7. THE EU BUDGET: THE NEW MFF AND THE RECOVERY INSTRUMENT: NEXT GENERATION EU

Pilar Más Rodríguez

7.1. ABSTRACT

The COVID-19 pandemic has shaken the world and Europe to its core, testing healthcare and welfare systems, society, economy, customs and living and working conditions. The scope of the crisis and the policy responses are unprecedented and the depth of the impact is still uncertain. The European Union (EU) and its Member States adopted emergency measures to preserve the health of citizens and prevent a collapse of the economy. This required a historic effort and an innovative approach, fostering convergence, resilience and transformation in the EU.

The Next Generation EU (NGEU) programme constitutes an important and well-timed step to support the recovery in Europe. The initiative entails a fiscal stimulus of 750 billion euros that could raise GDP by more than 4% in 2024 for some countries, according to EU estimates. NGEU will unlock the full potential of the European budget to kick-start the economy and boost Europe’s sustainability, resilience and strategic autonomy. It builds on the Union’s experience of harnessing market financing and expands it to achieve the scale of support that is urgently needed in the current circumstances.

A reinforced Multiannual Financial Framework (MFF) for 2021-2027, of 1074 billion euros, will guide the EU back from crisis to the path of long-term recovery, providing essential financing for immediate needs and for long-term investments in the green and digital transitions.

On 10 November 2020, the European Parliament and EU Member States in the Council reached an agreement on the next MFF and the NGEU, the largest package ever

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financed through the European budget. This is a great opportunity, not only to support the recovery but also to invest in the future of the European Union.

**Keywords**: Crisis; Digital; European Union; EU budget; Green; NGEU; Multiannual financial framework; Sustainability; Resilience.

### 7.2. INTRODUCTION

The COVID-19 pandemic has shaken the world and Europe to its core, testing healthcare and welfare systems, society, economy, customs and living and working conditions. The scope of the crisis and the policy responses are unprecedented and the depth of the impact is still uncertain.

The European Union and its Member States adopted emergency measures to preserve the health of citizens and prevent a collapse of the economy. This required a historic effort and an innovative approach, fostering convergence, resilience and transformation in the EU.

At the request of the Heads of State or Government, the European Commission presented at the end of May a very wide-ranging package combining the future Multiannual Financial Framework 2021-2027 and a specific recovery effort under Next Generation EU. In July 2020, after long negotiations, the European Council agreed on this recovery plan for Europe and the MFF 2021-2027, leading the way out of the crisis and laying foundations for a modern and more sustainable Europe.

More than 50% of the long-term EU budget and Next Generation EU (750 billion euros), a total of 1.8 trillion euros, will support modern policies and set Europe on the path to a sustainable and resilient recovery. As the President of the European Commission said, “The agreement is a strong signal of trust and a historic moment for Europe.”

The EU recovery plan will require huge investment to repair the economic and social damage caused by the pandemic, kick-start European recovery and protect and create jobs. This challenge is a great opportunity, not only to support the recovery but also to invest in the future of the European Union.

NGEU will be channelled through European programmes to support the necessary measures to help Member States recover and emerge stronger from the crisis, boost private investment and foster sustainable and resilient growth.

Through the MFF 2021-2027, the European Commission will create instruments and strengthen key programmes using the NGEU to direct investment where it is most needed, reinforce the Single Market, intensify cooperation in areas such as health and crisis management and provide the EU with a long-term budget that will be the engine of the green and digital transitions and foster a more resilient economy.

On 10 November 2020, the European Parliament and Member States in the Council, with the support of the European Commission, reached an agreement on the next MFF and the Recovery Plan, the largest package (1.8 trillion euros) ever financed through the EU budget.
This document presents the main elements of the next Multiannual Financial Framework 2021-2027 and the Next Generation EU.

7.3. THE EU MULTIANNUAL FINANCIAL FRAMEWORK

7.3.1. BACKGROUND AND CONCEPTS

Since 1988, the European Union has had Multiannual Financial Frameworks in which the annual budget is embedded. This has provided great stability to the negotiation of the budget and put an end to the interinstitutional conflicts of previous stages.

The Lisbon Treaty provides that a Council Regulation will establish the Multiannual Financial Framework, conferring on it a normative status that it lacked previously, as it only responded to an Inter-institutional Agreement.

The Multiannual Financial Framework defines the budget cycle of the European Union for a period of seven years. It is up to the European Commission to present a proposal and the Council and the European Parliament to approve it in a co-decision process. The configuration of European policies and the margin of financial flexibility largely depend on the final agreement.

The objective of the MFF negotiations is to define, in general terms, the maximum limits of the amount of money that the EU can spend, the Spending Programmes that determine where the money should be spent (spending structure) and the Rules that establish how to finance the expenditures.

**Spending limits**

The MFF sets the maximum limits for EU spending, both globally and for each of the main policies or headings. Limits are set for “commitment credits” or theoretical fund allocations (by headings and years) and for “payment credits”, based on what is considered executable annually without distinguishing, in this case, by headings.

On the other hand, according to the Treaty on the Functioning of the European Union (TFEU), the MFF must guarantee that expenditures evolve within the limit of the EU’s Own Resources, including the percentage of own resources used to finance the payment credits on the EU’s Gross National Income (GNI).

The MFF is accompanied by a Decision on Own Resources and is complemented by the annual budget approved by the Council and by the Parliament. The spending ceilings of the Framework must be respected by the European Parliament, the Council and the European Commission, in the preparation, approval and execution of the framework. The budget must be balanced in terms of income and expenditures.

The size of the MFF has historically been limited, standing at around 1% of EU’s GNI. Their policies do not replace national ones, but rather enhance them with others that require a European dimension.
Expenditure structure and financing

The spending structure of the MFF and the size of each heading has been adapted to the priorities of the EU and to the circumstances of each moment.

Initially, the budget mainly financed agricultural spending, the Common Agricultural Policy (CAP) being one of the pillars of the 1957 Treaty of Rome, which brought about the creation of the European Economic Community (EEC). The share of the CAP in EU budget has been gradually reduced, from 75% in the 70s to a third currently. In parallel, other policies have emerged, such as the regional one, which represents another third of the budget. The rest of policies (R&D, foreign policy, infrastructure or education) have also increased their weight in the last two decades. Investment is focused on programmes managed at European level in areas such as research and innovation, transport and energy networks, youth mobility programmes and external action.

Almost the entire European budget is financed from the EU’s Own Resources, which are classified into customs duties and levies (15% of the total), a resource based on Value Added Tax (VAT) (12%) and national contributions based on the weight of GNI of the country in the total (73%). The rest comes from other sources (fines, contributions from non-member states to certain programs, etc.).

7.3.2. NEW MULTIANNUAL FINANCIAL FRAMEWORK 2021-2027

A long and complex process of negotiations

The current 2014-2020 Multiannual Financial Framework expires on 31 December 2020 and since mid-2018 the new 2021-2027 framework is being negotiated. The environment in which the negotiations are taking place is particularly complex. On the one hand, there is a consensus on the need to respond to the main EU challenges (digital transition, climate, immigration and security, among others), to which are added the difficulty of the United Kingdom’s exit from the EU and the need to face the challenge of European reconstruction after COVID-19, the biggest health and economic crisis in Union history.

