European Economic and Social Committee

OPINION

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Euro area economic policy 2022

Recommendation for a Council recommendation on the economic policy of the euro area
[COM(2021) 742 final]

ECO/568

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Referral	European Commission, 07/01/2022
Legal basis	Article 304 of the Treaty on the Functioning of the European Union
Section responsible	Economic and Monetary Union and Economic and Social Cohesion
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Outcome of vote (for/against/abstentions)	229/2/10

1. Conclusions and recommendations

1.1 Current socio-economic development in countries of the euro area is accompanied by a high level of uncertainty associated with the uncontrolled and rapid spread of COVID-19. Therefore, the EESC welcomes the most recent Commission document on economic developments in the EU Member States and the analysis of consequences for the management process[1]. Simultaneously, it refers to the historic opportunity to accept and consistently implement without delay corresponding practical and effective policies on the road to the complex, though, in view of current developments, necessary transformation of the whole of society.

1.2 One of the greatest challenges in the area of internal macroeconomic imbalances is how to ensure gradual consolidation of public finances. The EESC is of the opinion that the current legislative framework in the form of the existing Stability and Growth Pact is no longer appropriate to the current conditions. Therefore, it emphasises that a reasonable and acceptable revision of fiscal rules[2] of the legislative framework focused on its simplification and monitoring is a clear requirement.

1.3 The EESC refers to the COVID-19 pandemic that struck as most countries were undergoing a process of correction of macroeconomic imbalances. The pandemic interrupted the reduction in debt-to-GDP ratios, while housing prices accelerated, suggesting an overall aggravation of macroeconomic conditions. In addition, the EESC refers to the largest external imbalances which are manifested in the Eurosystem – TARGET2[3]. These imbalances have been creating the largest differences between countries since their development.

1.4 The EESC is monitoring the rapid increase in inflation since the start of 2021. This increase, following years of low inflation, is mainly linked to the strong rebound in energy prices from historic lows during the pandemic, disruption of supply chains and increased transport costs. It is of the opinion that the current high inflation rate is the result of factors that relate to the pandemic and the reopening of economies, which are temporary in nature. Price growth can be expected to moderate in 2022 and 2023, with inflation levels declining to past average.

1.5 Completion of the process of financial union is a prerequisite for a well-functioning European Monetary Union. Despite the progress made in building the banking union, the EESC emphasises that the adoption and prompt approval of further action is needed. The fragmentation of capital markets in the Member States does not create sufficient scope for easier access for businesses to financial resources in the single capital market within the framework of the Capital Markets Union. Therefore, further progress in the completion of the Capital Markets Union is needed.

1.6 The EESC is closely following the deepening process of divergence between Member States, but also within the EU and euro area countries. It therefore supports the adoption of a combination of economic policies that make effective use of available domestic resources, both public and private, including the financial resources created within the framework of the NextGenerationEU

1 https://ec.europa.eu/commission/presscorner/detail/en/ip_21_5321.

2 https://www.ft.com/content/f3377da4-2ec6-4edb-b9b8-6a5af22bc2a2.

3 https://www.ecb.europa.eu/stats/policy_and_exchange_rates/target_balances/html/index.en.html.

and the Recovery and Resilience Facility. The effective and prudent implementation of these financial resources may lead to suspension and later to resumption of the convergence process.

1.7 The EESC is concerned about progressively deepening social instability. Since sufficient measures to combat the growth of inequality and poverty were not adopted and implemented following the global financial crisis, COVID-19 only further exacerbated these inequalities and the growth of poverty. Therefore, there is now an urgent need to develop and monitor appropriate indicators of inequality and poverty, even in the context of sustainable development goals.

1.8 The greatest existential threat for further life on the planet is the unprecedented negative climatic changes. The EESC calls for urgent measures to be taken and implemented to fight climate change, including the development of basic indicators to measure the socio-economic consequences of the crisis. Moreover, the EESC stresses that the negative impacts of the climate crisis will have a big impact on macroeconomic stability (growth in expenditure, price rises due to drought), but also on financial stability, particularly the insurance business[4], and social stability.

