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ΕΛΛΗΝΙΚΟ ΙΔΡΥΜΑ ΕΥΡΩΠΑΪΚΗΣ & ΕΞΩΤΕΡΙΚΗΣ ΠΟΛΙΤΙΚΗΣ
HELLENIC FOUNDATION FOR EUROPEAN & FOREIGN POLICY
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Greek & European Economy Observatory

9th Newsletter on the economic impact of the Covid-19 pandemic

European Developments (15-22/05)

"We need rapid economic recovery. That is why we want to launch a temporary fund of €500 bn for EU budget expenditure. In other words, this would not provide loans, but rather budget funding for the sectors and regions hit hardest by the crisis."
Angela Merkel, Chancellor of Germany

"We stand ready to provide the EU with further guarantees so it can provide more repayable loans to member states and businesses. What we cannot support — but what DE and FR propose — is that the EU borrows on the markets to finance non-repayable grants."
Gernot Blümel, Minister of Finance of Austria

"I do think the proposal put forward by Germany and France is the right response. It allows the EU to respond with solidarity, especially for members in southern Europe. This is absolutely necessary."
Jean-Claude Juncker, Former President of the European Commission

European Commission

- The European Commission approved state aid measures of 3 member states, of total value €32.1 bn.
- EU humanitarian aid increased by €50 m. to meet increasing demand for medical supplies in the Middle East and Africa.

Council of the EU

- The Council agreed on details of EU's employment support instrument. SURE will be activated as soon as all member states provide guarantees proportional to their share of EU's GNI. The instrument will be operational until 31/12/2022 unless the Council agrees on a 6-month extension.

22/05/2020

National measures (15-22/05)

Greece: The Prime Minister announced a new stimulus package which includes, inter alia, the estabishment of an employment support scheme and a reduction of VAT on transport services and holiday packages.

Slovenia: The Government will provide holiday vouchers worth €200 to all employed and self-employed citizens.

India: The Central Bank cut its benchmark rate from 4.4% to 4% and extended a loan moratorium by three months.

UK: Additional funds of £84 m. will be allocated to universities to support the development of a vaccine for Covid-19.

South Africa: The Central Bank further reduced by 0.5% its benchmark rate to 3.75%. Compared to its level prior to the crises, the rate is down by 2.5 pp.

Iran: The Government will provide low-interest loans worth $11.9 bn to small businesses.

International Monetary Fund

- From 15/05 to 21/05 the IMF has approved the requests of 6 countries for financial support through the Rapid Credit Facility, Rapid Financing Instrument and Catastrophe Containment and Relief Trust. Total amount approved: 1.16 bn SDR ($1.58 bn)

Breakdown of measures[6] (16/03 – 22/05)

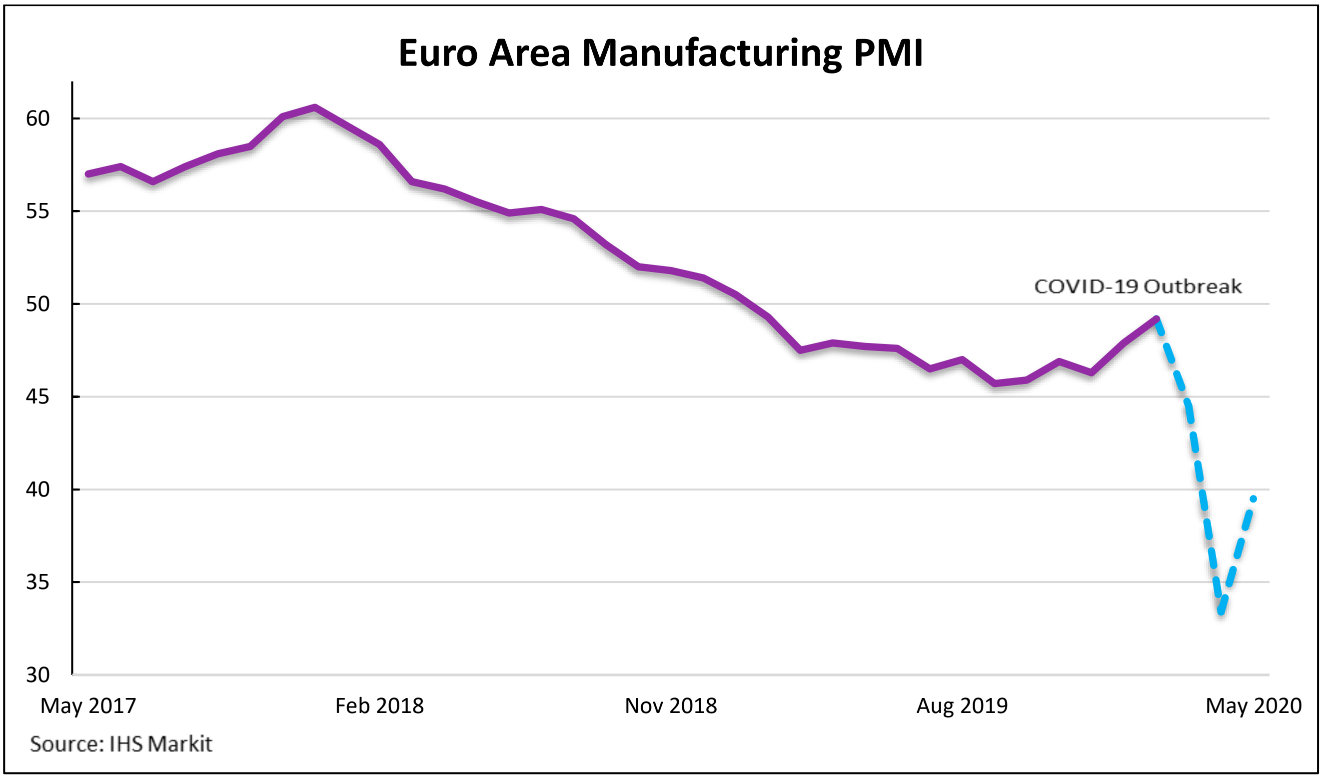
	EU	France	Italy	Germany	Netherlands	Austria	Denmark	Spain	Greece	Portugal	Ireland
A. Fiscal Measures[1]	€65 bn	€110 bn[2]	€52.5 bn	€156 bn	€20.1 bn	€12.2 bn	90.7 bn DKK	€31.2 bn	€14.5 bn[3]	€1 bn[1]	≈ €7.3 bn[1]
B. Monetary Measures (Total)	€1.99 tr.[4]	-	-	-	-	-	Bank credit facility increased	-	-	-	-
C. Loans/Guarantees	€305 bn	€337.9 bn	€530 bn	€819.7 bn	Min. €12.1 bn	€9 bn	70 bn DKK	€112.4 bn	Not Specified	€3.8 bn	€5 bn[1]
D. Tax Deferrals	-	Not specified	€27.5 bn	€500 bn	€36 bn	Up to €10 bn	208 bn DKK	Min. €14 bn	Not Specified	€7.9 bn	Not Specified
E. Labour Market Measures[5]	SURE: Fund to provide loans to member states targeted to employment schemes. Total value: €100 bn	Income support subsidy of 70% for workers in partial unemployment status	Temporary prohibition of redundancies and prolongation of unemployment benefit	Further financing of the existing income support scheme for the unemployed	Wage subsidy of up to 90% (for businesses reporting revenue reduction of at least 20%)	Progressive wage subsidy based on the size of salary of up to 90% of working time	Wage subsidy of up to 75% (for businesses reporting revenue reduction of at least 20%)	Wage subsidy of 70%[6]	Measures include the continuation of the special allowance to workers, a wage subsidisation scheme and the extension of the unemployment benefit	Wage subsidy of up to 75% (for businesses reporting revenue reduction of at least 40%)	Unemployment benefit increase and wage subsidy of up to 70% (capped at €410/week)

