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The 2020 Stability & Convergence Programmes

An Overview, with an Assessment of the Euro Area Fiscal Stance

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European Commission
Directorate-General for Economic and Financial Affairs

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Institutional Paper 131

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EXECUTIVE SUMMARY

The European Union is experiencing the deepest economic recession in its history. The ongoing crisis is set to have a large, and to this day still uncertain, impact on public finances. Following the activation of the general escape clause of the Stability and Growth Pact (SGP), Member States can temporarily depart from their adjustment path or their medium-term budgetary objective (MTO), provided that this does not endanger fiscal sustainability in the medium term. The activation has allowed Member States to take fiscal measures needed to deal with the sizeable challenges resulting from the COVID-19 outbreak. Overall, the Commission 2020 spring forecast estimates that discretionary fiscal measures taken in response to the pandemic amount to over 3% of GDP. In addition, euro-area governments have provided sizeable state guarantees and other liquidity support worth almost 24% of GDP.

In 2019, after having declined for eight consecutive years, the aggregate headline deficit had already marginally increased. The headline deficit increased in about half of Member States, sometimes sizeably due to fiscal loosening. Similarly, almost half of Member States departed further from or stayed away from their MTO. In the context of strong GDP growth, the aggregate fiscal effort measured with the expenditure benchmark methodology pointed to fiscal expansion. However, the debt-to-GDP ratio continued to decrease, and had fallen in the large majority of Member States, mostly due to still favourable cyclical conditions, revenue windfalls and a positive interest rate-growth differential.

The severe economic downturn and unprecedented fiscal policy response to the pandemic will cause public deficits and debt ratios to rise sharply in 2020. The EU deficit is foreseen to rise to 8.5% of GDP in 2020. Discretionary measures adopted directly in response to the pandemic account for almost half of the weakening of the aggregated headline balance, with the other half attributed to the operation of automatic stabilisers. The aggregate debt-to-GDP ratio is also projected to rise fast, reaching 103% of GDP in the euro area and almost 96% of GDP in the EU in 2020. However, this fiscal outlook is surrounded by high uncertainty, given the large unknowns on the duration and impact of the COVID-19 pandemic.

The euro area fiscal stance is projected to be strongly supportive in 2020 due to the sizeable fiscal measures taken by Member States in response to the COVID-19 pandemic. The strongly supportive fiscal stance is estimated to have a positive impact on real GDP of around 5 pps. in 2020, and to help keep workers and business afloat and limit permanent impact on potential GDP. Against this backdrop and given the high stabilisation burden already shouldered by monetary policy, the euro area fiscal stance is appropriate in 2020 based on the current macroeconomic projections. Given the uncertainty surrounding the forecast for 2021, it is premature at this stage to assess the fiscal stance beyond 2020.

Notwithstanding risks, the debt positions remain sustainable over the medium-term in all Member States, also given important mitigating factors. According to the Commission's latest debt sustainability analysis, even if the government debt positions deteriorate due to the COVID-19 crisis, the debt-to-GDP ratios are expected to be on a sustainable trajectory over the medium term in all Member States under the baseline scenario consistent with Member States remaining subject to the EU's economic and fiscal coordination and surveillance frameworks. Delayed economic recovery and contingent liabilities arising from the government guarantees put in place in response to the crisis, although necessary to support the economies, represent tangible risks. Nonetheless, the profile of government debt mitigates debt vulnerabilities in the euro area Member States, thanks to the lengthening of maturities over the past years and relatively stable and favourable financing sources.

INTRODUCTION

This annual paper provides an overview of the 2020 Stability and Convergence Programmes (SCPs) submitted by EU Member States.([1]) This review offers a cross-country aggregated view of fiscal policy plans in the European Union and includes an assessment of the fiscal stance and policy mix in the euro area. In light of the ongoing COVID-19 crisis, both the reporting requirements for Member States and the analysis produced by the Commission had to be adapted compared to previous years.

The Stability and Growth Pact (SGP) requires Member States to submit their SCPs annually in April.([2]) Guidelines on the format and content of the SCPs are set out in the Code of Conduct of the SGP.([3]) In light of the exceptional economic uncertainty this year, the Commission concurred with Member States' request to reduce the level of information provided in their SCPs. Accordingly, the content and the structure of this note has been adapted compared to previous years. In particular, unlike in the previous years, there are important differences in the content of the SCPs submitted by Member States, which affected the possibility to compare the various situations across the EU.

The note consists of four sections. Section 1 examines the implementation of SCPs in 2019. Indeed, while the economic developments of 2019 have become quickly outdated due to the COVID-19 outbreak, taking stock of the pre-outbreak situation is useful for assessing the impact of the current crisis. Section 2 presents the budgetary plans set out by Member States in their SCPs for 2020 and—to the extent possible—2021. Section 3 analyses and assesses the overall fiscal stance in the euro area. Section 4 studies longer-term fiscal sustainability implications of the plan through the lenses of the debt sustainability analysis conducted by the Commission in the context of the European Stability Mechanism's Pandemic Crisis Support. Following the practice introduced in last year's edition, the note contains a number of self-standing analytical boxes, which focus on saving-investment imbalances, the common EU response to the COVID-19 outbreak, and liquidity measures adopted by national authorities. Finally, an annex provides tables of the data available from both the SCPs and the Commission 2020 spring forecast.

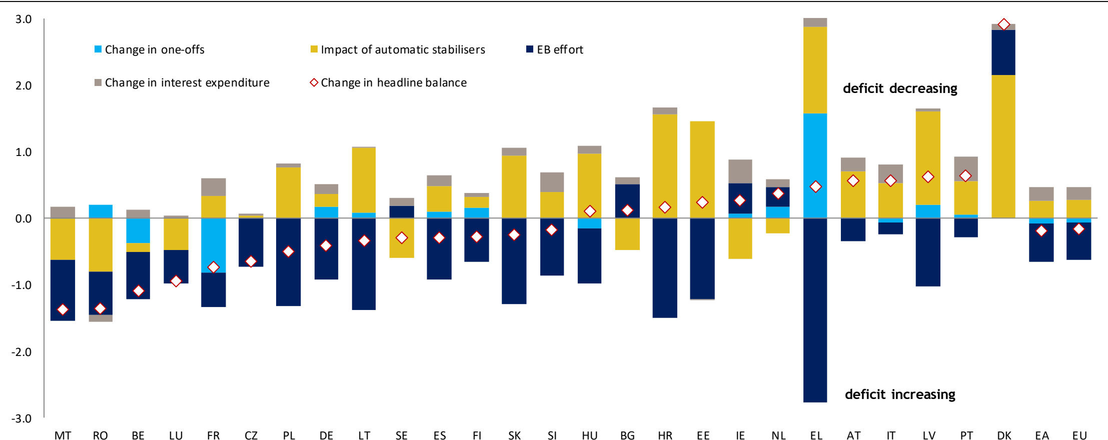
([1]) The analysis is built around data reported by Member States in their 2020 SCPs, unless otherwise specified.
([2]) Articles 4(1) and 8(2) of Regulation 1466/97, on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies (preventive arm of the Stability and Growth Pact).
([3]) http://data.consilium.europa.eu/doc/document/ST-9344-2017-INIT/en/pdf

