Reviving Investment in Europe

Jyrki Katainen
Vice-President, Jobs, Growth, Investment and Competitiveness, European Commission

Chair: Quentin Peel
Mercator Senior Fellow, Europe Programme, Chatham House

16 July 2015
Quentin Peel

Welcome, everybody. Welcome to Chatham House. I’m very pleased to welcome Jyrki Katainen from the European Commission now – although way back before, I think you were prime minister of Finland – anyway, vice-president for jobs, growth, investment and competitiveness, motherhood and apple pie. You’ve got the nicest portfolio of the lot. Yet when you came to the Commission, I suspect they all expected this man is going to be a real hard man, coming from Finland. Anyway, we won’t go into that.

I’m Quentin Peel. I’m a fellow attached to the Europe Programme here at Chatham House. The meeting that we have today is on the record, not under the Chatham House Rule. People can comment via Twitter using – I don’t know what this means – #CHEvents. I am registered on Twitter but I don’t use it. I bet you, being a Finn, use it all the time.

Jyrki Katainen has, as I said, a very nice-sounding portfolio in the Commission, although coming from Finland and having heard your successes in Finland, arguing in the whole eurozone negotiations, certainly you were expected to be a very tough member of the Commission. But you’re actually responsible for the real flagship programme of this Commission, and that’s something that I think we’re going to talk about today. I do want to try to throw this debate forward beyond the immediate, interminable crisis that we see in the eurozone and for the European Union more generally. Having said which, I’d also love to hear a bit in the course of our discussion about, if you like, the politics of being a senior member of the Commission and so on. So we might touch on that as well.

But let me start like this. It is absolutely inevitable that at this moment, all the headlines on Europe are dominated either by the Greek situation or, in this country, by the prospect of Britain trying to renegotiate its membership of the European Union. But what you’re responsible for – jobs, growth, investment and competitiveness – actually is fundamental to answering those two issues. I would love to hear from you how you see that, how you see that your portfolio could answer the debate that says ‘growth or austerity: it’s one or the other’. How do you see that?

Jyrki Katainen

Thank you very much. It’s very good that you connected growth and investment to the larger political context, because I see the situation exactly the same. Basically, all the negative feelings we have, and negative societal consequences we have, in Europe at the moment are coming from the fact that growth is too poor and the investment level is too low. If you look at the current investment level, it’s around 15 per cent lower than the long-term average. Even though it has a big negative impact on job creation and unemployment at the moment, if we don’t manage to turn it to a different direction it will create long-term negative effects to Europe, societal effects. We are lagging behind our competitors when it comes to competitiveness, when it comes to winning the deals.

Quentin Peel

But what’s actually caused that investment gap? Sitting in Germany, where I was for the previous four years, there’s a real investment problem in Germany. This, you know, [indiscernible] Kind, this wonderful child of economic performance, but they’ve got a real investment problem. But a very big part of that investment problem for the private sector is they make more money by investing in China than they ever will in Germany. So don’t you have to tackle that issue?
Yes, exactly. When talking about investment, I am mostly talking about private investment. If you're looking at the situation at the moment in Europe's economy, we are not lacking liquidity. Europe is full of liquidity but it does not go to the real economy. There are plenty of reasons. One reason is that many countries, for different reasons, are lacking competitiveness. In some countries, the labour market is too rigid. In some countries, the energy price is too high, taxation is not encouraging, etc. So that is the reason the Commission has studied and paid more attention to the structural side of our societies and not only to fiscal targets. Fiscal policy is, of course, very important but the reason for the current crisis is many times more coming from structural weaknesses than from the size of public debt, for instance.

So structural reforms are needed. This may sound a little bit like a mantra. We have been talking about the reforms for ages.

On structural reforms, what do you mean? Labour market?

Labour market in some countries.

So this is neoliberal reform – Euro neoliberal.

I am very pragmatic. I like the value of pragmatism, because if something doesn’t function, it's better to correct. If the labour market doesn’t function, it's better to correct. Also, some commodity markets don’t function, you have to correct it, liberalize it, regulate it, if that is the problem. Things like that. Pension reform. So there are different types of reforms which must be done because the world around us has changed.

