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Basque vision for an EU Recovery Plan

Background

European authorities consider the COVID19 pandemic to be an "unusual circumstance beyond the control of the public authorities". Aware of the serious and exceptional nature of the situation right from the onset, European institutions reacted rapidly and adopted, with uncommon agility, the flexibility required to deal with both the health crisis and the economic consequences that it is causing.

The impact of those economic consequences has recently begun to be noted. Eurostat has thus released the estimate for the Eurozone as a whole and for the European Union. In the first case, the downturn on the previous quarter stood at 3.8% and was 3.5% in the second case. The respective year-on-year rates were -3.3% and -2.7%. The Spanish economy contracted even more intensely and was down 5.2% quarter-on-quarter, which is 4.1% year-on-year. All of these figures are unprecedented in the recent history of European economies. The situation is no better on the other side of the Atlantic. The longest period of growth in US recent history ended with a quarter-on-quarter downturn of 4.8%, even though in this case the year-on-year rate is still slightly positive (0.3%).

The second quarter figures will shed further light on this historic contraction of the world's economies, given that the consequences of the lockdown measures on the economy were only in the two last weeks of the first quarter.

The main EU institutions, without waiting for these figures, have launched important quantitative and qualitative actions to mitigate the economic consequences, including:

- The action by the ECB with its debt acquisition to the tune of €750 billion to keep the borrowing costs EU countries in check;
- The two programmes launched by the European Commission CRII and CRII+, ("*Coronavirus Response Investment Initiative*"), which have enabled a swift and effective response to release outstanding cohesion funds from the 2014-2020 period to meet the economic and health costs arising from the crisis;
- The approval by the Eurogroup on 9 April and subsequent confirmation by the European Council on 23 April of €540 billion in liquidity facilities for the States (through the European Stability Mechanism), for companies (through the European Investment Bank) and to avoid mass redundancies (through the new SURE Programme).

Nonetheless, the European Commission recognises that the main response will come from the budgets of the Member States, given the limited size of the EU budget. On 19 March, the European Commission adopted a Temporary Framework to allow Member States to fully harness the flexibility envisaged in the rules regarding state aid to support the economy in the context of the COVID-19 outbreak. This Temporary Framework was reviewed to extend the authorised types of aid on 3 April.

The Framework is based on Article 107 of the Treaty on the Functioning of the European Union (TFEU) in that regard. Thus, under the exception in Section 3.b of Article 107 of the TFEU, the Temporary Framework provides for five types of aid:

- Direct grants, selective tax advantages and repayable advances;
- Aid in the form of guarantees on loans by banks to companies;
- Subsidized interest rates on loans to companies;
- Safeguards for banks that channel state aid to the real economy;
- Short-term export credit insurance;

On 3 April, the authorised types of aid were extended to include:

- Support for coronavirus-related research and development (R&D);
- Support for the construction and upscaling of testing facilities;
- Support for the production of relevant products to tackle the coronavirus outbreak;
- Targeted support in the form of deferral of tax payments or suspensions of social security contributions;
- Targeted support in the form of wage subsidies for employees;

However, the mixed capability of the States of the Union to deploy this type of “bazookas” will lead to new distortions between countries and weaken the internal market. In fact, there is a clear risk of the internal market collapsing as the burden of the main response lies on the States. The application of the Temporary Framework will exacerbate the asymmetries between countries depending on their ability to assume new deficits, resort to new debt, etc. Those asymmetries will also be further aggravated by the different impact that the health crisis has had on the different EU States (measured in terms of hospital admissions, ICU admissions, deaths and their ratios in terms of population). Similarly, the productive structure of the States and their sectoral specialisation will condition the economic impact of the health crisis, as far as there will be no level playing field regarding the consequences of the lockdown measures and their subsequent de-escalation.

All these considerations point to the need for a second response level by the European institutions. Adopting a European Recovery Plan is thus essential to shore up the internal market in the medium term. That recovery plan will have to address the sharp contraction of the European economy overall and drive the bounce back of the internal market that will be weakened and fragmented by measures such as the Temporary Framework and others related to the pandemic. This Recovery Plan will have to foster sustainable and inclusive growth, by strengthening the resilience of EU territories, with priority given to the worst hit States and regions (NUTS 1 and 2) according to the following criteria:

1. Less budgetary manoeuvring ability
2. Degree of affectation of the pandemic
3. And the relative weight of the productive sectors worst hit by the economic consequences of the lockdown.

It is not just a matter of solidarity with the most exposed States and regions according to those three criteria, but also a question of safeguarding the internal market. In that regard, the aim is not to further deepen the imbalances and the asymmetries that erode away at the correct operating of the single market in general and of the euro in particular. Furthermore, those asymmetries end up exacerbating populist movements. They may have a real impact of the volume of direct foreign investments in infrastructures and, therefore, in strategic areas of the EU, thus threatening the future of the European project.