1.9 The evolutionary technological process is leading to the rapid introduction of digitisation and financial innovations. The EESC welcomes the ECB and Commission's decision to open discussions on the introduction of the digital euro. The introduction of the digital euro can bring potential benefits to euro area citizens and businesses, considering all the advantages.

1.10 Partly thanks to all the measures taken and implemented following the global financial crisis, the banking sector in the euro area countries appears to be relatively stable at least for now. The EESC points out potential insolvency problems, especially for small and medium-sized enterprises. Adverse developments in the insolvency of small and medium-sized enterprises could be disruptive to stability in the financial sector, mainly the banking industry. In line with this, the EESC calls for more consideration to be given to introducing the necessary measures to safeguard the stability of the financial system.

1.11 The EESC draws attention to a prudent approach in combating the still unresolved and ongoing COVID-19 crisis, but above all stresses the need to prepare for potential other viral crises. Policies aimed at building a strong immune system among the population can create the conditions for reducing healthcare expenditure caused by the spread of disease and, simultaneously, create better conditions for the health of all workers involved in creating value in society.

2. Background

2.1 In comparison with the last EESC opinion on economic policy in the euro area, current developments are characterised by high inflation, which is mainly driven by energy commodity prices, notably oil and natural gas.

2.2 Wholesale prices of natural gas and electricity have increased by an average of 429% and 230%, respectively, since 2019[5]. The growth in retail prices is not significant as yet – it represents 14%

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4 https://www.imf.org/en/News/Seminars/Conferences/2021/11/17/9th-statistical-forum-measuring-climate-change.

5 COM/2021/660 final.

(or 7%). Recently published short-term forecasts suggest that wholesale prices may continue to rise until the last quarter of 2022.

2.3 Inflation has increased strongly since the beginning of the year, following years of low inflation, and repeatedly exceeding forecasts. In November it reached 4.9%[6]. The main factor behind this rapid price growth is the surge in commodity prices – in particular oil and gas – from their historic lows back to, or above, pre-pandemic levels. In addition, disruptions to production and logistics persist in many parts of the world, which are pushing up prices of goods, in particular, in times of a surge in aggregate demand. Inflation is expected to decline as of early 2022.

2.4 Despite encouraging expectations for a recovery in the real economy in the first half of 2021, it now seems that the recovery process is more complicated due to the rapid spread of the third wave of the epidemic. The battle against COVID-19 is far from over and its impact on the real economy might last for several more years. The persistent problems associated with energy input prices and the unavailability of some types of commodities required in the production cycle represent major constraints both in the use of production capacities and in the investments and consumption under consideration.

2.5 The use of financial instruments in the framework of the NextGenerationEU could have a positive impact on the performance of the real economy and overcoming problems associated with COVID-19. In this context, the ongoing allocation of funds by means of the REACT-EU instrument, as well as the Recovery and Resilience Facility focused on the recovery, resilience and sustainability of individual economies, are perceived as very timely.

2.6 Historically, the biggest drop in economic growth since the start of European integration was recorded in 2020. This year, real economic growth in the EU Member States is expected to reach approx. 5%, while in 2022 real economic growth of 4.3% is expected. In 2023, real economic growth of 2.5% in euro area Member States can be expected. The main driver of economic growth in 2021 was household consumption, which reached 3.5% in the euro area in the second quarter.

2.7 It is necessary to point out the existing risks when assessing the development of economic growth. These are linked to a decline in trade in goods, but also, on the demand side, to the consequences of the impact on the production process and the increase in costs in the euro area manufacturing industry. In addition, the disruption of global value chains and the relatively high dependence of manufacturing industries on imports of raw materials and microprocessors in the euro area are other factors.

2.8 COVID-19 has taken a heavy toll on public finances. After the epidemic, euro area Member States will face major challenges in consolidating public finances. In 2020, a deficit of 7.2% GDP was recorded, while no country achieved a fiscal surplus. The deficit is expected to decline slightly to 7.1% GDP in 2021. A more significant fall can be expected in 2022, and continue in 2023, with the deficit projected to decrease to around 2.5%, which is a substantially higher deficit than that recorded before the COVID-19 outbreak (0.6% of GDP in 2019).

