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The EU's recovery fund faces two stumbling blocks

Opposition from the 'frugal four' and the allocation of funds call into question whether this can truly be Europe's moment

The 'Next Generation EU' (NG-EU) plan is the new clothes of the Recovery Fund, 'embedded within a powerful, modern and revamped long-term EU budget'. In announcing the plan, EU Commission President Ursula von der Leyen trumpeted: 'This is Europe's moment'. I'm inclined to believe that indeed it *may* be Europe's moment.

The Covid-19 pandemic has magnified many of the past EU weaknesses 'and created the risk of an imbalanced recovery, an uneven playing field and widening disparities', as the Commission writes. However, if the recovery plan will be passed later this month by the European Council, a milestone *may be* reached. Uncontrolled and uncoordinated growth in national public debts *may be* limited as a Community-level, larger, mainly grants-based budget instrument would be deployed, supported by an unprecedented common borrowing facility. At last the European phoenix of peace, prosperity and solidarity *may* rise from the ashes of the Covid-19 pandemic. A phoenix that *may* turn out to be economically and socially stronger than ever before and at the same time gentler to European citizens.

Still, there are a few details to be ironed out before rejoicing and relaxing.

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First, there is the stubborn opposition of the 'frugal four' (joined by Finland) to the NG-EU's €500bn grants as well as the strict conditionality they wish to see applied to the recipient countries. An official at the Dutch Ministry of Finance has recently said that loans are always to be preferred to grants – on the ground that loans create stronger incentives to an efficient use of money.

Even though there might be some micro-economic argument supporting the statement, all of these arguments sink in the face of the additional macro-stability costs implied by loans in the present EU context. The Dutch should know well: frugal Holland is sitting on one of the highest mountains of debt in the EU (350 per cent of GDP, of which 300 per cent private debt), followed by Sweden (329 per cent, of which 294 per cent private). The legendary profligate Italy has a total of 300 per cent (165 per cent as private debt), by far and large surpassed by Spain, Portugal and France.

It should also be noted that the frugal four have government expenditure per-capita far higher than the EU average (set equal to 100): Denmark 181; Sweden 156; Austria 148; Netherlands 134. On the other hand southern countries are below the EU average: Italy 98; Spain 76; Portugal 60; Greece 55. It seems that the self-praised frugal four are actually traditional 'tax and spend' countries, not less but more so than France and Germany.

A fair share of the pie

Second, the country allocation key for the NG-EU. On 27 May, the Commission staff released a working document aimed at assessing Europe's recovery needs. In the final pages of the document there was an 'allocation key' table, simulating how much each country would get from the NG-EU (both as grants and loans). The table was made public by Siegfried Mureșan, a Romanian Member of European Parliament, on his Facebook page. Subsequently, it received a lot of attention, despite the explanatory note stating that the table was purely illustrative 'for the sole purpose of the preliminary estimation of the potential impact of the recovery package'.

However, the table revealed a potential political problem. Poland, according to the table, was to receive €64.5bn, the fourth largest amount in the entire European Union, topped only by Italy (153bn), Spain (149.3bn) and France (78bn).

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These are not the figures one can read in the press. All the same, Poland's Prime Minister Mateusz Morawiecki told his fellow 'Visegrad' heads of government that Poland is ready to support approval of the Economic Recovery Fund 'to the extent that it will fulfil our expectations and needs'. But the Polish economy has been one of the least affected by the coronavirus crisis and the 'expectations and

needs' of Warsaw on its share of the NG-EU funds should accordingly be rather on the scant side. Moreover, the Polish government has faced criticism over its approach to the rule of law and, not long ago, the Commission was planning to withhold funds from EU governments that endanger the rights of its citizens.

The purely 'illustrative allocation key' emphasises low GDP per capita with respect to EU average (it inflates the funds going to relatively poor Eastern countries) rather than the actual population size and the impact of the Covid-19 crisis – as measured, for instance, by the national share (with respect to the EU total) of infected people or the national share of deaths (which would bias the allocation in favour of Spain, Italy, Germany and France). On the contribution side, payments were apparently only linked to GDP, making the landing even softer for the Visegrad group, as well as Romania and Bulgaria.

The frugal four (and Germany) are penalised more by the 'illustrative allocation key' than by any alternative, reasonably weighted algorithm, coupled by a contribution key only based on population, as I previously suggested. It wouldn't be surprising if the frugal four made a new political stumbling block out of a simple technical slipup to let the whole process derail.



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