[1] The total value of these measures is greater as the cost of several measures has not been estimated yet.
[2] Includes tax deferrals that are not specified separately.
[3] Includes tax deferrals and loans/guarantees.
[4] Includes the Pandemic Emergency Purchase Programme (PEPP), totalling €750 bn, the additional asset purchases of €120 bn within the framework of the Asset Purchase Programme (APP), additional liquidity of €1 tr. provided to banks through the TLTRO III programme and capital relief of €120 bn due to easing of regulations. These figures represent the total value of assets and bank liquidity that will have been added to ECB's balance sheet by the end of the respective programmes. For further details on the evolution of ECB's asset purchases, see the diagram of Weekly Net Asset Purchases below.
[5] The amount of these measures – if specified – is included in the fiscal measures.
[6] Main source: IMF Policy Tracker. Other sources: OECD Country Policy Tracker & official government announcements.

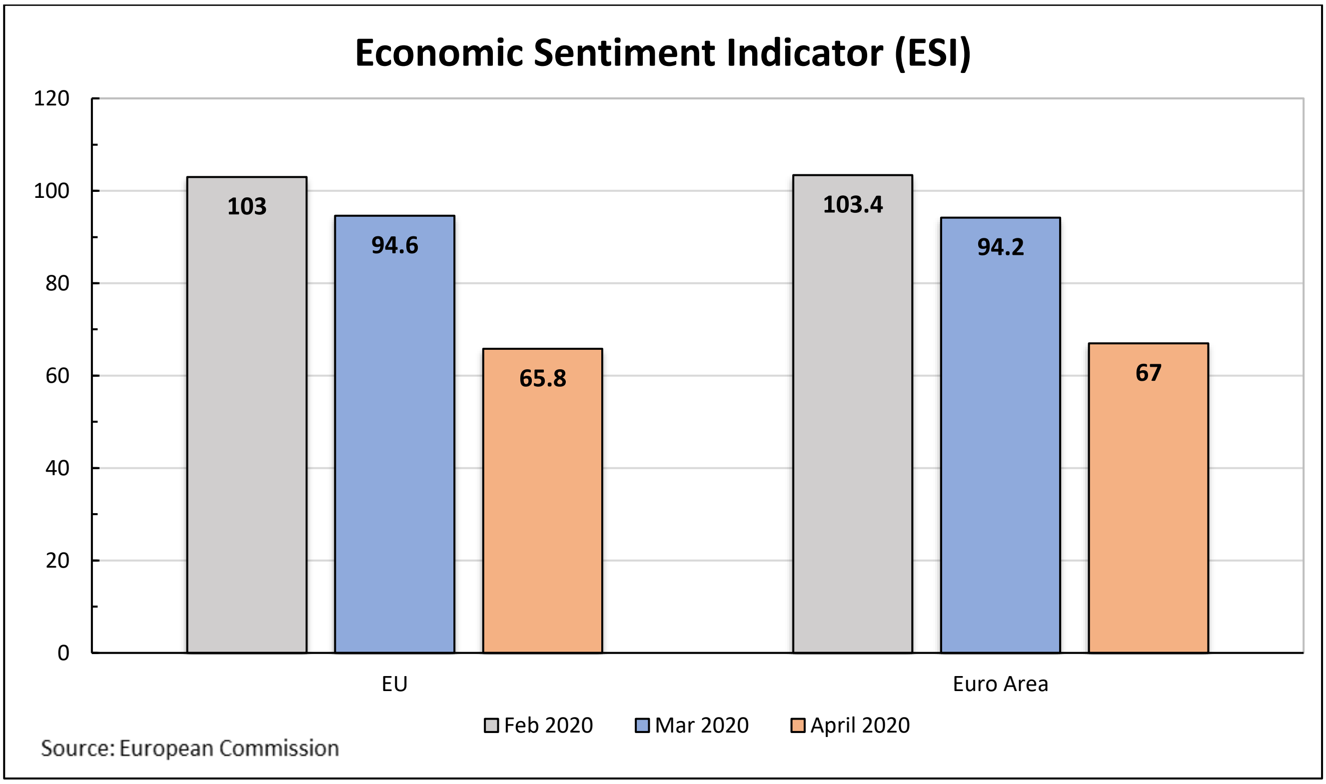
	USA	Canada	Australia	UK	Japan	Russia	India	Brazil
A. Fiscal Measures[7]	≈$1.7 tr.	108.3 bn CAD	193.8 bn AUD	£120.1 bn	¥117.1 tr.[8]	500 bn RUB[8]	9.45 tr. INR[8]	≈ 470 bn BRL[8]
B. Monetary Measures (Total)	Unlimited	Not Specified	Min. 90 bn AUD	Min. £645 bn	Unlimited	Not Specified	Min. 3.7 tr. INR	≈ 1.2 tr. BRL
B1. Asset Purchases	Not Specified	Not Specified	Not Specified	Min. £645 bn	Not Specified	Not Specified	Not specified	-
B2. Bank Liquidity	Not Specified	Not Specified	Min. 90 bn AUD	Min. £190 bn	Not Specified	500 bn RUB	Min. 8 tr. INR	≈ 1.2 tr. BRL
C. Loans/Guarantees	$1.242 tr.	65 bn CAD	35 bn AUD	£330 bn[9]	Min. ¥2.1 tr.	Not Specified	-	Min. 36 bn BRL
D. Tax Deferrals	$561 bn	85 bn CAD	-	Min. £3.1 bn	Not Specified	Not Specified	Not Specified	Not Specified
E. Labour Market Measures[10]	$250 bn (Unemployment benefit increase)	Allowance of 2000 CAD/month to workers whose income was impacted & wage subsidy of 75% for affected businesses	Wage subsidy of 1500 AUD per employee per fortnight	Wage subsidy of 80%	-	Reduction of social security contributions for SMEs & unemployment benefit increase	Wage increase for those working in state employment schemes for the agricultural sector	Allowance of $120 for the unemployed and informally employed