The negotiations on the new Multiannual Financial Framework 2021-2027 have evolved from an initial proposal presented by the European Commission in May 2018, which amounted to 1,134,583 million euros (at 2018 prices), 1.11% of the EU-27 GNI. This introduced significant changes with respect to the current Framework:

• Changes in spending composition, increasing the weight of policies aimed at addressing new priorities of the Union (border control, defence, migration, security, development cooperation and research, etc) and reducing agricultural and cohesion policies. The structure was streamlined with seven new rubrics across 17 policy groups. The number of spending programmes was reduced, from 58 to 37.
• Special budgetary instruments were included to improve budget flexibility: the Flexibility Instrument (1,000 million euros per year), the Reserve for Emergency Aid (600 million euros), the EU Solidarity Fund (600 million euros), the European Globalization Adjustment Fund (200 million euros), the European Peace
Support Fund and the European Investment Stabilisation Function (loans of up to 30,000 million euros during the MFF period). The European Development Fund (EDF) is integrated into the MFF.

- The revenues side was modernised by introducing new categories of Own Resources based on the revenue of the EU emissions trading scheme, a contribution from Member States based on their plastic waste.

On 14 November 2018, the Parliament presented its detailed mandate, which included amendments to the Commission proposal relating to the MFF Regulation and a set of figures broken down by heading and programme. In particular, Parliament’s report specified the following:

- The MFF ceiling for commitments should be increased, from 1% of EU-28 GNI to 1.3% of EU-27 GNI. This represented a maximum of 1,324,089 million euros (at 2018 prices), 16.7% higher than the one proposed by the European Commission.

- The allocations for the CAP and cohesion policy should remain unchanged in real terms. On the other hand, a number of priorities should be further strengthened, including programmes for the heading ‘Single market, innovation and digital economy’ (in particular, Horizon Europe), for ‘Cohesion and values’ (Erasmus+ and a new Child Guarantee) and for ‘Natural resources and environment’ (the Environment and Climate Action programme and a new Transition Fund).

- Funding for decentralised agencies involved in migration and border management should be higher, from around 3 billion euros to more than 12 billion. The contribution of the EU budget to the achievement of climate targets should be set at a minimum of 25% of MFF 2021-2027 spending, be integrated into all relevant policy areas and reach 30% as soon as possible. The mid-term review of the MFF should be mandatory and proposed no later than 1 July 2023.

In November 2019, the Finnish Presidency of the Council presented a proposal that included provisional figures for MFF 2021-2027 (1.087 trillion euros at 2018 prices in commitment credits). Nevertheless, this was severely criticized as Parliament considered it was well below expectations.

In May 2020, the European Parliament requested that the Commission present, before 15 June 2020, a proposal for an MFF contingency plan to provide a safety net and protect the beneficiaries of Union programmes.

Following the COVID-19 crisis and the huge economic consequences, at the end of May the European Commission presented a significant review of MFF 2021-2027. The proposal included a total amount of 1074.3 billion euros and an additional recovery instrument, the Next Generation EU programme, with 750 billion euros, 390 billion euros of grants and 360 million of loans (see Figure 1).
Finally, on 10 November 2020, the European Parliament and EU Member States in the Council, with the support of the European Commission, reached an agreement on the largest package ever financed through the EU budget, of 1.8 trillion euros. The package will play an essential role in the recovery process of Europe. The strengthened multiannual framework will boost the recovery path after the crisis, providing funding for immediate needs and investments in the green and digital transitions for medium and long-term. The success of this recovery plan will depend not only on its size and ambition, but also on the speed of action and the ability to adjust the response to the evolution of the uncertain situation.

7.4. NEXT GENERATION EU (NGEU)

7.4.1. INITIAL RESPONSE TO COVID-19: SURE, ESM, EIB

The unprecedented crisis led to a prompt comprehensive European policy response, both monetary and fiscal. In April 2020, the European Union agreed an aid package of more than half a trillion euros to provide immediate support for Member States, whose economies had been severely hurt by the coronavirus outbreak. This response was added to the strong reaction of the European Central Bank (ECB), through liquidity (TLTRO), extension of QE and a new temporary QE programme (PEPP, in two phases: 700 billion euros and 650 billion euros).

European leaders discussed progress on the several dimensions of the response to the pandemic and agreed to coordinate as much as possible to ensure a gradual and orderly lifting of restrictions. They welcomed the Joint Roadmap for Recovery which set out import-
ant principles such as solidarity, cohesion and convergence, as well as four key areas for action: a fully functioning Single Market, an unprecedented investment effort, a global sphere of action and a functioning system of governance.

The European Council endorsed the agreements on three important safety nets for workers, businesses and sovereigns, amounting to a package worth 540 billion euros (see Table 1), and called for the package to be operational by 1 June 2020. It also agreed to establish a Recovery Fund and tasked the European Commission to present a proposal targeted towards the most damaged sectors and regions.

**TABLE 1. INITIAL RESPONSE: 3-SAFETY NETS APPROVED AT EARLY STAGES OF COVID**

<table>
<thead>
<tr>
<th><strong>ESM</strong></th>
<th><strong>EIB</strong> (EU level)</th>
<th><strong>SURE</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit Line, Pandemic crisis support</td>
<td>Guarantees</td>
<td></td>
</tr>
<tr>
<td>FOR GOVERNMENTS, Health care, cure and prevention</td>
<td>FOR FIRMS (Small companies)</td>
<td></td>
</tr>
<tr>
<td>Credit line, 12 months, very low cost, maturity: 10 years</td>
<td>Loans to firms backed by a guarantee fund (€25 billion)</td>
<td>Loans to governments backed by guarantees (€25 billion)</td>
</tr>
<tr>
<td>€240 billion</td>
<td>€200 billion</td>
<td>€100 billion</td>
</tr>
</tbody>
</table>

Source: Own preparation based on European Commission data.

7.4.2. NEXT GENERATION EU: MAIN FEATURES

In July 2020, the European Council reached an agreement on Next Generation EU, together with the approval of the Multiannual Financial Framework 2021-2027. The overall quantity of NGEU (750 billion euros) and the relatively generous distribution to periphery and Eastern European countries remained unchanged from the European Commission proposal, although the proportion of grants was lowered from 66% to 52%.

NGEU constitutes an important and well-timed step to support the recovery in Europe. The fiscal stimulus of 5.4% could raise GDP by more than 4% in 2024 for some countries, according to European Commission estimates. Moreover, the fund is strongly redistributive. Only the grants component of the Recovery and Resilience Facility implies that rich countries will contribute with around 2% of their annual GDP. NGEU will be a great opportunity but also a big challenge: the capacity of absorbing such massive support and spend it on relevant projects will be tested.
TABLE 2. MAIN FEATURES OF NGEU

<table>
<thead>
<tr>
<th>Main features of NGEU</th>
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<tbody>
<tr>
<td><strong>Size</strong></td>
</tr>
<tr>
<td><strong>Composition</strong></td>
</tr>
<tr>
<td><strong>Funding</strong></td>
</tr>
<tr>
<td><strong>To be spent fast</strong></td>
</tr>
<tr>
<td><strong>Allocation</strong></td>
</tr>
<tr>
<td><strong>Conditionality</strong></td>
</tr>
<tr>
<td><strong>Rebates</strong></td>
</tr>
<tr>
<td><strong>EU budget</strong></td>
</tr>
<tr>
<td><strong>Rule of Law</strong></td>
</tr>
</tbody>
</table>

Source: Own preparation.

