following the first wave, the pace of the global recovery lost some momentum over the summer months of 2020.

With hope now secured by the vaccine, there is more chance of a more positive outlook. Yet as the first vaccines become available[216] en masse, the focus is shifting from the heroic effort of developing them to the equally difficult task of distributing them. Vaccine diplomacy will be needed as countries and regions work out who should get the vaccines when and in which order. In addition, emerging data suggests that a quarter of adults globally would refuse a vaccine. Meanwhile, as economies bounce back from the pandemic, the recovery will be patchy, as local outbreaks and clampdowns come and go – and governments turn from keeping companies on life-support to helping workers who have lost their jobs.

Pre-pandemic trends will remain the same, but will be exacerbated. These include the ageing population; rising inequalities between socio-economic groups, generations, genders and regions; new forms of work; and greater wage polarisation[217] between higher and lower paid workers.

6.1.1. Pre-crisis employment trends exacerbated

Labour market conditions have come under significant pressure during the pandemic, with sharp falls in hours worked.[218] This has be observed in all countries, with the largest falls in Greece, Spain, Italy and Portugal and the smallest in Finland and Sweden. At the same time, in many countries, reductions in employment rates have been limited so far, owing to job retention measures, such as short-time work schemes or wage subsidies. Overall, employment decreased[219] from 73.1 % in the last quarter of 2019 to 72.4 % in the third quarter of 2020. By May 2020, job retention schemes[220] were supporting approximately 50 million jobs across OECD economies, about 10 times as many as during the 2008 global financial crisis. Unemployment has edged up only gradually in the euro area, with lower-wage employees and younger workers relatively hard hit.

The World Economic Outlook[221] reports a significant rise in income inequality compared with the early 1990s. According to the Gini index,[222] the change is for example, 1.30 percentage points (pp) in the UK, 2.50 pp in Italy, 3.90 pp in Spain and 4.20 pp in Germany. As a result of the pandemic, on average[223] and in the absence of suitable policy responses, a substantial increase of 1.1 pp in the Gini index can be expected, following a long period of relative stagnation.[224]

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[216] 'The World in 2021', *The Economist*, 16 November 2020.

[217] EPRS, Global Trendometer, July 2018.

[218] See Eurostat 'Hours of work – quarterly statistics'. The levels of total actual hours worked are influenced by the total number of persons working, as well as the number of hours worked by each of these persons.

[219] Eurostat, Employment – quarterly statistics, January 2021.

[220] OECD, Economic Outlook, Interim Report, September 2020.

[221] IMF, World Economic Outlook, October 2020.

[222] The change is calculated as the latest available minus the Gini coefficient in 1990. For more information see OECD Income inequality.

[223] European Commission, 2020 Annual Report of the Social Protection Committee, November 2020.

[224] Eurostat, Gini co-efficient of equivalised disposable income – EU-SILC Survey, December 2020.

In the OECD countries[225] more than one in three people do not have enough financial assets to keep their family above the poverty line for at least three months, should their income suddenly stop. The risk is especially high in households headed by people younger than 34 and people without a higher education, as well as for couples with children. In addition to business closures, school closures have put enormous pressure[226] on families and will have had a negative effect on the educational outcomes[227] of many children in the longer term. Reported financial distress[228] reached a historical peak[229] of 17.4 % of the EU population in March 2014, before gradually declining to 12.7% and remaining stable from February to May 2019; it has however slowly risen since then. In May 2020, 13.7 % of the population – an increase of 1.3 pp compared with the same month one year earlier – declared the need to either draw on savings (9.9 %; +0.8 pp) or run into debt (3.8 %; +0.5 pp). However, no strong effect of the coronavirus crisis was detected in the April and May 2020 data. Financial distress increased disproportionately for those on low incomes. In May 2020 this indicator value reached 23.3 % (+2.0 pp) for the lowest quartile of incomes, in contrast with 7.6 % (+1.0 pp) for the wealthiest quartile.

In connection with the above, despite policy measures, poverty[230] is expected to increase by 0.1 pp on average in the EU when using the non-anchored at-risk-of-poverty (AROP) rate.[231] This non-anchored indicator shows that the poverty line is dropping substantially owing to the income shock of the coronavirus crisis. The change in the AROP rate is the same as that experienced between 2008 and 2009 as a result of the financial crisis. The poverty rate anchored to its pre-crisis level is expected to increase substantially on average by 1.7 pp in the EU under the policy response scenario and by 4.8 % under the no-response scenario. When the poverty rates are anchored to their 2019 values, poverty is expected to rise in all countries. In addition, the risk[232] of homelessness will rise and access to healthcare is set to fall.

Some of the measures necessary in the short-term could have adverse effects over the longer-term.[233] For example, short-term measures[234] are aimed predominantly at stabilising income and employment (often simultaneously reducing activation measures, e.g. up- and reskilling), while temporarily detaching income from work and economic activities. This can lead to longer-term inefficiencies[235] in the labour market. In addition, the introduction of temporary state aid rules – allowing governments to provide the economy with liquidity to support citizens and companies, in particular SMEs, and save jobs in the EU – might create divisions within the single market.

In addition, long-term unemployment (when people are jobless for more than 12 months) might also be a risk for the economy. This can further intensify negative trends of financial distress that, in

[225] OECD, Covid 19: Protecting people and societies, March 2020.

[226] D. Chircop, Education in isolation in the pandemic. Following the path of Isaac Newton, EPRS, European Parliament, June 2020.

[227] F. Reimers and A. Schleicher, Schooling disrupted, schooling rethought – How the Covid 19 pandemic is changing education, OECD 2020.

[228] Reported financial distress is defined as the need to draw on savings or to run into debt to cover current expenditures, based on personal perceptions.

[229] European Commission, Employment and Social Developments in Europe – Quarterly Review, June 2020.

[230] European Commission, 2020 Annual Report of the Social Protection Committee, November 2020.

[231] The at-risk-of-poverty rate is the share of people with an equivalised disposable income (after social transfer) below the at-risk-of-poverty threshold, which is set at 60 % of the national median equivalised disposable income after social transfers. This indicator does not measure wealth or poverty, but low income in comparison with other residents in that country, which does not necessarily imply a low standard of living. The expression 'non-anchored' is used in opposition to anchored i.e. anchored to an earlier threshold).

[232] European Commission, Proposal for a Joint Employment Report 2021, 18 November 2020.

[233] P. Gluckman, Reflections on the evidentiary-politics interface, INGSA, 11 May 2020.

[234] IZA Institute of Labour Economics, Crisis Response Monitoring.

[235] P. Cahuc, Short-time work compensation schemes and employment, IZA World of Labour.

turn, have a negative impact on labour markets and the economy at large. People who are unemployed for a long-term period find it more difficult to find new jobs as time goes by. Long-term unemployed persons often have limited employability, owing to their low level of educational attainment, loss of skills and the substantial expenditures that are necessary to restore these skills. They also face significantly lower earnings and restricted career prospects.

6.1.2. Education and skills, labour market situation, age and gender are all determining factors

Certain groups[236] have been hit much harder than others by the coronavirus crisis, and their prospects for recovery also vary a great deal. In generational terms, most hard hit have been the 14.4 million young people aged between 15 and 24. Their share in the total number of employed people declined from 7.9 % in the last quarter of 2019 to 7.5 % in the third quarter of 2020. Differences between women and men are not really significant in this age group. While the employment rate shrank for young men by 1.9 pp between the last quarter of 2019 and the third quarter of 2020, reaching 33.7 % in the third quarter of 2020, it decreased by 2.1 pp for young women, reaching 28.8 % in the third quarter of 2020. However, it should also be noted that since 2015 the employment rate among the youngest generation had been steadily growing, reaching 33.3 % by the last quarter of 2019, then dropping to 32.8 % in the second quarter of 2020.

These numbers are in contrast to the middle age group of 140.9 million people between the ages of 25 and 54. This age group accounted for almost three in four employed people (73.7 %) in the third quarter of 2020 and in the last quarter of 2019. Their employment rate dropped from 80.6 % in the last quarter of 2019, to 79.8 % in the third quarter in 2020. Men's participation fell by 0.7 pp and women's by 0.9 pp. This difference is all the more significant given that there are more women than men. The oldest, 55 to 64 year old, age group has been the least affected. This group numbers 35.9 million people and represents 18.8 % of the workforce. Their employment rates showed a slight change from 59.6 % of the last quarter of 2019 to 59.7 % in the third quarter of 2020. However, they may be worse affected in the longer term, as they could be subject to mass dismissal. Men in this age category registered a 0.1 pp decrease and women a 0.3 pp increase in employment between the last quarter of 2019 and the third quarter of 2020.

Educational level[237] also seems to have been a determinant factor in unemployment risk. Those most at risk are women with low education levels. While the gender gap in the employment rate is and has remained the smallest among the women and men with the highest levels of education.

The fact that teleworking is less likely to be possible in lower-paying jobs has led to a major setback in progress made on income inequality since the global financial crisis. One study[238] estimating the telework possibilities (teleworkability) across 35 advanced and emerging economies has found that there is generally less possibility to telework for low-income earners than high-income earners. Workers least likely to work remotely tend to be young, without a college education, working on non-standard contracts, employed in smaller firms, and at the bottom of the earnings scale.

Additional groups whose employment has been affected by the crisis have been people on temporary or part-time contracts. The number of people on temporary contracts decreased from 11.6 % in the fourth quarter of 2019 to 10.4 % in the third quarter of 2020. In the European Union, the number of employed people dropped by 3.0 million between the last quarter of 2019 and the third quarter of 2020. More specifically, the number of employed people with temporary contracts shrank by 2.6 million, falling from 22.2 to 19.6 million. The fall in temporary contracts represents

[236] Eurostat, Employment – quarterly statistics, January 2021.

[237] Eurostat, Employment in detail – quarterly statistics, January 2021.

[238] M. Brussevich et al., Who will bear the brunt of lockdown politics? Evidence from teleworkability measures across countries. IMP Working Paper, No 20/88.

87 % of the total decrease in employment. This also helps to explain the disproportionate decline in youth employment as in the third quarter of 2020 young people aged 15 to 24 accounted for 28.8 % of total temporary contracts, but only 7.5 % of total employment among people aged 15 to 64.

According to figures relating to the 26 EU Member States for which data are available, the proportion of part-time workers in total employment grew in eight countries, was stable in two and dropped in 16 countries between the last quarter of 2019 and the third quarter of 2020. In the second quarter of 2020, this figure stood at 16.5 %, with underemployed part time workers[239] significantly accounting for 3.2 % of the total employed in the second quarter of 2020.

