An Overview of the European Commission's Next Generation EU Instrument

Introduction

The European Commission announced an economic and financial plan on the 27th of May to help the European economy recover from the COVID-19 pandemic[1] . The plan consists of two key elements. The first is the standard Multi-annual Financial Framework (MFF) from 2021-2027. The new proposals suggest that this will amount to €1.1 trillion and will be funded by the EU budget and contributions from EU member states[2]. Countries were already negotiating the specifics of this prior to the COVID-19 pandemic, however, now in addition to the MFF there will be a "Next Generation EU instrument". This will amount to an additional €750 billion and will be temporary from 2021-2024. While the standard MFF will be funded by EU contributions, the European Commission will fund the Next Generation EU instrument by borrowing from capital markets. To implement this recovery plan, all Member States would need to agree to it.

A number of fiscal measures had already been implemented to support European economies in dealing with the COVID-19 pandemic. These measures are listed below:

- Relaxation of EU State Aid and Fiscal Rules[3].
- Pandemic Credit line to Eurozone countries worth €240 billion which will be facilitated by the European Stability Mechanism[4].
- A €100 billion employment support scheme (i.e. SURE- Supports to mitigate Unemployment Risks in an Emergency) where the European Commission will raise money backed by €25 billion of contributions from Member States[5].
- EIB Guarantee Fund for businesses and workers worth €200 billion[6].

EU Multi-annual Financial Framework

In its paper, the Commission proposed changes to the Multi-annual Financial Framework (MFF) for the years 2021-2027 in addition to the establishment of the Next Generation EU instrument. Table 1 shows the requests for the seven main headings of the EU budget and provides some granular data on funding lines related to economic recovery after the COVID-19 pandemic.

1 https://ec.europa.eu/commission/presscorner/detail/en/ip_20_940
2 https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0442&from=EN
3 https://www.euractiv.com/section/economy-jobs/news/commission-proposes-unprecedented-suspension-of-eus-fiscal-rules/
4 https://www.esm.europa.eu/content/europe-response-corona-crisis
5 https://euobserver.com/coronavirus/148419
6 https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0442&from=EN

Table 1: Multi-annual Financial Framework Spending Breakdown

	MFF 2021-2027	Of Which: Next Generation EU
	Eur Billions	**Eur Billions**
Total MFF	**1,850,0**	**750,0**
1. Single Market, Innovation and Digital	**210,5**	**69,8**
Horizon Europe	94,4	13,5
InvestEU fund,	31,6	30,3
of which, Investing in the EU economic recovery	15,3	15,3
of which, Strategic Investment Facility	15,0	15,0
EU Solvency Instrument under EFSI	26,0	26,0
2. Cohesion and Values	**984,5**	**610,0**
Cohesion Policy	373,2	50,0
Recovery and Resilience Facility	560,8	560,0
of which, loans	250,0	250,0
of which, grants	310,0	310,0
3. Natural Resources and Environment	**402,0**	**45,0**
Common Agricultural Policy	373,2	50,0
Of which, Pillar 11(Rural Development)	90,0	15,0
Just Transition Fund	40,0	30,0
4. Migration and Border Management	**31,1**	
5. Resilience, Security and Defence	**29,1**	**9,7**
Civil Protection Mechanism (rescEU)	3,1	2,0
Health programme	9,4	7,7
6. Neighbourhood and the World	**118,2**	**15,5**
Neighbourhood, Development and International Co-operation	86,0	10,5
Humanitarian Aid	14,8	5,0
7. European Public Administration	**74,6**	

Source: European Commission (2020) The EU budget powering the recovery plan for Europe

The MFF will be funded from the usual sources (i.e. customs duties and contributions from the Member States that are based on VAT and Gross National Income). Under the current proposals the European Commission suggests introducing a number of additional measures to increase resources from 2021-2027[7]. If these measures were introduced by 2024, the Commission claims Member States' national contributions to the 2021-2027 Multi-annual Financial Framework could decrease as a share of their economy compared to their payments in 2020. These additional measures include an extension of the Emissions Trading System to the maritime and aviation sectors (could raise €10 billion per year), a carbon border adjustment mechanism (which could raise between €5 billion and €14 billion), an own resource based on operations of companies that draw huge benefits from the EU single market (could raise €10 billion a year) and a digital tax (which could raise €1.3 billion a year).

7 https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0442&from=EN

Next Generation EU Instrument

This fund will provide €750 billion of additional expenditure for the sectors and regions most affected by the COVID-19 pandemic. The fund is expected to be temporary (from 2021-2024) and not a permanent programme. It is specifically targeted to mitigate the difficulties caused by the pandemic and its corresponding economic disruption.