For instance, taking the example of my country, Finland. It’s a schoolbook example of a country which must be reformed. The budgetary cuttings are not enough. Finland is a country where the population is aging faster than any other population in Europe. It's competing with Japan in speed of aging of the population. Second, the industry is in a transformation process. Pulp and paper companies are becoming biofuel companies or bioenergy companies. The telecomm sector is changing. So basically, because of the population, because of the changes in the market, you have to reform the country. It's not just an austerity or neoliberal policy. It's just the politics of common sense. The world around us has changed and our societies must change accordingly.

Sorry to ask a frivolous question for a moment. How come a country with the worst aging problem in Europe gets a prime minister when he was still in his thirties?
Jyrki Katainen

I have a theory that grandparents are usually voting for their grandchildren more than their own children.

Quentin Peel

As my daughter is about to produce a baby, I can sympathize with that. It’s very interesting though because Finland comes way up the tables for all the important things like very good quality of education, wonderful quality of transparency and actually pretty high up the tables of contentment. So we’ll come back to the parts of the European Union that are not content, but if you’re looking at the countries that seem to be doing very well, how do you shake them up?

Jyrki Katainen

Finland is doing quite well on many fronts but as I said, it’s going through a period in which you have to reform almost everything. Societal structures. I did it together with my six party colleagues, in which there were the extreme left party and everybody, and I was representing conservatives.

Quentin Peel

But you’re called the National Coalition.

Jyrki Katainen

Yes, that’s right. It’s widely accepted that we have to reform because of the biological reasons. There is less and less working-age population. Less and less people who are paying taxes from their salaries. That’s why the country must reduce a number of [indiscernible]. For instance, they must do something to healthcare. They must do something to the education system in order to get even better results, because it’s a precondition of productivity, etc. So if you stick to target, which is to be a welfare society which brings money from abroad, because a small country cannot finance its welfare model by relying on the internal market only or domestic consumption, you have to bring money from abroad, as the country is doing – 42 per cent of GDP comes from export. So it sets a standard. The global market sets a standard for the welfare society in [indiscernible]. There’s no other solution but to be competitive.

Quentin Peel

Yes. And it’s expensive. I must come back to your investment thing, the core of your portfolio. You’ve got now this European Union investment plan. We call it the FSI. I never know what these acronyms mean, what does it stand for?

Jyrki Katainen

European Fund for Strategic Investment.

Quentin Peel

Right, okay. But it isn’t just strategic investment, because it’s actually also small companies. Anyway, this is what you’re responsible for. It’s gone through the legal process amazingly quickly. You’ve set up a fund which is intended to mobilize €315 billion through the magic process of only putting up €21 billion of
public money initially. So you’re hoping to really generate a huge amount of private sector interest. How the hell are you going to do it?

**Jyrki Katainen**

Actually, it’s not a magic trick. EIB is doing it almost every day. Just three years ago, member states –

**Quentin Peel**

And the EIB is very much involved in this programme.

**Jyrki Katainen**

Yeah, the FSI is part of the EIB structure. Three years ago, member states capitalized EIB by €10 billion. Since then, EIB has financed projects worth €180 billion. So the delivered [indiscernible] has been times 18. Now we’ll use part of the European budget, €21 billion.

**Quentin Peel**

It’s €21 billion and €5 billion from EIB.

**Jyrki Katainen**

Actually, it’s €5 billion plus €16 billion. So this €21 billion is a guarantee scheme, which guarantees potential losses to EIB. So €21 billion allows EIB to finance projects worth €60 billion. So there is leverage times three. It’s a very conservative assumption but it basically means that if there €60 billion investments, one-third can collapse and the losses are covered.

This €60 billion, according to historical data, is supposed to mobilize around €250 billion from private sector. As I said, €10 billion mobilized €180 billion. So now we are using a bit more modest leverage tracing in our assumption. So it’s not a trick, it’s quite normal leveraging in banking.

But if I may come back a bit to investment and the political side, you mentioned also Britain. We are reforming the EU also very fast at the moment, because the world around us has changed and we have to reform societies. We have to reform the EU. Part of the investment plan, the most important part of the investment plan, is deepening and widening of the internal market. So we will create a new market, create level playing fields for the companies in digital trade, in the energy market and in the capital market. Those are European structural reforms. We have a relatively well functioning internal market in goods and services, but we have to improve services internally. Then we bring three additional elements in.