The crisis has also led to the largest increase between two consecutive quarters in the rates of 15 to 24 year-olds not in employment, education or training (NEETs)[240] since the start of Eurostat series in 2006 (from 10.4 % to 11.6 % between the first and second quarters of 2020). In 2019, one in ten young people aged 18 to 24 left education or training with a qualification below upper secondary education, and more than a quarter of people aged 30 to 34 did not have a qualification with direct labour market access (secondary vocational education and training or tertiary education qualification).

Non-EU migrants had seen an improvement in their average employment rate between 2017 and 2019 (from 61.5 % to 64.2 %). However, since the crisis began, the employment rate for this group dropped significantly (down to 60.8 % in the second quarter of 2020), owing to their over-representation among temporary workers and in sectors impacted strongly by the crisis. Non-EU migrant workers have nevertheless played a crucial role in key frontline occupations during the pandemic. Furthermore, first-generation migrant workers are more likely to be found in lower skilled occupations, even when they have tertiary education qualifications.

6.1.3. Time for a new state-citizen contract?

Social protection is generally provided by the state and involves a state-citizen contract,[241] in which both state and citizen have rights and responsibilities towards each other. There is also an (economic and social) security dimension, in terms either of social justice[242] or of the International Labour Organisation's concept of social protection floors.[243] This dimension should consist of at least four basic social security guarantees: essential healthcare and basic income security throughout the three main stages of the life-course – childhood, adulthood and old age – for all residents and all children as defined in national laws and regulations.

In the first two decades of the 21st century, due to the shifting balance[244] between individuals and institutions, people have had to take increasing responsibility for their economic outcomes as workers, savers and consumers. Already prior to the pandemic many, particularly those in precarious work situations, were tending to fall through the cracks[245] in the immediate social assistance measures. This was particularly the case concerning access to unemployment benefits, where some countries are significantly stricter than others but many of those countries with strict criteria also

239 An underemployed part-time worker is a person aged 15 to 74 working part-time who would like to work additional hours and is available to do so. Part-time work is recorded as self-reported by individuals.

240 European Commission, Proposal for a Joint Employment Report 2021, 18 November 2020.

241 E. Browne, Social protection: Topic guide, University of Birmingham, 2015.

242 In *A theory of social justice* John Rawls claims that an institution is fair if its rules are made to function to the advantage of all citizens and not just some of them.

243 ILO Social Protection Floor Recommendation, (No 202), 2011.

244 McKInsey Global Institute, The social contract in the 21st century, 5 February 2020.

245 S. Avlijaş, The dynamism of the new economy. Non-standard employment and access to social security in EU-28, LSE 'Europe in Question' Discussion Paper Series, No. 141/2019.

offer advantages to specific vulnerable populations. Moreover, access to maternity and particularly to sickness benefits is still challenging in some countries, especially for the self-employed.

As the pandemic evolved in spring 2020, unemployment benefit schemes and short-term work schemes were mobilised. Twenty-two of the 27 Member States[246] improved access to unemployment protection, while 21 improved its adequacy. All Member States deployed some targeted measures for the most vulnerable, including increased benefits, or introduction of supplementary benefits; extended coverage and improved access; direct support for household expenses; suspension of loans; support for carers; measures for the elderly; and in-kind benefits.

However, even in countries with the most advanced social protection systems,[247] workers with non-standard jobs and the self-employed have been missing out. They are often not covered by insurance-based unemployment and sickness benefit schemes. Others, who were already out of work before the crisis, now face protracted hardship. At the same time, the assistance function of social protection systems – providing last-resort minimum-income benefits for those with little or no other resources – have been put to a severe test. The accessibility and generosity of these programmes differ markedly across countries; even in normal times, many households in urgent need receive insufficient support. Finally, while the newly designed programmes are essential, they are sometimes poorly targeted and may need to be reconsidered as broader fairness and fiscal considerations re-impose themselves. Post-crisis social protection systems should be reformed to close the gaps and support inclusive growth.

6.1.4. Effects of the pandemic confirm previous trends between Member States

The differences between the economic and social situations in the various Member States depend largely on[248] the way the pandemic evolved in each country, but also on the structure of their economies and their capacity to respond with stabilising policies and funding programmes. When it comes to employment and unemployment these differences are considerable. In the third quarter of 2020,[249] the only Member States where the employment rate of people aged 20 to 64 was above 80 % were Germany and Sweden. By contrast, the lowest employment rates were reported in Greece (61.2 %), Italy (62.2 %) and Spain (65.6 %), where fewer than two out of three people were employed in the same period.

In general, the employment rate fluctuated to varying extents in the EU Member States between these two quarters. In Estonia, the employment rate declined from 81.1 % to 78 %, corresponding to a decrease of 3.1 pp. By contrast, the employment rate increased by 0.8 pp in Malta and by 0.4 pp in Poland. Nevertheless, these figures follow trends that were already present prior to the pandemic.[250]

Gaps between male and female employment rates also varied across countries. Among the 20 EU Member States where the male and female employment rate decreased differently, four recorded a gender gap between the evolution of their male and female employment rates higher than or equal to 1.0 pp. The largest gap was observed in Portugal, where the employment rate decreased by 3.0 pp for men but by only 0.9 pp for women. By contrast, the decrease in the female employment rate exceeded by 1.1 pp, or more the decrease recorded for men in Slovenia and in Cyprus.

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[246] European Commission, 2020 Annual Report of the Social Protection Committee, November 2020.

[247] OECD, Supporting livelihoods during the Covid 19 crisis: Closing the gaps in safety nets, 20 May 2020.

[248] C. Midões, Risking their health to pay the bills: 100 million Europeans cannot afford two months without income, Bruegel, May 7 2020.

[249] Eurostat, Employment Quarterly Statistics.

[250] D. Gros, Europe's good crisis, Project Syndicate, July 7 2020.

Historically,[251] national social protection systems have primarily been developed to protect people in standard employment. This is particularly the case for insurance-based schemes, i.e. those based on social contributions from the employee and the employer. By contrast, benefits and services financed by taxes (e.g. family allowances, some forms of healthcare and long-term care) and certain means-tested benefits (e.g. social assistance and minimum income provisions for older people) are granted in many European countries regardless of the employment status of an individual. People in non-standard employment have always been in a more insecure and precarious situation regarding access to schemes and receipt of insurance-based benefits. There is strong variation across the EU-28 (now EU-27) when it comes to the proportion of non-standard workers and self-employed people on the labour market, meaning that some countries have a high incidence of temporary and/or part-time work (i.e. non-standard work), while in others self-employment is much more common.

A country's policy towards flexible working,[252] and whether to make it more or less difficult by reforming social benefits and programmes, cannot be examined in isolation from the country's labour market conditions or its growth model. In the same vein, countries have different spending patterns[253] when it comes to social protection expenditure relative to GDP: there are high spenders (Nordic and continental European countries), medium spenders (southern European countries) and low spenders (central and eastern European countries). Lower income countries[254] have often worse provision than higher income countries. For example, in the case of the widely used short-term work schemes, only in the Netherlands, Denmark and Ireland did allowances cover 100 % of original pay and then only for limited periods. The lowest level was 40 % of the national average wage in Poland. Moreover, many people from those countries work abroad (for example, 15.5 % of Romanian citizens were living in another EU Member State in 2019), often in insecure jobs that are the first to disappear in a crisis situation.

6.2. Relevant social governance tools of the European Union

The challenge is how to tackle the immediate crisis, while also supporting long-term recovery and building resilience. Resilience[255] refers to the ability to withstand and respond to shocks and challenges, and recover quickly in a fair, sustainable and inclusive manner. Research[256] in the field even goes a step further and emphasises that in addition to the ability to recover and adapt so as to ensure survival in the future, resilience even covers the potential to take advantage of new or previously hidden opportunities following crises and to improve the system through broader systemic changes. Similarly, the resilience framework[257] that was developed by the Joint Research Centre and served as a starting point for the resilience dashboard of the first Foresight Report[258] of the European Commission in 2020 emphasises three types of resilience capacity: absorptive (stability), adaptive (flexibility) and transformative (change).

[251] S. Spasova et al., Access to social protection for people working on non-standard contracts and as self-employed in Europe. A study on national policies, April 2017.

[252] S. Avlijaş, The dynamism of the new economy. Non-standard employment and access to social security in EU-28, LSE 'Europe in Question' Discussion Paper Series, No. 141/2019.

[253] S. Spasova and T. Ward, Social protection expenditure and its financing in Europe, ESPN, October 2019.

[254] B. Vanhercke et al. (eds), Social policy in the European Union; state of play 2020, OSE-ETUI, 2021.

[255] European Commission, staff working document, Guidance to Member States , Recovery and Resilience Facility, SWD (2020)205 final.

[256] W. Hynes et al., 'Bouncing forward: a resilience approach for dealing with the Covid 19 and future systemic shocks', *Environment Systems and Decisions*, May 2020, pp. 1-11.

[257] A.R. Manca et al., Building a scientific narrative, Towards a more resilient EU society, Part 1: Conceptual Framework, JRC, 2017.

[258] European Commission, 2020 Strategic Foresight Report, 9 September 2020.

The first EU cross-country measurement[259] along these lines in response to the 2008 financial and economic crises showed substantial differences between countries' performances in each of the resilience indicators considered. There was a difference of around two standard deviations between the most consistently resilient countries (such as Germany and Poland) and the least resilient (such as Greece and Cyprus) in any given indicator. Having tested over 200 potential pre-determined characteristics for their association with resilience, the study also showed that the strongest predictor of absorptive short-run resilience, adaptive medium-run resilience, and bouncing forward capacity are, respectively, high government expenditure on social protection, political stability and a favourable business environment. Net creditor countries vis-à-vis the rest of the world have also tended to be more resilient in most dimensions. In addition, there has been also a strengthening nexus between resilience, sustainability[260] and well-being in European policy thinking in the last decade.

There is no European comprehensive, regulated social governance framework to compare with those that exist for economic governance. Governance is often defined in contrast to government: government is about hierarchy and bureaucracy, and governance about decentralised markets and networks. Social governance[261] is defined as a process of governing societies in a situation where no single actor can claim absolute dominance. In the European Union it is referred to mainly in relation to social policies and objectives, and increasingly with the idea of putting economic and social objectives on an equal footing. Several 'soft' social governance tools are available, however, while economic governance influences and impacts the social realm.

These include: EU minimum standards, the social open method of coordination (OMC), the impact assessment of policies and programmes, the renewed social dialogue, the European Semester with more focus on social and employment issues, and the European funds designed to support Member States in achieving upward economic and social convergence.