**Total amount, grants and loans**

NGEU is the recovery fund for which the European Commission will borrow up to 750 billion euros on the capital markets on behalf of the EU. This Own Resources Decision is limited in time - until the end of 2026 - and scope – it will address the challenges of the crisis. The fund will consist of a very large Recovery and Resilience Facility (672.5 billion euros) and several smaller limbs. More than half of the total will be constituted by grants (390 billion euros) and the rest by loans (360 billion euros).

**Strong redistribution**

The Recovery and Resilience Facility (RRF), the main limb of the NGEU, will support public investments and reforms and will contribute to economic, social and territorial cohesion within the EU. It will help Member States address the economic and social impact of the pandemic whilst ensuring that their economies undertake the green and digital transitions, becoming more sustainable and resilient in the medium and long term.

The distribution of funds will take into account the uneven effects of COVID-19 across countries. The RRF will offer Member States 312.5 billion euros in grants (at 2018 prices), of which 70% would be committed in 2021 and 2022 and 30% by the end of 2023 (see Table 5).

The allocation key for 2021-2022 will consider for each country its population, the inverse of GDP per capita and the relative unemployment rate over the past 5 years. In the allocation key for 2023, the unemployment criterion will be replaced, in equal proportion, by real GDP growth in 2020 and over the period 2020-2021, initially based on the Commission Autumn 2020 forecasts and updated by 30 June 2022 with the latest published figures.

Moreover, 360 billion euros of additional loans for reforms and investments will be provided to Member States. As a rule, the maximum volume of such loans will not exceed 6.8% of the GNI of each country.

NGEU will be strongly redistributive. According to European Commission estimates, only the grants component of the Recovery and Resilience Fund (RRF) implies that rich countries will contribute with around 2% of their GDP. Including the loans component,
which admittedly is not a net transfer as they will have to be repaid in the long term, these countries will make a net contribution of around 4% of their annual GDP, while Spain will receive 6.5%. France will be also a net contributor. These estimates are assumed to be the same for all loan and guarantee components.

However, the regulation proposal explains that each instrument of the package will be allocated differently and there may even be no cross-country allocation key at all. According to Bruegel estimates based on European Commission and IMF data, some countries would obtain 15% of their GNI in grants and guarantees and others less than 1%. So, NGEU contains a strong redistributive elements that will mainly benefit the countries hardest hit by the crisis and with the lowest GNI per capita (see Table 3).

### TABLE 3. CROSS-COUNTRY ALLOCATION OF THE NGEU AND THE 2020 ANNUAL BUDGET AMENDMENT: GROSS GRANT AND GUARANTEE PAYMENTS TO MEMBER STATES

<table>
<thead>
<tr>
<th></th>
<th>Grants</th>
<th></th>
<th></th>
<th>Guarantees</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>€ billion</td>
<td>% total</td>
<td>% 2021 GNI</td>
<td>€ billion</td>
<td>% total</td>
<td>% 2021 GNI</td>
</tr>
<tr>
<td>Total</td>
<td>433</td>
<td>100.0%</td>
<td>61.59</td>
<td>100.0%</td>
<td>4.7%</td>
<td>9.6%</td>
</tr>
<tr>
<td>Italy</td>
<td>85.9</td>
<td>19.8%</td>
<td>5.2%</td>
<td>18.25</td>
<td>29.63%</td>
<td>1.10%</td>
</tr>
<tr>
<td>Spain</td>
<td>80.9</td>
<td>18.7%</td>
<td>7.0%</td>
<td>8.01</td>
<td>13.00%</td>
<td>0.69%</td>
</tr>
<tr>
<td>France</td>
<td>43.2</td>
<td>10.0%</td>
<td>1.8%</td>
<td>13.11</td>
<td>21.29%</td>
<td>0.56%</td>
</tr>
<tr>
<td>Poland</td>
<td>38.2</td>
<td>8.8%</td>
<td>8.1%</td>
<td>0.38</td>
<td>0.62%</td>
<td>0.08%</td>
</tr>
<tr>
<td>Germany</td>
<td>33.8</td>
<td>7.8%</td>
<td>1.0%</td>
<td>9.79</td>
<td>15.09%</td>
<td>0.27%</td>
</tr>
<tr>
<td>Greece</td>
<td>23.2</td>
<td>5.4%</td>
<td>13.5%</td>
<td>2.31</td>
<td>3.76%</td>
<td>1.35%</td>
</tr>
<tr>
<td>Romania</td>
<td>20.1</td>
<td>4.7%</td>
<td>9.6%</td>
<td>0.31</td>
<td>0.50%</td>
<td>0.15%</td>
</tr>
<tr>
<td>Portugal</td>
<td>16.0</td>
<td>3.7%</td>
<td>8.1%</td>
<td>0.98</td>
<td>1.59%</td>
<td>0.50%</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>9.3</td>
<td>2.2%</td>
<td>16.0%</td>
<td>0.05</td>
<td>0.08%</td>
<td>0.08%</td>
</tr>
<tr>
<td>Czechia</td>
<td>8.9</td>
<td>2.1%</td>
<td>4.7%</td>
<td>0.24</td>
<td>0.39%</td>
<td>0.13%</td>
</tr>
<tr>
<td>Netherlands</td>
<td>8.8</td>
<td>2.0%</td>
<td>1.2%</td>
<td>1.6</td>
<td>2.60%</td>
<td>0.21%</td>
</tr>
<tr>
<td>Hungary</td>
<td>8.5</td>
<td>2.0%</td>
<td>6.7%</td>
<td>0.35</td>
<td>0.58%</td>
<td>0.28%</td>
</tr>
<tr>
<td>Slovakia</td>
<td>8.1</td>
<td>1.9%</td>
<td>9.0%</td>
<td>0.15</td>
<td>0.24%</td>
<td>0.17%</td>
</tr>
<tr>
<td>Belgium</td>
<td>7.6</td>
<td>1.7%</td>
<td>1.6%</td>
<td>1.9</td>
<td>3.09%</td>
<td>0.41%</td>
</tr>
<tr>
<td>Croatia</td>
<td>7.5</td>
<td>1.7%</td>
<td>15.4%</td>
<td>0.24</td>
<td>0.39%</td>
<td>0.49%</td>
</tr>
<tr>
<td>Sweden</td>
<td>5.5</td>
<td>1.3%</td>
<td>1.2%</td>
<td>0.9</td>
<td>1.46%</td>
<td>0.20%</td>
</tr>
<tr>
<td>Austria</td>
<td>4.8</td>
<td>1.1%</td>
<td>1.3%</td>
<td>1</td>
<td>1.63%</td>
<td>0.26%</td>
</tr>
<tr>
<td>Lithuania</td>
<td>3.9</td>
<td>0.9%</td>
<td>8.6%</td>
<td>0.06</td>
<td>0.10%</td>
<td>0.14%</td>
</tr>
<tr>
<td>Finland</td>
<td>3.9</td>
<td>0.9%</td>
<td>1.7%</td>
<td>0.79</td>
<td>1.28%</td>
<td>0.35%</td>
</tr>
<tr>
<td>Latvia</td>
<td>2.9</td>
<td>0.7%</td>
<td>9.9%</td>
<td>0.04</td>
<td>0.06%</td>
<td>0.13%</td>
</tr>
<tr>
<td>Denmark</td>
<td>2.8</td>
<td>0.6%</td>
<td>0.9%</td>
<td>0.35</td>
<td>0.58%</td>
<td>0.12%</td>
</tr>
<tr>
<td>Slovenia</td>
<td>2.7</td>
<td>0.6%</td>
<td>5.9%</td>
<td>0.12</td>
<td>0.19%</td>
<td>0.26%</td>
</tr>
<tr>
<td>Ireland</td>
<td>2.4</td>
<td>0.5%</td>
<td>0.9%</td>
<td>0.99</td>
<td>1.61%</td>
<td>0.39%</td>
</tr>
<tr>
<td>Estonia</td>
<td>1.9</td>
<td>0.4%</td>
<td>7.2%</td>
<td>0.01</td>
<td>0.01%</td>
<td>0.03%</td>
</tr>
<tr>
<td>Cyprus</td>
<td>1.5</td>
<td>0.3%</td>
<td>7.6%</td>
<td>0.1</td>
<td>0.16%</td>
<td>0.51%</td>
</tr>
<tr>
<td>Malta</td>
<td>0.4</td>
<td>0.1%</td>
<td>3.2%</td>
<td>0.01</td>
<td>0.02%</td>
<td>0.11%</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>0.3</td>
<td>0.1%</td>
<td>0.7%</td>
<td>0.03</td>
<td>0.05%</td>
<td>0.08%</td>
</tr>
</tbody>
</table>