The Next Generation EU fund will consist of grants (which don't have to be repaid), loans (will have to be repaid) and guarantees. The current proposals suggest that €440 billion in grants and €250 billion in loans and €60 billion in guarantees would be available for Member States

The Next Generation EU instrument will have three main pillars:

1) Supporting Member States to recover, repair and emerge stronger from the crisis
2) Boost private investment and support ailing companies
3) Reinforce key EU programmes to make the single market stronger and more resilient.

Details of the schemes under each of these three pillars is outlined in the table below.

Table 2 Next Generation EU Instrument

Pillar	Scheme	Description
Pillar 1: Support to Member States with investments and reforms	Recovery and Resilience Facility	This accounts for the majority of funds available under Next Generation EU instrument. It will amount to €560 billion and will be split between €310 billion in grants and €250 billion in loans. It will provide funding for investment and reforms. All Member States will be able to avail of these supports, however, funding will be concentrated in the Member States that were most affected by the pandemic.
	REACT EU initiative	This will provide additional funding to existing cohesion policy programmes. These additional funds will be allocated based on the economic impact of the crisis.
	Just Transition Fund	Additional funding will be provided to help Member States achieve climate neutrality.
	European Agricultural Fund for Rural Development	Provide additional funding for rural areas in making the structural changes necessary in line with the European Green Deal.
Pillar 2: Kick-starting the EU economy by incentivising private investments	Solvency Support Instrument	Provides solvency to companies
	InvestEU	This will provide additional funding to mobilise private investment.
	Strategic Investment Facility	Provides funding to help boost the resilience of strategic sectors (i.e. green and digital technologies).
Pillar 3: Addressing the lessons of the crisis	Health Programme, EU4Health	Funding to improve health infrastructure and prepare for future health crises
	RescEU	Additional funding to help prepare for a future crisis.
	Horizon Europe	Fund research in health, resilience and green and digital technologies.
	External Action	Additional funding for humanitarian aid.

Source: European Commission (2020) The EU budget powering the recovery plan

Timeline

The European Commission hopes that the European Council will agree to the proposals by July. This will enable some funding streams (e.g. RescEU, solvency support instrument and the European fund for sustainable development) to become available as soon as possible. It then hopes to finalise an agreement with the European Parliament and the European Council by early Autumn. This would enable the new long-term budget to be up and running by January 2021.

Issues to consider

There are a number of important issues to consider:

- The Next Generation EU instrument will be funded by borrowing from capital markets. The European Commission has stated that the borrowed money will be paid back. However, repayments won't take place before 2028 or after 2058[8].
- The financial reputation of the EU means the European Commission will be able to borrow at low interest rates. However, financial markets could perceive that the liability is jointly held between Member States and countries with good fiscal records could face higher costs, if other countries struggle to repay, given the potential reputational damage to the EU and their own country[9].
- The media are reporting that four countries - Denmark, Sweden, Austria and the Netherlands – have concerns about the proposed plan[10] They would prefer if the funds were made available to Member States in the form of loans as opposed to grants. This would mean responsibility would align more clearly with the country, and other countries would not bear ultimate responsibility for the commonly issued debt.
- The impact of the COVID-19 pandemic will vary across the EU. It will depend on the prevailing economic structure, whether the country is heavily reliant on sectors that have been adversely affected by the pandemic such as tourism and whether the economy has the capacity to absorb a significant and sudden shock. For example, GDP loses are expected to be significant in countries like Italy and Spain[11]. It is unlikely that Ireland will experience the same negative shocks to GDP as ICT and pharmaceuticals (which haven't been as badly affected by the pandemic) account for a significant share of Irish GDP. This was seen in Q1 data as GDP in Ireland grew by 4.5% while it is estimated that GDP across the EU-27 fell by 2.6% over the same period[12]. This could mean that Ireland will receive a relatively small share of the funds that are targeted at countries most affected by the pandemic.

8 https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0442&from=EN
9 https://www.politico.eu/article/germany-conservatives-eurobond-awakening/
10 https://www.ft.com/content/add218ac-f63d-4b65-af5c-3c4e9033e015
11 European Commission (2020), Identifying Europe Recovery Needs
12 https://ec.europa.eu/eurostat/documents/2995521/10294996/2-09062020-AP-EN.pdf/8a68ea5e-5189-5b09-24de-ea057adeee15