1. 2019 AT A GLANCE: BUDGETARY DEVELOPMENTS

Overall budgetary developments in 2019

Aggregate headline balances declined marginally in 2019 despite an increase in about half of Member States (Graph 1.1). After improving for eight years since 2010, the aggregate headline balance reached a high of -0.4% of GDP in 2018 and declined to -0.6% in 2019 in the EU, with similar outcomes in the euro area. The drop in headline balance exceeded 0.5 pps. of GDP in seven member States (Belgium, Czechia, France, Luxembourg, Malta, Poland and Romania). The aggregate outcome was driven by an overall negative fiscal effort of about 0.6 pps. of GDP (estimated according to the expenditure benchmark methodology([4])), with sizeable fiscal loosening of more than 1 pps. of GDP in several Member States. In Romania, the negative fiscal effort and sizable revenue shortfalls resulted in an excessive deficit of 4.3% of GDP in 2019. At the same time, headline balances increased in twelve countries, thanks to revenue and interest rate windfalls. Almost all Member States also benefited from improved cyclical conditions.

Graph 1.1: **Drivers of the change in the headline balance between 2018 and 2019 (pps. of GDP)**

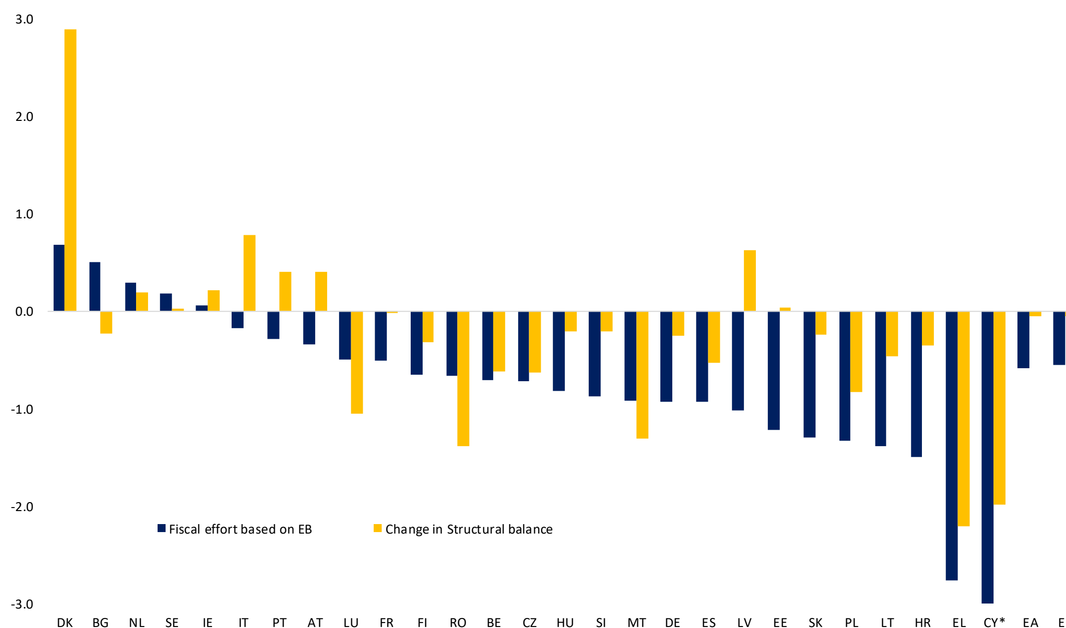


Note: The graph shows the changes in the headline balances between 2018 and 2019 due to fiscal effort based on the expenditure benchmark (EB) methodology, change in interest expenditure, change in one-offs and the impact of automatic stabilizers (measured as a change in cyclical components plus residual items, such as revenue windfalls/ shortfalls). A positive (negative) value means contributing to an improvement (worsening) of the headline balance. Cyprus falls outside of the graph as the headline balance increased by 5.4 pps. of GDP in 2019 due to a large one-off support to the banking sector (in the order of 8% of GDP) in the preceding year.
Source: European Commission 2020 spring forecast.

Using the change in structural balance – directly affected by revenue and interest rate windfalls – provides a more benign picture of the aggregate fiscal effort than the expenditure benchmark measure (Graph 1.2). The aggregate structural balance decreased in 2019 by 0.1 pps. of GDP in both the EU and in the euro area, which points to a neutral fiscal stance. However, the fiscal effort estimated on the basis of the expenditure benchmark methodology points to an expansion by 0.6 pps. of GDP in both areas. This result was mainly driven by two large Member States: Germany, which used some of its fiscal space, and Spain although without fiscal scope (both around 1 pp. of GDP). Slightly expansionary fiscal policies based on the expenditure benchmark were pursued also by other highly indebted Member States (Belgium, France and Portugal), while Italy recorded a broadly neutral fiscal effort. The difference between the two indicators of fiscal effort is explained by lower interest expenditure and positive revenue windfalls, which had a positive impact on the structural balance but which were excluded from the

([4]) For additional information on the computation of the expenditure benchmark see European Commission (2019). "Vade Mecum on the SGP". European Economy, Institutional Paper 101, pp 28-32. Available online: https://ec.europa.eu/info/sites/info/files/economy-finance/ip101_en.pdf

Graph 1.2: **Fiscal effort in 2019 (pps. of potential GDP)**



Note: The graph shows the fiscal effort in 2019 based on the expenditure benchmark (EB) methodology and change in the structural balance. The fiscal effort based on the EB methodology is computed using the outturn data for GDP deflators and medium term potential growth in 2019, while the country-specific recommendations for expenditure benchmark developments in 2019 were based on GDP deflators and medium term potential growth as projected in the Commission 2018 spring forecast.
*In 2019, for Cyprus the fiscal effort based on the expenditure benchmark goes beyond the range of the axis being around -6ppt of GDP. This stance is affected by sizeable one-offs that increased gross fixed capital formation (GFCF) in 2018. In the expenditure benchmark GFCF is smoothed over four years which, in this case, implies lower expenditure net of one-offs in 2018 and higher in 2019.
Source: European Commission 2020 spring forecast.

