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Interparliamentary Conference on Stability, Economic Coordination and Governance in the EU

(IPC – SECG)

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Session 3: Strengthening Europe's economic resilience – preparedness for future crises

Czech Presidency of the Council of the European Union

Parliamentary Dimension

Introduction – Current (global) challenges

Europe had barely recovered economically from the effects of the financial and debt crisis, when it was hit by the coronavirus crisis. As a result of this crisis, and in particular due to the measures taken by individual governments against the spread of COVID-19, the GDP in the EU fell by 5.7% interannually in 2020, with an even larger fall of 6.1% in the euro area. By 2021, the economies have returned to growth. GDP growth in the EU reached 5.3 and the euro area 5.2%. However, the total value of GDP remained below the level of 2019 (pre-pandemic).

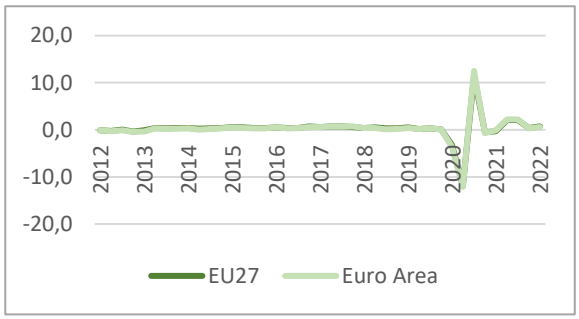
Annual real GDP growth in the EU and euro area since since 2019 (%)

	2019	2020	2021	2022*	2023*
EU	1.8	-5.7	5.3	2.7	2.3
Euro area	1.6	-6.1	5.2	2.7	2.3

* 2022 and 2023 data – European Commission estimate

Source: Eurostat, EC Spring Economic Forecast

Quarterly GDP growth in the EU and euro area

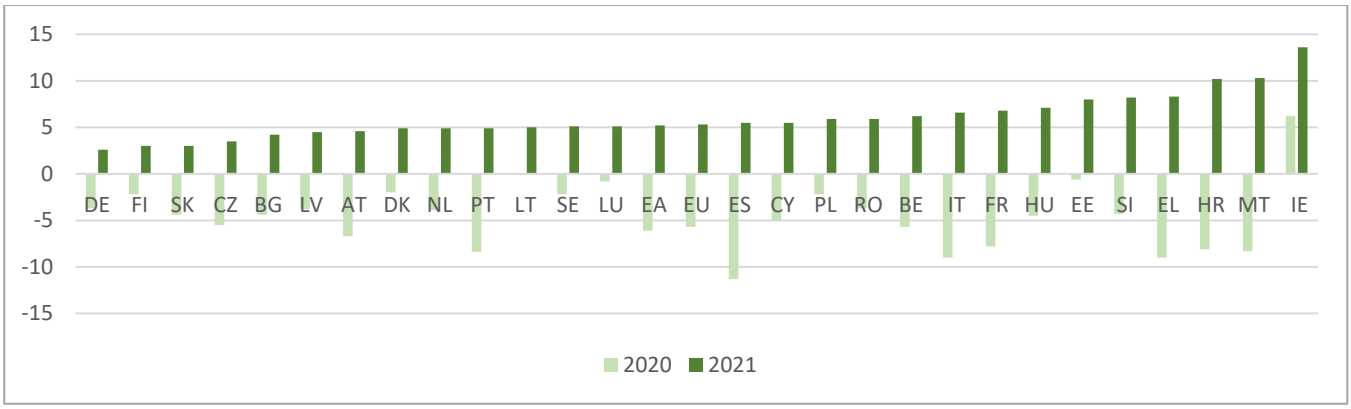


Source: OECD, Eurostat

The post-pandemic economic recovery brought with it the downside of rising prices. Energy prices in global markets started to rise as early as in 2021, mainly due to the surge in consumption associated with the economic recovery. The negative pressures associated with the economic recovery were expected to subside during 2021.

However, the positive development was halted by the Russian invasion of Ukraine. The war in Ukraine is exacerbating the existing negative effects on the economy and slowing GDP growth. In its Spring Economic Forecast, the Commission lowered its GDP growth estimates for 2022 and 2023 to 2.7% and 2.3% respectively compared to the winter forecast (the winter forecast had estimated GDP growth at 4% and 2.8% respectively).

