The New MFF and Recovery Vision - what does it mean for the EU?

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INTRODUCTION

The COVID-19 pandemic, its ensuing crisis and the severe criticism faced by the EU for its lack of response prompted the European Commission to propose a revamped Multiannual Financial Framework (MFF), as well as a new recovery tool dubbed Next Generation EU (NGEU). Facing two opposing approaches from the Council – a Franco-German grants-based one and the loans-based one pushed by opponents of big spending – the Commission seemingly opted to merge the two and let the Council battle it out, thereby avoiding any further criticism that the EU has not done enough to remedy the crisis. It reflects the new priorities of the Commission and features some ambitious and controversial plans, such as a whole new range of funding for the EU in the form of various new levies on businesses..

This note presents how the change of priorities affected the EU's long-term budget; initial reactions of main political stakeholders in the Member States and the European Parliament; how the money will be allocated in immediate responses to the economic crisis; and finally presents in the Annex the breakdown of the MFF proposal compared to its defunct 2018 predecessor.

THE NEW MFF AND HOW IT COMPARES WITH THE COMMISSION'S PREVIOUS PROPOSAL

The top-line number of roughly €1.1 trillion for the MFF is **slightly lower** than the Commission's original proposal in 2018. It is nonetheless **slightly higher** than the **compromise proposal** put forward by European Council President **Charles Michel** in February, which was ultimately **rejected** by the Member States. To compensate for the MFF's overall reduction and to address the new reality of the crisis, the Commission proposes a new recovery instrument – **the Next Generation EU** – which will raise money by temporarily lifting the own resources ceiling to 2% of EU GNI, allowing the Commission to use its strong credit rating to **borrow €750bn on the financial markets**. This additional funding will be **channelled through EU programmes** and repaid over a long period of time throughout future EU budgets – not before 2028 and not after 2058.

The proposal reflects some **shifts** in EU priorities compared to the 2018 MFF blueprint as a result of the COVID-19 crisis, including reductions for spending on **defence**, space, some **research programmes,** and **administration**. Other areas, however, such as **climate change, agriculture, cohesion,** and **healthcare** will receive significant boosts.

AFFECTED AREAS

Defence has been one of the most severely affected areas in the new Commission blueprint. The planned spending for the **European Defence Fund** and military mobility would be reduced, with **no compensation** from recovery funding. Some **research and innovation** programmes, too, will be trimmed down. Proposed investment in **digital infrastructure** through the **Connecting Europe Facility 2.0 digital** is **reduced** from **€2.6bn** in the 2018 proposal to **€1.8bn** now. Similarly **CEF2.0 energy** is also down from **€7.7bn** in 2018 to **€5.1bn** now. Europe's **public administration** spending has also been **reduced by €1bn** without being compensated from Next Generation EU, and **space policy** has similarly received a **€1bn reduction** with no compensation from NGEU, moving from **€14.4bn** in 2018 to **€13.4bn** now.

BOOSTED PRIORITIES

The Commission appears to have sought to **compensate** for cuts in some areas by adding spending in other programs as a part of the recovery package, including efforts to **bring the economy** up to speed, **combat climate change**, **Horizon Europe**, and **increase health preparedness**. For instance, spending on the **Common Agricultural Policy** would be **increased**, as well as funding for the **environmental** and **climate action.** In this regard, the Commission is increasing the **Just Transition Fund's** original €7.5bn budget by €32.5bn in borrowed money, bringing the total to **€40bn.** Additionally, compared to the 2018 Commission proposal, **Cohesion spending** would now receive a major top-up **of €50bn** borrowed in the markets.

On **research programmes** for **digital infrastructure**, the **Digital Europe Programme** funding remains at **€8.2bn** over seven years. The Commission trimmed the budget allocation for the Union's largest R&I programme **Horizon Europe** by €5.6bn, compared to the 2018 proposal, but it now **compensates the programme with €13.5bn of borrowed money**, leading to an **overall increase of €7.9 bn**. This approach to funding Horizon Europe with borrowed money could, nonetheless, render the programme **less attractive** to industry participation, as borrowed funds traditionally come with **conditionalities** and/or **requirements** for stakeholders to match public contributions.