Source: Bruegel estimates based on European Commission data.
Rapid implementation

Launching the NGEU quickly will be crucial to turn the tide on the economic crisis. In July 2020 the European Commission invited Member States to come forward before the October European Council with proposals on how to accelerate and facilitate procedures in each country.

Conditionality

Conditionality and continued control will be unavoidable. Resources will be approved if they are aligned to the European Semester’s guidelines (i.e. economic stability, innovation, digitisation and productivity, green deal and social fairness) and if the country reaches the targets previously committed. This is a powerful incentive for countries such as Spain that do not score high on reforms (outside a crisis period) and that can improve in the design or implementation of European projects.

European Commission will assess if funds follow the country-specific recommendations with more political control by the European Council (qualified majority).

Rebates and repayment

Richer countries will continue to receive rebates for the period 2021-2027 from the multi-year budget to reduce the net contributions based on GNI.

As proposed by the Commission, the borrowing by the EU will be repaid not later than 2058 and not before 2027 unless new own resources have been introduced.

Funding

NGEU will be funded through debt issuances, 70% up to 2022 and the rest in 2023. NGEU bonds will be rather liquid (the total amount outstanding would reach 750 billion euros by 2023, which compares with EIB 460 billion euros; ESM 100 billion, EFSF 200 billion, Germany 1.5 trillion, France 1.8 trillion, Italy 2 trillion and Spain 1 trillion). Moreover, the bonds would be well demanded, as they are expected to receive a high grade from rating agencies. Their main competitors would be core bonds.

The amounts of the Own Resources ceilings, the capacity to ask countries to contribute to the EU budget, will be temporarily increased by 0.6 percentage points, with the purpose to cover all liabilities of the EU resulting from its borrowing to address the consequences of the COVID-19, until all these liabilities have ceased to exist and at the latest until 2058. In any case, new Own Resources could be introduced or discussed after 2021, including a new one based on non-recycled plastic waste, to be introduced and applied as of 1 January 2021; proposals on a carbon border adjustment mechanism and on a digital levy in the first Semester of 2021 (at the latest by 1 January 2023); and other own resources, which may include a Financial Transaction Tax in the next MFF 2021-2027.
Evaluation

Europe reached an agreement to tackle the strong differences across countries and to maintain the size of the recovery fund that adds to the previous 3 safety nets already approved (SURE, ESM, EIB, together reaching 540 billion euros, or 4% of EU GDP) and EU countries’ fiscal stimulus of around 8% in 2020. This could help to prevent different fiscal responses across countries, bolster the functioning of the single market and support the economic recovery across the region, while strict control on the use of the funds will be positive in ensuring that investment and reforms increase potential growth and facilitate the transition to a green and digital economy. In addition, the increase in supranational debt to finance the NGEU will strengthen and complement the ECB’s stance (asset purchases programme), while reinforcing fiscal coordination. Although we are still far from it, it could be the seed for common fiscal stabilisers at the European level.

7.4.3. MAIN PILLARS AND INSTRUMENTS OF NEXT GENERATION EU

NGEU will be rolled out under three pillars: tools to support Member State efforts to recover, repair and emerge stronger from the crisis; measures to boost private investment and support ailing companies; and the reinforcement of key EU programmes to draw lessons from the crisis and make the single market stronger and more resilient (see Table 4).

TABLE 4. THREE PILLARS OF NGEU

<table>
<thead>
<tr>
<th>Pillar 1: Supporting Member States to recover</th>
<th>Pillar 2: Kick-starting the economy and helping private investment</th>
<th>Pillar 3: Lessons learnt from the crisis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recovery and Resilience Facility</td>
<td>Solvency Support Instrument</td>
<td>Programmes to build resilience and strengthen cooperation</td>
</tr>
<tr>
<td>REACT-EU</td>
<td>Enhanced InvestEU: Strategic Investment Facility</td>
<td></td>
</tr>
<tr>
<td>Cohesion policy</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reinforced Just Transition Mechanism</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rural areas</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Own preparation based on European Commission information.

PILLAR 1: Supporting Member States to recover, repair and emerge stronger from the crisis

Public investment will play a crucial role to reach a balanced and sustainable recovery. In fact, more than 80% of the funding from Next Generation EU will be used to support public investment and structural reforms in Member States, concentrated where the crisis impact and resilience needs are highest.
The Recovery and Resilience Facility (RRF), together with cohesion policy and the Just Transition Mechanism, will be essential to achieve these important goals. In addition, the reinforced European Agricultural Fund for Rural Development will support rural areas to make the structural changes necessary under the European Green Deal.

❖ RECOVERY AND RESILIENCE FACILITY: THE CENTRAL PILLAR OF NGEU

The Recovery and Resilience Facility, embedded in the European Semester, will be a central pillar of NGEU. It will offer large-scale financial support for investments and reforms, including in the green and digital transitions, to make economies more resilient. It will be concentrated in the most affected areas of the EU, helping to balance divergences between Member States and to prepare the economies for the future.

