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Bringing Europe’s Economic Governance Down to Earth

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The European Green Deal commits the EU to the pursuit of green growth. The European treaties mandate national governments to make sure their GDP is in line with their public debt. Is the European Union hooked on growth? The *Green European Journal* asked European Commissioner for Economy Paolo Gentiloni and Co-President of the Greens/EFA Group in the European Parliament Philippe Lamberts if Europe can fight inequality and protect the planet without growth.

Jamie Kendrick: Should the European Union accept that economic growth is over?

Paolo Gentiloni: I sincerely hope not. Two distinct but connected conversations are overlapping here. First, there is a conversation on “beyond growth”, meaning quality, sustainable growth beyond GDP. It is a reflection on how to enlarge our assessment of growth away from traditional parameters to include other qualitative measures such as the Sustainable Development Goals. This sustainable growth is exactly what is needed. Then there is a parallel conversation on whether we need growth.

The easiest part is, yes, we definitely need growth. Beyond growth, there is recession, stagnation, and austerity. The discussion on fiscal policies, innovation and green transformation are all also about growth. I am okay with the message we can’t rely only on the traditional definition of growth as measured by GDP. But arguing that the era of growth is behind us would be very dangerous. In a low-growth – let alone a no-growth – environment, tackling inequalities and the green transition becomes very, very challenging.

OK, but pushing for more growth means pushing harder against environmental limits and the limits of people too. Isn’t there a contradiction between prosperity and growth?

Philippe Lamberts: The question is whether something called sustainable growth can exist. Growth is the size of the economy measured in monetary terms, right? So growth means a bigger economy. We can only have that if we absolutely decouple the size of the economy from its material and climate impact on the planet. The science so far hasn’t found that to be possible.

The question is whether something called sustainable growth can exist. – Philippe Lamberts

Energy is ultimately at the heart of the economy, so growing your economy means that you’ll always need more and more energy. In the second half of 2022, the European Union cut its energy consumption by 20 per cent without shrinking its economy by 20 per cent. That’s an achievement, it’s relative decoupling. But if we want to absolutely decouple the economy from energy and materials and lower our emissions, I don’t know whether that’s possible. At some point, you’ll hit a limit, so I question the feasibility of endless growth.

If we accept that there are limits to economic growth on a finite planet, then the distribution question becomes much more important. When the pie is growing, everyone can have a slice. In reality, the person on street doesn't get as much as the CEO and the Davos people but everyone gets some. That is the politically difficult point where we are today.

Paolo Gentiloni: It's our job to find a positive answer to that question and show that sustainable growth is possible. Otherwise, we are in a very difficult situation. We need to do everything we can across policies to reduce our impacts: energy savings, biodiversity protections, product design, right to repair and so on. But we still need growth.

Looking at history, addressing inequality has been achieved through growth. Who knows about the future, but the low growth in the European Union over the last 10-15 years of has only made inequality worse.

Philippe Lamberts: That was a political decision. People at the lower end of the income distribution have borne the brunt of the effort since the global financial crisis and the eurozone crisis. It didn't have to be that way. Bank shareholders and bondholders should have shouldered the losses… But we were worried about growth and the economy, and ultimately, they got richer than ever.

Paolo Gentiloni: I'm not denying that theory, not at all. But look at the history of inequality. Take Thomas Piketty's *A Brief History of Equality*: the trend of inequality was reduced substantially in periods of high growth. Could we in theory do it differently? Possibly. But human nature is what it is and it is a lot easier to work for sustainable growth than to try to reach increased prosperity and equality with a declining economy.

A lot of people are considering different relationships with work or different ways of moving around our cities.
– Paolo Gentiloni

The European Union has committed to green growth to solve the climate problem. The United States and China are doing the same. Doesn't Europe's green transition need a new social model rather than entering a new race for competitiveness, with all the pressure it places on people and planet?

Paolo Gentiloni: I see the risk. We say, okay, we go for green, for net-zero industry, but then we rush to compete over a horizon based on the same model, same systems, and exploiting the same old mechanisms. But if we want to look at things positively, I also see a cultural and behavioural shift.

The COVID lockdowns changed our relationship with our jobs and how we work. I've never seen such an enormous shift in the behaviour of consumers, households and families. This is bringing the green transition down to earth. A lot of people are considering different relationships with work or different ways of moving around our cities. The European conversation on working time has re-opened.

If we push in the right direction, keeping competitiveness together with sustainability, the circular economy and redistribution, we can make progress. It is not easy in times of high inflation. The redistribution message is important because right now we are facing a loss of purchasing power for many people and high profits in some sectors. That was the logic of the EU-level solidarity contribution energy firms' excess profits.

Philippe Lamberts: I wouldn't look at competitiveness as a bad word. Competitiveness is essentially a comparison of two ratios: the ratio between the value you can produce and the cost and the same ratio for somebody else. We tend to limit competitiveness to wages, but actually that is cost competitiveness. Europe cannot be a low-cost continent. We don't want to be a low-cost continent but a high-value continent.

The green transition can be a competitiveness play for Europe because we're targeting the high-value space. It is the only way to guarantee high living standards. We should be trying to create the highest-value goods with low resource and energy costs and high wages and working conditions.

In many European countries, we're seeing high tensions in the labour market and the bargaining power should lie in favour of the workers to the detriment of the owners of capital. They are competing to keep the best people. If the basic conditions of the labour market already ensure that the distribution of added value is fairer, you already solve part of the problem and you do not need distribution policies to do so much of the work.