According to the Commission's Proposal for Joint Employment Report 2021 (JER),[262] there needs to be a good balance between supporting and saving jobs but also investing in the future: triggering structural change in the labour markets, providing for workforce re-and upskilling (including digital skills), promoting collective bargaining and social dialogue, setting adequate minimum wages, reforming tax benefit systems, investing in the renovation of residential and social housing and investing in healthcare capacity. Paying particular attention to vulnerable groups when building the European education area, promoting a work-life balance, including gender-balanced leave policies, pay transparency, adjustments to the tax benefit system, migrant integration into the labour market and active labour market policies, should also be central to future initiatives. The JER suggests several measures, mainly making use of the European Social Fund Plus (ESF+) (with additional resources made available from Recovery Assistance for Cohesion and the Territories of Europe (REACT-EU)) and the new Recovery and Resilience Facility (RRF).

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[259] L. Alessi et al., 'The resilience of EU Member States to the financial and economic crisis', *Social Indicators Research*, Vol. 148, 2020, pp. 569–598.

[260] Here sustainability mainly means that one should not preserve current societal well-being in a way that comprises that of future generations. For more on the relationship on resilience and sustainability see footnote 2 in L. Alessi et al., 'The resilience of EU Member States to the financial and economic crisis', *Social Indicators Research*, Vol. 148, 2020, pp. 569–598.

[261] N. Milotay, Social governance in the European Union. Managing complex systems, EPRS, European Parliament, May 2020.

[262] European Commission, Proposal for a Joint Employment Report 2021, 18 November 2020.

6.2.1. EU policy initiatives

The Commission work-programme for 2021[263] envisages several legislative and non-legislative initiatives to support Member States in their endeavours to boost recovery and build resilience. In its fair economy package, the Commission is planning: an action plan for the European Pillar of Social Rights (social pillar) for the implementation of all its principles as set out in the communication on a strong social Europe for just transitions; a European Child Guarantee to support free access for vulnerable children to early childhood education and care (ECEC), education, health, housing and nutrition; a communication on a new occupational health and safety strategy; and action plan for the social economy. It envisages a legislative initiative to improve the working conditions of platform workers; and a follow-up on the European education area initiative, and on the updated skills agenda, so as to make quality education and training, as well as upskilling and reskilling more accessible for all; and a legislative initiative on micro-credentials and learning accounts to widen learning and skills development opportunities, and further shape the lifelong learning dimension in higher education. Further relevant initiatives include an update on the new industrial strategy for Europe; a proposal for a directive on sustainable corporate governance to support companies in a longer-term value creation and to better manage sustainability related issues; a communication for the long-term vision of rural areas to enable them to respond to demographic, digital and other challenges and several initiatives in the area of taxation, including the introduction of a digital levy as a new own resource of the EU.

6.2.2. Social aspects of economic governance

As for economic governance, and in particular the European Semester, the 2021 Semester is an exceptional one. In this Semester cycle Member States will prepare combined national reform programmes and recovery and resilience plans (national recovery and resilience plans – NRRP) in accordance with the 2019 and 2020 country specific recommendations (CSRs) and the recommendations of the JER. In the 2021 cycle, Member States receive recommendations only in relation to their draft budgetary plans.

A review[264] of the economic governance framework was launched at the beginning of 2020. The main aim of the review is to assess the effectiveness of the current framework – especially the reforms undertaken in response to the 2008 crisis. In practice, this means examining whether the economic and fiscal surveillance elements were effective in ensuring sustainable government finances and growth, avoiding macroeconomic imbalances, enabling more coordination of economic policies in the euro area and more convergence of economic performance among Member States. As for the social field and particularly public spending, social spending – in many cases close to one third of public spending – often fell victim to budget cuts owing to the post-2008 austerity measures. The review procedure, including public consultation, was interrupted by the outbreak of the pandemic.

In the 2021 annual sustainable growth survey[265] the Commission emphasised that Member States should focus their NRRPs on challenges and priorities generating the most lasting impact and strengthening growth potential, job creation, health systems and economic and social resilience and regional cohesion. It also added that due to the temporary nature of the EU funds available under the RRF, these funds should not replace recurring national budget expenditures or revenues *per se*, but instead be used as additional financial resources for achieving EU value added objectives

[263] European Commission, 2021 Commission work programme.

[264] European Commission, Staff working document, Economic Governance Review, SWD(2020) 210 final.

[265] European Commission, communication on the Annual Sustainable Growth Strategy 2021, COM(2020) 575 final.

to be set out in the RRF Regulation.[266] Finally, in the 2021 alert mechanism report[267] the Commission stresses that the RRF is an opportunity for Member States to implement reforms and investments in line with the macroeconomic imbalance procedure (MIP)[268] – related recommendations that address the underlying and long-standing structural causes of existing macroeconomic imbalances.

Parliament's report[269] on employment and social policies in the euro area also stressed 'that in order to fuel the recovery, the EU's investment effort through the Recovery Plan and the MFF should stimulate economic growth with a strong social dimension, particularly by strengthening welfare systems and investing in stable social security systems, healthcare, education, housing, employment, culture, justice, and adequate and accessible public social services in order to combat the social impact of the crisis and eradicate poverty'. It also recommended complementing the social scoreboard[270] with relevant indicators reflecting all 20 principles of the social pillar, developing social targets, including for poverty reduction, and establishing a method to integrate the social aspects of environmental, social, and governance factors. Parliament also stressed the importance of ex ante evaluations and thorough ex post evaluations of the NRRPs.

Over the years, critics[271] of the social dimension of economic governance in general, and the European Semester in particular, have developed three claims: that social objectives are subordinate to economic goals, where the main emphasis is on macroeconomic policies, competitiveness and fiscal discipline; that economic policy actors dominate social and employment actors in the decision making process – noting that economic actors dominate in fields where there is 'hard' legislation at EU level, whereas their social counterparts are in fields where there are only 'soft' tools available; and finally, that for many the Semester process is a centralised mechanism that imposes structural reforms on Member States, including in areas of national competence (such as social and employment policy) strengthened by threats of sanctions under the stability and growth pact (SGP) and the MIP.

In contrast to these criticisms, another body of research[272] argues that there has been a gradual socialisation of the European Semester. This argument sees a growing emphasis on social objectives in the Annual Growth Survey and the CSRs, intensified monitoring of national and EU policies by social and employment actors and their enhanced role in drafting, reviewing and amending CSRs, with less hierarchical decision-making arrangements within the Semester. Finally, the fact that the EU has limited power to 'impose' the implementation of the CSRs is an ongoing problem. From the regular annual assessment published by the Commission in its country reports, it emerges that just over half the CSRs (53 %) are implemented on average, with at least some progress over the 2012-2018 period.

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[266] European Commission, Proposal for a regulation establishing the recovery and resilience facility, COM(2020) 408 final.

[267] European Commission, 2021 Alert Mechanism Report, COM (2020) 745 final.

[268] A. Delivorias, The macroeconomic imbalance procedure: an introduction, EPRS IDA, October 2020.

[269] European Parliament, Employment and social policies of the euro area 2020, 2020/2079(INI).

[270] The social scoreboard that accompanied the European Pillar of Social Rights has been the main monitoring tool for social and employment situations in the European Semester since 2018. Its 14 headline indicators are used to compare Member States' performance in the yearly Joint Employment Report.

[271] P. Copland and M. Daly, 'The European Semester and EU social policy', *Journal of Common Market Studies*, February 2018.

[272] See S. Bekker, 'EU economic governance in action: coordinating social and employment policies in the third European Semester', Tilburg Law School Research Paper No 14, 2014, and J. Zeitlin and B. Vanhercke, 'Socialising the European Semester: socialising the European Semester: EU economic and social policy coordination in crisis and beyond', *Journal of European Public Policy*, Vol. 25, 2018.

6.2.3. Funding

The World Economic Outlook[273] emphasises the need to safeguard critical social spending in the short term so as to ensure that the most vulnerable are protected while also supporting activity, given that the outlays will go to groups with a higher propensity to spend their disposable income than more affluent individuals. Gaps in the safety net should be filled through, for example, enhanced paid family and sick leave, expanded eligibility for unemployment insurance, and strengthened healthcare benefit coverage adjusted to needs.

The EU budget is only a very small percentage of Member States' social spending. The EU budget represents just over 1 %[274] of the combined EU's national wealth, while national budgets across Member States represent on average 47 % of national wealth. That is why the mechanisms guiding policies in the Member States are as important as the budget itself when implementing policies. They can help the EU budget function as a genuine incentive for positive transformation and innovation.

The European Commission's renewed budget proposal of May 2020[275] responding to the unfolding crisis caused by the coronavirus pandemic outlined an EU budget for recovery resilience with three main chapters. This proposal adds to three important immediate safety nets for workers, businesses and sovereigns endorsed by the European Council already on 23 April 2020[276] and amounting to a package worth EUR 540 billion, including the European instrument for temporary support to mitigate unemployment risks in an emergency (SURE), the European Stability Mechanism (ESM) pandemic crisis support and the European Guarantee Fund of the European Investment Bank for workers and businesses. The adopted MFF, together with the Next Generation EU (NGEU) instrument, includes promising avenues for increasing and strengthening implementation in areas relevant for updating national welfare states (investing in human capital, activation and protection) and labour markets.

Table 5 below shows all the funds relevant to social and employment policies. It demonstrates that close to three quarters (75.5 %) of the MFF can be used in this field.

[273] IMF, World Economic Outlook, October 2020.

[274] European Commission, Fact check on the EU budget

[275] European Commission, The EU budget powering the recovery plan for Europe, COM 2020/442 final

[276] European Council, Report on the comprehensive economic policy response to the COVID 19 pandemic, Eurogroup press release, 9 April 2020.

Table 5 – MFF funds and programmes benefiting social and employment policies

	2021-2027 MFF (€ million, 2018 prices)
Heading 1 – Single market, innovation and digital	
Digital Europe	6 761
InvestEU (including social investment and skills)	2 800
Connecting Europe Facility	18 396
Horizon Europe (including InnovFin for enterprises)	75 900
Single Market programme	3 735
Heading 2 – Cohesion, resilience and values	
European Regional Development Fund	200 360
Cohesion Fund	42 556
Erasmus+	21 208
European Social Fund+	87 995
Creative Europe	1 642
Rights and Values	841
REACT-EU	
Heading 3 – Natural resources and environment	
European Agricultural Guarantee Fund	258 594
Agricultural Fund for Rural Development	77 850
European Maritime and Fisheries Fund	5 430
Just Transition Fund	7 500
Total under the 2021-2027 MFF	**811 568**
As % of the 2021-2027 MFF	**75.5 %**
Outside the 2021-2027 MFF:	
European Globalisation and Adjustment Fund	1 300
Total	**812 868**

Source: EPRS, Visualising the proposed European Union 2021-27 multiannual financial framework and the recovery instrument (Next Generation EU).