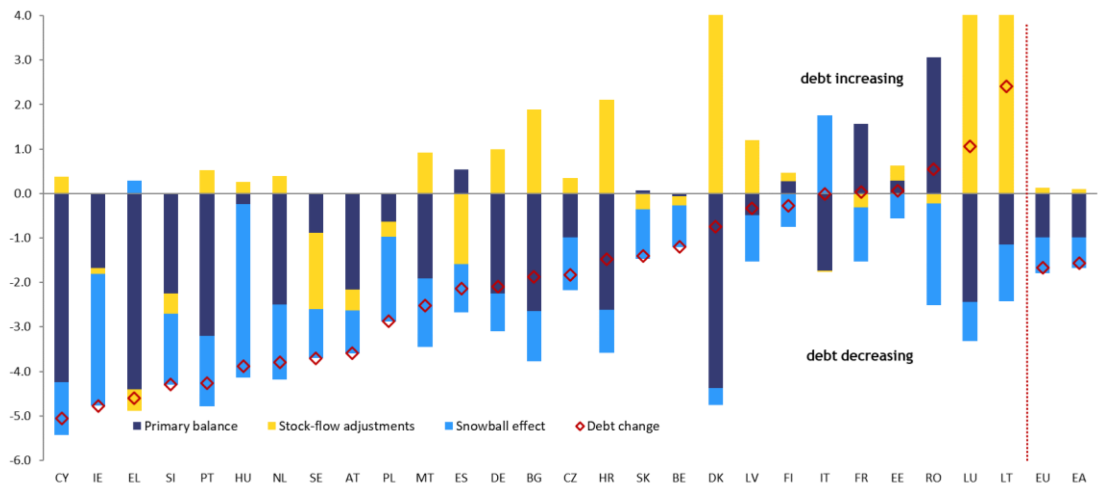
expenditure benchmark calculations. While the aggregate direction of the fiscal stance in 2019 was broadly appropriate as it responded to a slowdown of the euro area economy and low inflation dynamics, the geographical composition was clearly suboptimal.

Ten Member States recorded a structural balance at or above their medium-term budgetary objective (MTO) in 2019 while twelve departed further or stayed away from their MTO. Among the 11 Member States that had been at or above the MTO in 2018, only Malta deviated from its MTO in 2019. As for the other sixteen Member States in the preventive arm, five (Ireland, Italy, Latvia, Austria and Portugal) moved closer to their MTO in 2019, two (Estonia and France) kept their structural balance constant, while nine (Belgium, Spain, Lithuania, Hungary, Poland, Romania, Slovenia, Slovakia and Finland) worsened their structural position. Considerably more negative indications come from the fiscal effort based on expenditure benchmark methodology as out of those sixteen Member States, a negative effort was recorded in all but one (Ireland).

The aggregate debt-to-GDP ratio continued to decrease in 2019 for the EU and the euro area (Graph 1.3). The aggregate ratio fell by 1.7 pps. of GDP to 79.4% of GDP in the EU and by 1.6 pps. to 86.0% of GDP in the euro area, about 9 pps. below the 2014 peaks.([5]) Similarly to 2018, the decline was driven by primary surpluses and a debt-decreasing snowball effect, the latter due to GDP growth exceeding the implicit average cost of servicing the outstanding debt.

([5]) Aggregate debt figures are not consolidated for intergovernmental lending amounting to around 1.5% of GDP in the EU and 2% of GDP for the euro area. Excluding intergovernmental lending, in 2019 the debt ratio was 77.8% of GDP in the EU and 84.1% in the euro area.

Graph 1.3: **Contributions to the change in the debt-to-GDP ratio in 2019 (pps. of GDP)**



Note: The graph disaggregates the changes in debt-to-GDP ratios in 2019 between the contributions of the primary balance, stock-flow adjustments and the snowball effect, the latter of which refers to the interest rate-growth rate differential. Negative (positive) values indicate that the concerned factor contributed to a decrease (increase) in the debt-to-GDP ratio, i.e. primary balances are shown with an opposite sign.
Source: European Commission 2020 spring forecast.

Debt-to-GDP ratios fell in the large majority of Member States (Graph 1.3). The exceptions were Estonia, Lithuania, Luxembourg and Romania (where the ratios increased), and France and Italy (no change). Most Member States recorded a primary surplus in 2019, which contributed to debt reduction. The exceptions were Estonia, Spain, France and Romania, which recorded primary deficits also in 2018, and Slovakia and Finland. The snowball effect remained favourable in all Member States but Italy. Stock-flow adjustments, which mainly refer to financial transactions and discrepancies between cash and ESA2010 figures, were broadly neutral in aggregate terms in the EU and the euro area. However, they had a substantial upward effect on public debt of more than 1% of GDP in Bulgaria, Croatia and Latvia, and especially in Denmark, Lithuania and Luxembourg where the debt-increasing impact exceeded 4% of GDP. By contrast, the stock-flow adjustment had a sizeable downward impact in Spain and Sweden.

Comparison between the 2019 outturn and the 2019 Stability and Convergence Programmes

The 2019 aggregate headline balance turned out better than planned in the 2019 SCPs owing to better-than-planned revenue developments (Table 1.1). Real GDP growth was weaker-than-planned in the EU and the euro area, while the output gap stayed broadly unchanged in 2019 in both areas. At the same time, inflation (measured using the GDP deflator) turned out slightly higher. The lower increase in the 2019 headline deficit compared to the 2019 SCPs stems from revenue windfalls, among others thanks to more positive employment and wage developments. These windfalls explain better-than-projected changes in the headline and structural balance of around 0.2 pps. of GDP. Interest expenditure also turned out slightly lower than projected in the 2019 SCPs. By contrast and as mentioned earlier, the fiscal effort based on the expenditure benchmark methodology, which is not affected by revenue and interest windfalls, turned out more negative than planned in both the EU and the euro area.

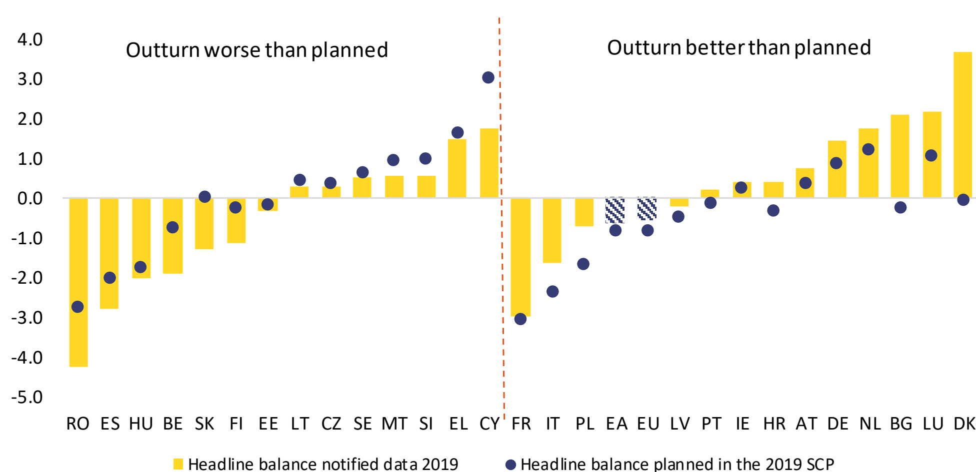
About half of the Member States reached or over-performed the 2019 headline balance target set in their 2019 SCPs (Graph 1.4). The over-performance mostly reflected a higher-than-planned increase of the structural balance (Bulgaria, Denmark, Germany, Croatia, Italy, Luxembourg, Netherlands and Poland). In contrast, where the target was missed, this was primarily because of a larger-than-planned fall in structural balance (Belgium, Cyprus, Romania and Slovakia) and partly also due to a less positive impact of the cycle on the budget outcome (Spain, Romania, Slovakia and Finland).