In September 2020, the European Commission set out strategic guidance for the implementation of the Recovery and Resilience Fund in its 2021 Annual Sustainable Growth Strategy (ASGS) and on 11 November, the Facility was adopted by the European Parliament. The Facility will provide an unprecedented 672.5 billion euros in grants and loans to support EU countries for four years: grants worth a total of 312.5 billion euros (see Table 5) and loans a total of 360 billion euros.

The new ASGS is fully aligned with the previous one, in which the European Commission launched a new growth strategy based on the European Green Deal and the competitive sustainability concept. The four dimensions of environmental sustainability, productivity, fairness and macroeconomic stability identified in the previous one remain the guiding principles underpinning national recovery and resilience plans and their reforms and investments. These dimensions lie at the heart of the European Semester and ensure that the new growth agenda helps to build foundations for a green, digital and sustainable recovery.

European Parliament agreed that the Recovery and Resilience Facility should only be available to Member states that respect the rule of law and the EU’s fundamental values. National recovery and resilience plans should be consistent with six priorities – green transition, digital transformation, economic cohesion and competitiveness, social and territorial cohesion, institutional crisis-reaction and crisis preparedness – as well as with NGEU policies, which include the European Skills Agenda, the Youth Guarantee and the Child Guarantee. The Parliament also considers that each plan should contribute at least 40% of its budget to climate and biodiversity and at least 20% to digital actions. The plans should also have a lasting impact on European countries in both social and economic terms and provide comprehensive reform and a robust investment package.

EU funding should be visible and implemented transparently. The European Commission, responsible for the Recovery and Resilience Facility implementation, will submit to the Parliament twice a year a report on how the targets have been implemented as well as the amounts paid to each country. The recipients should ensure that spending under the Facility is visible by clearly labelling the projects as “European Union Recovery Initiative”.

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An allocation key will fix a maximum amount for the grant of the Recovery and Resilience Facility per Member State. For 70% of the total grants, the allocation key will take into account the population, the inverse of GDP per capita and the average unemployment rate over the period 2015-2019, compared to the EU average. For the remaining 30%, the 2015-2019 unemployment rate will be replaced by the observed loss in real GDP in 2020 and the observed cumulative loss in 2020-2021. For loans, the maximum volume for each Member State will not exceed 6.8% of its GNI. However, an increase will be possible in exceptional circumstances subject to available resources.

**TABLE 5. RECOVERY AND RESILIENCE FACILITY: GRANTS**

![Allocation key](image)

<table>
<thead>
<tr>
<th>Allocation Key</th>
<th>2021-2022</th>
<th>2023</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population share</td>
<td>€218.75 billion</td>
<td>€93.75 billion</td>
</tr>
<tr>
<td>Inverse GDP per capita</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unemployment 2015-2019</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Own preparation based on European Commission information.

There has been some debate about the Recovery and Resilience Facility allocation criteria and structural objectives. The allocation criteria are based on indicators with a certain cyclical component while the Facility’s objectives are structural (green and digital transformation, macro stabilisation and fiscal unity).

❖ **RECOVERY ASSISTANCE FOR COHESION AND THE TERRITORIES OF EUROPE (REACT-EU)**

Recovery Assistance for Cohesion and the Territories of Europe (REACT-EU) is an initiative to increase cohesion support and make economies more resilient and sustainable. It will help to bridge the gap between the initial response to the pandemic (Coronavirus Response Investment Initiatives) and longer-term recovery, contributing to a green, digital and resilient recovery.

Through REACT-EU, the European Commission will provide 55 billion euros of additional cohesion policy funding between 2020 and 2022 (almost 50 billion euros from Next Generation EU in 2021 and 2022 and 5 billion euros as early as 2020 by adapting the current financial framework).

REACT-EU will be based on the current cohesion rules, including the emergency flexibility introduced by the Coronavirus Response Investment Initiatives. Under these proposals, additional funding will be provided in 2020-2022 for the current cohesion.
programmes as well as the Fund for European Aid to the Most Deprived, allowing funding for key crisis repair measures and support to the most deprived to continue without interruption.

The REACT-EU funding will be distributed among Member States taking into account the severity of the economic and social impacts of the crisis, including the level of youth unemployment and the relative prosperity of Member States. The European Commission proposed that 50% of REACT-EU additional resources for 2020 will be paid to Member States as pre-financing immediately, following the approval of the programme amendment concerned, and pre-financings in the following years will be paid with additional resources allocated to programmes. The generous EU-financing rate will contribute to a fast roll-out of this additional funding.

❖ **COHESION POLICY**

*Cohesion policy* will be crucial to ensure a balanced recovery in the longer term, avoiding divergences of growth between countries. For this purpose, the European Commission considers it essential to launch the new cohesion policy programmes at the beginning of 2021, in parallel with other funds available for the current programmes until the end of 2022.

The Commission is adjusting its proposals for the future cohesion policy to give even stronger support to recovery investments, for example in resilience of national healthcare systems, in sectors such as tourism and culture, small and medium-sized enterprises, youth employment, education skills and child poverty.

Young people are likely to be particularly hard hit by the crisis. So, Member States with youth unemployment levels above the European average should allocate at least 15% of their European Social Fund Plus resources to help this group. The Commission also proposed that at least 5% of the Fund should be used to reduce child poverty.

To ensure sufficient support to most needed Member States and areas, the European Commission also suggests a review of national cohesion allocations in 2024, according to the latest available statistics. This review will lead to upward adjustments of only up to 10 billion euros for all Member States.

❖ **REINFORCED JUST TRANSITION MECHANISM**

The *Just Transition Mechanism* (JTM) will be a key tool to ensure that the transition towards a climate-neutral economy happens in a fair way. With this Mechanism it is expected to mobilise up to 150 billion euros through three pillars: a new Just Transition Fund, InvestEU and the European Investment Bank (EIB) public sector loan facility (see Table 6).
TABLE 6. JUST TRANSITION MECHANISM

<table>
<thead>
<tr>
<th>Just Transition Fund (up to €89-107 billion)</th>
<th>InvestEU (up to €30 billion)</th>
<th>EIB loan facility (up to €30 billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>JTF €40 billion</td>
<td>Investment generated by €1.8 billion</td>
<td>Investment generated by €1.5 billion EU budget and €10 billion EIB lending</td>
</tr>
<tr>
<td>ERDF/ESF+ transfers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nacional co-financing</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Primarily grants</td>
<td>Crowds in private investments</td>
<td>Leverages public financing</td>
</tr>
</tbody>
</table>

Source: Own preparation based on European Commission information JustTransitionMechanism

The Just Transition Fund (JTF) will be equipped with 40 billion euros, an amount corresponding to fresh money made available to support European countries in their transition (10 billion euros should come from budget appropriations), while the remaining additional resources, covering the period 2021-2024, will constitute external assigned revenue stemming from the European Recovery Instrument.

To unlock funding from the JTF, Member States will have to match each euro received from this Fund for the share financed from the Union budget (10 billion euros) with 1.5 to 3 euros from their resources of the European Regional Development Fund (ERDF) and the European Social Fund Plus (ESF+). This spending from the EU budget will be supplemented by national co-financing according to cohesion policy. The total financing capacity of the JTF could reach between 89 billion euros and 107 billion euros.