One novel aspect of the proposal which was received with enthusiasm by healthcare stakeholders is the creation of a new stand-alone **€9.4bn health programme** called **EU4Health**, which was complemented with increased funding for **rescEU**. The Commission's plan is to reinforce national health systems to deal with this crisis, forecast future virus outbreaks, and procure medical supplies. The longer-term plans envision efforts on **prevention** and **access** to diagnosis and treatment, and on the creation of a **European Health Data Space**.

OWN RESOURCES

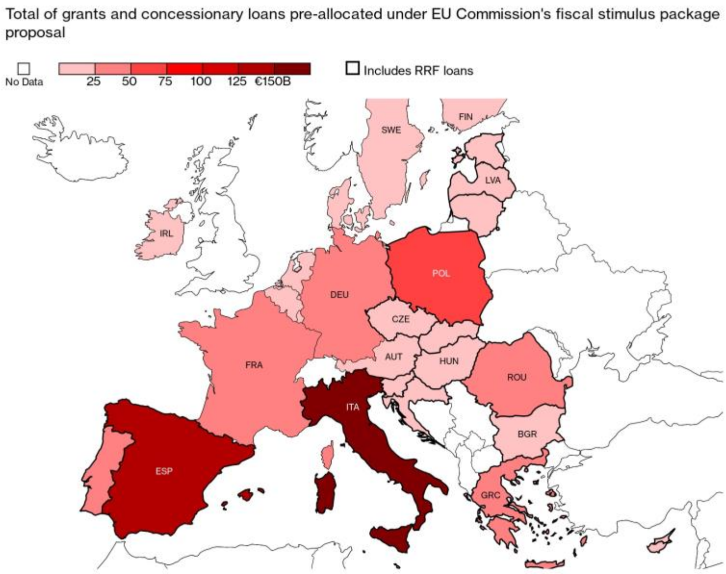
The Commission emphasised that all the borrowing envisioned under the recovery fund could theoretically be repaid by creating **new revenue streams**. National capitals have **continually resisted** permitting the Commission to establish new "own resources", but the Commission believes that such proposals would be **more tolerable** to Member States **than the alternatives** – **future spending cuts** or **higher national contributions** to the MFF. New resources include a **digital tax** (either based on the currently negotiated OECD one or as the EU's stand-alone), a **carbon border tax**, expanding the **EU's Emissions Trading System** to aviation and maritime, and a new **"corporate tax" on operations of large enterprises**.

The mechanisms of the functioning of and the mathematics behind these new taxes remain unclear and a cause for concern. On the issue of the "corporate tax", the Economy Commissioner **Paolo Gentiloni (S&D, IT)** stated that the Commission considered promoting a minimum corporate tax rate for EU companies **only if there is no global agreement** on the issue, which has been discussed at OECD since 2019 without major success. Corporate taxation has been a sensitive issue for countries like **Ireland** and **Luxembourg**, making it very difficult for Member States to reach a unanimous deal needed on such a proposal in the months to come.

INITIAL STAKEHOLDER REACTIONS TO THE MFF

While it came as a no surprise that the European Parliament overwhelmingly lauded the proposal, focussing mainly on increasing their own role in the upcoming negotiations, the differences among Member States remain as significant as ever. In addition, the traditional rift between net contributors and beneficiaries of the EU budgets has been exacerbated by the new recovery plan disproportionately favouring some countries (see the picture). It is likely the battle within the Council and between the Council and the Parliament will mark the rest of 2020.

Whilst the initial reactions focussed on the MFF and its nature, the true fight should be expected once the details, especially on own resources, start emerging.



MEMBER STATES' REACTIONS

French President Emmanuel Macron (RE) called for the Council to promptly adopt the proposals. Both him and the Minister of the Economy and Finance Bruno Le Maire focused on the "centrality" of the Franco-German agreement.

German Chancellor Angela Merkel (EPP) reacted to the proposal with more moderation, noting that the upcoming Council negotiations will be difficult. It is important to note that Germany was among those countries that initially rejected the idea of EU grants allocations and that the Commission's proposal for recovery exceeds the Franco-German one. Merkel's reserved reaction may result from dual concerns: as a country taking over the Presidency, Germany will have to play a role of a neutral mediator; and her party CDU (EPP) and their electoral base have consistently been among the opponents of the big spending and large EU budgets.

