BRIEFING ON THE EU BUDGET DEAL

1. THE DEAL

On 21st July, after five days of intense discussions, **EU leaders agreed on the Next Generation Europe recovery package and the next EU budget**, the Multiannual Financial Framework (MFF), respectively representing €750 billion and €1.074 trillion.

EU leaders across the bloc have expressed their satisfaction with the deal. President Macron hailed the final package as ***"a historic change of our Europe and eurozone"***. Chancellor Merkel similarly said she was *"very happy"* with the final proposal, adding that *"**Europe has shown that it is able to break new ground** in an exceptional situation".* Dutch PM Mark Rutte was less enthusiastic and declined to describe the deal as "historic" but pointed to the **concessions he had secured on the governance model** for the recovery fund.

The approval of the plan marked a **triumph for Germany and France**, which had proposed a €500 billion debt-for-grants program earlier in May, adopted by the European Commission which added to it a €250 billion loan program. While EU countries have borrowed jointly on financial markets at a small scale in the past, including in response to the eurozone debt crisis in 2010, the new plan marks a **giant leap towards potential fiscal integration** by establishing a precedent that can be drawn on again in future.

The **final agreement settled on grants worth €390 billion** – less than the original Franco-German proposal, but nevertheless a significant package that has been **warmly welcomed by southern Member States** including Greece, Italy and Spain. The **'Frugal Four'** (Austria, Denmark, Sweden and the Netherlands) have secured concessions including an "emergency brake" on payments if beneficiaries fail to fulfil their reform commitments. The frugal nations also secured **increases in the rebates** used to cap their overall contributions to the EU budget, at the regret of the French President who wanted to remove these from the new MFF.

The **Visegrad Group**, composed of Czech Republic, Hungary, Poland and Slovakia, succeeded in toning down proposals to link payments to respect of the rule of law and democratic norms. The final proposals include a **mechanism which could see sanctions imposed by a qualified majority in the Council**, but its scope is limited to the protection of the EU's financial interests.

Following the leaders' agreement, the **European Parliament** acknowledged the recovery fund as a *"historic move"* but **deplored the significant reduction of grants and cuts to flagship EU programmes** on climate protection, digital transition, health or research, in a resolution adopted on 23rd July. While members of Parliament (MEPs) will not vote on the recovery instrument, they have to give their consent to the budget, directly tied with the recovery plan. MEPs already declared to be *"prepared to withhold their consent"* on the MFF until a satisfactory agreement is reached in the upcoming negotiations between Parliament and the Council, preferably by the end of October at the latest.

2. WHAT THIS MEANS FOR OUR CLIENTS

The agreement will allow EU Member States to invest and promote areas such as health, research and innovation, digital and transport among others. Below the areas that will be significantly promoted:

- **Climate**

30% of the full budget package will be earmarked for climate objectives. The creation of the Just Transition Fund, to support EU regions heavily relying on fossil fuels to successfully **transition to cleaner energies,** was also agreed. It will receive €17.5 billion.

- **Health**

€1.7 billion will be given to the new health programme. Potential plans to add about €8 billion to health were terminated during the negotiations, leaving the health budget to a rather low amount compared to other EU initiatives. Worth noting that the budget will be complemented by the €3 billion **RescEU**.

- **Research and innovation**

Horizon Europe will get €80.9 billion in total, with €75.9 billion coming from the MFF and €5 billion from the recovery fund. Research & Innovation is one of the biggest losers of the deal, where budgetary efforts were shifted to priorities different from traditional EU programs.

- **Digital**

€6.8 billion for the Digital Europe program will be dedicated to funding high-performance computing, artificial intelligence, and cybersecurity. Compared to the €183 million dedicated to digital under the current MFF, this amount reflects clearly that **digital is a priority** for the EU, seeking to foster its strategic autonomy in this area.

- **Transport**

Transport infrastructure will receive €11.4 billion, topped by a dedicated €10 billion from regional funding, including: €1.4 billion for railways; €5.2 billion for energy infrastructure; €1.8 billion for digital infrastructure and €13.2 billion for the bloc's space program.

- **Agriculture**

The **Common Agricultural Policy budget is set at €336.4 billion**, comprising **€258.6 billion for the first pillar** (direct payments to farmers for the most part) and **€77.9 billion for rural development,** focusing on green and social schemes. The **new deal also includes €7.5 billion in rural development grants** from the EU recovery plan that will support farmers in meeting the EU's new climate ambitions.

- **Cohesion**

Cohesion policy, which seeks to reduce disparities across the EU, **will receive €330 billion**, amplified by **an additional €47.5 billion under the new ReactEU program**, part of the recovery fund.

- **Defence**

The European Defence Fund and the Military Mobility Initiative are respectively expected to get **€8 billion and €1.5 billion**. While these numbers are significantly lower than the Commission's proposal (€13 billion and €6.5 billion), they still signal the EU's willingness to improve its military capabilities and strategic autonomy.