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6 https://ec.europa.eu/eurostat/documents/2995521/11563351/2-29102021-AP-EN.pdf/70e9c60b-8bca-12cc-859e-41af561b5a08#:~:text=Euro%20area%20annual%20inflation%20is,office%20of%20the%20European%20Union.

2.9 Labour market developments continue to be accompanied by structural problems in individual euro area countries. Despite this, the unemployment rate is relatively low, due mainly to the wide implementation of job retention schemes. The current labour market in most euro area economies faces a relative shortage of skilled labour. Despite the lower than expected unemployment rate due to COVID-19, there are a whole range of unresolved problems in the labour market related to necessary requalification, especially in the context of the transformation process under way.

2.10 The EU and euro area as a whole have registered a current-account surplus, but with readings varying markedly across countries. Some countries continue to record large current-account surpluses. On the other hand, countries with important cross-border tourism sectors have generally seen a marked increase in current-account deficits or a reduction in their modest surpluses. This is expected to correct gradually with the recovery in travel. When assessing the level of external imbalances within euro area Member States, it is necessary to consider the unprecedented increase in imbalances in the TARGET2 payment system, which, this year, has reached the highest level since its inception[7].

2.11 At present, due to the rapid and uncontrollable spread of the virus, additional corrections to the presented relatively promising development in economic growth can be expected. The current process of introducing restrictive measures as a result of the epidemic could significantly negatively impact real economic growth and the already unsustainable level of public debt in some Member States, including deepening inequality and rising poverty.

3. General comments

3.1 The EESC is following the current economic and social developments associated with the high degree of uncertainty with concern. This degree of uncertainty is associated with two negative factors: the unprecedented accumulation of public debt and the rise in inflation. The growth in consumer prices is leading to a deterioration of the social situation of households and negatively affecting living standards. As debt ratios were already high in some euro area Member States before the crisis, the rapid deterioration of the fiscal position means it will be key for those euro area Member States to adopt and implement fiscal consolidation measures in the medium term, once economic conditions allow.

3.2 The EESC welcomes the gradual recovery of the real economy. In this context, it supports the intentions to increase both public and private investment. It also recognises that, in the context of creating a comprehensive NextGenerationEU framework, there is scope to use these resources effectively to support real qualitative economic growth.

3.3 The EESC believes that the sharp rise in inflation will not lead to a restrictive ECB monetary policy, as the drivers of inflation appear to be temporary and originate mainly on the supply side. Therefore, the EESC supports the focus of economic policy on strengthening the resilience, flexibility, autonomy and functionality of strategic structures to be able to face repeated symmetric shocks in the future.

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7 https://sdw.ecb.europa.eu/reports.do?node=1000004859.

3.4 The EESC supports fundamental historic systemic changes accompanying the transformation to a green, digital and socially just economy. Despite the complexity and unpredictability of further developments regarding COVID-19, the EESC supports the European Green Deal[8] and considers it a historic opportunity for sustainable economic and social development on the old continent. In this context, the EESC supports the acceptance and consideration of all important factors focused on preserving life on the planet for the present and future generations.

3.5 The EESC calls for the urgent adoption and implementation of measures aimed at the progressive reduction of inequalities and poverty in the eurozone member countries[9]. In this context, it sees potential for the use of all practical revenue and expenditure instruments, including reducing counter-productive expenditure, fighting corruption, the black economy and non-transparent operations, including a long-delayed solution to the tax haven issue.

3.6 In view of the complexity and unpredictability of current developments, the EESC agrees that individual Member States should adopt fiscal policies taking into account the state of the recovery, fiscal sustainability and the need to reduce economic, social and territorial divergences.

3.7 The EESC is aware that fiscal policy should be sufficiently active and flexible to face potential waves of virus spread and mutation. In this context, it supports additional and necessary expenditure on healthcare until an overall gradual return to normal.

3.8 In addressing the current complex economic and social developments, the EESC recommends implementing a consistent mix of macroeconomic policy. In view of the overall recovery strategy, expansionary monetary policy combined with consistent expansionary fiscal policy can play a fundamental role. The adoption and implementation of the mix of macroeconomic policy should also be coordinated with social partners.

