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The discussion on the supply and finance of public goods at European level is part and parcel of the broader discussion on the revision of European economic governance. This paper argues that there exists a mismatch between, on the one hand, the need and popular demand for European Public Goods, especially after the pandemic, and on the other, a continued reluctance to increase their supply and finance them. Whilst the emblematic Next Generation-EU represents a breakthrough, it offers public goods "by aggregation", rather than "pure" European Public Goods. This mismatch can be explained by the political economy of national decision-making priorities. In this context, we offer a simple analytical framework for analysing and potentially increasing the supply of European Public Goods by operating on changing political incentives and institutional dynamics.

An unsatisfied demand for European Public Goods

The pandemic has reminded us of the importance of robust and resilient health systems and rekindled the discussion on the importance of providing goods such as health at a scale that transcends the nation-state. At the same time, and in a different policy area, recent events on the global front (the precipitous retreat from Afghanistan and the France-AUKUS submarine issue) have highlighted the need for progress on a common EU defence policy.

In an environment of increased interconnectedness but also heightened vulnerability, with rampant externalities and spillovers (positive and negative), there seems to be an objective need for more European Public Goods (hereafter, EPGs). Health and defence may be the newest entrants in the discussion, but the list is long: it extends from traditional policy domains such as security and development cooperation, to R&D in large and risky projects, and of course climate change mitigation and an adequate digital infrastructure (Fuest and Pisani-Ferry 2019, Papaconstantinou 2020).

There is no direct evidence about demand for EPGs, but - along with a general move in the state/market boundaries and from pre-market to in-market policies - the pandemic seems to have accentuated a majority view in member states towards more confidence to and reliance on European-level solutions. Eurobarometer data suggest a strong majority of Europeans favour a common policy across diverse policy areas, ranging from free movement to defence, energy, trade, health, foreign policy, even

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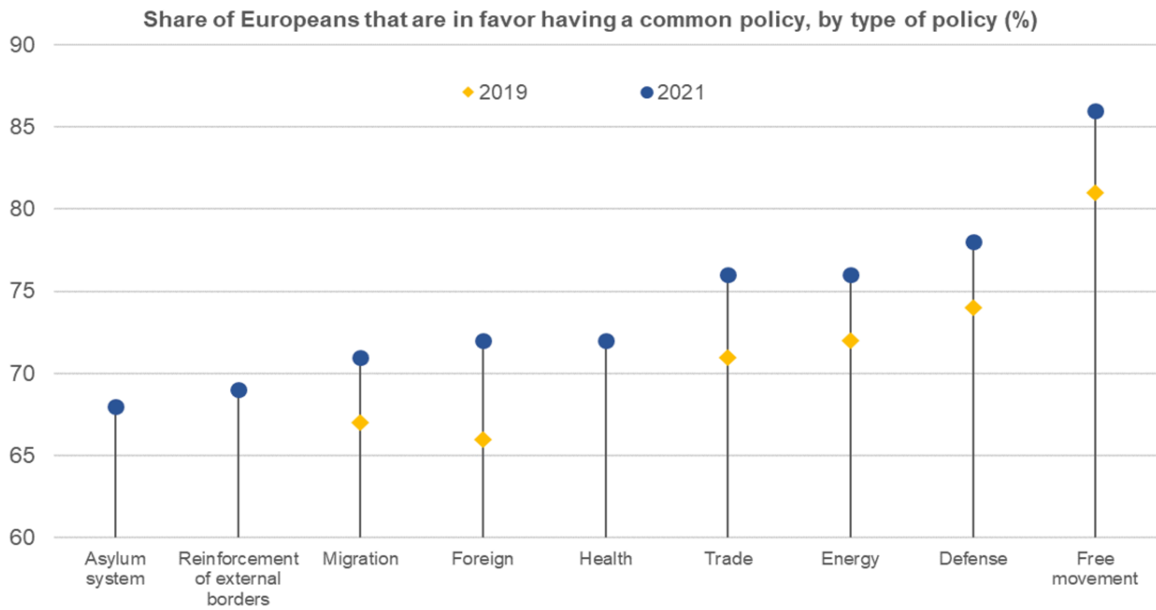
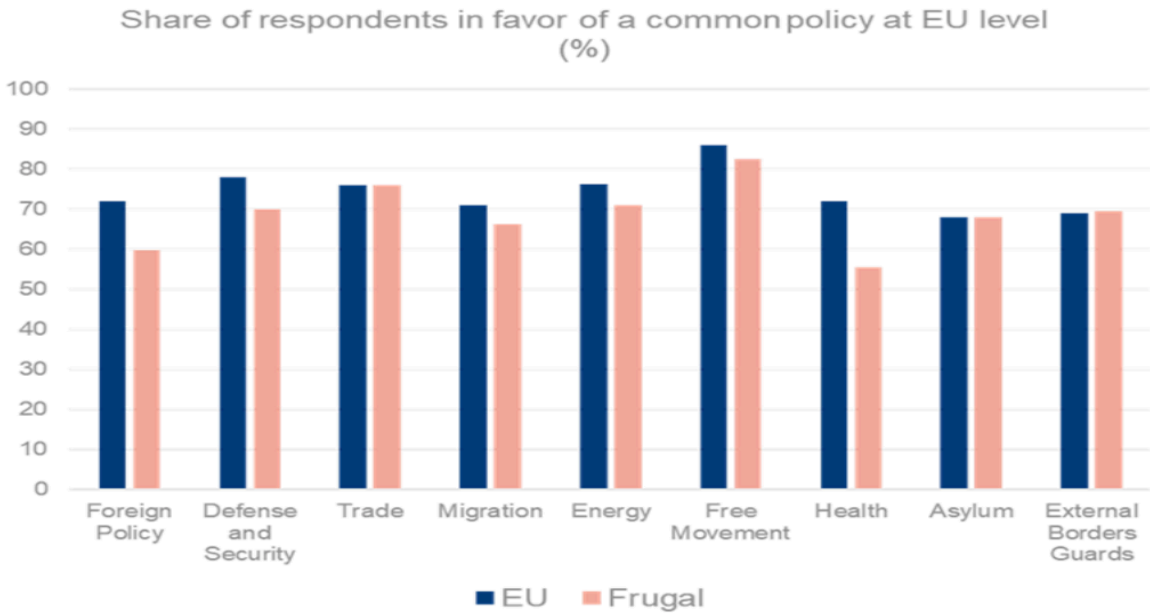
migration and asylum; what is more, despite national differences, the result holds even for the so-called "frugals" (see Figure 1). The attitude of EU citizens seems to be more favourable to the supply of EPGs than what policy makers are able and willing to deliver.