The Fund will help to alleviate the socio-economic impacts of the climate transition in the most affected territories, by supporting the re-skilling of workers, helping small and medium enterprises to create new economic opportunities and investing in clean energy and circular economy.

The increase in InvestEU funds means that the second pillar of the Just Transition Mechanism will also be reinforced. Up to 1.8 billion euros will be focused on just transition goals. However, InvestEU will not only support investments in just transition territories, but also in other regions and in a wider range of projects (energy and transport infrastructure, including gas infrastructure and district heating; decarbonisation; economic diversification and social infrastructure). The final use of InvestEU will remain demand-driven and will depend on the project pipeline and the capacity of the regions concerned.

Finally, with a contribution from the EU budget of 1.5 billion euros, the public sector loan facility will enable the EIB to lend 10 billion euros, which is expected to mobilise
between 25 and 30 billion euros of public investments supporting a just transition over the period 2021-2027.

These loans would provide the public sector with resources to implement measures to facilitate the climate-neutral transition. Supported investments will range from energy and transport infrastructure, district heating networks, energy efficiency measures including renovation of buildings, as well as social infrastructure.

❖ RURAL AREAS: EUROPEAN AGRICULTURAL FUND FOR RURAL DEVELOPMENT

Rural areas will have a vital role to play in delivering the green transition and reaching the environmental targets. To that end, the budget for the European Agricultural Fund for Rural Development will be reinforced with 15 billion euros to support farmers and rural areas in making the structural changes necessary in line with the European Green Deal.

PILLAR 2: Kick-starting the economy and helping private investment

Urgent action is needed to kick-start the European economy and to create the conditions for a recovery led by private investment in key sectors and technologies – from 5G to artificial intelligence (AI) and from clean hydrogen to offshore renewable energy. This investment holds the key to Europe’s future and will need at least 1.5 trillion euros in 2020-2021.

Different instruments will be used to reach these objectives. A new Solvency Support Instrument will provide urgent equity support for companies damaged by the crisis. This will also help companies in their green and digital transformation.

Moreover, InvestEU will be used to mobilise investment in sustainable infrastructure and digitisation, and a new Strategic Investment Facility will be created to invest in key value chains, which are very important for the future and strategic autonomy of Europe.

❖ SOLVENCY SUPPORT INSTRUMENT

The European Commission proposed a new Solvency Support Instrument to mobilise private resources and provide urgent support to viable companies from economic sectors that are suffering due to the crisis. This instrument will be temporary and will help to avoid massive capital shortfalls and possible defaults of viable firms.

It will mobilise private investment in troubled companies by providing partial guarantees against losses. The EU budget will provide a guarantee of about 75 billion euros to the European Investment Bank, which will ensure rapid delivery. The instrument will aim for an investment level of 300 billion euros in solvency support. The guarantee will be calibrated to ensure that investments are targeted at those companies that are in greatest need of capital, particularly in Member States less able to intervene through state aid and sectors with severe crisis effects.

In addition, the capital of the European Investment Fund will be increased in order to provide support to a wide range of small and medium-sized enterprises, including through implementation of the Solvency Support Instrument. This would further add
to building a comprehensive package for European recovery, also in conjunction with the measures agreed by the European Council in April. This capital increase of up to 1.5 billion euros will be financed both under the present and the next Multiannual Financial Framework.

❖ ENHANCED INVESTEU: STRATEGIC INVESTMENT FACILITY

A Strategic Investment Facility will be created as an additional window under InvestEU. This facility will support projects contributing to building strong and resilient value chains across the EU and enhancing the autonomy of the Union’s single market, while maintaining its openness to competition and trade in line with its rules. This will enhance the resilience of the EU economy whilst providing the resources for important companies to prosper and grow.

With provisioning of 15 billion euros from Next Generation EU, the new facility would provide an EU budget guarantee of 31.5 billion euros and could generate investments of up to 150 billion euros to encourage European industrial leadership in strategic sectors and key value chains. The window will ensure that such investments exploit the potential of the Single Market, with the EU budget guarantee supporting companies and becoming a powerful instrument of recovery.

PILLAR 3: Lessons learnt from the crisis and addressing Europe’s strategic challenges

❖ PROGRAMMES TO BUILD RESILIENCE AND STRENGTHEN COOPERATION

Next Generation EU will provide targeted reinforcement for key programmes that power growth and strengthen Europe’s ability to survive and overcome future crises. These reinforcements are in addition to the European Commission’s initial proposals for the future framework, recently approved by the Parliament.

A new programme to strengthen health security and cooperation

The crisis has shown that investments in healthcare systems must be reinforced in the future financial framework. To this end, the European Commission proposed an ambitious stand-alone EU4Health programme, amounting to 9.4 billion euros. The programme will help ensure that the EU is well prepared to react to future health crises.

The first component of the programme will address health security and crisis preparedness. It will support investments in health infrastructure, tools, structures, processes, and laboratory capacity, including tools for surveillance, forecasting, prevention and management of outbreaks. It will also support the establishment of a mechanism to develop, procure and manage health crisis relevant products such as medicines (vaccines) and treatments, their intermediates, active pharmaceutical ingredients and raw materials, and medical devices and medical equipment such as ventilators, protective clothing and equipment, diagnostic materials and tools. It will help create a new EU-wide risk communication framework covering all phases of a crisis.
The second component will support a longer-term vision of improving health outcomes via efficient and inclusive health systems across the Member States, through better disease prevention and surveillance, health promotion, access, diagnosis and treatment, and cross-border collaboration in health. The programme will support, among others, capacity building in countries, training programmes for staff and digital transformation of the health sector.

The programme will link up with relevant support provided under other European programmes and will establish new ways to implement joint actions. It will work with a reinforced rescEU, focused on direct crisis response capacities in emergency situations.

*Reinforcing the EU response capacity to emergencies: rescEU*

One of the lessons learnt from COVID-19 is that we must be able to react more quickly and flexibly in severe crises given the size of the potential disruption to the economy and society. To reinforce the EU’s civil protection capacity to ensure a timely and effective response to large-scale emergencies, the Union’s civil protection mechanism, rescEU, will be reinforced.

Its financial allocation will be 3.1 billion euros, financing investments in emergency response infrastructure (storage capacity, transport of medicines, doctors and patients) within the EU or bringing them in from outside the EU. The upgraded rescEU will give Europe the capacity and the logistical infrastructure needed to cater for different types of emergency, including those with a medical component, complementing the new EU-4Health programme.

*Horizon Europe – investing in innovation and preparedness for the future*

At the end of September 2020, the European Council finalized its position on the proposed regulation establishing Horizon Europe, the EU framework programme for research and innovation in 2021-2027 (Horizon Europe regulation) and on the proposed decision on the specific programme implementing Horizon Europe (specific programme decision).

The main outstanding issue of the *Horizon Europe regulation* concerns the internal break-down of Horizon Europe’s budget, including funds to be made available under NGEU. The Council also agreed on provisions regulating international cooperation and the association of third countries as well as provisions ensuring synergies with other programmes.