[7] Does not include funds allocated for tax deferrals and loans/guarantees.
[8] It includes the funds allocated for tax deferrals and/or loans/guarantees, as the exact breakdown of the package is not specified.
[9] Supported by the BoE
[10] The amount of these measures – if specified – is included in the fiscal measures.

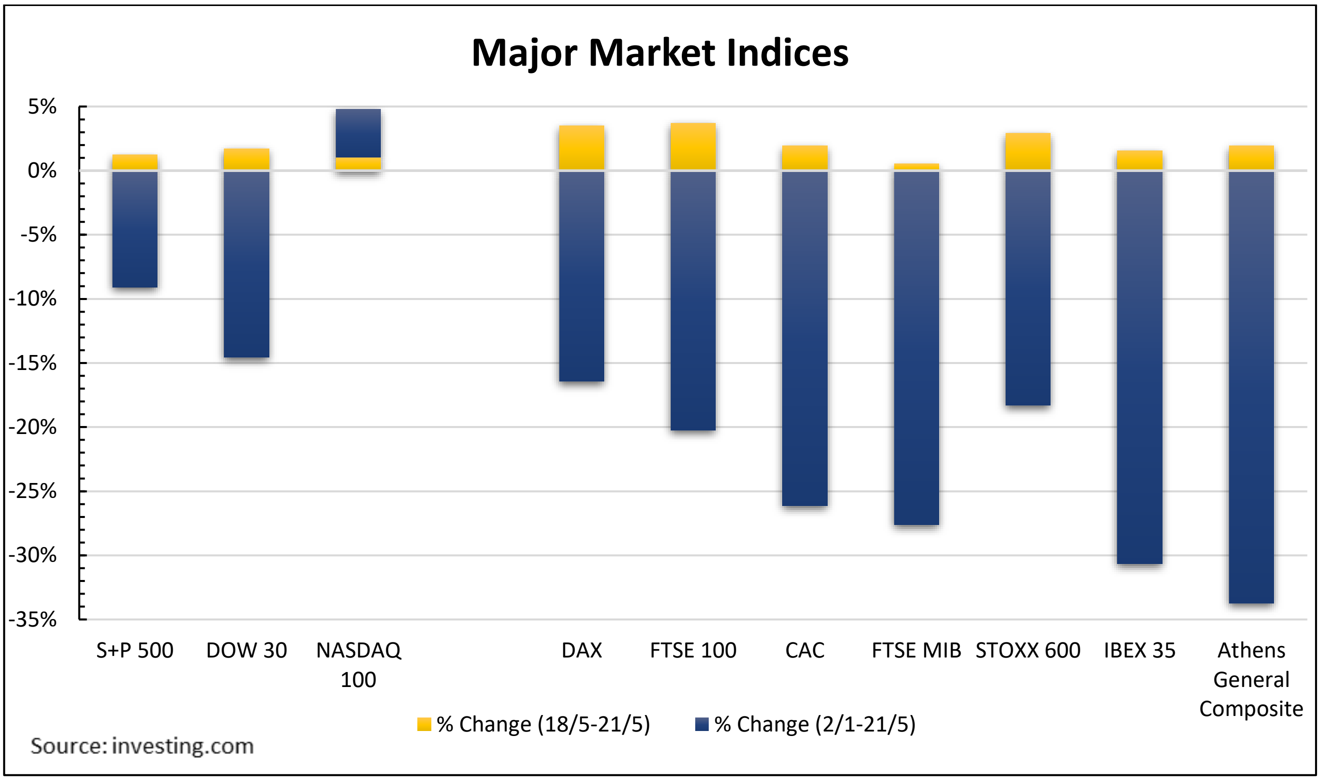
Recent Economic Developments (18-21/05)