In addition to quantity of spending, quality of the spending, i.e. the extent to which it really manages to target problems and groups of people on the ground and even manages to trigger structural change, is an essential issue. Many of the Commission's new programme proposals made in May 2018[277] and then as a response to the coronavirus in May 2020 attempted to improve the quality of spending. Mentioned below are the funds that might have a particularly important role in the social and employment policy field, in strengthening the social aspects of economic governance, including the promotion of a social investment[278] approach to financing.

[277] European Commission, Legal texts and factsheets on the EU budget for the future

[278] A more elaborate taxonomy of the social investment concept, developed recently, defines three complementary policy functions. These include: raising the quality of human capital 'stock' that contributes to better productivity, easing the 'flow' of labour market transitions and thus supporting high employment of both genders, and

In the context of the negotiations on the 2021-2027 MFF, the Commission put forward a number of proposals for regulations on EU spending programmes and funds. Although at time of writing this study most of them are still awaiting final approval, there seems to be a general acceptance of the need for a new approach to EU spending and organisation of funds. The changes proposed aimed to achieve a more strategic approach to some relevant existing funds and consequently more synergy between them, by:

- creating ESF+[279] (incorporating the European Social Fund (ESF), the Youth Employment Initiative (YEI), the Fund for European Aid to the most Deprived (FEAD), and the EU Programme for Employment and Social Innovation (EaSI);
- establishing a stronger link between the European Semester and the European structural and investment funds[280] (ESI funds);
- changing the allocation principle under the Common Provisions Regulation[281] (CPR);
- and simplifying the rules for accessing the ESI funds.

The Commission proposal earmarked at least 25 % of the ESF+ for promoting social inclusion and tackling poverty, at least 2 % for material support for the most deprived and 10 % for tackling youth unemployment. It also proposed a stronger link between the Semester and the ESI funds by doing more to connect the funds and the CSRs. The latter would be considered both in the programming of the funds and the design of cohesion policy. The Commission also proposed new indicators in the CPR, such as 'climate change' and 'reception and integration of migrants', and slight modification of the allocation criteria. Finally, it proposed that access to funds should be conditional upon fulfilment of conditions or achievement of results. According to the new May 2020 proposal, Member States with youth unemployment levels above the EU average were to programme at least 15 % of their ESF+ resources under shared management to support young people. Moreover, the Commission also proposed that at least 5 % of total expenditure under the ESF+ should be used to help lift children out of poverty.

Although the new proposal was welcomed, concerns were raised in relation to: the overall reduction of the volume of the ESI funds, the ever-stronger link to the Semester, and the decision to maintain macroeconomic conditionalities. Parliament rejected[282] the proposed measures linking EU regional funding to macroeconomic conditionalities. Several Parliamentary committees emphasised that cohesion policy does not share the same goals as the European Semester referring to Parliament's previous position that activities linked to the European Semester and EU governance processes should not impede the main purpose of cohesion policy, which is to reduce disparities in the level of development between regions. Parliament also proposed[283] to increase the financial envelope, to

compensating and mitigating social inequity at the micro level through income 'buffers'. This taxonomy describes three pillars of the welfare state: human capital development, activation and protection.

[279] European Commission, Proposal for a regulation on the European Social Fund Plus (ESF+), COM 2018/382 final. The original proposal also contained the EU Health programme. As a result of the pandemic, the EU4Health programme has become a stand-alone programme.

[280] There are five ESI funds: the European Regional Development Fund (ERDF); the European Social Fund (ESF); the Cohesion Fund (CF); the European Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF).

[281] The proposal for a Common Provisions Regulation (CPR) sets out common provisions for seven shared management funds. Therefore, the single rulebook will cover the European Regional Development Fund, the Cohesion Fund, the European Social Fund+, the European Maritime and Fisheries Fund, the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument. Additional specific regulations will add certain provisions needed to cater for the particularities of individual funds, in order to take into account their different rationales, target groups and implementation methods. The suggested proposal will not replace the existing Regulation (EU) No 1303/2013, which will continue to govern the programmes adopted in the 2014-2020 period.

[282] European Parliament, Common Provisions on ERDF, ESF Plus, etc., 2018/0196(COD).

[283] European Parliament, European Social Fund Plus (ESF+) 2021-2027, 2018/0206(COD).

raise the allocation for social inclusion to 30 %,[284] and to add an extra €5.9 billion to the European Child Guarantee, a new instrument to ensure equal access for all children to free education, early childhood education and care, nutrition, health and housing. It also suggested investing 3 % of resources under shared management to targeted actions and structural reforms aimed at promoting youth employment, the transition from education to work and second chance education. Finally, concerns[285] were voiced that by integrating the YEI and the FEAD into the ESF+, they would lose some of their counter-cyclical function. At the time of finishing this chapter no interinstitutional agreement had been reached on this fund.

The Commission also proposed to increase the budget for other relevant funds, such as Erasmus+. The May 2020 Commission proposal suggested an additional €3.4 billion from NGEU to the programme. Parliament proposed[286] to triple the budget for Erasmus+ and to lift barriers so as to make the funds accessible to more people. According to the political agreement[287] on the programme, it will have a dedicated allocation of €21.2 billion under MFF with an additional top up of €2.2 billion based on the outcomes of the negotiations between the Parliament and the Council on the 10th November 2020.[288]

The proposal for the European Globalisation and Adjustment Fund (EGF)[289] also had an increased amount (even further increased in the 2020 May proposal). Parliament suggested[290] changing its name to the European Fund for Transition to show its strong links to the issue of just transition and introduce the possibility of integrating NEETs into the target group. The political agreement on EGF[291] widens the fund's scope in terms of eligibility factors beyond redundancies, with a focus on impacts of restructuring and the coronavirus crisis. It lowers the threshold of redundancies and speeds up the allocation procedure, reducing the involvement of Parliament and Council. It also allows the contribution to the cost of services be increased up to the highest co-financing rate under the ESF+ in any given Member State. This will facilitate the use of the EGF in less developed regions.

In 2016, social investment[292] in the European Fund for Strategic Investments (EFSI) was modest: less than 4 % was used for social infrastructure and 1 % for social services. Partly in response to this criticism, the new proposal for the 2021-2027 period, called InvestEU,[293] dedicated a €4 billion budget (expected to yield a €50 billion investment) to 'social investment and skills'. The main of this proposal was to streamline several EU financial instruments (in the form of guarantees, loans, risk-sharing or equity) and to create a single investment mechanism for internal action for the 2021-2027 MFF. These were supported in the 2014-2020 period by several programme funds, such as the EFSI, the Connecting Europe Facility (CEF), the EU programme for the Competitiveness of Enterprises and Small and Medium-sized Enterprises (COSME), and the EU programme for Employment and Social

[284] Member States should allocate at least 27 % of their ESF+ resources to specific objectives in the field of social inclusion, and at least 3 % of their resources to the specific objective of social inclusion of the most deprived and/or to alleviating material deprivation.

[285] L. Andor, Resources for a prosperous Europe. Redesigning the EU budget, Friedrich Ebert Stiftung, Vol. 18, 2018.

[286] European Parliament, Erasmus programme 2021-2027, 2018/0191(COD).

[287] European Commission, press release, 11 December 2020.

[288] Council of the European Union, Multiannual Financial Framework 2021-27 and Next Generation EU (Commitment in 2018 prices).

[289] European Commission, Proposal for a regulation on the European Globalisation Adjustment Fund, COM/2018/380 final - 2018/0202 (COD)

[290] European Parliament, EGF 2021-2027, 2018/0202(COD).

[291] European Commission, press release, 17 December 2020.

[292] S. Fernandes, Social investment and the Juncker Plan, Jacques Delors Institute, July 2017.

[293] European Commission, Proposal for a regulation establishing the InvestEU programme, COM(2018) 439 final – 2018/0229(COD).

Innovation (EaSI). Parliament suggested[294] further broadening the general objectives of the fund to include increasing the EU employment rate, creating high-quality jobs, and achieving the UN sustainable development goals (SDGs) and the Paris Climate Agreement goals, as well as economic, territorial and social cohesion. The May 2020 Commission proposal for InvestEU reflected the partial agreement already reached between Parliament and Council in 2019. The text increased the initially proposed financial envelope and broadened the scope of the proposal, adding a fifth policy window devoted to investment in strategic sectors, notably those linked to the green and digital transition, and in key value chains in the internal market. In addition, Member States would be able to implement part of their recovery and resilience plans through InvestEU. In the final compromise[295] the strategic European investment window was built into the original four policy windows and the dedicated budget for the social window is €2.8 billion.

The Just Transition Fund[296] was set up to secure the Just Transition Mechanism as part of the European Green Deal in January 2020 (amended in May 2020).[297] The fund is to be implemented as part of cohesion policy, including national co-financing. It will also be governed by the CPR and support the specific objective of enabling regions and people to address the social, economic and environmental impacts of the transition towards a climate-neutral economy. In the May 2020 proposal, additional funding was given to the fund, which can in turn give joint support alongside the ERDF, the ESF+ and the Cohesion Fund to actions under the 'Investment for jobs and growth' objective. Under the Next Generation EU instrument, REACT-EU[298] should further finance and give technical assistance for recovery and the long-term transition to a green and digital economy. The Just Transition Mechanism should be further supported by resources under InvestEU and a public sector loan facility (with the European Investment Bank backed by the EU budget). While the European Council cut the Commission proposal for a core budget of €10 billion (with an additional €30 billion from Next Generation EU) to €7.5 billion, the European Parliament proposed[299] to increase the core budget to over €25 billion. Funding would be available to all Member States, while focusing on regions with the biggest transition challenges. According to the political agreement[300] on the fund, the overall budget has been set at €17.5 billion, of which €7.5 billion will come from the MFF and €10 billion from NGEU.

In May 2018, the Commission also proposed two financial convergence instruments: the reform support programme[301] and a budget for the euro area,[302] both with the potential to strengthen the social aspects of economic governance. Their aim was to provide support for structural reform. The former went beyond the existing technical support provided by the structural reform support service[303] and also offered financial support for the implementation of reforms and the improvement of administrative capacity. It was also to help Member States join the euro within a set timeframe. The latter, the European investment stabilisation function, was to be a budgetary instrument designed to function in synergy with other stabilisation functions, such as the European

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294 European Parliament, InvestEU programme, 2018/0229(COD).

295 European Commission, press release, 8 December 2020

296 European Commission, Proposal for a regulation establishing the Just Transition Fund, COM(2020) 22 final

297 European Commission, Amended proposal for a regulation establishing the Just Transition Fund, COM(2020) 460 final.

298 Based on the Coronavirus Response Investment Initiative (CRII) from April 2020, and modifying the current Common Provisions Regulation.