As for **Southern Europe**, Portugal, Italy, Spain, and Greece unsurprisingly welcomed the Commission's proposal to allocate a considerable part of the recovery funds to these Member States. **Portuguese Prime Minister António Costa (S&D)** commented that the proposal represents an ambitious response to the coronavirus challenge and underlined the fact that it is essential that it is based on grants. Similarly,, **Giuseppe Conte (NI), the Italian Prime Minister**, hailed the Commission's blueprint. **Spanish PM,** Pedro Sanchez **(S&D), and Greek PM, Kyriakos Mitsotakis (EPP)**, also voiced their support for the proposal, calling for its prompt adoption at the Council.

The "Frugal Four" appear to be less united at the moment. The Netherlands and Sweden are adhering to their strong opposition, whilst Austria and Denmark seem open to the possibility of a compromise. The **Dutch Prime Minister Mark Rutte (RE)** stated that The Netherlands' position remains as of today the same as presented in the Frugal Four's proposal and emphasized that the negotiations will need to clearly define national measures supported by the fund's allocation and corresponding conditionalities. **Swedish Prime Minister, Stefan Löfven (S&D)**, reconfirmed the country's rejection of the proposals, saying that they go beyond what Sweden will support and that the lack of repayment requirements presents an additional issue.

Austrian Chancellor Sebastian Kurz (EPP) surprisingly referred to the proposals in more positive terms. He described it as "a starting point", praising its time limitation as a guarantee that national debts will not be mutualized. **Danish Foreign Minister Jeppe Kofod (S&D)** echoed Kurz's statement, underlining that the division between grants and loans represents an important step towards the Danish position but also, said that the overall proposed allocation is too ambitious. Kofod pledged that the government would defend Denmark's interests during the upcoming negotiations but acknowledged that a compromise will have to be found.

Another country that has shown reservations on the Recovery proposal is Finland whose **Europe Minister, Tytti Tuppurainen (S&D)**, has voiced concerns over the total grants allocation proposed by the Commission. However, Finland had previously welcomed the Commission's intention to focus the recovery strategy on the green transition, so Helsinki's position remains to be clarified.

The Visegrad 4 Group also seems divided on the EU budgetary issue, with **Poland (ECR) and Slovakia (EPP)** supporting the proposal as two of the countries that will most benefit from the recovery funds.
On the other hand, **Czech Prime Minister Andrej Babiš (RE)** raised concerns about the size of the budget and the repaying scheme. **The Hungarian Prime Minister Viktor Orbán (EPP)** also rejected the proposal, saying the rich would be financed by the money of the poor.

Croatian Prime Minister Andrej Plenković (EPP), on behalf of the outgoing Presidency, welcomed the proposal and announced that the European Commission had reserved €10bn for Croatia, €7.3bn of which as grants. On the same line, the **Slovenian Government (EPP)** also supported the proposed recovery allocation and **Romanian Prime Minister Ludovic Orban (EPP)** welcomed the proposals regarding both the recovery instrument and the revised MFF budget.

REACTIONS FROM THE EUROPEAN PARLIAMENT

European People's Party (EPP) generally supported the Commission's proposal, welcoming the fact that it does not contain provisions on the mutualization of existing debt. ITRE Committee Chair, **Cristian Bușoi** (Romania) added that the recovery should be led by innovations such as for the green and digital transformations, however EPP's ITRE coordinator and Rapporteur for Horizon Europe, **Christian Ehler** (Germany) voiced concerns over the budget's priorities, noting that an ambitious green recovery without an adequate research allocation (namely through the Horizon Europe) would be "suicidal".

Progressive Alliance of Socialists and Democrats (S&D) hailed the Commission's decision to mainly base the recovery fund on grants to allow member states to obtain fair access to financing. The S&D also called for the MFF to be voted based on a qualified majority voting (QMV) procedure to speed up the process. However, it is unlikely that the Frugal Four states will accept such a procedure. It is worth noting that the three Nordic countries opposing the MFF proposal – Denmark, Finland and Sweden – all have S&D governments in power, which could lead to further turbulence between the North and the South in the Group.

Renew Europe (RE) lauded the proposed grants scheme and the conditionality providing that the funds' allocation will have to be in line with the rule of law. Curiously enough, even MEPs from the governing Dutch VVD voiced support for the proposal, despite their government's open rejection.

Greens–European Free Alliance (Greens/EFA) expressed hope the MFF would support European values such as the Green transition and Gender equality. Their Co-Chair **Ska Keller** (Germany) stressed the need for the implementation to avoid austerity measures and "blind market ideologies".