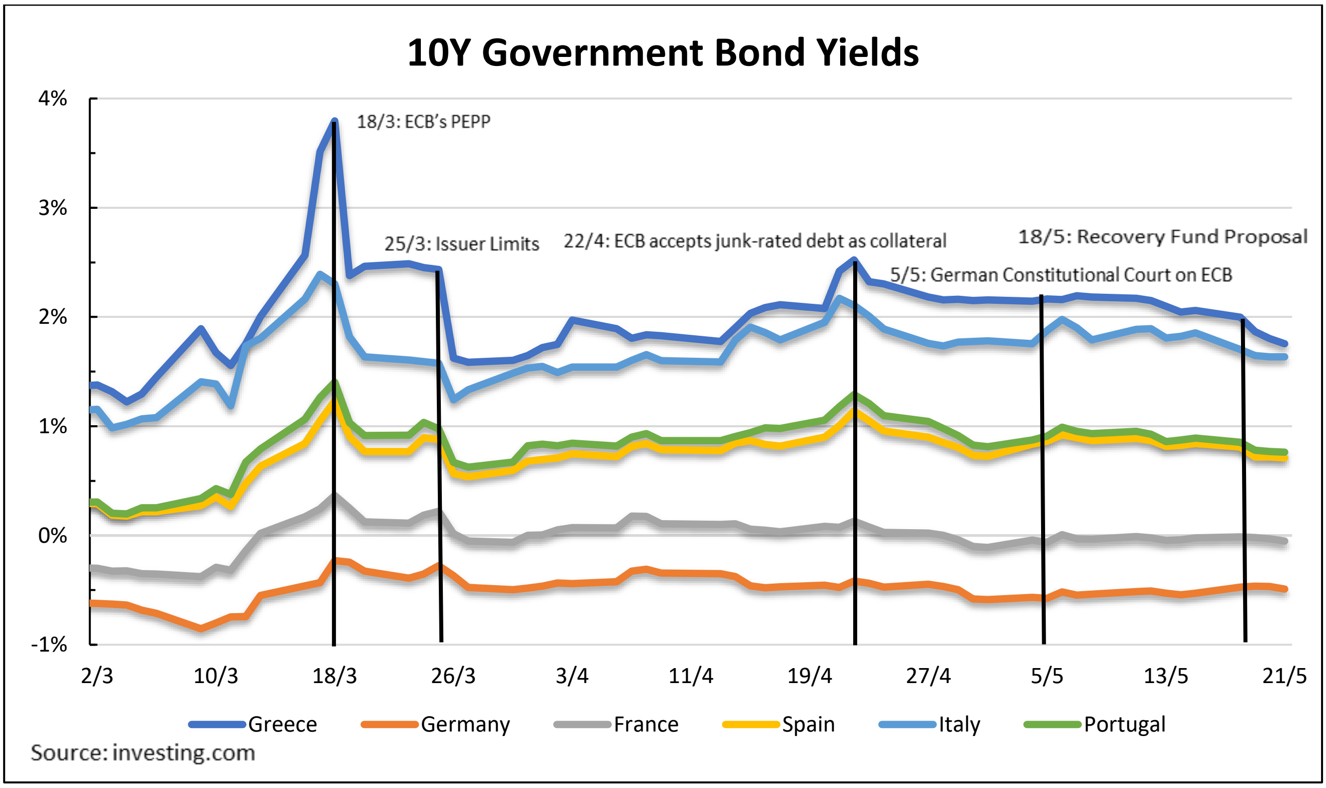
According to IHS Markit (21/5), the Eurozone manufacturing PMI rose to 39.5 in May from 33.4 in April. The economic sentiment is improving as economic activity seems to bounce back.



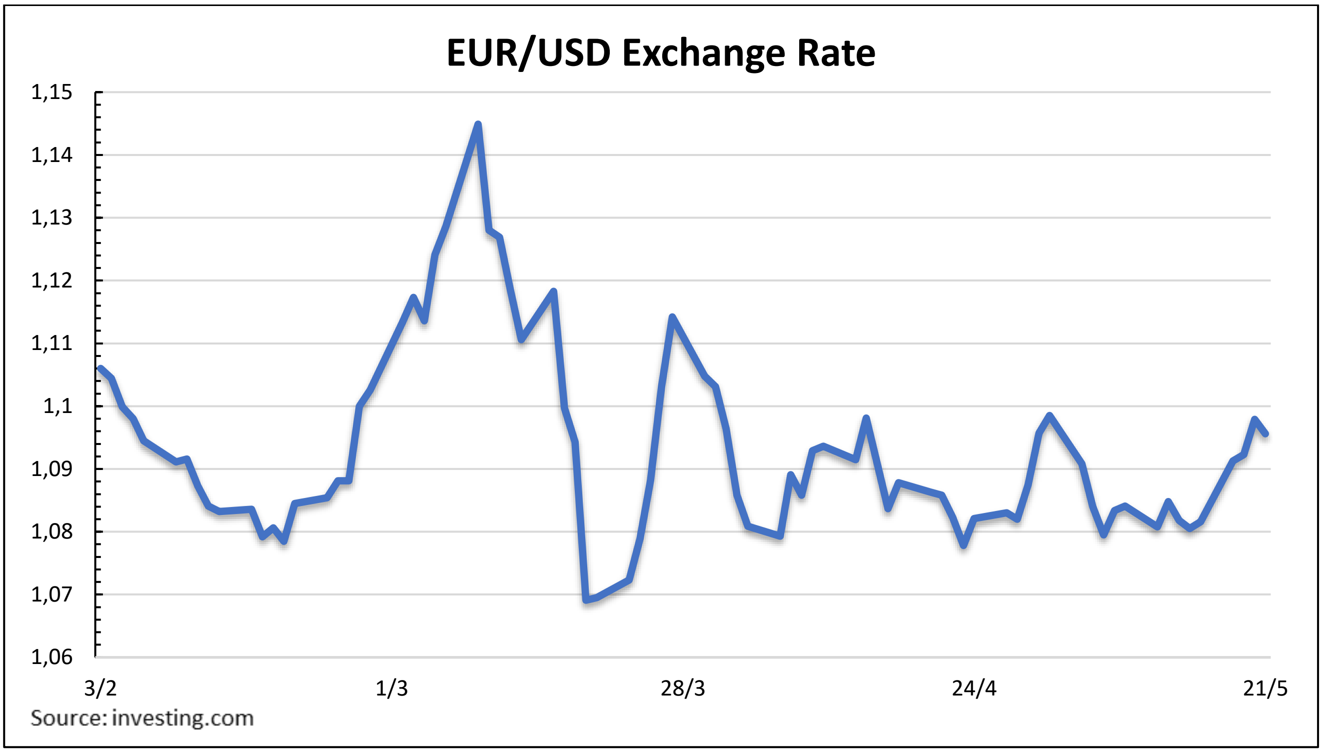
In April 2020, the Economic Sentiment Indicator (ESI) crashed in both the EU and the Euro Area. According to the European Commission "this was the strongest monthly decline in the ESI on record since 1985 surpassing by far the previous negative record from March."