Figure 1. Attitudes towards common policies





Note: Frugal countries include AT, FIN, NL, SWE, DK.
Source: Eurobarometer, Spring 2019/Spring 2021

Next Generation-EU: a breakthrough with a *caveat*

It is largely recognised that the Next Generation-EU (hereafter, NG-EU) initiative is a potentially ground-breaking programme. The innovations on both the spending and revenue side as well as its governance arrangements cross "red lines" that were thought to be unmoveable not long ago.[2]

dNG-EU offers important lessons on the issues to be addressed when pushing for more European public goods. On the one hand, the direction in the national Recovery and Resilience Plans (RRPs) to ensure that at least 37% and 20% of the funds are allocated to the green and digital transition, respectively, incorporate overarching EU goals. Therefore, although delivery takes place at national level, reforms and investments respond to European priorities. On the other hand, the final July 2020 decisions involved a reallocation against the "pure" public good element that was present in the original Commission proposals: as shown in Table 1, the overall envelope of 750bn was maintained, but there was a shift from programmes more akin to EPGs (second and third pillar) to transfers to national governments (first pillar).

Table 1. NextGenEU proposals and outcomes

PROGRAMME	COM PROPOSAL MAY 2020	EUCO CONCLUSION JULY 2020	DIFFERENCE
First Pillar: Supporting MS	**655 bn**	**737.5 bn**	**+ 82.5 bn**
Recovery and Resilience Facility (RRF)	560 bn	672.5 bn	+ 112,5 bn
	Grants: 310 bn	Grants: 312.5 bn	+ 2.5 bn
	Loans: 250 bn	Loans: 360 bn	+ 110 bn
Other programmes	95 bn	65 bn	-30 bn
2nd Pillar: Private sector support	**56.3 bn**	**5.6 bn**	**-50.7 bn**
InvestEU	30.3 bn	5.6 bn	- 24.7 bn
Solvency Support Instrument	26 bn	0	- 26 bn
3d Pillar: Lessons from the crisis	**38.7 bn**	**6.9 bn**	**- 31.8 bn**
Research and Health	21.2 bn	5 bn	- 16.2 bn
Other programmes	17.5 bn	1.9 bn	- 15.6 bn
TOTAL	**750 bn**	**750 bn**	0

Source: European Commission.