We also have a very ambitious trade agenda which also can be seen as structural reform, international structural reforms. This is exactly what are very important for the UK. You connected growth to politics. So I do hope that we can deliver as fast as we did with EMSI, all those proposals which my colleagues in the Commission are doing when creating a digital single market or capital markets, because it will create economic growth. It’s politically very important and we need the UK to influence those areas which have traditionally been very important for the UK.
Quentin Peel

I want you to put your finger on one or two specific examples. We hear constantly that the internal market in services is not complete. What do we need? Someone was quoting to me the other day, well, for example, what about the market for architectural services? I said, as far as I could see, most of the big projects in Berlin were done by British architects. I don’t think that seems to be a problem. What is the problem actually? Are we not exaggerating? What about pharmacies, for example? That doesn’t really need to open up, does it, to make a big difference? I just wonder if we aren’t exaggerating the problem.

Jyrki Katainen

Maybe slightly we are exaggerating the problem, but we have a list.

Quentin Peel

Give me a couple of really difficult examples.

Jyrki Katainen

For instance, in Germany the number of regulated professions is quite high. This has traditionally been a very difficult issue for Germans.

Quentin Peel

Can you name a couple?

Jyrki Katainen

I don’t remember.

Quentin Peel

Are we talking accountants and that sort of thing?

Jyrki Katainen

Yes. Also in commodities. For instance, in Greece they had a regulation where the baby milk was allowed to sell only in pharmacies, but the previous government actually liberalized this particular product, and the price of the product came down 20 per cent. So now you can buy baby milk from the supermarkets. These may sound quite ridiculous examples but Europe is full of those.

Quentin Peel

Are there ones in Finland?

Jyrki Katainen

Yes, for instance, the retail shop sector is too concentrated. The Commission has constantly proposed that we should liberalize, or the country should use the land policy – I don’t know what it is in English.
Quentin Peel
Property ownership?

Jyrki Katainen
How you keep a piece of land to private investors. So land policy should be liberalized or something like this. Make it possible that foreign chains could enter the market easier.

Quentin Peel
But if we’re talking about making the European Union more popular, more accessible to people, sometimes these changes in the internal market really irritate people, because they’re being forced to give up their nice little national certainties.

Jyrki Katainen
At least in the short term, it can be the case. But if we believe that the internal market really creates better quality, cheaper price and gives opportunities for SMEs to sell products across borders, then we just have to do it. This bears more fruit than the temporary, short-term losses may bring.

Quentin Peel
Let me start first with the Greek issue. How are you going to make your investment programme make a difference now to get growth into the Greek economy, get those investments into Greece that they really need to get growth back off the ground and to prove that it’s not just all about austerity? I remember we were talking about this just before the meeting. The Germans sent a huge business delegation down to Greece when the crisis broke, to see precisely where are the investments that we could get in, that German investors could get involved in and boost the economy in Greece. They came back and they said: the entire legal situation is impossible, property ownership is simply not recognized, a foreign investor is going to have a dreadful time. How are you going to get over that problem?

Jyrki Katainen
First of all, Greece needs structural reforms. This kind of issue, like judicial reform, seems to be one of the areas in which they need to do changes. It doesn’t cost anything. Nobody is losing anything if you just streamline the judicial system, just like Italy is doing at the moment. Italy is pushing through very ambitious judicial reform in order to shorten the time that is needed for private companies to get licences, for instance, to invest. So this is one thing.

But then if you manage, I hope, to find a solution which stabilizes Greek society as soon as possible, and the private sector would see opportunities in the future, they wouldn’t need to fear what happens to my country the next day – we could use EFSI as an instrument to raise risk financing to SMEs in Greece, or finance some other private projects. EFSI, as I said, is part of EIB and it concentrates on –

Quentin Peel
It’s part of EIB or it’s working with EIB?
Jyrki Katainen

It’s part, it’s legally part of EIB. So basically it goes like this. A Greek hotel owner or hotel chain owner would like to renovate ten hotels. They cannot get financing from Greece because of its reasons, or at least at any reasonable price. The owner of the chain calls directly to EIB and says, I have this kind of project. EIB analyses the project and says okay, this is economically viable but too risky for our normal operations. Let’s send it to EFSI, which is the risk fund. EFSI says okay, this is fine, and they guarantee the loan or do equity investment or do something like this. So EFSI covers different types of risks. In Greece obviously it’s mostly the country risk. This could help.