299 European Parliament, Just Transition Fund, 2020/0006(COD).

300 European Commission, press release, 11 December 2020.

301 European Commission, Proposal for a regulation on the establishment of the reform support programme, COM(2018) 391 final.

302 European Commission, Proposal for a regulation on the establishment of a European investment stabilisation function COM(2018) 387 final.

303 European Commission, Structural reform support programme.

Stability Mechanism (ESM), in the event of major asymmetric shocks. Both the reform support programme and the Budgetary Instrument for Convergence and Competitiveness (BICC)[304] were to be strongly linked to the European Semester and run by the Commission.

In the light of the NGEU instrument, and in particular its biggest building block, the RRF, the BICC was however withdrawn and the reform support programme was replaced by a technical support instrument within the RRF. The six policy areas that can be financed by the RRF, along with its two principle objectives, are: the green transition, including biodiversity; digital transformation; economic cohesion and competitiveness; social and territorial cohesion; policies for the next generation, children and youth, including education and skills; and institutional crisis-reaction and crisis preparedness. The technical support instrument will support Member States, in particular, in the preparation and implementation of their NRRPs. The co-legislators have agreed to provide Member States the possibility to finance the instrument through additional contributions.

As for the general governance[305] of the RRF, every two months, the Commission (responsible for monitoring implementation of the RRF) may be invited by Parliament's committees to discuss the state of the EU recovery and how the targets and milestones have been implemented by the Member States. The Commission will take Parliament's opinions, including its resolutions, into account. To facilitate this discussion, the Commission will transmit the Member States' plans to Parliament and Council at the same time. Moreover, to provide comparable information on how funds are being used and allow their use to be properly checked, the Commission will make an integrated information and monitoring system available to the Member States. Finally, Member States will need to put in place strong measures to protect the financial interests of the Union, especially to prevent fraud, corruption and conflicts of interest.

6.3. Outlook

2021 should see the start of both short-term recovery and the building of longer-term resilience. Ideally, it should also pave the way towards a new social contract,[306] as the crisis has placed a great strain on the relationship between governments, business and the general public, and led to increasing divergence, instead of convergence and cohesion. The RRF guidelines[307] show the centrality of social considerations when designing policies, as its main objectives include: the promotion of social cohesion, the strengthening of social resilience and the mitigation of social impacts of the crisis. The guidelines imply that resilient economic structures can promote social outcomes by combining the positive employment effects of effectively-functioning labour and product markets with active labour market policies to support the search for new opportunities, including possibilities for lifelong learning and an effective social safety net. They also suggest that sustainable and well-targeted social security systems are among the key means to cater for such social needs in the face of shocks and during economic transitions. The guidance for Member States offered by the Proposal for a Joint Employment Report takes a similar approach, recommending action to trigger structural change on the labour markets, promote re- and upskilling, improve social protection systems with a focus on vulnerable groups and active labour market policies, and fight long-term unemployment.

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[304] European Commission, Proposal for a regulation on a governance framework for the budgetary instrument for convergence and competitiveness for the euro area, COM(2019) 354 final.

[305] Covid 19: deal to go ahead to the new RRF, press release, 18 December 2020.

[306] Tackling inequality in the pandemic: a new social contract for a new era. UN Secretary General Antonio Guterres, 18th Nelson Mandela Annual Lecture, July 2020.

[307] European Commission, Recovery and Resilience Facility.

6.3.1. Is structural change possible?

As inequalities between age groups and professional groups, nations and regions have grown, it is important to look at what can be expected from the new initiatives and financial tools in terms of combatting these inequalities and triggering the necessary and, in some cases, long overdue structural changes, including updating welfare states and labour markets to the new realities of life and work.

The MFF and NGEU have certainly been designed to bring about changes in the institutional set up that can strengthen the budgetary and financial capacity of the EU to complement its monetary policy. This could result in greater solidarity and cohesion and, ultimately, more (upward) convergence and integration. Experts would claim that the current changes to the budget and, in particular, the combination of the MFF and NGEU, bring new dynamism to the EU financing mechanism. The Commission will be empowered to borrow on the capital markets on behalf of the Union, exclusively for actions to mitigate the impact of the pandemic. In addition, the agreement on the financial package envisages the gradual introduction of new own resources to facilitate the repayment of NGEU borrowing, as strongly advocated by Parliament.

The RRF should help to improve long-term resilience and thus develop good quality governance, particularly in the countries where this was lacking. Evidence[308] has shown that in many countries, especially some of the southern Member States hardest hit by the coronavirus crisis, resilience is a major sticking point. All too often, in some of these countries, the poor quality of governance[309] has had a negative impact on their resilience, as the relatively large size of their GDP shocks has demonstrated. It is crucial therefore that RRF programmes devote sufficient attention (and resources) to improving the quality of governance in these countries.

In this context, approaching the funds as a means for collective problem solving (missions)[310] on the ground, including social problem-solving in line with the UN SDGs,[311] can also help to develop better governance methods and renew the strained social contract. This approach can help with sharing risks and rewards[312] between governments, business and citizens, lead to pre-distribution (alongside redistribution), and also improve public sector capabilities.

The real question, however, is whether the MFF and NGEU will bring the necessary changes on the ground. The EU's budget contributes only a small percentage to Member States' public spending. That is why the various EU (social) governance mechanisms to guide policies in the Member States are equally important for successful policy implementation and reform. They can help the EU budget function as an incentive for positive transformation and innovation. In this way, the integrity of the EU's (social) governance tools (including the economic governance mechanism) can become a driver for combating inequalities, as opposed to a tools for the surveillance of budgetary discipline and the scapegoat for austerity measures. Moreover, while the EU can trigger change in the social

[308] A. Sapir, Why has Covid 19 hit different European Union economies so differently?, Bruegel, September 2020.

[309] Calculated by adding up country's scores for the six parts of the World Bank Worldwide Governance indicator: voice and accountability; political stability and absence of violence; government effectiveness; regulatory quality; rule of law; and control of corruption. Scores for each of the six indicators can vary from -2.5 to 2.5, so the overall indicator can vary from -15 to +15. In 2018, the latest year available, the quality of governance in the 26 EU Member States measured averaged 6 (using a simple rather than a weighted average) and ranged from 0.9 in Romania to 10.6 in Finland. It averaged 4 for the four southern Member States (Greece, Italy, Portugal and Spain) and 9.8 for the 'frugal four' (Austria, Denmark, Netherlands and Sweden).

[310] M. Mazzucato, 'Mission-oriented Innovation Policy: Challenges and Opportunities', UCL Institute for Innovation and Public Purpose Working Paper, (2017-01).

[311] J. D. Sachs et al., 'Six transformations to achieve the UN Sustainable Development Goals', *Nature Sustainability*, Vol 2, September 2019, pp. 805–814.

[312] A. Laplane and A.-M. Mazzucato, Socialising the risks and rewards of public investments: Economic, policy and legal issues, UCL Institute for Innovation and Public Purpose, Working Paper Series (IIPP WP 2019-09).

and employment policy field, most of the budget and action still comes from national governments. However, according to some experts[313] the budgetary plans and NRRPs are an opportunity for the EU to influence national governments' plans.

Although the €390 billion in grants represents less than 3 % of EU GDP (€14 000 billion), the transfers could make a big difference to some countries. Some experts[314] have stressed from the outset the need for the EU to put the plan on the right track. They claim that the EU should acknowledge and emphasise that the main goal of the RRF is not to contribute to immediate relief or a Keynesian stimulus, but to foster structural transformation, especially in less-advanced and harder-hit Member States (mainly central, eastern and southern European Member States). In addition, they highlight the importance of a 'narrow-conditionality' approach, in which reforms that strongly complement intended investments should be identified and bundled with that investment. Moreover, each bundle of investments and reforms should be focused on the limited set of policy measures that need to be implemented to maximise the impact of EU-financed investment. Finally, there should be a dialogue with each Member State on the sectoral allocation of EU funding and the overall architecture of their NRRPs. As the provider of the funds, the EU has the leverage and legitimacy to be demanding in these discussions and thus ultimately influence the design of the NRRPs. In addition, there might be problems with the absorption capacity[315] of these Member States, as past experience has shown, also because it will be not viable to use the loans and grants mainly for public investment.

Other experts,[316] however, have real doubts as to the actual ability of the European Commission, or for that matter stronger involvement of the European Parliament, to use the European Semester to ensure that the RRF is really used for structural reforms and not just the immediate recovery. Given the strong political incentives among both Member States and the Commission for expeditious and complete disbursement of the RRF funds, they have real doubts that the EU can materially affect the detailed use of RRF funds. They also argue that the Member States are not likely to adhere to detailed EU instructions on how to spend this money, still less to the many CSRs they have already been ignoring for years.

In addition, some evaluations[317] also express concern about the fact that important actors primarily focusing on advancing social and employment issues in the European Semester (i.e. the European Commission's Directorate-General for Employment, the EPSCO Council formation and its advisory bodies – the Employment Committee and the Social Protection Committee, and the European social partners and EU-level non-governmental organisations) , who have become more influential over the years, are losing their voices to the newly established recovery task force. The latter was set up in August 2020 within the European Commission's Secretariat-General and works in close cooperation with the DG for Economic and Financial Affairs (DG ECFIN). It is responsible for guiding the implementation of the RRF and reports directly to the President of the Commission.

6.3.2. Supporting welfare state renewal in a diverse landscape

Many experts[318] emphasise that – despite the proposals of academic research at the height of the 2008 global crisis – most countries relied on substantial cuts in public investment and social spending, except for pensions. They stress that although each country has different public finance

313 J. Pisani-Ferry, Europe's recovery gamble, Bruegel, September 2020.

314 J. Pisani-Ferry, European Union recovery funds: strings attached but not tied up in knots, Bruegel, October 2020.

315 C. Alcidi et al., Who will really benefit from the Next Generation of EU Funds, CEPS, October 2020.

316 J. F Kirkegaard, What role for the European Semester in the recovery plan? Economic Governance Support Unit, European Parliament, October 2020.

317 Vanhercke et al. (eds), Social policy in the European Union; state of play 2020, OSE-ETUI, 2021.

318 Z. Darvas and G. Wolff, An anatomy of inclusive growth in Europe, Bruegel, October 2016.

structures and levels of effectiveness, spending[319] in the areas of education, health, public infrastructure and government effectiveness[320] (i.e. the extent to which they manage to meet each and everyone's needs) can be useful for all. In a similar vein, a recent analysis[321] also emphasises that the problem is not public indebtedness, so no austerity measures should be launched to counteract it. Far more important is how unemployment evolves and the extent to which, as a consequence of the economic shock, tax revenue reduces and welfare spending increases for a long time, potentially resulting in a persistent shortfall in public finances.