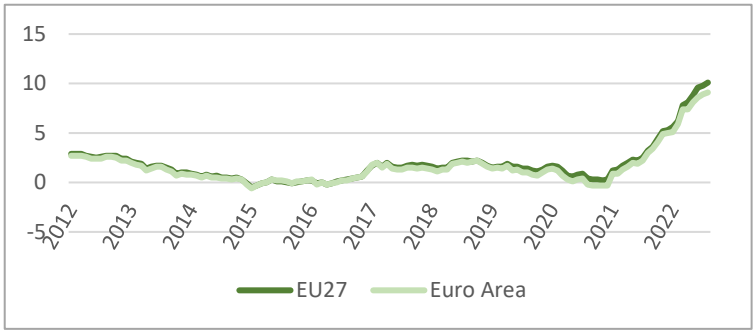
Chart 2: Annual GDP growth of EU Member States in 2020 and 2021



Source: Eurostat, (data as of 20 September 2022 – subject to change)

The war in Ukraine is amplifying upward pressure on commodity prices. Rising energy prices are accompanied by uncertainty over energy supplies. Moreover, the war threatens the production and export of agricultural crops, leading to rising prices in this area. In its spring forecast, the Commission estimates annual inflation rates for 2022 at 6.8% in the EU27 and 6.1% in the euro area. For 2023, the estimates stand at 3.2% for the EU27 and 2.7% for the euro area.

Monthly inflation rate since 2012 (%)



Source: Eurostat

Inflation and especially rising energy prices rank among the biggest challenges today. In August, the annual inflation rate reached 10.1% in the EU27 and 9.1% in the euro area. In June, inflation in some Member States reached above 15%. These were Estonia (25.2%), Latvia (21.4%), Lithuania (21.1%), Hungary (18,6%), the Czech Republic (17.1%) and Bulgaria (15%).

It is necessary to be prepared for further increase of energy prices as well as for a complete cut-off of gas supplies from Russia. The possibility of another COVID-19 pandemic remains a risk to economic development. Uncertainty and rising costs are also holding back investment. As a result of the war, EU countries are facing a wave of refugees from Ukraine.[1]

Strengthening EU resilience

Multiannual Financial Framework 2021–2027

The Multiannual Financial Framework 2021–2027 (MFF) was prepared in response to the coronavirus crisis as a post-pandemic recovery plan and it was complemented by the *Next Generation EU* (NGEU) recovery plan. In total, this represents funding of EUR 2 trillion (EUR 1 211 billion under the MFF and EUR 807 billion under the NGEU). More than half of the funding is earmarked for research and innovation, climate and digital transformation, recovery and strengthening resilience and preparedness for future crises.

Recovery and Resilience Facility[2]

The EU's main instrument to support recovery and build resilience of the economy is the temporary Recovery and Resilience Facility (RRF), which is part of the NGEU recovery plan. The RRF was established by Regulation (EU) 2021/241 on the RRF with a financial envelope of EUR 723.8 billion (in current prices) in the form of loans (EUR 385.8 billion) and grants (EUR 338 billion). The NGEU is intended to strengthen economic resilience and recovery and to achieve the objectives of climate neutrality and digital transformation.

In response to the energy market development and rising energy prices, the Commission has prepared a new REPowerEU plan, containing an amendment of the RRF Regulation to include new chapters on new energy measures in its national recovery and resilience plans.

New proposed financing facilities for European resilience

REPowerEU

In May this year, the Commission presented the REPowerEU plan in response to global energy markets development and the war in Ukraine. The plan sets out a series of measures to ensure a rapid reduction in the EU's dependence on Russian fossil fuels. This is to be achieved through energy savings, diversification of energy supplies, rapid replacement of fossil fuels by accelerating Europe's transition to clean energy. These three

[1] For data on the number of refugees from Ukraine in the EU, see the background materials to Session 1 – Interparliamentary Conference on Stability, Economic Coordination and Governance in the EU (IPC - SECG).
[2] For more information on the Recovery and Resilience Facility, see the background materials to Session 1 – Interparliamentary Conference on Stability, Economic Coordination and Governance in the EU (IPC – SECG).

measures are to be supported by smart investments and reforms that will link REPowerEU and the RRF. Therefore, REPowerEU is a complement to the RRF.

RRF financial resources are to be increased by EUR 20 billion (in the form of grants) for the REPowerEU objectives. These additional resources can be used by Member States after they update their national RRPs and supplement them with REPowerEU chapters. The funds are to be raised from the sale of EU *Emissions Trading System* (ETS) allowances. At the same time, there is still the possibility to use the RRF funds in the form of loans, which some Member States have not yet used.