European Conservatives and Reformists (ECR) appeared somewhat divided on the proposal. Italian and Polish MEPs who present the core of the Group presented moderate positions, likely because their Member States stand to benefit plenty from the proposals. On the other hand, **Derk Jan Eppink** (Bureau member and ECON Vice-Chair, The Netherlands) firmly rejected the proposal as an EU attempt to gain more supranational powers, supporting the Dutch government's stance despite being from the opposition party.

European United Left–Nordic Green Left (GUE/NGL) Manon Aubry (ECON Coordinator, France) bemoaned the proposal as not ambitious enough and called for the crisis debt to be cancelled, for direct perpetual loans to Member States, and for public support to be conditional on social considerations.

Identity and Democracy (ID) strongly rejected the proposal, echoing Eppink's position. The MEPs agreed on the proposal being an attempt from the EU to obtain additional supranational powers at the expense of the European taxpayers. The ID Group has been dominated by the Italian Lega that previously criticised the EU for the lack of solidarity.

THE RECOVERY INSTRUMENT: SAVING THE EU'S ECONOMIES

What was previously known as the Economic Recovery Plan, and the Economic Recovery Instrument, has a new name – **Next Generation EU** (NGEU), and will consist of €750bn (€500bn in grants + €250bn in loans).

THE DAWN OF A MORE AUTONOMOUS EU?

The NGEU foresees some elements of a more centralised approach to some areas, such as the Internal Market, while seemingly supporting the EU's overall global competitiveness in the changed world, including on trade, industrial strategy and own competition rules.

A new Single Market Enforcement Task Force will identify and address barriers that arise to identify improper application or enforcement of the single market, and will ensure the full implementation of the Single Market Enforcement Action Plan. It could possibly play a role in the **planned "corporate tax"** scheme.

Reviewing the EU's **Competition Framework** to ensure that competition rules remain fit for the world of tomorrow will be based on **'Open Strategic Autonomy',** to help Europe prevent, protect and withstand future economic shocks. This does not go as far as the **Franco-German call for European Champions**, but certainly allows for such interpretations. It is also linked with the need to strengthen the security of supply, of essential things like pharmaceutical ingredients and raw materials and a **new Action Plan on Critical Raw Materials** (TBD), which should look at how crucial markets for e-mobility, batteries, renewable energies, pharmaceuticals, aerospace, defence and digital applications can be strengthened in a sustainable way.

In the spirit of the model of 'Open Strategic Autonomy', the EU will also undertake a **Trade Policy Review**, to ensure the continuous flow of goods and services worldwide. Calls for a more combative EU approach to trade have already been voiced by the Parliament and a **reinforced Foreign Direct Investment Screening Mechanism** should help protect European strategic assets, infrastructure and technologies from foreign direct investment that could threaten the EU's security. The Commission will by June publish a White Paper on an instrument on foreign subsidies, and will also encourage a swift agreement on the proposed **International Procurement Instrument**. To protect companies operating under stricter climate enforcement rules in Europe, the Commission will propose a **Carbon Border Adjustment Mechanism** in 2021, which will be compatible with WTO rules and whose revenues will serve as a new own resource to the EU Budget.

THE FUNDAMENTALS OF THE RECOVERY

All NGEU money, both loans and grants and divided between three pillars, will be channelled through EU programmes, but the lion's share was earmarked for Member States (see table below).

