The battle of the budget

Why the epic fight over EU spending is a wasted opportunity

Hotel rooms have been booked for the extra-long weekend. Spreadsheets are being readied. Bogus arguments and blackmail strategies are being honed. As European leaders prepare for their seven-yearly epic battle over the EU's budget, they will now be on their worst behaviour.

Herman Van Rompuy, the president of the European Council, who will chair a special budget summit on November 22nd and 23rd, has told leaders to be prepared to stay in Brussels for several nights. Veterans of past budgets say reaching agreement at the first attempt would be remarkable. This time the economic crisis in the euro zone raises the stakes. A stalemate would only feed the uncertainty that already surrounds the European project.

The bitterness that the EU budget generates is disproportionate to its importance. It accounts for just 1% of the union's GDP, or about 2% of government spending; the disputed amount is a fraction of this. Still, over the seven years of the "multi-annual financial framework", the pot of money at stake is about €1 trillion ($1.3 trillion).

For poorer countries in central and eastern Europe, net transfers from the EU are a big boost, for some approaching 5% of national GDP. For southern countries deep in recession, such as Greece and Spain, they are a lifeline. For Italy, which has become the biggest net contributor and fears its position will worsen, paying in to the EU makes getting its finances in order even harder.

Countries are coalescing around loose (yet often divided) groups. There are the "friends of cohesion": the net recipients of regional spending, such as Poland, Hungary and the Baltic states. And there are the "friends of better spending": the net contributors, such as Germany, France, Britain and several northern European states. Less organised are the supporters of farm subsidies under the common agricultural policy who straddle both camps, including France, Spain, Italy, Ireland and Romania.

At the furthest end of the tug-of-war stands the European Parliament, the friend of all EU spending. It wants the union to have more "own resources", meaning revenues independent of national treasuries, and is covetous of the financial-transactions tax that 11 countries plan to introduce. If it does not get new own resources, says the parliament, it will veto the budget.

Tugging hard alongside is the European Commission. It has revised its draft budget to €1,033 billion, after adding money for Croatia, which joins next year. It has resorted to the old fiscal trick of keeping some items off-budget. When these are added, its proposal comes to €1,091 billion—a 6% increase in real terms.

At the other end of the rope stands Britain, with few real friends these days. It wants spending frozen at 2011 levels. And it wants the budget set using the actual sums paid out, which are lower than the "commitments" in today's budget (that makes for some fuzziness in the British bid: it seeks to reduce the commission's request by between €100 billion and €200 billion, depending on who does the sums). The British say that, for a country sharply cutting expenditure to curb its budget deficit, a real-terms freeze for the EU is generous. David Cameron, Britain's prime minister, says he too is ready to cast his veto.

The British are also at the centre of another fight, about their budget rebate. Over the years other states have secured reductions; now the Danes want one too. The commission proposes to simplify the complex system of abatements. But regardless of the merit of reform, no Tory prime minister could touch the rebate won in 1984 by Margaret Thatcher. Many now ask whether Mr Cameron really wants a compromise, or would prefer—for domestic reasons—to cast his veto, as he did last December. The cost of stalemate, apart from isolation, would be to roll over the 2013 budget plus inflation (meaning that the budget would be bigger than Britain seeks) and mess up planning for regional funds.

All will be watching mighty Germany. It says the budget should be capped at 1% of the EU's gross national income (reducing the commission's plan by about €130 billion), but is being pulled in many a direction. As an advocate of austerity, it sympathises with the British. But as a big recipient of farm subsidies, and as the other half of the Franco-German partnership, it may collude with France to preserve agricultural spending. And it will want to keep supporting the EU's ex-communist members around and beyond its eastern border.

Looming over the fight are two broader questions: the future of the euro zone and the future of Britain in the EU. The euro zone is talking about "fiscal capacity", jargon for creating a separate budget to stabilise the currency. At the last summit in October, Mr Cameron argued long and hard over the degree to which the two budgets were "unrelated". Some fear he wants to use the "fiscal capacity" to demand cuts in the EU budget. More likely, he wants to set a marker for the looming treaty renegotiation, in which Britain may seek to loosen its ties.

Dreadful deadlock

So after all the hue and cry, the most likely outcome is a budget that offers little change. The partisans of farm subsidies, regional funds and the rebates will fight each other to a standstill. The most likely casualties are sensible growth-promoting forms of spending, such as cross-border infrastructure and research, that have no entrenched lobbies.

If the EU were starting anew, it would not come up with today's budget. It would not spend 40% of its cash on agriculture. It would not need all sorts of rebates. And it would not have a budget of absurd rigidity, in which even unspent money must remain in "national envelopes". Even if a deal is reached next month, the summit will be a wasted opportunity. If this crisis is not the time for radical reform, when is?

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