Alongside EU budgetary tools, several future EU policy initiatives, mainly grouped around implementation of the principles of the social pillar but also in education and training, and taxation, should support these endeavours and help to update of welfare states and labour markets.

There are competing narratives in the literature on how to update welfare states so as to meet each and every individual's needs in a world of new risks and opportunities, now exacerbated by the coronavirus crisis. These include: rapid aging, low growth rates, shrinking tax bases putting fiscal pressure on social security systems, a shift in gender roles and family structures, and structural changes in the labour market, including wage polarisation. Territories, social groups, families and individuals are facing situations of unforeseen need and insecurity. Thinking along the traditional welfare state models described by Esping Andersen[322] no longer appears to be the answer to these challenges. In addition, the financing of the welfare state is generating ever more problems. The rising numbers of new forms of work and working relationships make a purely insurance-based mechanism no longer feasible. At the same time, the digital transformation has also led to a fall in middle-skilled routine jobs,[323] leading in turn to the decline of the middle class. This also calls into question a financing mechanism based on tax revenues, as the main source of this revenue – the middle class – is squeezed.

For the future of the welfare regime, several scenarios[324] can be imagined. One could be a move towards a multi-layered welfare system with a high level of engagement from many public and private sector players, with a redefined role for government. In this scenario, governments would have responsibility for the governance of the supply side of the new multi-layer welfare system. There is a greater chance of achieving the ideal scenario if policies are directed towards supporting 'social effervescence', i.e. boosting solidarity. These considerations are in line with the above-mentioned 'missions' approach and collective problem-solving. Moreover, the EU can apply its various social governance tools to play an active support role.

In addition, many also emphasise that now is the time for strengthening the social investment[325] logic (i.e. investing more in human capital throughout the lifecycle). Investing in more and better human capital increases the potential for innovation as well as the potential to absorb new knowledge emerging from technological progress. Hence it also decreases the digital divide and telework-ability – two factors that if not addressed properly might even contribute to rising inequalities in the post-pandemic era. This social investment approach can be strengthened by

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[319] Z. Darvas, Economic growth and income distribution implications of public spending and tax decisions, October 2020.

[320] D. Kaufmann, et al., Governance Matters IV: Governance Indicators for 1996-2004. Policy Research Working Paper, No 3630, World Bank, 2005.

[321] 'The right kind of discipline', *The Economist*, November 2020.

[322] G. Esping-Andersen, *The three worlds of welfare capitalism*, 1990. He talks about liberal, conservative corporatist and social democratic worlds, and also the later-defined southern European and central and eastern European or post-socialist regime.

[323] OECD, Under pressure: the squeezed middle class, May 2019.

[324] G. Pasi and G. Miscuraca, 'Welfare 2.0. future scenarios for social protection systems in the digital age', *Policy Design and Practice*, Vol. 3(2), 2020.

[325] A. Hemerijck and R. Huguenot-Noel, The Covid 19 welfare wake-up call, EUIdeas, September 2020.

better EU fiscal rules and institutions[326] within the EU's economic governance framework currently under revision.

In that context there might also be a strong case for fiscal co-insurance across EU countries. Automatic stabilisers[327] (unemployment benefits or lower taxes paid as a result of job losses and/or a decrease in market incomes), can partly reduce the toll on household income and consumption. These stabilisers[328] are estimated to have absorbed 49 % of the drop in households' market income on average in the EU following the immediate impact of the coronavirus crisis. This proportion is estimated to have been larger in countries with progressive tax systems and more comprehensive social benefits.

There is also concern that the SURE temporary instrument should not replace[329] the plan for a permanent European unemployment reinsurance scheme. The idea of a permanent scheme first appeared as early as the 1970s, when the debate on the monetary union began, and the idea of a fiscal capacity for the euro area has been analysed as an instrument of stabilisation and redistribution. Since the 1970s, various models[330] have been promoted. The idea reappears in Ursula von der Leyen's political guidelines, where she proposes to come forward with a scheme that will protect citizens and reduce the pressure on public finances during external shocks. Several challenges[331] arise in relation to the design of such a scheme: the risk that its resources would flow permanently from certain countries with low unemployment rates; uncertainty concerning its fiscal rules; the role of social partners; and the legal basis. A recent study[332] clearly shows that social insurance practices (regarding unemployment benefits and active labour market policies) differ widely across Member States, as does their effectiveness in smoothing economic shocks and reducing long-term unemployment. It shows that, depending on the nature of the measure, the average rate of waste for unemployment benefits is between 26 % to 53 % of expenditure, leading to an estimated total waste of between about €41 billion and €80 billion per year. Based on a simulation exercise with historical data, the study concludes that a limited amount of co-insurance, with a maximum expenditure of 0.2 % GDP per annum per country, introduced in the 2000s, while being roughly in equilibrium along the period, would have reduced the GDP cumulative loss by €175 billion between 2009 and 2012 (€44 billion per year). Hence, the study clearly supports the introduction of a European unemployment scheme to complement national ones, supporting national systems in the event of relevant economic shocks.

Finally, focusing in particular on vulnerable groups in the recovery and in building up longer-term resilience can also pave the way for more generationally balanced welfare states.[333] Higher inequality is associated[334] with less intergenerational social mobility, i.e. economic disadvantage is passed on from one generation to the next. In this context, pro-child, pro-youth and pro-family policies can help to rebalance the generational divide,[335] while also strengthening the workforce.

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[326] D. Boldi, Thematic Digest on EU economic governance review, Economic Governance Support Unit, European Parliament, October 2020.

[327] V. Almeida et al., Households' income and the cushioning effect of fiscal policy measures during the great lockdown, JRC Working Papers on Taxation and Structural Reforms No 06/2020.

[328] European Commission, 2020 Annual Report of the Social Protection Committee, November 2020.

[329] C. Aldici -F. Corti, SURE, July 2020.

[330] C. Luigjes et al., The design of a European unemployment (re)insurance scheme: lessons from US experience, SSRN Research Paper, 2019/06.

[331] European Economic and Social Committee, Integrating the European Pillar of Social Rights into the roadmap for deepening the economic and monetary union, April 2019.

[332] J. Saulnier, Improving the quality of public spending in Europe, Budgetary 'waste rates' in EU Member States, EPRS, European Parliament, October 2020.

[333] S. Birnbaum et al., *The generational welfare contract, Justice, institutions and outcomes*, Elgar Publishing, 2017.

[334] D. Andrews and A. Leigh, 'More inequality, less social mobility', *Applied Economic Letters*, Vol. 16(15), 2009.

[335] T. Chen &al, Inequality and poverty across generations in the European Union, IMF, January 24, 2018.

Balanced generational welfare contracts provide for more extensive social citizenship rights[336] – establishing the universal nature of entitlements independently from work or residence status – for all age groups and thus encourage a positive-sum solution in generational politics. More extensive social citizenship rights make a positive contribution to various outcomes, such as lower poverty rates, higher levels of subjective well-being and trust in others. They are also more sustainable in social terms and have the potential to trigger choices that are environmentally sustainable too, such as the promotion of green taxes[337] as opposed to carbon taxes that can lead to energy poverty.

336 L. Yalçin-Heckmann, 'Introduction: claiming social citizenship', *Citizenship Studies*, Vol. 15 (3-4), 2011.

337 A green tax is a tax that is levied on actions that are deemed to be detrimental to the environment, e.g. green tax on non-recyclable plastic bags.

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8. Annexes

Annex 1 – EU spending allocation by Member State in 2019 (€ million)

Heading	1		2	3	4	5	9	
Subheading	1a	1b						
2019 *(€ million)*	**Competitiveness for growth and jobs**	**Economic, social and territorial cohesion**	**Sustainable growth: natural resources**	**Security and citizenship**	**Global europe**	**Administration**	**Special instruments**	**Total expenditure**
BE	1 724.1	613.9	673.8	349.5	0.0	5 415.6	0.1	8 776.9
BG	115.0	914.1	1 127.7	36.0	0.0	11.9	0.0	2 204.8
CZ	187.4	3 776.8	1 275.9	19.1	0.0	16.3	0.0	5 275.5
DK	328.5	87.0	993.9	19.6	0.0	71.3	0.0	1 500.3
DE	2 839.6	2 836.8	6 134.1	169.5	0.0	234.3	0.0	12 214.2
EE	114.9	726.0	279.8	36.7	0.0	11.8	0.0	1 169.2
IE	227.5	203.0	1 549.9	24.7	0.0	65.7	0.0	2 070.8
EL	385.7	1 812.6	2 497.7	526.8	0.0	34.4	0.5	5 257.7
ES	1 415.7	2 583.7	6 942.9	203.8	0.0	120.9	0.1	11 266.8
FR	2 626.0	2 231.4	9 618.4	170.1	0.0	439.7	0.0	15 085.6
HR	84.7	1346.0	597.3	34.0	1.1	10.5	0.0	2 073.7
IT	1 660.0	3 448.8	5 420.5	368.5	0.0	211.2	277.2	11 386.2
CY	68.5	86.4	82.6	22.3	0.0	6.5	0.0	266.4
LV	91.8	772.3	481.2	19.6	0.0	9.7	0.0	1 374.5
LT	120.0	728.9	642.2	47.5	0.0	11.1	0.0	1 549.7
LU	210.8	59.1	68.1	49.1	0.0	1 674.0	0.0	2 061.1
HU	134.6	4 171.0	1 827.3	52.8	0.4	16.7	0.0	6 202.5
MT	22.7	147.3	30.1	52.0	0.0	8.0	0.0	260.0
NL	1 242.8	130.1	831.2	250.9	0.0	102.0	0.0	2 557.1
AT	385.4	265.9	1 271.0	63.1	0.0	29.3	8.2	2 022.8
PL	338.9	11 307.8	4 561.9	125.6	0.0	31.3	0.0	16 365.5
PT	294.2	2 668.3	1 292.0	62.5	0.0	48.6	0.8	4 366.5
RO	169.2	2 165.6	2 691.7	78.1	24.1	20.4	8.2	5 133.2
SI	109.2	526.1	270.7	20.4	0.0	9.8	0.0	936.2
SK	129.3	1 477.5	671.0	14.4	0.0	12.2	0.0	2 304.4

FI	351.9	203.0	904.5	35.7	0.0	46.9	0.0	1 542.0
SE	380.7	213.3	957.4	112.2	0.0	41.7	0.0	1 705.2
UK	1 521.1	1 921.1	3 936.2	117.3	0.0	140.0	0.0	7 635.8
EU-28	17 280.3	47 423.9	57 630.6	3 081.9	1.1	8 851.9	295.0	**134 564.6**
earmarked	1 555.1	6 230.4	1 720.9	96.2	1 140.5	482.2	0	**11 225.2**
other	1 707.0	127.0	18.8	18.0	1 495.9	460.3	0	**3 807.0**
non-EU	1 205.3	5.9	150.5	60.0	7 490.6	586.4	0	**9 498.7**
Total	**21 747.6**	**53 787.2**	**59 520.7**	**3 256.2**	**10 108.1**	**10 380.7**	**295.0**	**159 095.5**

Data source: European Commission, EU expenditure and revenue 2014-2020.