Programme	Total Budget (MFF+NGEU)	NGEU Budget	Mechanism	Possible Means of Accessing Funds & Allocation
Pillar I: Support to Member States with investments and reforms				
Recovery and Resilience Facility – To offer financial support to Member States for investments and reforms	€560 bn	€560 bn	Grants (€310 bn) & Loans (€250bn)	Public Procurement, PPPs and projects via Member States
REACT-EU: Extra Cohesion money(2020-2022)	€55 bn	€55 bn	Mainly grants	Allocation to the most affected regions: Liquidity support, employment subsidies and short-time work schemes via Member States
The Just Transition Fund: For those hardest affected by the energy transition	€40 bn	€30 bn	Mainly grants	Allocation to Member States based on set criteria.
European Agricultural Fund for Rural Developments: To assist the implementation of the Biodiversity and Form to Fork Strategies	€90 bn	€15 bn	Mainly grants	Support for farmers and the agricultural sector
Pillar II: Incentivising private investment to 'kick-start' the EU economy				
A New Solvency Support Instrument: To mobilise private resources	€31 bn	€26 bn	Provisioning of budget guarantee	Guarantees or financing to investment vehicles; Channelled to companies in the sectors, regions and countries most affected. Most likely via the EU.
An upgraded InvestEU: To invest in the EU Economic Recovery	€15.3 bn	€15.3 bn	Provisioning of budget guarantee	Projects via the EU
A New Strategic Investment Facility built into InvestEU: Focus on Strategic Autonomy across key technologies and value chains	€15 bn	€15 bn	Provisioning of budget guarantee	Projects & IPCEIs via Member States
Pillar III: Addressing the lessons of the crisis				
EU4Health Programme	€9.4 bn	€7.7 bn	Grants and Procurement	Investments and Procurement via the EU and Member States.
Reinforced rescEU: To the Union's Civil Protection Mechanism	€3.1 bn	€2 bn	Grants and procurement	Public Procurement via the EU and Member States
Horizon Europe: To fund research in health, and the green and digital transitions	€94.4 bn	€13.5 bn	Likely grants and loans	Calls for proposals; projects, partnerships and missions via the EU and Member States
External Action: Neighbourhood and the World	€118.2 bn	€15.5 bn	Support to global partners, including humanitarian aid	Grants, contracts, and budget support via the EU

THE EUROPEAN GREEN DEAL: THE EU'S 'GROWTH STRATEGY'

As in the European Green Deal, all NGEU public investments should respect the green oath '**Do no harm'**. In practice, this means that all **public investments** should be aligned with the European Semester, the National Energy and Climate Plans (NCEPs), and the Just Transition plans, and all **private investments** must be guided by the **EU Taxonomy**.

Aside from the much discussed **Renovation Wave,** which should lead to the creation of green jobs while contributing to the EU's overall climate goals, one of the main objectives of the recovery is to unlock investments in **key clean technologies and value chains** via **Horizon Europe**. As key technologies, the recovery plan specifically mentions **renewables and energy storage technologies, clean hydrogen, batteries, carbon capture and storage and sustainable energy infrastructure.** In this regard, the **European Battery Alliance** will be given a new push and a **Clean Hydrogen Alliance** will be launched accompanying an **EU Hydrogen Strategy**. Furthermore, offshore renewables will be given a boost, and the Commission will also publish an **Offshore Renewable Energy Strategy** by the end of this year.

When public investment is made into the **transport sector,** the NGEU underlines that the investment should come with "a commitment from industry to invest in cleaner and more sustainable mobility" such as **sustainable vehicles and vessels, alternative fuels and installation of charging points**.

To ensure a fair and just transition an additional €32.5bn has been allocated to the **Just Transition Fund** (originally proposed €7.5bn). This money will come from both the MFF and the NGEU and is meant to alleviate the economic impacts of the energy transition by primarily supporting the new jobs and re-skilling of workers.

The different initiatives will primarily be funded through the following pillars of Next Generation EU:	
Commission Initiative	**NGEU funding programme(s)**
The Renovation Wave	The New Recovery and Resilience Facility (Pillar I – Support to Member States) InvestEU (Pillar II – Incentivising Private Investments)
Clean technologies and Value Chains (Including the Clean Hydrogen Alliance, the European Battery Alliance and offshore renewable energy)	Reinforced Horizon Europe (Pillar III – 'Lessons learned') The New Strategic Investment Facility (Pillar II – Incentivising Private Investments)
Sustainable transport (Including alternative fuels, charging points)	InvestEU (Pillar II – Incentivising Private Investments)
EU Biodiversity Strategy and Forest Strategy	Invest EU (Pillar II – Incentivising Private Investments)
Common Agricultural Policy and the Farm to Form Strategy	The European Agricultural Fund for Rural Development (Pillar I – Support to Member States)

THE DIGITAL RECOVERY: A DEEPER AND MORE DIGITAL SINGLE MARKET

Europe's digital recovery will primarily be funded through:

- **The Recovery and Resilience Facility -** Due to its nature, the fund is expected to prioritise projects at a macro level most likely by creating public procurement opportunities and PPPs.
- **InvestEU** will provide crucial support to companies in the recovery phase and will increase the risk-taking capacity of the European Investment Bank Group and National Promotional Banks. Funds of Invest EU will most likely be channelled through projects.
- **Strategic Investment Facility (€15bn - provision of budget guarantee) -** focussed on building resilient value chains. The programme, falling in line with EU tech sovereignty, will benefit corporates established and operating in the European Union in the form of projects, including IPCEIs.