Table 1.1: **Economic and budgetary developments in the EU and the euro area in 2019**

		2019 SCP planned	COM spring forecast
EU	Real GDP growth	1.6	1.5
Euro area		1.4	1.2
EU	Nominal GDP growth	3.3	3.5
Euro area		3.0	3.0
EU	Inflation (GDP deflator)	1.7	1.9
Euro area		1.6	1.7
EU	Output gap	0.4	1.2
Euro area		0.4	1.1
EU	Headline balance	-0.8	-0.6
Euro area		-0.9	-0.6
EU	Interest expenditure	1.6	1.5
Euro area		1.7	1.6
EU	Change in output gap	-0.1	-0.1
Euro area		-0.1	-0.1
EU	Change in the headline balance	-0.3	-0.2
Euro area		-0.3	-0.2
EU	Change in structural balance	-0.2	-0.1
Euro area		-0.2	-0.1
EU	Fiscal effort based on EB	-0.3	-0.6
Euro area		-0.3	-0.6

Source: European Commission 2020 spring forecast and 2019 SCPs.

Graph 1.4: **Headline balance in EU Member States in 2019, outturn vs 2019 SCPs (% of GDP)**



Notes: The graph plots the notified 2019 headline budget balances (vertical axis) against the planned headline budget balance (horizontal axis). Member States above (below) the 45-degree line are those where the 2019 outcome was better (worse) than planned.
Source: European Commission 2020 spring forecast.

2. BUDGETARY PLANS FOR 2020 AND BEYOND

2.1. CONTEXT: THE ACTIVATION OF THE GENERAL ESCAPE CLAUSE

The Stability and Growth Pact (SGP) allows Member States to deal with the sizeable challenges resulting from the COVID-19 crisis. On 13 March 2020, the Commission adopted a Communication on a coordinated economic response to the COVID-19 outbreak.([6]) It proposed that the Union institutions should apply the full flexibility existing within the EU fiscal framework, including for 'unusual events outside the control of the government' to help Member States address the outbreak. As the gravity of the economic downturn resulting from the COVID-19 outbreak became apparent, the Commission considered in its Communication of 20 March 2020 that the economic conditions warrant the activation of the general escape clause of the Stability and Growth Pact.([7]) The general escape clause does not suspend the procedures of the Pact. It allows Member States to depart from the budgetary requirements that would normally apply, provided that this does not endanger fiscal sustainability in the medium term, while enabling the Commission and the Council to undertake the necessary policy coordination measures within the framework of the Pact. On 23 March 2020, the Ministers of Finance of the EU Member States supported that view.

The activation of the general escape clause allows Member States to depart temporarily from their fiscal adjustment path or the MTO. In particular, articles 5(1) and 9(1) of the preventive arm (Regulation (EC) 1466/97) allow Member States to temporarily depart from the adjustment path towards the MTO "in periods of severe economic downturn for the euro area or the Union as a whole (…) provided that this does not endanger fiscal sustainability in the medium term". For the corrective arm (Regulation (EC) 1467/97), articles 3(5) and 5(2) stipulate that in the case of a severe economic downturn in the euro area or in the Union as a whole, the Council may also decide, on a recommendation from the Commission, to adopt a revised fiscal trajectory. This is the first use of the clause since its introduction the context of the reform of the SGP in 2011.

The general escape clause responds to the current situation in the EU, in which all Member States have been subject to a significant negative economic shock. Its activation allows Member States to take broader temporary measures than the measures with a direct link to the COVID-19 outbreak that would be eligible under the unusual event clause or classified as one-offs. The reporting of such measures in the context of the stability and convergence programmes allows the Commission and the Council to coordinate the EU's fiscal response to the crisis.

The fiscal elements of the 2020 country-specific recommendations reflect the activation of the general escape clause. Given the symmetric nature of the shock, Member States are recommended to take all necessary measures to effectively address the pandemic, sustain the economy and support the ensuing recovery. When economic conditions allow, fiscal policies should aim at achieving prudent medium term fiscal positions and ensuring debt sustainability, while enhancing investment.

2.2. OVERVIEW OF MEMBER STATES' PROGRAMMES

The European Union is experiencing the deepest economic recession in its history. The COVID-19 pandemic is the most devastating health crisis the EU has experienced since its establishment in 1957. The outbreak led to drastic containment measures, which have profoundly disrupted the European economy, affecting all Member States (albeit to a various extent). The Commission 2020 spring forecast expects a severe contraction of economic activity of 7.5% in 2020 (Graph 2.1). Real GDP is forecast to

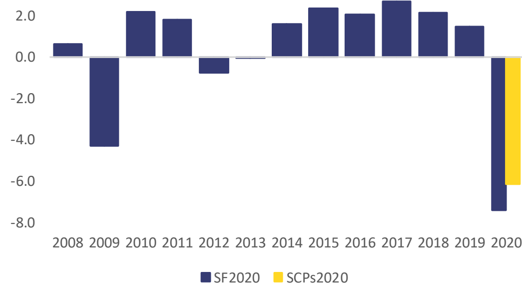
([6]) https://ec.europa.eu/transparency/regdoc/rep/1/2020/EN/COM-2020-112-F1-EN-MAIN-PART-1.PDF
([7]) https://ec.europa.eu/info/sites/info/files/economy-finance/2_en_act_part1_v3-adopted_text.pdf

fall in all EU Member States, from -4¼% in Poland to -9¾% in Greece. In aggregate, the 2020 SCPs also predict a sizeable, albeit slightly lower, contraction of -6.2% in 2020.