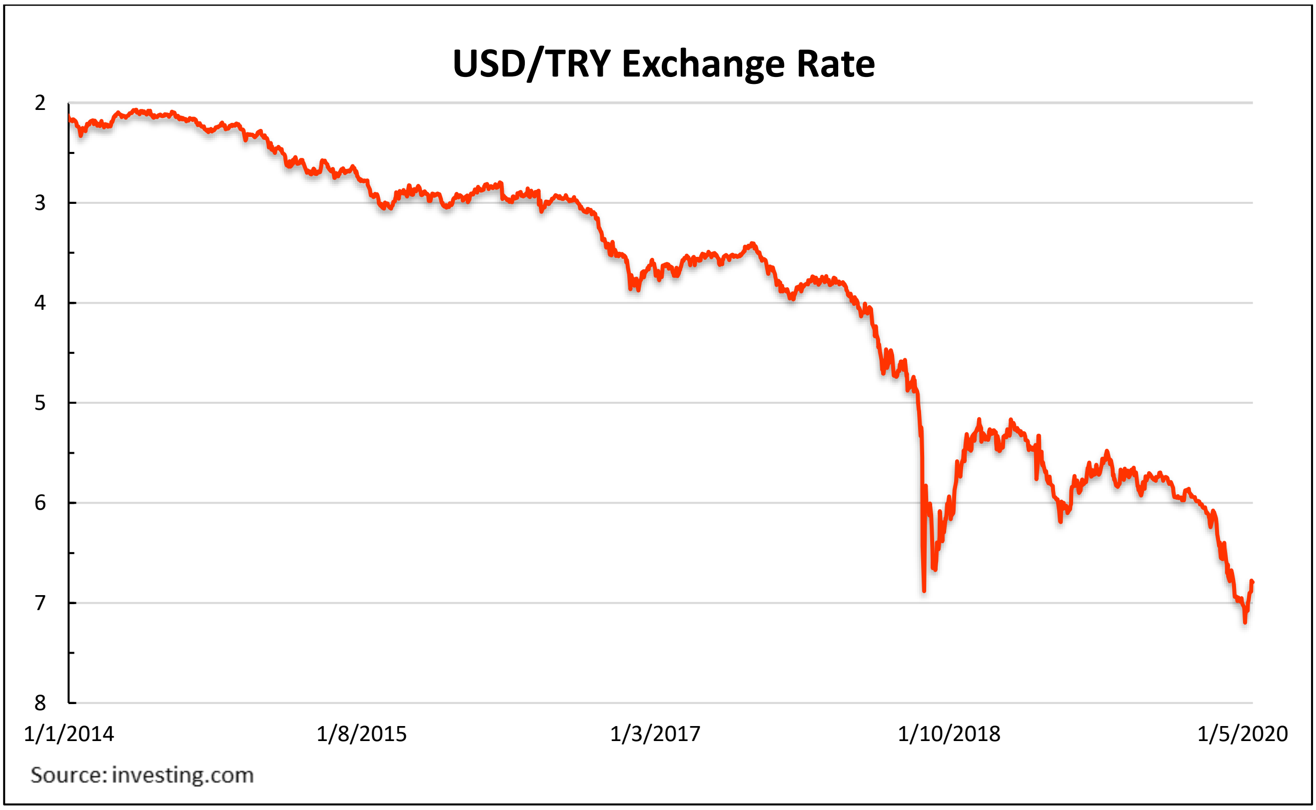
Both Wall Street and European indices climbed, as there is optimism about the easing of the lockdowns and the restart of the global economy.



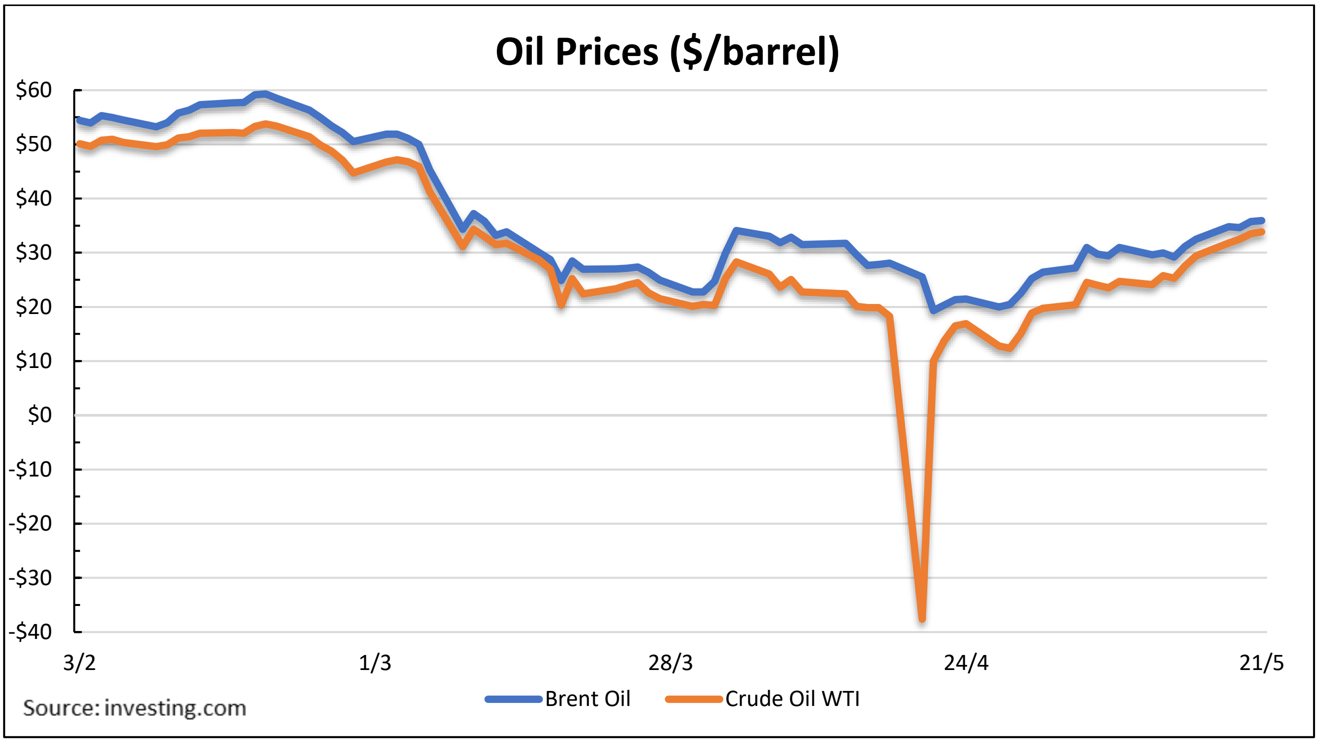
Most European government bond yields fell after Germany and France proposed a €500 bn recovery fund on 18/5.