Interdependencies within the internal market are so great that they could lead to it fracturing in the current climate of trade wars, combatting climate change and the demographic and digital transition. That would end up eroding the foundations of the European Union irreversibly.

The interdependencies within the European Union underline the mutual need between all the countries. Thus, it should be noted that:

1. A lower appreciation of the euro has favoured exporting countries;

2. The Cohesion Policy has benefitted the countries in two ways: on the one hand, by means of the transfers received and, on the other hand, by the effect of enlarging the internal market;

3. The EMU has incentivised credit policies favouring surplus countries that have taken advantage of the risk premiums of deficit countries to place their capital to get better returns.

The gravity of the current situation requires an interdependent and integrating project such as the European one that seeks to implement policies to strengthen the ecosystem of the Union.

Characteristics of the EU Recovery Plan: a proportionate combination between transfers and loans

In view of the above, the Recovery Plan for Europe should be developed with the aim of guaranteeing and strengthening the internal market.

This requires levelling the intervention abilities of the different countries taking into consideration the aforementioned three criteria (less budgetary manoeuvring ability, degree of affectation of the pandemic and the relative weight of the productive sectors worst hit by the economic consequences of the lockdown), which would determine the degree of access to the Recovery Fund.

Therefore, there needs to be a combination of transfers and loans to offset the imbalances generated in the first response phase and to provide greater help to the countries that have been worst hit economically, socially and in health terms.

EU countries have not been hit by the pandemic in the same way and the impact on their economies has also been different. However, the majority of the States have been forced to put their economies in a coma. In the same way that COVID-19 patients have required different health care depending on their degree of affection, European economies also have to receive help according to nature and severity of the impact suffered. In the same way that no infected patient who is cured using paracetamol will feel discriminated that another patient has needed a ventilator to do so, no EU State that has recovered thanks to loans should feel discriminated that another has needed transfers to do so. That should be the virtue of the EU.

Furthermore, this Recovery Plan should be aligned (and access to it conditional on) with the two main lines of action for the coming decade, namely the New Green Deal and the Digital Transition for the EU, two global challenges that require local responses.

New transfer mechanism 2021-2024

The largest transfer plan for Europe so far, the Marshall Plan (1948-1951), would stand at $230 billion in today's dollars[1]. The new transfer mechanism should be ambitious and its allocation equivalent to the effort of the earlier one. It should be a transfer programme in the form of non-repayable grants for the period 2021-2024. Their distribution by countries and regions (NUTS 1 and 2) would be determined by the aforementioned three factors: budgetary manoeuvring ability, impact of the pandemic and relative weight of the worst hit productive sectors.

Additionally, it would have to consider that the tax system of the beneficiary countries has not favoured the existence of tax havens.

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[1] The 13 billion of 1948 would be equivalent to $140 billion in 2020. If we also take into account that that amount would be just over €500 per inhabitant (taking the inhabitants of the 18 beneficiary countries of that plan), that would be equivalent to a total of €230 billion in the current EU-27.

The New Transfer Plan would finance investments and actions related to the EU Green Deal and its relevant replicates in EU States and regions (NUTS 1 and 2), along with the digital transformation. In any event, the impetus to both transformations should guarantee inclusive growth within each State and among EU-27 States.

New Investment Plan 2021-2024

Simultaneously, a New Investment Plan would be set up (in its initial design, in the form of the so-called Juncker Plan and its subsequent INVEST EU names, it had a budget of €315 billion). That Plan will be able to leverage both public and private initiatives. In the case of the public initiatives, those credits would not count for the effects of the Stability and Growth pact. Consistent with the New Transfer Plan, European companies based in tax havens in and outside the EU would be denied the credit facilities of this New Investment Plan. Furthermore, all the public, private or public-private initiatives would be aimed at addressing the challenges of the EU Green Deal and the Digital Transition.

A new Recovery Plan with two instruments (transfer and loans) aligned with the Cohesion Policy Funds and in the framework of the Multiannual Financial Framework Plus (2021-2027)

The launch of the Recovery Plan consisting of transfer and loans requires an ambitious commitment to increase the EU budget to at least 2% of its National Income.

In order for the Recovery Plan to be aligned with the MFF 2021-2027 in general and with the Cohesion Policy Funds in particular, a high degree of coordination and coherence needs to be achieved between both instruments, as they share the social, economic and territorial cohesion targets of the European Union.

The gravity of the moment requires an ambitious response by the EU (and by its members) which is facing its greatest challenge since it was founded. A daring and intelligent response is therefore necessary, which takes into account the European common interest and offers an eco-systemic solution that recognises the growing interdependencies between its members in such an extraordinary situation as the current one.

A response is needed that reconciles EU citizens with a project that, far from being worn out, is able to offer solutions that would be impossible to reach working separately. There is no point in a country progressing alone along the path towards sustainability, if its other partners do not do so. Progressing thus only means going quickly but not very far. Progressing collectively may mean going more slowly, but ensuring that they will reach further.