Outlook for GDP and headline deficit for 2020 and 2021

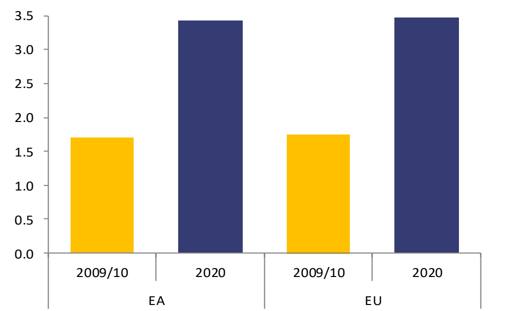
Nearly all Member States project a sharp recession in 2020, while the outlook for 2021 is much more uncertain (Table A1.1).([8]) In most Member States, these forecasts were prepared or endorsed by independent fiscal institutions (Box 2.1). By and large, the Commission and Member States forecast similarly sized contractions in 2020, with only Bulgaria, Greece, Hungary, the Netherlands and Romania projecting markedly more optimistic growth outcomes in 2020 than the Commission. In 2021, both the Commission and Member States expect a return to positive GDP growth, subject to a gradual abating of the pandemic in the second half of 2020. However, there is exceptional uncertainty surrounding the timing and size of the expected rebound, and several countries did not present growth forecasts for the next year (Bulgaria, Germany, France, Poland, Portugal and Romania). In response to this uncertain and severely negative economic outlook, European households have significantly increased their precautionary savings (Box 2.2).

Graph 2.1 **Real GDP growth in the European Union in 2008-2020 (%)**



Source: European Commission 2020 spring forecast and 2020 SCPs.

Graph 2.2: **Fiscal stimulus measures in 2009-2010 and 2020 (% of GDP)**



Note: The impact of discretionary measures adopted before the COVID-19 outbreak is also included in the 2020 total. This estimate includes measures implemented through the cut-off date for the Commission 2020 spring forecast of 23 April 2020. Additional measures have been taken adopted after the cut-off date.
Source: European Commission (2009). "*Report on Public Finances in EMU*". *European Economy 5/2009*, chapter I; European Commission 2020 spring forecast.

([8]) The only exceptions are the Netherlands (which based its stability programme on an outdated macroeconomic scenario predating the COVID-19 crisis) and Portugal (which did not include a complete macroeconomic scenario in its stability programme). The assessment of the Dutch stability programme also took into account the more recent Spring Budget Memorandum of 24 April 2020. Italy's projections for government deficit and debt took into account the government decree adopted on 13 May 2020.

Box 2.1: Independent production or endorsement of the macroeconomic forecasts underpinning the 2020 Stability and Convergence Programmes

Prudent macroeconomic forecasts play an important role in budgetary processes. In the euro area, Member States are required to base their national medium-term fiscal plans on independent macroeconomic forecasts,([1]) defined as "forecasts produced or endorsed by independent bodies".([2]) In spring 2020, 18 euro area Member States included macroeconomic forecasts in their stability programmes, and they were all either prepared or endorsed by independent fiscal institutions. In particular:

- Four Member States relied as usual on macroeconomic forecasts prepared by external independent producers (Luxembourg, Netherlands, Austria and Slovenia).
- In Belgium, exceptionally, the macroeconomic forecast was prepared jointly by the Federal Planning Bureau (the traditional independent producer) and the central bank.
- In Finland, the macroeconomic forecast was produced autonomously by the Ministry of Finance's Economics Department, in line with the applicable arrangements.
- In 12 euro area Member States, the official macroeconomic scenario was produced by the government and subsequently endorsed by an independent fiscal institution, either a national fiscal council (Estonia, Ireland, Greece, Spain, France, Italy, Cyprus, Latvia, Lithuania and Malta) or an expert committee tasked with assessing the forecasts (Germany and Slovakia). Nearly all institutions emphasised the extraordinary uncertainty surrounding the forecasts. In some cases, the endorsement publications signalled that the official GDP projections were on the upper side of the endorseable range (for example, Estonia and Greece). In the German case, the stability programme was initially prepared on the basis of ad-hoc projections, but the endorsement was provided for the government's fully fledged spring forecast (depicting similar trajectories to the programme's scenario).

Portugal did not include a complete macroeconomic scenario (or budgetary projections) in its stability programme and therefore the Public Finance Council was not in a position to carry out its customary analysis underpinning an endorsement decision.

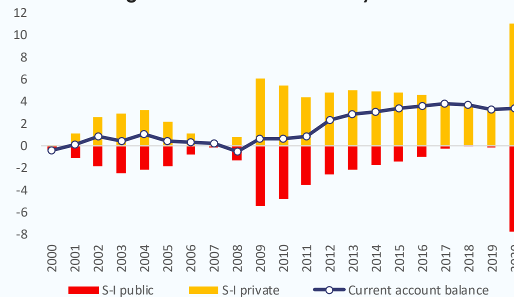
There is no corresponding legal requirement outside the euro area and practices vary. Independent fiscal institutions typically opine on the realism of macroeconomic projections, especially in the context of annual budgets, but their opinions have no institutional bearing on the policy-making process. In the context of the 2020 SCPs, the Czech Committee on Budgetary Forecasts and the Romanian Fiscal Council assessed the macroeconomic forecast underpinning the programmes as optimistic.

([1]) Article 4(4) of the Two-Pack Regulation (EU) No 473/2013.
([2]) Article 2(1b) of the Two-Pack Regulation (EU) No 473/2013.

Box 2.2: Euro area: more public investment to reduce the saving glut?

Savings continue to exceed investment in the euro area. The global financial crisis triggered a long-lasting deleveraging trend in both private and public sector (Graph 1). Private sector investment remains significantly lower than private savings. While the former is hindered by structural factors, the latter also reflect precautionary action to cater for the future in the face of an ageing population. Public sector investment remains below the levels prevailing before the economic and financial crisis and, in recent years, has been fully financed by public savings. The COVID-19 pandemic will significantly affect investment and savings developments. The private sector excess of savings relative to investment is expected to jump to unprecedented levels in 2020 due to business investment collapsing and a sharp increase in precautionary household savings. By contrast, public savings are set to turn significantly negative, reflecting the substantial fiscal response to the COVID-19 pandemic. These savings/investment developments have resulted in a rising current account surplus in the euro area since 2009. Based on the Commission 2020 spring forecast, the surplus is projected to amount to 3¼% of GDP in 2020, slightly higher than in 2019, but still slightly below the peak of 3¾% reached in 2017. High uncertainty surrounds this forecast.

Graph 1: **Euro area excess of savings relative to investments by sector and current account (% of GDP)**



Source: European Commission 2020 spring forecast.

The COVID-19 crisis is expected to trigger an unprecedented increase in the euro-area private savings, with public savings falling. The rise in private savings in 2020 is forecast to be much bigger than the one recorded following the financial crisis in 2009 (5¾ pps. vs 1¾ pps. of GDP respectively). High private savings levels of more than 30% of GDP are expected in Germany and the Netherlands, with Italy, Greece and Germany expected to record the strongest increases. These hikes in private savings will be accompanied by even larger falls in public savings, which for the euro area aggregate are set to be twice than in 2009 (-7¼ pps. vs -3¾ pps. of GDP).

The drop in private capital formation is expected to be sizeable. Private capital formation decreased steeply in the euro area in 2009 (by 3 ½ pps. of GDP), also due to a very large destocking. A significant fall is expected also in 2020 (1¾ pps of GDP). The sizeable liquidity and budgetary support put in place at national level and by the European institutions as well as a more resilient financial sector should limit the risk of an even bigger drop in private capital formation.

