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The EU Recovery fund

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Background: the EU Recovery Fund (RRF)

1. In April 2020, in response to Covid-19, the Eurogroup finance ministers agreed to extend a €540 billion credit line to stressed sovereigns via the European Stability Mechanism (ESM).

2. The July 2020 European Council agreed a €750 billion recovery fund, comprising:

- €390bn in grants; these do not need to be repaid.
  - Grants do not increase national debt burdens.
- €360bn in loans.
- Funds will be raised via a Commission bond issue – the first time the Commission has undertaken such an issue.
- This requires an 'Own Resources' Decision to provide the Commission with the statutory authority to raise the funds on the open market.
- The Own Resources Decision requires, in turn, ratification by the EP and all Member governments.
- Bonds will range from 3–30 year maturities.
- Borrowing will cease in 2026 at the latest.

A budget for European recovery and resilience

SURE / ESM Pandemic Crisis Support / EIB Guarantee Fund for Workers and Businesses	**EUR 540 billion**
Next Generation EU	**Temporary reinforcement** **EUR 750 billion**
Multiannual Financial Framework	**EUR 1100 billion**

Background

- The 'Recovery and Resilience Fund (RRF)' is in addition to the €1.1 trillion Multiannual Financial Framework (the 'General Budget', 2021–2027).
- The RRF provides a "temporary reinforcement" of the General Budget for 2021–24.
- The Frugal Four also insisted upon the application of the 'rule of law' principle in relation to the Budget.
- This means the member state milestones and targets must be met.

Negotiating the RRF

- The negotiations saw deficit countries push for the RRF to comprise €500 billion in grants. The negotiating position was amended to €400 billion.
- Ultimately, the 'Frugal Four' (Austria, Denmark, Netherlands, Sweden + Finland) would not accept more than €390 billion in grants.
- Frugal Four + Finland and Germany were rewarded with side payments, including reductions in their net contributions to the MFF.
- Originally, the Council discussed carbon and digital economy taxes to repay the grants. However, only a plastic waste tax was agreed.
- Merkel was concerned that the entire RRF had to be sufficiently "massive" to have an impact. Both macroeconomic and market credibility factors were decisive in driving Berlin to agree to a significant fund size.

EURF allocations

Recovery and Resilience Facility (RRF)	€672.5 billion, comprising:	
Loans:	€360 billion	
Grants:	€312.5 billion	
ReactEU:	€47.5 billion	
Horizon Europe: (R&D)	€5 billion	Cut from $13.5bn*
InvestEU:	€2.1 billion	
Rural Development:	€7.5 billion	
Just Transition Fund (pollution transition)	€10 billion	Cut from €40bn
RescEU:	€1.9 billion	Disaster mgmt
NDICI:	€3.5 billion	
TOTAL:	€750 billion	

Implementation

- All member governments must prepare recovery and resilience plans for 2021–23, subject to Commission review.
- Final funds allocations for 2023 will be in accordance with Commission assessments of the plans.
- The critiera will include:
  - strengthening economic growth potential;
  - job creation; and,
  - economic and social resilience.
- Deviations from plans are subject to Commission referral to ECOFIN and to the European Council.
- EP will be able to set the guidance for national plans.
- Council involvement and Council sanctions (e.g., withholding of Budget funds from Member states) should be regarded as exceptional.

Conditionalities

- Member states' plans are required to undertake reforms, targeting:
  - The carbon-neutral economy.
  - Green jobs.
  - Digital economy.

Outcomes

- Is the Commission suddenly both an EU financial institution, as well as a financial intermediary? It has been "borrowing capacity entrusted to the European Commission.en described."
- RRF reinforces fiscal solidarity, as well as euro's role as a reserve currency; it has sunk to ~20% of global reserves, as Covid-phase funds have sought safe havens in the $US, Treasuries and gold.
- Market reaction has been largely positive. Fixed income funds, in particular, welcome the reductions to sovereign risk.

Outcomes

- The Commission Covid bond issue avoids:

  (a) the monetization of EU/EZ debt by the ECB;

  (b) compelling Merkel to circumvent or amend the ECB statute;

  (c) initiating a politically-damaging German internal constitutional conflict;

  (d) binding member country loans to specific targets, monitored by the Commission and ECOFIN.

  (e) competing with sovereign bond issues; the RRF reinforces the sustainability of lower sovereign bond yields. But it is not large enough to compete with sovereign issues.*