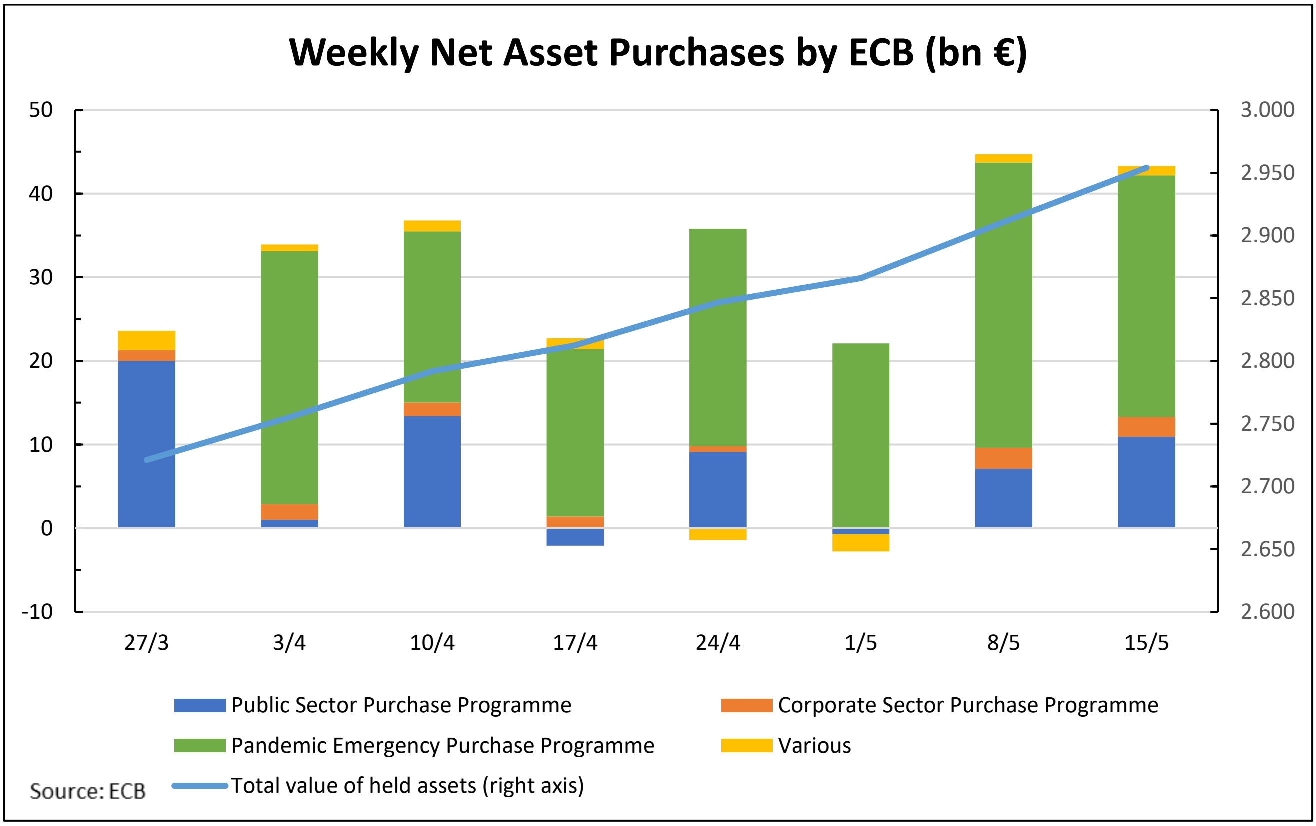
In the foreign exchange market, the EUR/USD exchange rate increased after the proposal of a €500 bn recovery fund on 18/5 and is currently at 1.0956 $/€.



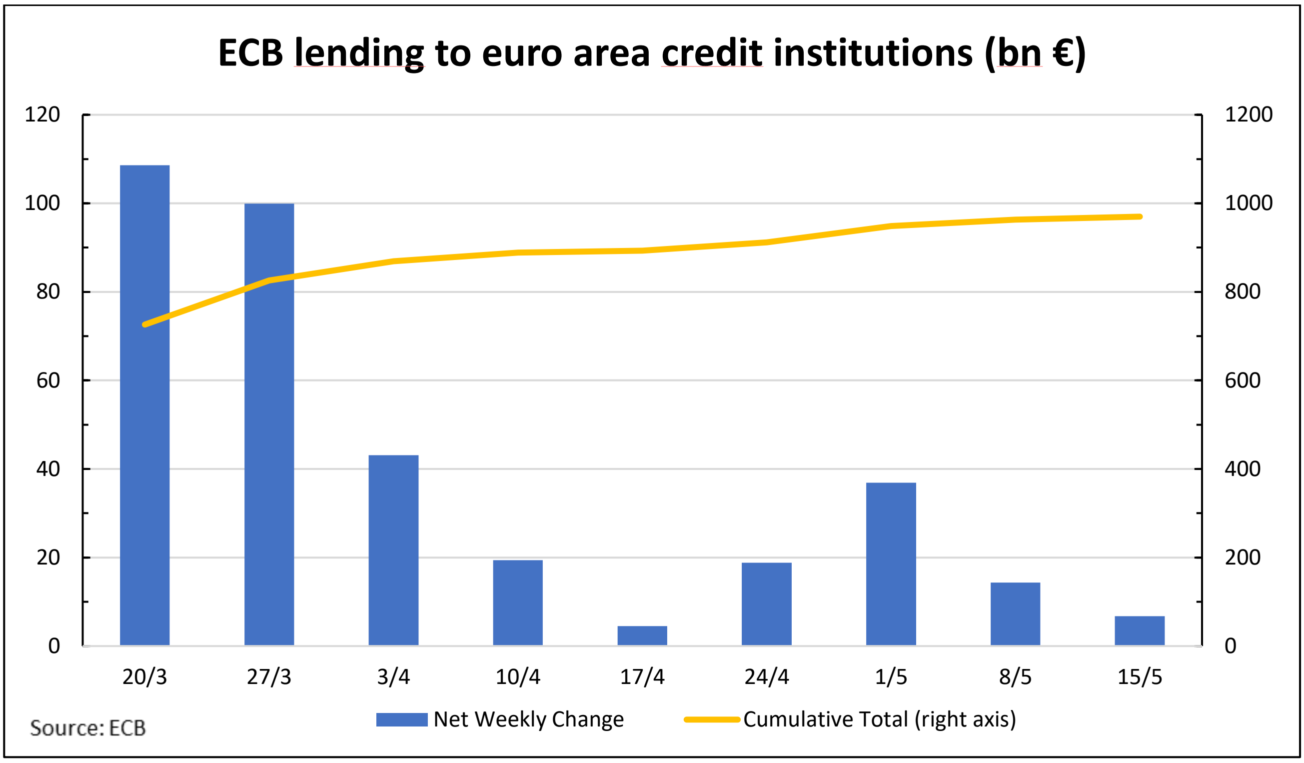
The COVID-19 pandemic has affected the currencies of the emerging economies, especially those in need of foreign reserves. The Turkish Lira has declined since February, despite the efforts of the Central Bank to prevent the exchange rate depreciation. The exchange rate is currently around 6.78 TRY/USD.