3. WHAT HAPPENS NEXT

The political agreement reached at the level of the European Council on 21 July **does not conclude the process for the adoption of the EU's long-term budget** for the years 2021 to 2027. It is only the starting point for negotiations between the co-decision makers, the Parliament and Council.

The European Parliament has a **binding say over the seven-year budget negotiated by EU leaders**, which means MEPs still have to vote and give their greenlight through an absolute majority. It is unlikely that MEPs will veto the agreed budget, as most MEPs will not want to delay the response to the COVID-19 pandemic but they have made it clear that they want their views to be taken into account and the Council may have to make some concessions to meet Parliament's requirements.

In particular, MEPs are seeking a strong rule-of-law mechanism, higher long-term investment into **key research and development programmes** such as Horizon Europe and Digital Europe as well as for the Parliament to be involved in the governance of reconstruction funds.

With discussions between the Parliament and the Council to last well into autumn, the adoption of the revised MFF, with the European Parliament's consent may be expected by the end of the year, possibly **December 2020**.

4. CONCRETELY – HOW THE DEAL WOULD BE IMPLEMENTED

Bearing in mind the health impact of COVID-19, EU leaders agreed that the emphasis should be on mitigating socio-economic damage and that **an unprecedented effort and innovative approach**, fostering convergence, resilience and transformation in the EU was required.

To do so, the spending package comprise two components:

A. NEXT GENERATION EU RECOVERY INSTRUMENT

In the words of the Council, **the instrument is significant** (with far-reaching effects), **focused** (targeting regions and sectors most hit by the crisis) and **limited in time** (MFF remaining the basic frame for the EU's budgetary planning and implementation).

To raise funds, the **Commission will borrow on the capital markets on behalf of the EU**, up to the amount of €750 billion at 2018 prices. All new net borrowing activity will stop at the latest at the end of 2026. The EU will use the funds borrowed on the capital markets for the sole purpose of addressing the consequences of the COVID-19 crisis.

To access funds, Member States will have to **submit national recovery and resilience plans**, where effective contribution to the green and digital transition will be a prerequisite. These plans will be **assessed by the European Commission and then approved by the Council**, by qualified majority on a Commission proposal.

70% of the Recovery and Resilience Facility funds will be committed in 2021-2022, based on criteria including unemployment level in 2015-2019. The remaining 30% will be allocated by the end of 2023, based on the loss of GDP in 2020-2021.

Breakdown of the Recovery instrument - €750 billion to be distributed as follows:

- ***Recovery and Resilience Facility (RRF)***, the core of the package representing €672.5 billion, divided in:
  - Loans €360 billion;
  - Grants €312.5 billion;
- ***ReactEU,*** €47.5 billion - extension of the EU crisis response and crisis repair measures;
- ***Horizon Europe***, €5 billion – the Research & Innovation framework programme of the EU;

- ***InvestEU***, €5.6 billion – investment plan in 4 areas[1], where the EU can attract private investment;
- ***Rural Development***, €7.5 billion – improving the competitiveness of the agriculture sector and promoting diversification of economic activity in rural areas;
- ***Just Transition Fund***, €10 billion – supporting most affected EU regions to successfully transition to a low carbon economy;
- ***RescEU***, €1.9 billion - preparing the Union to respond to future crises.

B. NEXT MULTIANNUAL FINANCIAL FRAMEWORK (MFF)

This current MFF remains lower than the one covering the 2014-2020 period and the Commission's original proposal in 2018. Ursula von der Leyen, **European Commission's President, expressed her regret** that in order to reach a compromise on the MFF, far-reaching adjustments had been needed, including the removal of the solvency instrument – to help recapitalise struggling companies - and cuts to what was proposed for health, migration, external action and InvestEU.

The more **frugal nations succeeded in securing increased rebates** in exchange for relaxing their opposition to recovery grants, which will lead Sweden, Denmark, Germany, the Netherlands and Austria to receive substantial discounts to their EU budget contributions.

Breakdown of the MFF - €1,074.3 billion to be distributed as follows:

- *Research & Innovation* – Horizon Europe budget agreed is €75.9 billion;
- *Neighbourhood and the world* – €98 billion;
- *Migration* – €22.6 billion;
- *Just Transition Fund* – €7.5 billion to be allocated, less than the €10 billion proposed by the Commission (which would be supplemented by €30 billion from the recovery fund);
- *Security & Defence* – €13 billion
- *New streams for own resources* – including non-recycled plastic waste, carbon border adjustment mechanism and on a digital levy, revised ETS scheme (possibly extended to aviation and maritime);
- *New Brexit impact fund*, with €5 billion proposed for a aBrexit Adjustment Reserve.

For further information on how to access EU Funds, please contact:

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[1] Sustainable growth; Research, Innovation and Digitalization; Small & medium businesses; Social investment & skills.