5G as a key enabling technology is addressed both as a means for positive spill-over effects and as an end-goal for enhancing EU's digital supply chains. This falls in line with the **Commission's Industrial strategy**, as well as the draft Council conclusions on **Shaping Europe's Digital Future** that call for increased investments in 5G technologies. Therefore, 5G is expected to draw funds from all the programs to develop capacities both at Member State level and support innovative businesses.

Key technologies prioritised in the NGEU are **AI, Cybersecurity, data and cloud infrastructures, 5G and 6G networks, high-performance computing, quantum and blockchain** to enhance Europe's industrial and technological presence in strategic parts of the digital supply chains. This aligns with the EU's narrative of technological sovereignty and reflects the evolution of the discussion around tech sovereignty from calls for a European style of "Made in America" at the start of the mandate, to a broader focus around reducing the EU's digital dependency to third countries. It calls for more European data ownership and greater self-sufficiency when it comes to cybersecurity. Funding for key technologies is likely to originate from the Strategic Investment Facility to promote European businesses, as well as the Recovery and Resilience Facility to support Member States in enhancing their infrastructures.

Genuine Single Market for data will be supported through a **"High Impact Project" on European data spaces and cloud federations** and additional measures to facilitate data sharing and governance, as well as the Data Act, as envisaged in Europe's data strategy. Furthermore, the Commission will propose to make high-value datasets available for the public interest. The emphasis on data economy and data sharing indicates that technologies, such as AI and data and cloud infrastructures, will likely be prioritised in funding allocation.

Digitisation of public procurement will be prioritised and funds will be supported through the development of national e-procurement systems and platforms, likely in the form of public procurements at national level.

By enhancing cybersecurity, referred to as a means of increasing strategic digital capacities, the NGEU is expected to channel funding towards R&I. Beyond this, DG Connect has highlighted that the EU is lagging behind in the commercialisation of European research. As a result, funds are also expected to **promote cybersecurity solutions provides by European businesses and SMEs**.

Programme	MFF (May 2020) *In 2018 Prices	Next Generation EU (Top Up) *In 2018 Prices	MFF (2018) *In 2018 Prices	Total Difference *In 2018 Prices
I. Single Market, Innovation and Digital	€140.65bn	€69.8bn	€166.3 bn	**+** €44,15bn
a. Space Policy	€13.4bn	-	€14.04bn	**–** €0.64bn
b. Horizon Europe	€80.9bn	€13.5bn	€86.59bn of which €3.1 under Invest EU	+10.91bn
c. Digital Europe Programme	€8.19bn	-	€8.19bn	**-**
d. Connecting Europe Facility - Transport	€12.88bn & €10bn under Cohesion Fund	-	€11.38bn & €10bn under Cohesion Fund	**+** €1.5 bn
e. Connecting Europe Facility - Energy	€5.18bn	-	€7.67bn	**–** €2.49bn
f. Connecting Europe Facility - Digital	€1.83bn	-	€2.66bn	**–** €0.83bn
II. Cohesion and Values	€374.46bn	€610bn	€391.97bn	**+** €592.49bn
III. Natural Resources and Environment	€357.03bn	€45bn	€336.62	**+** €66.03bn
a. Common Agricultural Policy	€333.26	€15bn	€324bn	**+** €24,26bn
b. Just Transition Fund	€10bn	€30bn	€7.5bn	**+** €32.5bn
IV. Migration and Border Management	€31.12bn	-	€30.82bn	**+** €0.3bn
V. Resilience, Security and Defence	€19.42bn	€9.7bn	€24.32bn	**+** €4.8bn
a. European Defence Fund	€8bn	-	€11.45bn	**–** €3.4bn
b. Health programme	€1.67bn	€7.7bn	-	-
VI. Neighbourhood and the World	€102.7bn	€15.5bn	€108.92bn	**+** €9.3bn
VII. European Public Administration	€74.6 bn	-	€75.60bn	**–** €1bn