NG-EU confirms that what counts for national leaders at the end of the day is nationally attributed funds; for national policy-making, "success" is about what you bring home. Perhaps not surprisingly, while the European Commission has guided the Member States in the design and implementation of RRPs, it had to accept the general framework that RRP projects are national projects.

It seems therefore that in the current framework, the best that can be hoped for is a second-best approach: if Member States are covering common ground in the projects of their national RRPs, the Commission would stress the interdependence and strive for consistency in the implementation phase. Some joint projects between countries come closer to fulfilling the European public good notion, but

[2] Several chapters in Buti (2021) discuss the innovations and analyses the factors that made the EU response to the pandemic much more ambitious than that to the global financial crisis.

bottom up and *ex post*, rather than top down and *ex ante*.[3] All this remains a major advancement, but falls short of a first-best solution of more public goods projects that are funded and executed at EU level.

Delivery and financing of European programmes

When thinking about providing and financing EPGs, a number of questions arise. In addition to breadth and coverage, what is the optimal level of EPGs when externalities abound, and market pricing cannot act as a guide? The classic fiscal federalism literature provides a conceptual framework for identifying the institutional level at which public goods and policies should be delivered. But it gives little operational guidance as to how to remove the political obstacles to a more adequate supply of EPGs. For financing however, the answer can be more practical: at EU level, it mainly involves using the mechanisms of the EU budget and NG-EU; to that can be added incentives at national level (by "earmarking") through for example a redesign of fiscal rules to encourage more investment into activities akin to EPGs.

A simple conceptual framework may help frame the analysis. In Table 2, we distinguish between delivery and financing of European programmes.[4] "Pure" EPGs are those delivered and financed at the EU level. Recent examples are the common procurement on vaccines and the creation of the European Health Emergency Preparedness & Response Authority (HERA).[5]

The other three combinations involve Member States either in the delivery or financing, or both. Where the delivery takes place at national level, we are in the realm of EPGs "by aggregation". A notable example is the projects to foster the double transition in the RRPs. The screening of the projects by the Commission, including the application of the Do No Significant Harm (DNSH) principle, aims at ensuring that the targets of at least 37% of the funds allocated to the green transition and 20% to the digital transition are credibly attained.

The possibility to deliver EPGs at the EU level whilst maintaining the financing at national level is foreseen via the so called 'external assigned revenue', i.e. funds conferred by member states and non-EU countries to the EU budget to be spent on community actions.[6] Third country participation in Erasmus uses this budgetary technique. In the economic sphere, the Commission proposal of a European Investment Stabilisation Fund (EISF) in 2018 foresaw the creation of a fund outside the EU budget to be filled by national contributions by Member States representing external assigned revenue for the EU budget.

The projects where both financing and delivery takes place at national level can still qualify as EPGs "by aggregation", provided that they are consistent with a clearly defined a common European goal.

[3] The Commission proposed seven flagships (three each in the areas of green and digital transitions, one in the area of social transition) and promoted cross-border projects. However, the political appetite with MS on such initiatives remains weak. It would seem that supply at national level of EPGs financed at EU level is not a promising avenue.
[4] Broadly in line with our distinction, D'Apice and Pasimeni (2020) and Buti and Messori (2021) discuss the coherence between EU and national projects.
[5] The common purchase of vaccines was financed initially via ESI, the EU budget emergency fund. Subsequently, the Member States were asked to top it up, based on their relative GDP, to achieve the necessary funding.
[6] From a legal standpoint, the funds borrowed in the markets to finance NG-EU are considered external assigned revenue. In our analysis, we take a narrower definition of externally assigned revenue.

An example of this are the Important Projects of Common European Interest (IPCEI) which allow state aid support for breakthrough innovations that would not otherwise materialize because of the market risks such projects entail. The most notable IPCEI is a pan-European project on a new generation of batteries.

Whilst EPGs "by aggregation" play an important role given the complexity of the EU system, there are potential shortcomings compared to "pure" EPGs: projects delivered at EU level but financed via national budgets may be called into question should national priorities change; similarly, EU financed EPGs delivered at national level may lack the cross-country coherence. Finally, EPGs financed and delivered by Member States may combine both weaknesses. Therefore, the issue of how to increase the supply of "pure" EPGs has to be addressed.

Table 2. Classifying European programmes

Delivered → / Financed ↓	EU	National
EU	R&D / Horizon Vaccine Financing/HERA European Space Program Connecting Europe Facility	Just Transition Fund Double transition under RRF (37% green and 20% digital) SURE
National	Projects financed by externally assigned revenue	CSRs-recommended projects with large externalities (e.g. resilience of health systems) IPCEI (batteries)

Source: Authors' elaboration. Entries in the table are non-exhaustive examples.