For a long time, there was an idea that governments needed to keep public debt levels lowto maintain high economic growth. Now governments are taking on debt to fight crises, invest in the green transition, reduce inequalities and rebuild their militaries. What do all these public commitments mean for the EU's macroeconomic governance?

Paolo Gentiloni: The debt levels of European countries have increased substantially in recent years. The EU treaties set a benchmark of a 60 per cent debt-to-GDP ratio for EU governments. It was not something that was proposed by a Nobel Prize winner. It was just the average debt of the 12 countries that signed the Maastricht Treaty. Now the average debt of those 12 countries is 83 per cent.

> *We will have to face higher debts and we need to avoid the same mistake made after the financial crisis when we cut public investment year after year. – Paolo Gentiloni*

This continuous increase in debt is not good. Some countries have excessive debt levels that could be a problem for stability. But at the same time, we have in the past interpreted the rules of the Stability and Growth Pact in a way that placed all the emphasis on stability and almost nothing on growth. It was a mistake then and it would be a big mistake now, seeing the mountain of investment that we have ahead of us, for the green transition and competitiveness. Of course, these challenges require mainly private investments but you also need a role for government. No one denies that, not in the US, not in China, and not in Europe.

The mindset is changing in Brussels. Is it enough to change the mindset, with no money? In 2020, Europe made the big decision to create an unprecedented programme to fund the recovery from the pandemic with 800 billion euros. If we are serious about the green transition, we also need a common commitment. The green transition will be an enormous effort and there will be a period when we face many costs without new revenues to pay them off. That is true from the car industry to the renovation of buildings. We can't address these challenges only by loosening state aid rules and crowding in private investments, because otherwise, we risk seeing too much divergence between EU countries.

So, yes, we will have to face higher debts and we need to avoid the same mistake made after the financial crisis when we cut public investment year after year.

Philippe Lamberts: Public debt needs to be weighed against the net capital position of governments. If the debt corresponds to better energy infrastructures, higher education levels of populations, the ability to create useful goods and services, resilience against environmental disasters – basically the firm stuff – it's fine. If you fund ordinary expenditures with debt, then you have a problem.

We should never forget that there are two ways to fund public expenditure : debt and tax. I know the T-word doesn't please everyone, but higher and fairer taxes are a democratic choice to be made. If we look at the fiscal rules of the European Union, we need an intelligent approach to the sustainability of public finances. We owe it to taxpayers that we spend money most efficiently and effectively. We do need arbitration, pressure and democratic scrutiny. Otherwise, the risk is that you build white elephants like the 12 or so useless regional airports that were built during Spain's construction boom.

The Greens/EFA group in the European Parliament has studied the impact of the timing of climate action on the sustainability of public finances. The outcome was that the sooner you invest, the better your public debt sustainability will be. If you are going to spend 100 billion euros of public money on the climate, better do it now rather than face a bigger bill later.

> *Climate change and its impacts cannot be excluded from our economic models. – Philippe Lamberts*

The economy works in cycles and right now we have to catch up in terms of private and public investment. When you accelerate investment, we can expect higher debt. But investments like high-quality water systems and railway networks are long-lasting goods that will be paid off throughout our lives and those of our children

One of the proposals made by postgrowth and beyond GDP economists is that a whole range of wellbeing indicators should be at the centre of our economic decision-making. Since we are reforming the EU's fiscal rules, couldn't we look as closely at, for example, air pollution or the quality of public housing as much as the two fairly reductive measures of debt and GDP?

Paolo Gentiloni: There are several moves in this direction, but there is also the stubborn fact that money is money, debt to GDP is debt to GDP, and the rest is a Christmas tree.

For the past 12 years, as part of its economic surveillance, the EU has published an Annual Growth Survey. But since 2020, this document has been renamed the Annual *Sustainable* Growth Survey, to factor in more fully the social and employment dimension and, more recently, the Sustainable Development Goals. I fully agree that our debt sustainability analysis also has to factor in environmental issues. Central banks and businesses are doing this too. Entering this new mindset is difficult and it is a process. Here, the contribution of the European Parliament to our proposals can be very important, because this necessity is to a certain extent more clearly perceived there than among the Member States.

Philippe Lamberts: It is almost a theological debate because some people consider the benchmarks of 3 per cent deficit spending and 60 per cent debt levels as holy. Many economic models are based on assumptions that are completely ignorant of the realities of this world, starting first with energy.

Fossil fuels concentrated energy built up over millions of years. They are a geological miracle that created the illusion of cheap and abundant energy. Producing energy by wind by solar is much less efficient than burning oil that just springs from the ground. We have to relearn the harsh reality of how energy behaves and factor it into our models.

The same is true for the cost of non-action. Wallonia in Belgium is a region whose public finances are really not in top shape. Suddenly in 2021, Wallonia was hit by floods that cost 5 billion euros, much of which will be borne by the public sector. So climate change and its impacts cannot be excluded from our economic models. If you look at the European economy as a whole, we need new models that can pre-empt and prevent those kinds of shocks.

The Beyond Growth conference is an exercise of collective thought. What we are trying to do is make progress on the thinking around the systemic implications and try to integrate that new complexity into how we think about Europe's economy and European societies.

This conversation is part of an interview series led by the Green European Journal and EU Observer as media partners of the European Parliament's Beyond Growth 2023 Conference.

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