Oil prices settled higher following the announcement of the International Energy Agency (20/5) that the US oil production could be 2.8 million barrels per day lower than at the end of 2019.



On 18/3, the ECB announced a new asset purchase programme (PEPP) totaling €750 bn. Furthermore, the ongoing APP, which is in force since October 2014, was boosted on 12/3 with an additional envelope of €120 bn. The bars represent weekly net asset purchases per programme whereas the line represents the weekly evolution of the cumulative value of all assets held by ECB as part of all past and current asset purchase programmes.



On March 12, 2020, the ECB announced a package of measures, easing terms on providing loans to banks through the TLTRO III programme. The package included the reduction of the interest rate of the programme from June 2020 and the increase of the lending limit for credit institutions effective immediately. In this direction, a further easing regarding conditions on accepting claims and other assets as collateral was announced on April 7, 2020.

In Focus

Commentaries, analyses, forecasts on the economic dimensions of the pandemic

In a commentary about the Franco-German initiative for a €500 billion euro Recovery Fund, Daniel Gros of the Centre for European Policy Studies, argues that what makes the proposal attractive politically is that **nobody has to pay now**. Instead, additional expenditure will be financed with bonds, which do not have to be repaid over the lifetime of the next financial framework of the EU, i.e. not before 2028. The real fight over who pays for the additional 'corona' expenditure has thus been postponed. For the time being, no country will be forced to increase its contribution to the EU budget. This aspect will also soften the opposition from the so-called frugal coalition.

The joint Franco-German declaration for a new EU Pandemic Recovery Fund has marked **a remarkable U-turn for Germany and the whole EU**. Jacob Funk Kirkegaard in PIIE argues that this initiative is a step forward towards further fiscal integration since this fund applies to all member states and not only members of the Eurozone. Come to pass the unanimity vote, this fund will mobilise €500 bn from contributions of member states according to the GNI of each country. Furthermore, the debt is to be repaid in several decades, in order not to put additional economic strains on the member states. All in all, the proposal is groundbreaking and indicates that there is still the spark of integration, solidarity, and mutual understanding within the EU.

The rescue phase of the COVID-19 crisis response is now completed, and it is time for governments to plan for a recovery phase. In an article on Project Syndicate, Bertrand Badré and Mathilde Lemoine write that governments and central banks have responded with decisiveness to the crisis so far, averting a complete economic fallout. However**, now is the time to expand the 2008-2012 playbook** by creating a European Recovery Fund that will mobilise the right kind of investments and by establishing a European Redemption Fund that will ensure liquidity while bypassing the Eurobond redline. To succeed, this recovery plan must transform billions into trillions, direct investments towards real social needs and minimise inequalities.

With the crisis still unfolding, Catarina Davies and Roberto Merrill of Social Europe call for **an unconditional basic income** to tackle unemployment and obtain a social equilibrium. The authors suggest that the ECB should define the amount of the income up to €350 per adult. The unconditionality of this funding would avoid red-tape and would sustain demand. Finally, this measure could be an ideal show of European solidarity, and a proof of the role of the EU in our lives against Euroscepticism. Monica de Bolle, writing for the Financial Times, proposes the extension of a basic income scheme to the developing world, whereby citizens receive direct payments from the state.

Maria Demertzis of Bruegel argues that markets are capable of sifting through the risks the EU currently faces and identifying who is the fittest to survive. She calls for the formation of **a capital markets union**, as the EU did with the Banking Union during the previous financial crisis. This could take the shape of a '28th regime': a distinct legal jurisdiction, separate from any national jurisdiction. By design, it should encourage more private capital involvement, domestically and across member states.

In a policy paper under the Jacques Delors Centre, Grund, Guttenberg and Odendahl propose a **Pandemic Solidarity Instrument to share the costs of the crisis**. This Instrument should be set up as an EU instrument: the EU would borrow 440 billion euros in the market, backed by the EU budget and by guarantees of the member states. As this would be EU debt, it would not count as debt of individual member states. The EU-issued bonds would have long maturities and could be refinanced in the market at the end of their terms; otherwise, they would be repaid upon maturity according to the future state of economic strength of member states. The funds would be used for four purposes: 1) Grants to member states to partially cover health-related costs; 2) Guarantees to the European Investment Bank to provide liquidity to European companies; 3) Subsidies to member states so they can fund short-time work schemes and short-term unemployment benefits; 4) Co-financing of national stimulus packages once confinement measures have been lifted.

Southern Europe countries and France face higher risks to employment due to Covid-19, according to Sebastian Doerr and Leonardo Gambacorta of the Bank for International Settlements. Regions in Italy, Greece, and Spain but also in northwest Germany, the Baltic States and the UK display high shares of employment in sectors that are severely affected by the unfolding crisis such as transportation, retail trade and hospitality. Regions with high shares of small firms, mostly located in France as well as in Southern and Eastern Europe, are also expected to be hard-hit. On the contrary, regions in Northern Europe face low risks to employment while Eastern and Central European regions have intermediate risk indices.

The new EU instrument to mitigate unemployment risks during an emergency, **SURE, is too modest to have a significant impact** on the COVID-19 crisis beyond being a first step in the overall recovery plan – Grégory Clayes argues on Bruegel. Firstly, SURE's effect on public finances will be very marginal as the programme is too small (€100 billion) to lead to significant savings in interest costs. Secondly, there is a risk of a stigma being attached to the use of the programme. Markets could interpret a request as a sign of weakness and therefore ask for higher rates when countries issue new bonds, thus erasing savings generated by the lower cost of SURE loans. In addition, unlike an ESM credit line, a loan from SURE would not make a country eligible for the ECB's Outright Monetary Transactions scheme (OMT).