Horizon Europe will amount to 94.4 billion euros to increase European support for health and climate-related research and innovation activities. This will also contribute to strengthened capacity to effectively and rapidly respond to emergencies and invest in science-driven solutions.

In the health sector, the reinforcement will be used to scale up research for challenges such as the pandemic, clinical trials, innovative protective measures, vaccines and treatments and diagnostics, and to translate these findings into public health policy measures.
**Global response and solidarity with the rest of the world**

The pandemic is a global challenge and the response must be global. Otherwise, every country and region in the world will remain vulnerable. The EU must continue demonstrating solidarity with its partners across the world in the fight against COVID-19.

The European Commission proposes to set the *Neighbourhood, Development and International Cooperation Instrument* at 87 billion euros, via a new External Action Guarantee, and the European Fund for Sustainable Development to support partners – in particular in the Western Balkans, the Neighbourhood and the rest of Africa – in cooperation with international financial institutions, such as the United Nations and the World Health Organization. A targeted adjustment to the current financial framework will allow 1 billion euros of additional support to be made available as early as 2020.

This support will provide liquidity to small and medium-sized enterprises, preserve investments in renewable energy projects and increase the capacity of funding in local currencies in other countries to reinforce health care systems and build manufacturing capacity for COVID-19 treatments and diagnostics. This will also help the most vulnerable countries and regions, addressing the severe social and economic effects of the crisis.

An increase of 5 billion euros will reinforce the *Humanitarian Aid Instrument*, reflecting growing humanitarian needs in the most vulnerable parts of the world. The impact of the pandemic and the economic fall-out, for example the loss of income due to collapsing oil and raw material prices and a drastic fall in remittances, are compounding existing needs, making it all the more important that the EU is prepared to demonstrate solidarity with the rest of the world.

**Long-term financial framework for a more flexible and resilient EU**

Strong measures to protect the European budget against fraud and irregularities are in place and the Commission will strengthen them further. The *European Anti-Fraud Office* (OLAF) and the *European Public Prosecutor’s Office* (EPPO) will exercise their control and investigation powers.

In addition to the reinforcements financed under NGEU, other programmes will be covered to address challenges heightened by the pandemic and make the EU more resilient. These include:

- A total of 8.2 billion euros for the *Digital Europe Programme* to boost the Union’s cyberdefences and support the digital transition.
- Investing in an up-to-date, high-performance transport infrastructure to facilitate cross-border connections, through an additional 1.5 billion euros for the *Connecting Europe Facility*.
- The *Single Market Programme* and programmes supporting cooperation in the fields of taxation and customs (3.7 billion euros, 239 million euros and 843 million euros, respectively), will create the conditions for a high-functioning single market.
- Investing in young people, through an additional 3.4 billion euros for *Erasmus Plus*, and in the cultural and creative sectors, increasing the *Creative Europe* to a level of 1.5 billion euros.
THE EURO IN 2021

- Strengthening the resilience of the agri-food and fisheries sectors and providing the scope for crisis management, through an additional 4 billion euros for the Common Agricultural Policy and 500 million euros for the European Maritime and Fisheries Fund.

- Reinforcing the Asylum and Migration Fund and Integrated Border Management Fund, reaching a level of 22 billion euros, to step up cooperation on external border protection and migration.

- Increasing the Internal Security Fund to 2.2 billion euros and the European Defence Fund to 8 billion euros, with the end of ensuring strong support for European strategic autonomy and security.

- Supporting our partners in the Western Balkans by bringing the Union’s pre-accession assistance to a level of 12.9 billion euros.

With these targeted adjustments, the European Union will have a long-term financial framework better aligned with its priorities and tailored to reach a resilient recovery in the future.

7.4.4. NGEU AND NATIONAL PLANS

EU Member States have to prepare recovery and resilience plans that set out a coherent package of reforms and public investment projects to be implemented up to 2026 in order to be supported by the Recovery and Resilience Facility (RRF). These plans must be aligned to the priorities of the European Semester (i.e. economic stability, digitisation and productivity, green deal and social fairness) and should demonstrate how the investments and reforms would effectively address challenges identified in this context, particularly the country-specific recommendations adopted by the Council (see Table 7). The national plans should also include measures to address the challenges faced by the countries regarding the green and digital transitions.

**TABLE 7. NATIONAL PLANS AND EUROPEAN SEMESTER**

<table>
<thead>
<tr>
<th>National plans should be aligned to the priorities of the European Semester</th>
</tr>
</thead>
<tbody>
<tr>
<td>Economic Stability</td>
</tr>
<tr>
<td><strong>Activation of the general escape clause: preserve jobs, help firms and support the recovery</strong></td>
</tr>
<tr>
<td><strong>A supportive fiscal stance is currently warranted</strong></td>
</tr>
<tr>
<td><strong>Activation of the general escape clause: preserve jobs, help firms and support the recovery</strong></td>
</tr>
<tr>
<td><strong>Activation of the general escape clause: preserve jobs, help firms and support the recovery</strong></td>
</tr>
</tbody>
</table>

Source: Own preparation based on European Commission information.
Member States can submit their recovery and resilience plans from the moment the Facility is legally in force (1 January 2021, according to Commission expectations) and before 30 April 2021. Given the comprehensive and forward-looking policy nature of the plans, there will be no need for the Commission to propose country-specific recommendations in 2021 for those countries that will have submitted it. Nevertheless, the European Commission will propose fiscal recommendations as envisaged under the Stability and Growth Pact.

**Climate transition**

Regarding the Green transition, NGEU is part of a broader policy package to drive the EU towards a net-zero emissions economy by 2050. It must be completed with carbon pricing policies that are both predictable and credible.

Member States should consider reforms and investments to maintain the climate transition as a priority. To follow the commitment of the European Council to achieve a climate mainstreaming target of 30% for both the multiannual financial framework and Next Generation EU, each national recovery and resilience plan will include a minimum of 37% of expenditure related to climate. Progress towards other environmental objectives is also important, in line with the European Green Deal.

The European Commission encouraged Member States to propose flagship investment and reform initiatives aimed at accelerating the development and use of renewables, improving the energy and resource efficiency of public and private buildings and accelerating the use of sustainable, accessible and smart transport. The reforms and investments included in the national plans will need to respect the ‘do no harm’ principle, meaning that they should not be to the detriment of climate and environmental objectives.

Member States will need to factor in the need to ensure a just and socially fair transition across green policy areas. In particular, national plans should be developed in full coherence with the proposed Territorial Just Transition Plans under the Just Transition Mechanism.

**Digital transition**

As part of the national plans, Member States should also ensure a high level of reforms and investments enabling the digital transition. The Commission proposed that each plan should include at least 20% of digital expenditure. This includes investing in 5G and Gigabit connectivity, developing digital skills through reforms of education systems and increasing the availability and efficiency of public services by using new digital tools.

7.4.5. **NEXT GENERATION EU: IMPACT AND IMPLICATIONS**

**Impact on economic growth: ‘fiscal multiplier’**

According to the European Commission's estimates, the new fiscal stimulus (5.4% of EU GDP) could raise GDP by more than 4% in 2024 for some countries. Together, the fiscal support, including automatic stabilisers, could reach 16% of GDP in three years.