Thinking about incentive compatibility

In the EU, second best solutions will always be part of the game. What is more, also for "non-pure" EPGs, one can get closer to the frontier by better incorporating the EU dimension and priorities. Nevertheless, if increasing the supply of "pure" EPGs financed and delivered at EU level is important, how does one nudge the process to deliver these? This seems to be a classic incentive compatibility problem:, whose solution is to tweak political incentives and institutional dynamics for a better outcome by making such projects politically viable. Critical will be the need to show that the EU level does not undermine what happens at national level - the opposite in fact.

We identify in Table 3 two principles that could help us think in this direction and increase the supply of "pure" EPGs. The first is a *threshold effectiveness* principle: it concerns goods where supplying at EU level enjoys scale and scope economies that are clearly superior to the supply at national level. This relates to the classic part of fiscal federalism theory and subsidiarity; but it may require a threshold effect to ensure political acceptance, as with the funding of a large and important project such as vaccine development at EU level.

Table 3. Principles for European public goods

Principles	Rationale	Normative implications
Threshold effectiveness principle	Show that supplying at EU level enjoy scale and scope economies	Overarching delivery systems at EU level
National interest principle	Demonstrate the additivity or non-harm of pursuing national goals	Project selection implications / show complementarities and leverage effects

Source: Authors' elaboration.

The second is a *national interest* principle: as the legitimacy of decision-making at the level of Member States indeed rests on national interest, it is important to demonstrate additivity or non-harm when pursuing European public goods. In security, a traditional domain for public goods, the recent AUKUS submarine issue already mentioned can lead to build critical mass at EU level. Agglomeration effects could be an incentive for the stronger countries to buy-in; for smaller countries, it would be spillover effects driving decision-making. In essence, the national benefit would not only arise *indirectly* via the attainment of the common good, but also *directly* by the fact that, if you do not supply these public goods at a supranational level, policy makers would not be able to attain some national goals either.

It goes beyond the scope of this paper to apply the principles sketched out above to the identification of specific EPGs. Nonetheless, examples of pure EPGs consistent with the above approach could be research and procurement on vaccines, hydrogen, connectivity, defence, big data infrastructures, semiconductors, a Climate Fund. Beyond these allocative public goods, a Euro-area stabilisation function that is financed and delivered at the EU level could be seen as representing a "pure" EPG.

The political economy of mindset change

The aim of the present paper was to start exploring the political economy of the insufficient supply of EPGs. Clearly, it requires further analysis and debate before it can be applied in an operational way.

The key is found in the juxtaposition between an EU budget made up of national contributions vs. a true EU-level resource. The former has proved extremely difficult to increase in order to invest on public goods; more generally, its inconsistency with future prospects of European integration has long been established (for an early criticism, see Sapir et al. 2003, Buti and Nava 2003).

Raising the national practice of earmarking resources in budgets for certain activities to the EU level help funding when the principle of separation is strongly present - at the same time allowing for direct accountability on spending. A more promising avenue however is true EU-level resources to bring decision-making on funding out of national optimisation and thereby help finance "pure" EPGs. There is a parallel to other policy areas where EU has exclusive competence: single market, trade. But it requires a mindset change for EU-level policy: from what we cannot do (the framework around trade and competition policy) to what we can do (supporting investment in EPGs).

The discussion on new own resources prompted by the funding of NG-EU represents a step in the right direction.[7] It rests on a solid economic rationale: as the need for EPGs goes up (as in health safety), so does need for the supply of public goods built on mechanisms for own resources that are linked to economic activity at EU level. It is a development which may also command public support (Maduro and Woźniakowski 2020).[8] The template for decisions currently foreseen however may be too limited for the broader ambitions on supplying EPGs. The future discussions on a possible permanent central fiscal capacity beyond NG-EU (see, e.g. Buti and Messori 2021) may provide the opportunity to raise the stakes.

[7] The European Commission came forward with proposals on new own resources in December 2021. They are based on Emission Trading System, Carbon Border adjustment and the forthcoming implementation of Pillar 1 of the OECD agreement on reallocation of profits of large multinationals. See European Commission (2021).
[8] A You Gov survey in 11 MS, conducted with the School of Transnational Governance of the European University Institute suggests that while Europeans are divided on the extent to which national budgets should provide more EU funding, they seem to support new own resources at a European level, such as those from supra-national levies on emissions (a carbon tax), internet companies, financial transactions or business profits in general.

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