The Commission also proposes to allow Member States to transfer up to 7.5% of the Structural Funds allocation to the RRF for the REPowerEU objectives, over and above the current 5%. At the same time, the proposal allows the Member States to transfer up to 12.5% of the funds allocated under the European agricultural fund for rural development.

The proposal to amend the RRF Regulation and related legislation in the context of the REPowerEU plan is currently under discussion in the European Parliament and the Council.

Social Climate Fund

In July 2021, the Commission presented a proposal for a Regulation establishing *a Social Climate Fund* (SCF). The proposal is part of the *Fit for 55* package under the *European Green Deal* (EGD). The aim of the EGD is to provide a framework for achieving the EU's climate targets for 2030 (reducing net emissions by at least 55% compared to 1990 levels) and 2050 (achieving climate neutrality). The purpose of the proposal is to create a new fund to mitigate the social impacts of the transition to a climate-neutral economy. Achieving climate neutrality and reducing dependence on fossil fuels will contribute to strengthening Europe's resilience.

Specifically, the proposal to create a new fund concerns the introduction of a new separate EU ETS for the buildings and road transport sectors. The Fund is to be used by Member States to finance the mitigation of the negative social impacts arising from the introduction of the new EU ETS.

Explicitly, the proposal enables the following use of the Fund's resources:

1) financing temporary direct income support for households placed at risk by the introduction of the new EU ETS;
2) support for emission-reducing measures and investments in the road transport and construction sectors.

Measures and investments can relate to practices reducing dependence on fossil fuels through, for example, renovating buildings and improving their energy efficiency; decarbonising heating and cooling in buildings; promoting low carbon and public transport, etc.

According to the Commission's proposal, the Fund is to be established for the period 2025–2032. The total financial envelope of the Fund is proposed at EUR 72.2 billion (in current prices), of which EUR 23.7 billion is intended for 2025–2027 and EUR 48.5 billion for 2028–2032.

The Fund is to be financed by the Union's own resources and from 2026 onwards by revenues from emissions trading for buildings and road transport (25% of the expected revenues). The projects supported by the Fund are to be financed by 50% from national resources. For this purpose, countries can use the revenues from the auctioning of their allowances under the ETS for the buildings and road transport sectors. Obtaining finance from the Fund is conditional on the preparation of a climate action social plan, which should include measures and investments, their expected costs, as well as milestones and targets. Such plan is subsequently to be assessed by the Commission. The final design of the Fund has not yet been approved.

Financing resilience in partnership with the European Investment Bank (EIB)

The role of the European Investment Bank is to provide funding for projects that meet the EU objectives. Together with the European Investment Fund, of which it is a majority shareholder, it is one of the main pillars of building a more resilient Europe. In addition to financing innovation, infrastructure or SMEs, the EIB is also a leader in green financing. By 2025, the EIB plans to increase its support for climate and environmental measures to 50% of all lending activities while promoting a just transition.[3] The aim is to promote green transition and strengthen economic resilience.

For example, the EIB is responsible for the implementation of 75% of the **InvestEU programme**, which provides long-term financing for EU objectives. It builds on the Investment Plan for Europe and is one of the main elements of the post-pandemic recovery plan under the NGEU. It should contribute to improving competitiveness, sustainable economic growth, employment, social resilience and cohesion, or to scientific and technological progress. Its specific objectives include support for research, innovation and digitisation, sustainable infrastructure, access to finance for SMEs and social enterprises. At least 30% of the Fund's resources are to be dedicated to the EGD objectives.

Member States can also invest the RFF funds into eligible projects through financial instruments, which may be implemented by the European Investment Bank. The EIB currently manages financial instruments of the RRF in three EU countries: Greece, Italy and Romania. In addition to resource management, the EIB can also help with additional financing and/or specialised advisory services.

Topics for discussion:

Do we need a new recovery and resilience plan as a response to the current crises?

How to increase Europe's resilience through investment? What are the best areas for direct investment?

How to finance the strengthening of Europe's resilience? Is it possible to use new instruments such as the forthcoming Social Climate Fund to mitigate the impacts of the climate transition?

Do we need to seek new paths for future management of crises (new (permanent) instruments) or should we work with already existing instruments?

Prepared by the Parliamentary Institute, Office of the Chamber of Deputies, Version of September 20

[3] Climate Bank Roadmap 2021-2025, EIB Group, November 2020