Another way to help Greece to grow is to distribute risk financing to SMEs through Greek banks. Of course everybody understands that we have to have well-functioning banks before, and banks must be sufficiently capitalized before they can do anything. But we can help.

I visited Athens just a little while ago and I spoke with entrepreneurs and industrialists. They say they have got used to living in uncertainty but if they could be sure that the country will grow and change and move forward, they could start investing.

Quentin Peel

That’s a chicken-and-egg problem, isn’t it?

Jyrki Katainen

That’s right.

Quentin Peel

They need to invest to get the growth going, but if the growth isn’t there they won’t invest. You’ve got to crack that one.

Jyrki Katainen

Actually, if there is a solution, which I believe there is, then it sets the next steps, how the country can recover. They have financing from the other eurozone countries and Greeks can see, okay, this and that will be changed or reformed. Taxation looks like this in the medium term. Even though the medicine is very bad-tasting, at least everybody knows how things will go. So the certainty or trust is at the core of this problem.

Quentin Peel

And that has got to be rebuilt, that’s part of the problem.

Jyrki Katainen

Yes.
Quentin Peel

I do want to ask you a slightly more political question, or almost philosophical question, about the eurozone crisis and the European Union. I think just as you were coming into office in the Commission, you expressed the worry or the fear that the eurozone crisis has really opened up the north-south divide in Europe. The divide between the good, honest, Protestant north and all those spendthrift southerners who don’t work and just play. Is that a real worry?

Jyrki Katainen

It was, but not anymore. I was very worried about this a year ago. But now, once many countries who have gone through the very ambitious reform programmes, who have enjoyed financial assistance from the other countries –

Quentin Peel

So Ireland, Portugal, Spain.

Jyrki Katainen

And also Cyprus is doing quite well. They have done their homework. They have reformed their countries. They have got very good economic growth. Spain last year managed to get 700,000 new jobs. They are expecting 1 million new jobs this year. So this has changed the atmosphere. So there is no division between south and north anymore, at least to the same extent as it was. So the big picture is much more harmonious. This may sound ridiculous today to say so.

Quentin Peel

I wonder, how do you go home to Finland – I know when you become a European commissioner, you just have a European hat. But one of the things you have to do is go home to your home country and try and say, this is what we’re doing, and try and persuade people. You’ve seen a rise in voters for what used to be the True Finns, now the Finns, who are very resentful of paying money to countries like Greece. How the hell do you sell it? I might beg to differ with your optimism. They’re rising in popularity in Finland.

Jyrki Katainen

First of all, I just read from the media when I was coming here that the Finnish government has accepted bridge financing in a form that the Commission had proposed.

Quentin Peel

The one that George Osborne doesn’t like?

Jyrki Katainen

Yeah, there are many people who do not like it. But there are not too many options or solutions, and we have to make sure that Greece won’t default before they get the new package. Also the government had got the mandate from the parliament to start negotiating on the third package. So basically the atmosphere in Finland is not negative towards the EU, but it’s very sceptical towards the way of living
where all the rules are stretched. The ordinary Finn tends to think that the European project is about replacing the rule of force by the rule of law. Law means 'as it has been written', because then it's the same for everybody, and it's fair.

So I would say more than a south and north division, we still have a crisis of fairness. Many people tend to think that the European project is not fair. The other countries think that because the others haven't followed the rules, they are in crisis, and that's why we have to pay them out of the crisis. They find it unfair. Some people, for instance here in the UK, think that it's not fair that other nationalities are coming to our country and taking our jobs and using our social benefits. There are many other countries who are thinking the same.

I personally think that we need a Europe which represents free movement of people, free movement of workers, free movement of students, free movement of human capital, and goods and other capital. But we don't need to accept social dumping, or we cannot accept social dumping nor social security shopping. This is a question of fairness. Some other countries think that the other Europeans haven't been solid enough towards us. They found this as a fairness issue. As a commissioner, I take this fairness issue very seriously. If we lose the sense of fairness, for whatever reason, then we are close to losing the legitimacy of integration.

**Quentin Peel**

Okay, splendid. I’ve got lots of other questions but I expect there’s going to be questions from the floor too, so let’s open up the debate.