The final effects of the COVID-19 crisis on savings and investment will depend on its length, which is uncertain now. ([1]) If the shock is temporary, then saving preferences are unlikely to change. However, if the shock is long-lasting due to multiple waves of infections, long spells of depressed

([1]) See Gavin Goy, Jan Willem van den End (2020). The impact of the COVID-19 crisis on the equilibrium interest rate. https://voxeu.org/article/impact-covid-19-crisis-equilibrium-interest-rate

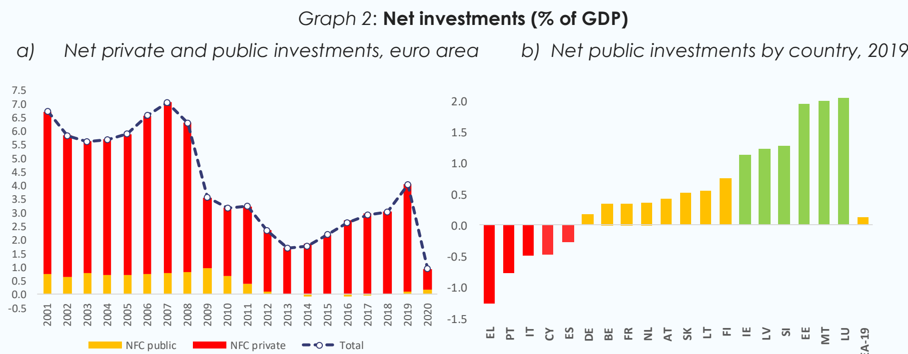
(Continued on the next page)

Box (continued)

investment opportunities and high precautionary savings should be expected.(2) The resulting further downward pressures on the natural interest rate in the euro area would amplify concerns about a prolonged low-interest-rate environment in Europe, with implications for the standard monetary policy.

Graph 2: **Net investments (% of GDP)**

a) Net private and public investments, euro area *b) Net public investments by country, 2019*



Note: Net investment is the difference between gross investment and net of consumption of fixed capital (or depreciation). Net public investment above 1% of GDP are in green as this level is consist with a public capital stock remaining at 50% of GDP in the euro area in the short term and gradually increasing in the longer term, to take into account the additional investment needs related to the Green Deal and the digital transformation.
Source: European Commission 2020 spring forecast.

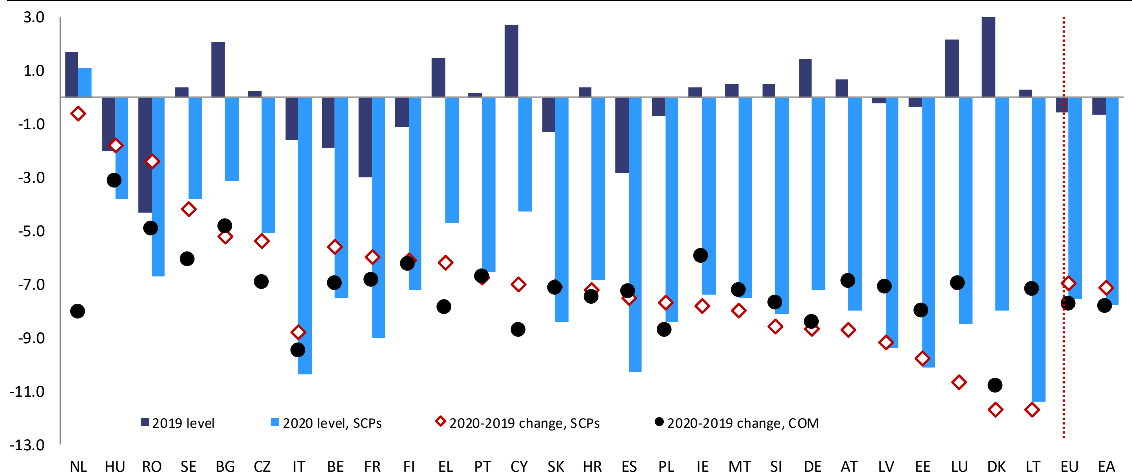
Fiscal and structural policies should support a recovery focused on sustainability and innovation. In the context of high uncertainty, entrenched excess savings and low net private investments (Graph 2a), higher public investments will play an important role in the recovery of the euro area. Unlike in the aftermath of the previous crisis, cuts in public investment should not be used to achieve sustainable fiscal positions. Instead, higher public investment together with ambitious structural reforms would need to support the green transition and digital transformation of European economies, consistent the EU Green Deal and the recovery strategy proposed by the Commission. (3) Higher public investment is also needed to address concerns about the ongoing erosion of the public capital stock in several Member States due to the low or even negative public investment net of capital depreciation (Graph 2b).

The Commission's Recovery Plan for Europe and the other measures taken at the EU level will be an essential element to support private and public investment in the coming years (Box 2.4). In the absence of a strong European policy response to the COVID-19 outbreak, growth would remain sluggish, with a permanently weakened corporate sector and high unemployment. Lower public and private investment in vulnerable Member States, sectors and regions would also result in growing divergences, a permanent distortion of the level playing field of the Single Market and increased divergence of living standards.

(2) Jordà, Ò, S R Singh, and A. M. Taylor (2020). Longer-run economic consequences of pandemics. *Covid Economics: Vetted and Real-Time Papers* 1: 1–15.
(3) https://ec.europa.eu/info/live-work-travel-eu/health/coronavirus-response/recovery-plan-europe_en

The unprecedented fiscal policy response to the pandemic will cause public deficits to rise sharply in 2020. In addition to support delivered by the automatic stabilisers, European policymakers provided swift fiscal support of magnitude much higher than during the global financial crisis (Graph 2.2). As a result, Member States predict the aggregate general government deficit to surge from 0.6% of GDP in 2019 to 7.4% of GDP in 2020, with headline deficits increasing in all countries (Graph 2.3). Record deficits of more than 8% of GDP are foreseen in a third of Member States (Estonia, Spain, France, Italy, Latvia, Luxembourg, Poland, Slovakia and Slovenia). The Commission forecasts an even bigger aggregate deficit of 8.5% of GDP in 2020, in particular due to a markedly different projection for the Netherlands: a deficit of 6.3% of GDP versus the authorities' forecast of a surplus of 1.1% of GDP (based

Graph 2.3: **Planned budgetary developments in 2020 (% of GDP)**



Note: The graph shows the headline budget balance in 2019 and 2020 according to the 2020 SCPs, and the change planned between 2019 and 2020 according to the 2020 SCPs and the Commission 2020 spring forecast. In the case of Portugal, the graph shows the data from the Commission 2020 spring forecast only.
Source: European Commission based on 2020 SCPs.