3.9 The evolutionary technological process is linked to innovations in the financial sector. The EESC welcomes the first steps by the ECB and Commission in the creation of the digital euro[10]. So far no decision on the introduction of a digital euro and its potential design features have been taken. With the process of introducing the digital euro, it could be possible to experience faster, more effective, lower-cost payment and clearance operations for both households and businesses, but implications for, e.g. clearance operations, should be taken into consideration. In this context, a contribution to the strategy of strengthening the international status of the euro could also be expected.

3.10 The EESC supports and welcomes the start of public consultations aimed at management (governance) of public finances. In this context, the orientation is towards: (a) the timing of the fiscal consolidation process; (b) the definition of rules for long-term measures linked to overcoming the consequences of the epidemic, but in particular the investments associated with the green and digital economy; (c) and simplification of fiscal rules. The EESC points to its

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8 https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en.

9 https://voxeu.org/article/income-inequality-eu-trends-and-policy-implications.

10 https://www.ecb.europa.eu/paym/digital_euro/html/index.en.html.

various opinions on economic governance and on fiscal rules in particular. In our latest opinion[11], in these regards, the EESC calls for the introduction of a golden rule for public investments in combination with an expenditure rule and points out that both national parliaments and the European Parliament need to be given a prominent role in the future EU economic governance framework. Moreover, the EESC calls for a greater involvement of civil society in the European Semester at both national and EU level and also for guidelines for a transition period, during which time the excessive deficit procedure should not be triggered.

4. Specific comments

4.1 The EESC welcomes the European Commission's approach to the current adverse energy price developments, including the proposed short-term and medium-term measures. In view of the unpredictability of energy prices, the EESC calls for substantive and systemic measures to be taken to mitigate systemic unforeseen shocks from the external environment, thus creating the conditions for a sustainable, stable, resilient and socially just life for all euro area residents.

4.2 The EESC greatly appreciates the initiation of public debate on the future setting of fiscal rules presented by the European Commission. This long-awaited initiative could lead to the creation of simple and easy-to-monitor rules that will correspond to the current situation at the start of the third decade of this century. In addition, the EESC points out that the process of gradual completion of fiscal union is also linked to the creation of the whole structure of the public finance management system, including the creation of the position of "Minister of Finance".

4.3 The EESC is following developments in the area of climate change with great concern. In this context, the EESC welcomes the adoption of the Fit for 55 package, including the EU Climate Target Plan. The Committee considers it crucial to adopt and implement measures to set generally adopted and accepted standards in the fight against climate crisis. As options are becoming limited and time is running out in the fight against climate change, the EESC urges the adoption of all urgent measures to combat climate change. Moreover, in the context of climate change, it will be necessary to analyse the impact on macroeconomic developments and their consequences, i.e. monetary and fiscal policy, including financial and social stability.

4.4 The EESC stresses the need to complete financial union. Despite the gradual creation of the banking union’s architecture[12], every effort must be made to complete it[13]. In addition, the EESC points to the need for effective functioning of the capital market within the EU states. In this context, efforts should be directed towards the further deepening of the Capital Markets Union[14][15].

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11 EESC opinion on Reshaping the EU fiscal framework for a sustainable recovery and a just transition (own-initiative opinion), OJ C 105, 4.3.2022, p. 11.

12 https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp210318_1~e2126b2dec.en.html.

13 https://www.europarl.europa.eu/doceo/document/TA-9-2021-0415_EN.html.

14 https://ec.europa.eu/commission/presscorner/detail/en/ip_21_6251.

15 https://ec.europa.eu/commission/presscorner/detail/en/IP_21_6307.

4.5 The EESC supports the continuation of policies aimed at reducing aggressive tax planning, combating tax avoidance, and effective and fair taxation, which can lead to a reduction in inequalities in individual countries and poverty.

4.6 On the journey towards a successful historic transformation, the EESC considers it of the utmost importance to systematically monitor and regularly evaluate the effectiveness of all measures adopted and implemented under individual national economic policies, and thus create favourable conditions for flexible responses to both changing internal shocks and unforeseen systemic shocks from the external environment.

Brussels, 19 January 2022

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