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The estimated impact is significant in those countries with income per capita below the EU average and those with high debt (Greece, Spain, Portugal, Italy), but rich countries also gain. On average, the mobilised investment is estimated to increase real EU GDP levels by around 1.75% in 2021 and 2022, rising to 2.25% by 2024 (see Figure 2). Due also to the productivity-enhancing nature of the supported investments, economic output remains persistently above baseline levels in the medium and long term (around 1%). It should be noted that these figures are estimated by considering several assumptions about the amount of funds to be spent, the implementation schedule, the distribution between grants and loans and the type of project, among others.

The theoretical literature reveals that ‘fiscal multipliers’ are higher in economic recessions since, as the economy is far from its potential capacity, the fiscal impulse is less likely to crowd out private investment. In any case, there is high uncertainty over the ‘fiscal multiplier’ levels to be applied to each public expenditure category. Theoretical and empirical models suggest that public investment expenditure has a larger and more durable impact on activity than government consumption or transfers to households. Public investment not only increases demand in the short term, but also helps to expand capital stock and potential growth. In particular, for Spain the literature releases a wide range of levels for public investment fiscal multipliers, from 0.5 to 1.3.

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Although factors associated with the current crisis (uncertainty, recession, EU coordination, etc) could point to higher multipliers, structural imbalances of each country (ageing, high public debt, etc) could indicate lower values. However, the magnitude of the fiscal multiplier will depend, to a large extent, on how the support will be invested and what structural reforms are implemented.

**An opportunity for Europe to go ahead with integration and financial stability**

NGEU is a great opportunity for Europe to go ahead with integration and financial stability. This is a way to walk towards a fiscal union which is forward-looking and not legacy-based. Together with the MFF 2021-2027, NGEU will ensure a coordinated European fiscal response to the economic fallout from the pandemic. While the 2008 European Economic Recovery Plan was only intended to coordinate national budgetary stimulus to be financed by each Member State, NGEU establishes a joint funding model to support government spending and reform the EU.

Even if the nature of the NGEU is temporary, it sets a precedent in different areas that could survive in the long term, unlike past attempts to evolve towards a fiscal union based on proposals of Eurobonds and/or mutualisation of legacy debt, which have met strong opposition from some countries. The fund will be financed through common bonds backed by all countries, a potential precedent of a safe European asset. This is the first time the EU issues debt to finance its own spending. The size of the fund implies that annual issuance will be equivalent to that of a large EU country, and could be used by the ECB for its QE purchases. This sort of eurobond could create a precedent for the future and increase the international role of the euro.

**TABLE 8. NGEU: POTENTIAL IMPLICATIONS**

| The NGEU agreement is a major step forward, with potential implications for several issues |
|---------------------------------|----------------------------------------------------------------------------------|
| Growth                         | Redistribution issues (net transfers favors most affected countries)               |
|                                 | Digital and Green, more sustainable growth                                      |
| Integration and financial stability | Higher role of fiscal policy to complement monetary policy                     |
|                                 | Safe asset for Europe                                                           |
|                                 | Step to Fiscal Union                                                            |
|                                 | Growing weigh of the euro as an international currency                         |
| Political                       | Enhanced role of the European Commission                                       |

Source: Own preparation based on European Commission information.

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A powerful countercyclical fiscal instrument

NGEU is a powerful countercyclical fiscal instrument that could lead in the future to an EU-wide fiscal stance, a recurrent demand by institutions such as the European Central Bank (ECB) and the International Monetary Fund (IMF). The fiscal stimulus will complement the efforts of monetary policy to sustain the economy. Again, it creates a precedent for a more permanent fiscal policy instrument at the EU level in the future.

NGEU is a very positive step forward but still, concerns of debt sustainability remain, given the magnitude of the crisis. It should improve the fiscal stance in more vulnerable countries even with conservative assumptions on fiscal multipliers, but it leaves some of them, such as Spain and Italy, in a dangerous zone in the medium-term, with still very high debt levels.

Moreover, with the NGEU the risk of euro break-up should be reduced and the role of the euro as an international currency reinforced. Not only is the risk of recession mitigated by the fund, but also the commitment shown by the response with the European project has been reflected in the reinforcement of the euro exchange rate over the past weeks.

It will be crucial to ensure that the fiscal support provided through NGEU is not counteracted by the early withdrawal of fiscal support funded at national level. Given the depth of the pandemic, the general escape clause set out in the Stability and Growth Pact was activated in March 2020 with likely extension through 2021. This will allow Member States to take the measures needed to combat the COVID-19, deviating from the adjustment requirements under the pact while not endangering fiscal sustainability.

NGEU opens the door to the creation of Own Resources, new taxes for the reimbursement of the debt issued by the EU. Though these new taxes need to be debated, they would eventually become permanent. Behind the scenes is the debate on digital, green and financial taxes, and the controversy of unequal corporate income taxes across countries.

The reaction to the crisis will also have implications for the future design and implementation of the European governance framework. While expansionary fiscal policy is necessary to sustain the recovery, going forward it will be important for the fiscal rules to effectively support the reduction of high government debt in good economic times. Moreover, NGEU constitutes a new and innovative element of the European fiscal framework. This innovation could imply lessons for Economic and Monetary Union, which still lacks a permanent fiscal capacity at supranational level for macroeconomic stabilisation in deep crises. The review of the economic governance framework provides a good opportunity to incorporate these important considerations.
7.5. CONCLUSIONS

At this time of extraordinary hardship and uncertainty, the European Union needed more than ever to show that it was ready and willing to act decisively and chart a path to a better tomorrow. Agreement on an ambitious recovery plan with the EU budget at its heart will give the EU the best possible chance of success.

NGEU will unlock the full potential of the EU budget to kick-start the economy and boost Europe’s sustainability, resilience and strategic autonomy. It builds on the Union’s experience of harnessing market financing and expands it to achieve the scale of support that is urgently needed in today’s circumstances.

A reinforced multiannual financial framework for 2021-2027 will guide the EU back from crisis to the path of long-term recovery, providing essential financing for immediate needs and for long-term investments in the green and digital transitions. The success of the recovery plan will depend not only on its scale and ambition, but also on the speed of action and the ability to adjust the response in the light of developments. Financial support is urgently needed in many parts of the Union to keep businesses afloat and support those in greatest need.

An early decision on the proposal to amend the current framework will allow additional funding to be made immediately available for REACT-EU, the Solvency Support Instrument and the European Fund for Sustainable Development, reflecting the urgency of these needs.

On 10 November 2020, the European Parliament and the European Commission reached an agreement on the NGEU and the next Multiannual Financial Framework, a package of 1.8 trillion euros, the largest ever financed through the EU budget. The success of this plan will be crucial for the recovery process and should help rebuild a greener, more digital and more resilient Europe.

[1] 1.25 billion euros from reflows from financial instruments and 250 million euros from the budget.


[3] The borrowing costs for the grant component of NGEU will be paid out of the EU budget. It is estimated that these costs will amount to up to 17.4 billion euros during the 2021-2027 financial framework.
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