The pandemic shock is likely to be asymmetric and lead to further economic divergence between Southern and Northern Europe. In a policy brief, Christian Odendahl and John Springford of the Center for European Reform name three ways in which COVID-19 will cause economic divergence. Firstly, lockdowns have enormous costs and are likely to last longer in countries with larger outbreaks. Secondly, regions in Southern Europe that are dependent on tourism and manufacturing are likely to suffer larger and more long-lasting recessions. Thirdly, Southern European governments are constrained by debt and therefore are less able to offset the costs of Covid-19. Further economic divergence is expected to make European politics even more fractious, providing fertile ground for the far right and left. The Franco-German proposal for a €500 bn recovery fund has the potential to forestall further divergence, but **Europe needs to reconsider its fiscal framework to stabilise debt levels** post-pandemic, and to let growth reduce debt.

In a North vs South comparison, the South may be more worried about the imminent implications on the tourism industry, but the bell tolls for the North too. A **wave of bankruptcies** is about to hit Europe, according to The Economist. 'Zombies' will be swept away, but even some healthy companies may not survive. Small and medium enterprises, which employ over 90 million people, will be particularly affected. According to SMEUnited, 90% of Europe's small firms are affected by the pandemic and 30% of them claim they are losing 80% of their sales or more. The heavily industrialized companies of the North are also affected with automobile industries in Germany, France and UK seeking governmental help, since mid-March. This applies to the steel industries as well, since the demand for steel is at an all-time low, with the revenues of Thyssenkrupp (one of the largest in Germany and the world) free-falling by 95% since last year. Another sector threatened is the aviation industry. On 19/05, Rolls Royce announced it is about to lay-off 9.000 jobs, 1/6th of its entire workforce; this is the largest cut since the company's privatization in 1987. This applies to Lufthansa too, which loses €1 mil./hour. Even though Germany is still mistrustful of automobile manufacturers, since the VW scandal back in 2015, the federal government has no other option than to stimulate this sector, too, as it is an essential part of the German economy.

Assenza et al. at VoxEU defend the thesis that **health and economic objectives are not mutually exclusive**. Their findings show that the dynamics of optimal policy are dictated by the dynamics of the epidemic and remain well grounded in basic economic principles: the shadow price of infection risks, the trade-off between mortality and economic prosperity, and dynamic immunisation and infection spillovers.

Nevertheless, coronavirus shutdowns around the world could undo three years of gains in alleviating poverty, said David Malpass, President of the World Bank. According to the group's estimates, **up to 60 million people will be pushed into extreme poverty** as the global economy shrinks by around 5%. 'Families have lost loved ones, millions of jobs and livelihoods are lost, the health systems are under enormous strain worldwide', David Malpass remarked. So far, the World Bank group has loaned money in 100 countries accounting for about 70% of the world's population, in response to the COVID-19 crisis. Another cause of poverty is that for many nations, flows of remittances, sent home by migrants working abroad, form a sizable chunk of the national economy. However, the coronavirus-related **lockdowns threaten to slash remittances by as much as 20% this year**, wreaking havoc on the economies that depend on labour diasporas, according to World Bank estimates. For example, in Haiti, the poorest country in the Western hemisphere, remittances account for almost a third of the GDP.

The experts of ELIAMEP write

"The more effective the common management and the stronger the European solidarity, the lower the risk of the rise of nationalism-populism. The final outcome has not yet been defined. The single market will not survive if economic Darwinism prevails, based on the ability of some states to keep their businesses alive, while those of others are collapsing. I hope that in the end, the rationale of the common interest will prevail in order to rescue the great European accomplishments."

Loukas Tsoukalis, President of the Board, ELIAMEP, *kathimerini.gr, 18.05.2020*

"Businesses eligible for state aid must prove that they were doing well prior to COVID-19, as well as demonstrate that they are not distributing dividends or engaging in stock-buybacks. If they have already received state aid, they should not be eligible to apply for aid from the European Recovery Fund should it be created. The risk is not a totalitarian Leviathan, but the undermining of the single market, because the large companies of strong governments will emerge much stronger that those of fiscally weak governments."

George Pagoulatos, Director General, ELIAMEP, *tanea.gr, 16.05.2020*

"The conflict between the fiscally conservative North and the (once again) afflicted South is likely to persist. However, a change in the German position, if confirmed, could be the catalyst, not only for the effective handling of the current crisis, but also for the move towards a real European economic union."

Dimitris Katsikas, Head of the Greek and European Economy Observatory, ELIAMEP, *tanea.gr, 20.05.2020*

"The European Parliament warns the Commission not to use misleading quantitative data, stressing that the front-loaded allocation of resources might help mitigate the immediate effects of the crisis, especially in terms of cohesion policy, but does not provide additional funding and cannot be advertised as such. The European Parliament calls on the Commission not to resort to financial alchemy and controversial multipliers in order to present to the public ambitious figures."

Alekos Kritikos, Senior Policy Advisor, ELIAMEP, *tanea.gr, 19.05.2020*

“I think that with the current form of the Lisbon Treaty represents the worst of both worlds. We have all the disadvantages of not having a more federal EU and none of the advantages of such a closer Union. The Federal Government of Germany or of the US does not need to approve the annual budget of each state before the vote in the state Parliaments. Yet this is exactly what is happening in the Eurozone. What if a state exceeds its budget? Resources are transferred from the rich to the poor. Thus, I believe we need more integration, not less. Not because the North needs to pay for the problems of the South, but in order to achieve real convergence, which has not been obtained by the euro so far despite the initial promises.”

Georgetta Lali, Senior Advisor, ELIAMEP, *metarithmisi.gr, 21.05.2020*

"The impact of COVID-19 on the energy market is wide and does not only concern the Eastern Mediterranean. The question is whether it is now necessary to adjust priorities and focus on further investment in renewable energy. It is positive that Greece is one of the EU member states, which have – from the outset – embraced the European Green Deal. "

George Tzogopoulos, Research Fellow, ELIAMEP, *tanea.gr*, 14.05.2020

"The risk of the Balkans suffering irreparably from the current crisis is greater than in other parts of Europe. The Balkans continue to struggle with volatile economies, limited public health capacities and weak democratic institutions, making them more vulnerable to various forms of crisis."

Bledar Feta, Junior Research Fellow, ELIAMEP, *tanea.gr, 15.05.2020*