Annex 2 – Own resources by Member State in 2019 (€ million and % of GNI)

	VAT-based resource	GNI-based Resource	UK correction	Netting of adjustments to the VAT and GNI-based own resources for previous financial years	Lump sum reduction granted for DK, NL, AT & SE (**)	Total national contribution		Traditional own resources (TOR), net (80 %)	Total own resources	
	1	2*	3**	4	5	6=1+2+3+4+5	% GNI	7	8=6+7	% GNI
BE	611.9	3 067.6	243.6	-97.9	31.8	3 861.9	0.81%	2 235.2	6 097.0	1.28%
BG	86.3	380.1	29.2	-11.7	3.8	488.3	0.80%	91.6	579.9	0.95%
CZ	289.9	1 347.6	107.5	-43.5	14.0	1 712.1	0.81%	286.9	1 999.0	0.95%
DK	358.5	2 090.9	164.1	-66.0	-122.4	2 405.6	0.75%	338.9	2 744.6	0.86%
DE	2 194.5	23 775.1	322.2	-753.1	244.4	25 820.0	0.73%	4 092.1	29 912.1	0.85%
EE	39.5	179.7	13.4	-5.4	1.7	229.2	0.83%	42.8	272.0	0.99%
IE	275.1	1 627.2	139.2	-56.0	18.2	1 995.6	0.75%	304.3	2 299.8	0.86%
EL	210.4	1 232.0	99.2	-39.9	12.9	1 516.6	0.81%	239.0	1 755.6	0.94%
ES	1 598.7	8 132.4	655.0	-263.4	85.5	10 221.1	0.82%	1 589.0	11 810.2	0.95%
FR	3 354.6	16 685.7	1 294.0	-520.4	168.8	21 008.8	0.85%	1 775.0	22 783.8	0.92%
HR	81.4	346.8	27.3	-10.9	3.6	448.6	0.84%	39.1	487.7	0.92%
IT	2 262.1	11 982.7	950.2	-382.1	124.0	14 956.0	0.83%	1 843.2	16 799.2	0.93%
CY	33.6	142.4	10.8	-4.4	1.4	184.1	0.87%	25.3	209.3	0,99%
LV	38.6	196.1	15.8	-6.3	2.1	246.5	0.81%	40.9	287.3	0.95%
LT	56.3	295.5	23.3	-9.4	3.0	369.3	0.79%	99.5	468.7	1,00%
LU	66.4	282.4	21.4	-8.6	2.8	364.8	0.84%	20.3	385.1	0.89%
HU	166.7	870.7	69.6	-27.7	9.1	1 089.6	0.79%	200.2	1 289.7	0.93%
MT	19.5	83.0	6.3	-2.5	0.8	107.3	0.89%	16.0	123.3	1.02%
NL	487.6	5 640.1	71.9	-168.0	-714.0	5 326.0	0.65%	2 729.1	8 055.1	0.99%
AT	529.4	2 634.9	36.0	-84.2	27.3	3 147.6	0.79%	221.1	3 368.7	0.85%
PL	742.0	3 276.7	261.6	-105.5	34.1	4 214.0	0.84%	826.9	5 041.0	1.00%
PT	308.2	1 331.5	105.8	-42.6	13.8	1 718.9	0.83%	185.6	1 904.5	0.92%
RO	237.6	1 383.4	108.8	-43.5	14.2	1 702.5	0.77%	197.3	1 899.9	0.86%
SI	68.8	317.6	25.2	-10.1	3.3	405.3	0.86%	78.9	484.1	1.02%
SK	102.7	610.5	49.5	-19.9	6.5	750.2	0.81%	84.3	834.5	0.90%

FI	312.4	1 608.9	127.1	-51.1	16.6	2 016.4	0.84%	150.2	2 166.6	0.90%
SE	305.1	2 954.0	41.9	-96.6	-167.1	3 042.2	0.63%	519.4	3 561.7	0.73%
UK	3 272.9	16 344.6	-5 100.5	-512.7	166.8	14 054.5	0.56%	3 092.5	17 147.0	0.69%
EU-28	18 104.8	108 820.3	-80.9	-3 442.9	6.9	123 402.9	0.75%	21 364.5	144 767.5	0.88%
								Surplus from previous year	1 803.0	
								Surplus external aid guarantee fund	0.0	
								Other revenue	17 347.1	
								Total revenue	**163 917.6**	

Data source: European Commission, EU expenditure and revenue 2014-2020.

(*) For simplicity, the GNI-based own resource includes the adjustment for Denmark, Ireland and the United Kingdom related to specific activities in the area of freedom security and justice (FSJ) in which they do not take part.

(**) Totals for UK correction payments and GNI reduction granted to NL and SE are not equal to zero on account of exchange rate differences.

Annex 3 – The EU budget 2020 and 2021

Headings and clusters presented according to the 2021-2027 MFF	2020 budget ((incl. AB1-8 and DAB10)) € million		2021 budget € million		Difference	
	CA	PA	CA	PA	CA	PA
SINGLE MARKET, INNOVATION AND DIGITAL	**21 868.956**	**19 154.734**	**20 816.560**	**17 191.587**	**-4.8%**	**-10.2%**
— Cluster 01 – Research and Innovation	13 962.503	12 658.431	12 646.070	10 716.493	-9.4%	-15.3%
— Horizon Europe	13 192.688	11 605.637	11 506.527	9 835.079	-12.8%	-15.3%
— Euratom Research and Training Programme	398.656	397.682	265.749	253.754	-33.3%	-36.2%
— International Thermonuclear Experimental Reactor (ITER)	365.069	638.955	863.994	613.639	136.7%	-4.0%
— Pilot projects and preparatory actions	6.090	16.156	9.800	14.022	60.9%	-13.2%
— Cluster 02 – European Strategic Investments	5 152.144	4 134.884	5 236.934	3 954.691	1.6%	-4.4%
— InvestEU Fund	812.587	1 736.981	653.555	1 080.965	-19,6%	-37.8%
— Connecting Europe Facility (CEF)	4 011.716	2 081.490	2 847.720	2 106.984	-29,0%	1,2%
— Connecting Europe Facility (CEF) - Transport	2 579.156	1 476.651	1 785.393	1 428.420	-30.8%	-3.3%
— Connecting Europe Facility (CEF) - Energy	1 281.033	479.683	784.950	471.391	-38.7%	-1.7%
— Connecting Europe Facility (CEF) - Digital	151.527	125.156	277.376	207.173	83.1%	65.5%
— Digital Europe Programme	86.116	91.748	1 129.577	158.591	1211.7%	72.9%
— European Fund for Strategic Investments (EFSI)					∞	∞
— Decentralised agencies	182.730	184.042	188.093	188.093	2.9%	2.2%
— Other actions			375.457	375.457	∞	∞
— Actions financed under the prerogatives of the Commission and specific competences conferred to the Commission	21.770	22.070	25.508	21.168	17.2%	-4.1%
— Pilot projects and preparatory actions	37.225	18.552	17.025	23.434	-54.3%	26.3%
— Cluster 03 – Single Market	865.731	821.317	899.253	832.706	3.9%	1.4%
— Single Market Programme (incl. SMEs)	607.230	569,559	575.019	547.136	-5.3%	-3.9%
— EU Anti-Fraud Programme	23.900	20.207	24.053	23.758	0.7%	17.6%

— Cooperation in the field of taxation (FISCALIS)	33.093	27.500	36.216	32.846	9.4%	19.4%
— Cooperation in the field of customs (CUSTOMS)	75.264	75.300	126.887	86.300	68.6%	14.6%
— Decentralised agencies	109.898	109.898	121.438	121.438	10.5%	10.5%
— Other actions	7.000	7.000	7.500	7.500	7.1%	7.1%
— Pilot projects and preparatory actions	9.350	11.854	8.140	13.727	-12.9%	15.8%
— Cluster 04 – Space	1 888.578	1 540.103	2 034.303	1 687.697	7.7%	9.6%
— European Space Programme	1 853.975	1 505.500	1 997.403	1 651.547	7.7%	9.7%
— Decentralised agencies	34.603	34.603	35.900	35.900	3.7%	3.7%
— Pilot projects and preparatory actions			1.000	0.250	∞	∞
COHESION AND VALUES	**66 213.601**	**62 054.462**	**52 861.899**	**66 153.766**	**-20.2%**	**6.6%**
— Of which: under Flexibility Instrument			76.383			
Economic, social and territorial cohesion	**58 568.101**	**55 208,642**	**48 190.516**	**61 867.898**	**-17.7%**	**12.1%**
Resilience and Values	**7 645.500**	**6 845.820**	**4 671.383**	**4 285.868**	**-38.9%**	**-37.4%**
— Of which: under Flexibility Instrument			76,382			
— Cluster 05 – Regional Development and Cohesion	44 077.110	40 710.514	35 410.370	45 755.417	-19.7%	12.4%
— European Regional Development Fund (ERDF)	32 160.785	30 280.816	29 240.315	33 870.955	-9.1%	11.9%
— Cohesion Fund (CF)	10 093.443	9 166.631	4 695.703	10 595.241	-53.5%	15.6%
— Cohesion Fund (CF), contribution to the Connecting Europe Facility (CEF) - Transport	1 780.568	1 213.462	1 442.366	1 250.074	-19%	3.0%
— Support to the Turkish-Cypriot Community	37.714	38.952	31.986	34.873	-15.2%	-10.5%
— Pilot projects and preparatory actions	4.600	10.654		4.274	-100%	-59.9%
— Cluster 06 – Recovery and Resilience	3 660.236	3 083.200	843.737	820.887	-76.9%	-73.4%
— European Recovery and Resilience Facility (incl. Technical Support Instrument)	86.725	56.730	116.364	109.182	34.2%	92.5%
— Protection of the euro against counterfeiting (the 'Pericles IV programme')	1.100	0.850	0.834	0,783	-24.2%	-7.9%
— Financing cost of the European Union Recovery Instrument			39.591	39.591	∞	∞
— Union Civil Protection Mechanism (RescEU)	574.899	267.706	90.203	193.532	-84.3%	-27.7%