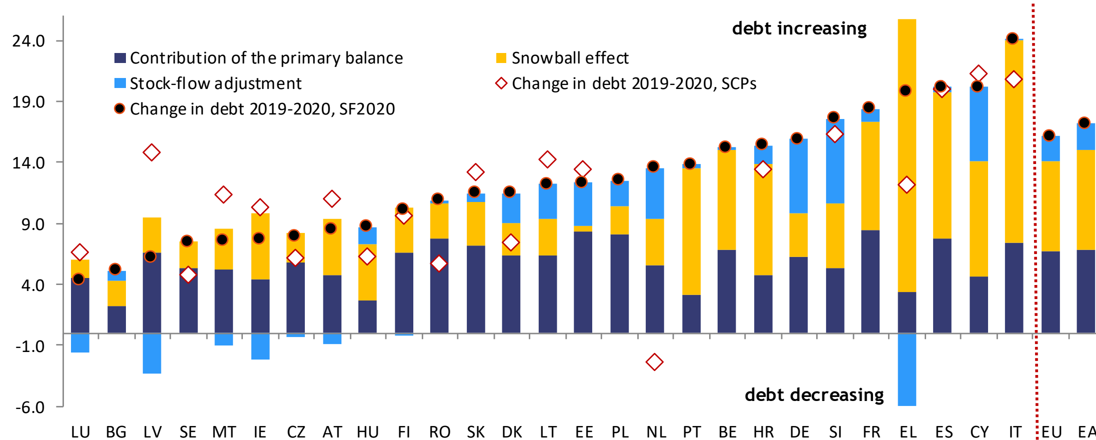
on the pre-pandemic macroeconomic scenario([9])). Following Member States' planned deficits in excess of the 3% of GDP Treaty reference value, the Commission adopted on 20 May 2020 reports under Article 126(3) TFEU in the context of the excessive deficit procedure (except for Romania, which is in the corrective arm of the Pact).([10])

In 2021, headline deficits are expected to ease, reflecting the anticipated unwinding of temporary measures adopted in response to the pandemic and the rebound of economic activity. According to the Commission 2020 spring forecast, the headline deficit will decrease to 3½% of GDP in the EU as a whole. While Member States concur with this view, many could not quantify the fiscal implications of the COVID-19 pandemic for the year 2021. Nine Member States were not in a position to provide fiscal forecasts for 2021 (Belgium, Bulgaria, Germany, Spain, France, Poland, Portugal, Romania and Slovenia)

The macroeconomic and fiscal outlook are surrounded by exceptionally high uncertainty, linked to the evolution of the COVID-19 pandemic. The economic outlook is primarily determined by the development of the pandemic. The Commission projections rest on a number of assumptions: that the major economic impact of COVID-19 will be observed in the second quarter of 2020; that containment measures will be gradually lifted in the coming months; and that the adopted measures to limit the negative economic effects prove effective. However, it is not excluded that the pandemic becomes more severe and last longer than assumed in the spring forecast, requiring more stringent and longer-lasting containment measures. This would result in worse economic and fiscal outcomes. It could also require further fiscal policy measures, resulting in worse fiscal outcomes while helping mitigate the economic impact. In addition, reaching the end of the transition period foreseen in the Withdrawal Agreement between the EU and the UK will dampen economic growth and presents a downside risk to the technical assumption of unchanged trading relations between the EU and the UK used in the forecast. Specific risks underlying the budgetary projections relate to contingent liabilities stemming from some public and private corporations and some overly optimistic revenue and expenditure projections. The volatility of sovereign bond yields also poses a risk, in particular for high debt Member States, though this risk is mitigated by European Central Bank's asset purchase programs (Section 3.2).

([9]) The Spring Budget Memorandum projects a deficit of 11.8% of GDP in 2020.
([10]) While the Commission concluded for all Member States except Bulgaria that the deficit criterion of the Treaty was not fulfilled, it considered that at this juncture decision on whether to place Member States under the excessive deficit procedure should not be taken. The outbreak of COVID-19 has had an extraordinary macroeconomic and fiscal impact, which is still unfolding. This creates exceptional uncertainty, including for designing a credible path for fiscal policy, which will have to maintain a supportive stance to close the output gap whilst ensuring the sustainability of public debt and eventually correcting the excessive deficit. The Commission will reassess Member States' budgetary situation on the basis of the 2020 autumn forecast, and the Draft Budgetary Plans to be submitted by euro area Member States by 15 October 2020.

Graph 2.4: **Contributions to the change in the debt-to-GDP ratio between 2019 and 2020 (pps. of GDP)**



Note: The graph shows the change in debt-to-GDP ratios between 2019 and 2020 according to the 2020 SCPs and the Commission 2020 spring forecast. The graph also disaggregates the 2019-2020 change into contributions of primary balance, the snowball effect (the interest rate-growth differential) and the stock-flow adjustment. Values below (above) zero indicate a decreasing (increasing) impact on the debt ratio. The contribution data come from the Commission 2020 spring forecast.
Source: European Commission 2020 spring forecast and 2020 SCPs.

Expected debt developments

Reversing its declining trend since 2015, government debt is projected to increase sharply in 2020 (Graph 2.4)**.** The aggregated debt-to-GDP ratio is projected to rise substantially, reaching a new peak of around 103% in the euro area and almost 96% of GDP in the EU, according to the Commission 2020 spring forecast. Debt-to-GDP ratios will exceed 100% of GDP in Belgium, Greece, Spain, France, Italy, Cyprus and Portugal. The debt projections in the Commission 2020 spring forecast are closely in line with those presented in the SCPs. The expected debt dynamics reflect the weakening of the primary balance and unfavourable snowball effect due to the strongly negative nominal GDP growth. In a few cases, there are also sizeable debt-increasing stock-flow adjustment, in particular in Germany (resulting from the set-up of the Economic Stabilisation Fund), Cyprus (due to a planned increase in cash reserves), and Slovenia (due to tax deferrals and pre-financing for 2021).

In 2021, under a no-policy-change assumption, the aggregate debt ratio is forecast to decline but remain above the pre-crisis ratio of 2019. According to the Commission 2020 spring forecast, public debt should recede in 2021 to 92.2% of GDP in the EU and 99.2% of GDP in the euro area. At the same time, it is likely to remain above 100% in the above-mentioned seven Member States.