— EU4Health	69.674	64.150	327.459	127.874	370%	99.3%
— Instrument for emergency support within the Union (ESI)	2 700.000	2 470.000		90.000	-100%	-96.4%
— Decentralised agencies	215.838	211.792	257.886	247.645	19.5%	16.9%
— Actions financed under the prerogatives of the Commission and specific competences conferred to the Commission	12.000	11.000	11.400	10.450	-5.0%	-5.0%
— Pilot projects and preparatory actions		0.971		1.831	∞	88.4%
— Cluster 07 - Investing in People, Social Cohesion and Values	18 476.254	18 260.748	16 607.791	19 577.462	-10.1%	7.2%
— European Social Fund (ESF)	14 528.705	14 537.080	12 812.132	16 147.354	-11.8%	11.1%
— Employment and Social Innovation	102.941	85.224	102.482	85.305	-0.4%	0.1%
— Erasmus+	2 885.368	2 739.451	2 662.616	2 407.562	-7.7%	-12.1%
— European Solidarity Corps (ESC)	186.699	172.741	135.713	126.613	-27.3%	-26.7%
— Creative Europe	223.572	197.422	306.382	236.542	37.0%	19.8%
— Justice	43.454	40.450	46,393	45.217	6.8%	11.8%
— Rights and Values	100.470	100.199	97.179	87.689	-3.3%	-12.5%
— Decentralised agencies	172.074	175.027	220.498	220.498	28.1%	26.0%
— Other actions	9.423	9.000	8.634	7.258	-8.4%	-19.4%
— Actions financed under the prerogatives of the Commission and specific competences conferred to the Commission	166.628	155.441	183.891	162.015	10.4%	4.2%
— Pilot projects and preparatory actions	56.920	48.715	31.870	51.410	-44.0%	5.5%
NATURAL RESOURCES AND ENVIRONMENT	**59 936.543**	**58 662.508**	**58 568.567**	**56 804.203**	**-2.3%**	**-3.2%**
— Of which: European Agricultural Guarantee Fund (EAGF) — Market related expenditure and direct payments	43 458.761	43 428.687	40 367.954	40 353.743	-7.1%	-7.1%
— Cluster 08 - Agriculture and Maritime policy	59 286.087	58 234,547	56 638.551	56 372.594	-4.5%	-3.2%
— European Agricultural Guarantee Fund (EAGF)	43 458.761	43 428.687	40 367.954	40 353.743	-7.1%	-7.1%
— European Agricultural Fund for Rural Development (EAFRD)	14 698.660	13 870.124	15 344.990	15 022.200	4.4%	8.3%
— European Maritime and Fisheries Fund (EMFF)	960.254	769.899	760.744	829.379	-20.8%	7.7%
— Sustainable Fisheries Partnership Agreements (SFPA) and Regional Fisheries Management Organisations (RFMO)	148.000	142.532	148.122	144.485	0.1%	1.4%

— Decentralised agencies	16.737	16.737	16.741	16.741	0.0%	0.0%
— Pilot projects and preparatory actions	3.675	6.569		6.047	-100.0%	-7.9%
— Cluster 09 - Environment and climate action	650.456	427.961	1 930.016	431.609	196.7%	0.9%
— Programme for Environment and Climate Action (LIFE)	589.563	371.882	738.505	371.472	25.3%	-0.1%
— Just Transition Fund			1 137.009	0.042	∞	∞
— Decentralised agencies	44.753	44.753	50.762	50.762	13.4%	13.4%
— Pilot projects and preparatory actions	16.140	11.326	3.740	9.333	-76.8%	-17.6%
MIGRATION AND BORDER MANAGEMENT	**2 367.812**	**2 168.044**	**2 278.830**	**2 686.246**	**-3.8%**	**23.9%**
— Cluster 10 - Migration	1 347,018	1 070.932	1 011.066	1 439.159	-24.9%	34.4%
— Asylum and Migration Fund (AMF)	1 228.690	952.604	873.255	1 301.348	-28.9%	36.6%
— Decentralised agencies	118.327	118.327	137.811	137.811	16.5%	16.5%
— Cluster 11 – Border Management	1 020.794	1 097.112	1 267.764	1 247.087	24.2%	13.7%
— Integrated Border Management Fund (IBMF) - Instrument for border management and visa (BMVI)	358.771	479.244	398.014	488.178	10.9%	1.9%
— Integrated Border Management Fund (IBMF) - Instrument for financial support for customs control equipment (CCEi)			135.480	32.964	∞	∞
— Decentralised agencies	662.023	617.868	734.270	725.945	10.9%	17.5%
SECURITY AND DEFENCE	**831.442**	**814.174**	**1 709.261**	**670.628**	**105.6%**	**-17.6%**
— Cluster 12 - Security	576.442	595.674	536.501	527.390	-6.9%	-11.5%
— Internal Security Fund (ISF)	195.197	193.558	175.643	180.582	-10.0%	-6.7%
— Nuclear decommissioning (Lithuania)	68.290	68.050	72.500	50.000	6.2%	-26.5%
— Nuclear Safety and decommissioning (incl. For Bulgaria and Slovakia)	110.160	132.800	69.205	78.355	-37.2%	-41.0%
— Decentralised agencies	179.316	179.316	197.614	197.614	10.2%	10.2%
— Actions financed under the prerogatives of the Commission and specific competences conferred to the Commission	21.480	21.450	21.539	20.839	0.3%	-2.8%

— Pilot projects and preparatory actions	2.000	0.500			-100.0%	-100.0%
— Cluster 13 - Defence	255.000	218.500	1 172.760	143.238	359.9%	-34.4%
— European Defence Fund (Research)			283.262	13.112	∞	∞
— European Defence Fund (Non Research)	255.000	200.500	662.436	108.962	159.8%	-45.7%
— Military Mobility			227.062	16.664	∞	∞
— Pilot projects and preparatory actions		18.000		4.500	∞	-75.0%
— Cluster 14 - Resilience and Crisis Response					∞	∞
— Union Civil Protection Mechanism (RescEU)					∞	∞
— Instrument for emergency support within the Union (ESI)					∞	∞
— EU4Health					∞	∞
— Decentralised agencies					∞	∞
— Pilot projects and preparatory actions					∞	∞
NEIGHBOURHODD AND THE WORLD	**10 848.581**	**9 603.264**	**16 097.196**	**10 810.999**	**48.4%**	**12.6%**
Cluster 15 - External Action	9 088.415	7 857.544	14 195.758	8 928.603	56.2%	13.6%
— Neighbourhood, Development and International Cooperation Instrument (NDICI)	6 962.973	6 063.750	12 070.958	6 514.257	73.4%	7.4%
— European Instrument for Nuclear Safety (EINS)	32.885	32.691	37.620	32,505	14.4%	-0.6%
— Humanitarian aid (HUMA)	1 586.824	1 275.289	1 503.000	1 900.103	-5.3%	49.0%
— Common Foreign and Security Policy (CFSP)	351.927	328.650	351.927	328.668		0.0%
— Overseas Countries and Territories (OCT) (including Greenland)	33.489	33.373	67.000	33.428	100.1%	0.2%
— Other actions	35.577	42.577	72.054	41.605	102.5%	-2.3%
— Actions financed under the prerogatives of the Commission and specific competences conferred to the Commission	80.740	78.184	93.024	77.994	15.2%	-0.2%
— Pilot projects and preparatory actions	4.000	3.030	0.175	0.044	-95.6%	-98.6%
Cluster 16 - Pre-Accession Assistance	1 760.166	1 745.719	1 901.438	1 882.396	8.0%	7.8%
— Pre-Accession Assistance (IPA III)	1 760.166	1 745.719	1 901.438	1 882.396	8.0%	7.8%
EUROPEAN PUBLIC ADMINISTRATION	10 222.258	10 225.262	10 448.313	10 449.588	2.2%	2.2%
Of which: Administrative expenditure of the institutions	7 906.140	7 909.143	8 035.825	8 037.100	1.6%	1.6%
— European Schools and Pensions	2 316.119	2 316.119	2 412.488	2 412.488	4.2%	4.2%
— Administrative expenditure of the institutions	7 906.140	7 909.143	8 035.825	8 037.100	1.6%	1.6%

— European Parliament	2 038.119	2 038.119	2 062.870	2 062.870	1.2%	1.2%
— European Council and Council	590.633	590.633	594.387	594.387	0.6%	0.6%
— Commission	3 681.839	3 684.842	3 724.183	3 725,458	1.2%	1.1%
— Court of Justice of the European Union	436.593	436.593	444.003	444.003	1.7%	1.7%
— European Court of Auditors	152.237	152.237	153.722	153.722	1.0%	1.0%
— European Economic and Social Committee	142.539	142.539	150.525	150.525	5.6%	5.6%
— European Committee of the Regions	101.508	101.508	106.741	106.741	5.2%	5.2%
— European Ombudsman	12.138	12.138	12.323	12.323	1.5%	1.5%
— European Data Protection Supervisor	19.477	19.477	19.463	19.463	-0.1%	-0.1%
— European External Action Service	731.056	731.056	767.608	767.608	5.0%	5.0%
APPROPRIATIONS FOR HEADINGS	**172 289.194**	**162 682.447**	**162 780.626**	**164 767.018**	**-5.5%**	**1.3%**
— Of which: under Flexibility Instrument			**76.383**	**628.462**		
Appropriations as % of GNI	***1.01%***	***0.96%***	***1.16%***	***1.18%***		
Thematic special instruments	**1 594.858**	**1 425.595**	**1 470.835**	**1 293.450**	**-7.8%**	**-9.3%**
TOTAL APPROPRIATIONS	**173 884.052**	**164 108.042**	**164 251.461**	**166 060.468**	**-5.5%**	**1.2%**
Appropriations as % of GNI	***1.02%***	***0.97%***	***1.17%***	***1.19%***		

This study, the fifth in an annual series, provides an overview of the economic and budgetary situation in the EU and beyond, and summarises the main economic indicators in the EU and euro area and their two-year trends. It also explains the annual EU budget, provides an overview of its headings for 2021, and sets out the wider budgetary framework – the post-2020 multiannual financial framework (MFF) and the Next Generation EU recovery instrument. This year's special 'economic focus' puts the spotlight on EU social and employment policies in the context of the coronavirus outbreak.

QA-CH-21-001-EN-N

This is a publication of the Members' Research Service
EPRS | European Parliamentary Research Service

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PE 679.062
ISBN 978-92-846-7722-1
ISSN 2600-2779
doi:10.2861/597358
QA-CH-21-001-EN-N