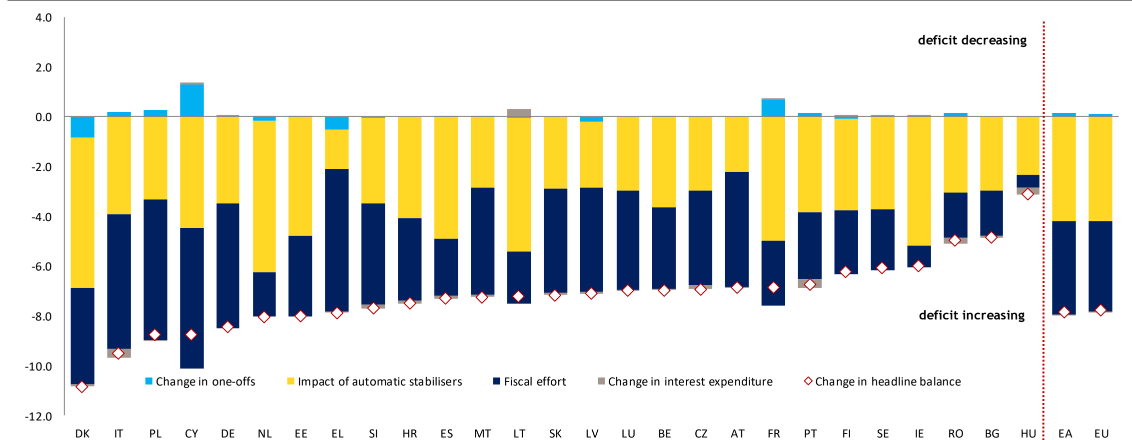
Analysing discretionary fiscal effort in 2020

The operation of automatic stabilisers—the non-discretionary part of fiscal policy—accounts for more than half of the evolution of the headline balance in aggregate.([11]) Automatic stabilisers are usually considered the most effective tool to stabilise the economy after temporary shocks as they are timely, temporary and targeted.([12]) The Commission 2020 spring forecast estimates that the automatic stabilisers amount to an average of 4.2% of GDP in 2020 (estimated after deducting the discretionary fiscal effort and the impact of one-offs from the decline of the primary balance; Graph 2.5). For several

([11]) This analysis is based on the Commission 2020 spring forecast only, as the 2020 SCPs—in line with the Guidelines issued by the Commission—have been streamlined in light of the exceptional economic uncertainty and the severe constraints that Member States are currently working under.

([12]) Automatic stabilisers timely rise during an economic downturn with no changes of the tax code or any additional government action needed. The support is temporary and gets withdrawn automatically when the economy improves. These instruments target spending and taxes affected by the business cycle, with unemployment benefits increasing to support newly unemployed and taxes decreasing in proportion to the falling household and corporate incomes. See for example Blanchard, O., G. Dell'Ariccia and P. Mauro (2010). "Rethinking macroeconomic policy", *Journal of Money, Credit and Banking*, 42(1): 199–215.

Graph 2.5: **Drivers of the change in the headline balance between 2019 and 2020 (pps. of GDP)**



Note: The graph shows the changes in the headline balances between 2019 and 2020 due to fiscal effort based on the expenditure benchmark methodology, change in interest expenditure, change in one-offs and the impact of automatic stabilizers (measured as a change in cyclical components plus residual items, such as revenue windfalls/ shortfalls). A positive (negative) value means contributing to an improvement (worsening) of the headline balance. In light of the activation of the general escape clause, the measures taken in response to the COVID-19 outbreak in 2020 are not treated as one-off.
Source: European Commission 2020 spring forecast.

countries, automatic stabilisers account for more than two-thirds of the overall fiscal response to the COVID-19 crisis (Ireland, Spain, Lithuania, Hungary and the Netherlands).

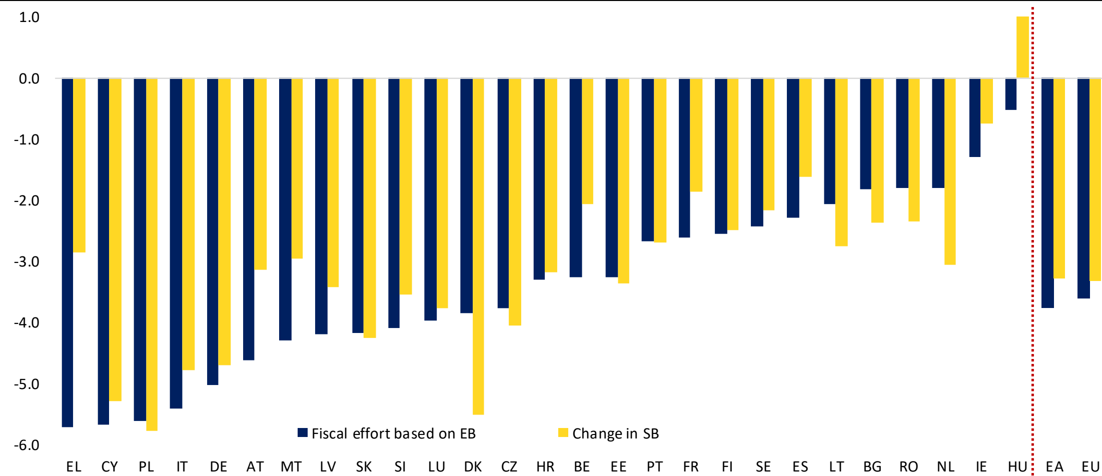
In addition, all Member States are implementing sizeable discretionary fiscal measures to mitigate the immediate health and socio-economic impact of the coronavirus pandemic. The Commission 2020 spring forecast estimates that discretionary fiscal easing, measured as the fiscal effort based on the expenditure benchmark methodology, amounts to 3.6% of GDP, or almost half of the weakening of the aggregated headline balance.([13]) In several countries, discretionary easing exceeds 5% of GDP in 2020 (Germany, Greece, Italy and Poland). Moreover, additional measures have been taken after the 23 April cut-off date of the forecast in response to the evolving economic conditions.

The stark increase in Member States' structural deficits and large deviations from the expenditure benchmark confirm the sizeable fiscal expansion in 2020 (Graph 2.6). The aggregate structural balance is expected to decline in 2020 by 3.3 pps. of GDP in both the EU and the euro area. As mentioned earlier, the fiscal easing based on the expenditure benchmark is estimated at 3.6 pps. of GDP in the EU and 3.8 pps. in the euro area. In some countries, the difference between the two indicators of fiscal effort is partially explained by revenue windfalls or shortfalls (for example in Denmark, Lithuania and Austria). Different underlying estimates of potential growth also contribute to the difference. In 2020, the Commission expects potential output to grow at less-than-half its pace in the previous year. However, the exact impact of COVID-19 on potential output is highly uncertain, which makes estimates of structural balances less precise than usual.([14])

([13]) In some countries, this effort includes the impact of discretionary measures adopted before the COVID-19 crisis. This estimate includes measures implemented through the cut-off date for the Commission 2020 spring forecast of 23 April 2020. Further measures have been adopted after the cut-off date, including an additional fiscal stimulus package of 3.8% of GDP in Germany and an economic rescue plan of additional 4% of GDP in France.

([14]) While some measures taken in response to the COVID-19 pandemic could in principle qualify as a 'one-off', the Commission opted not treat them as one-off given the specific circumstances and the very large uncertainty around their possible persistence beyond 2020. As a result, these measures are not excluded from the estimation of the structural balance, nor from the expenditure benchmark, but subject to the general escape clause.

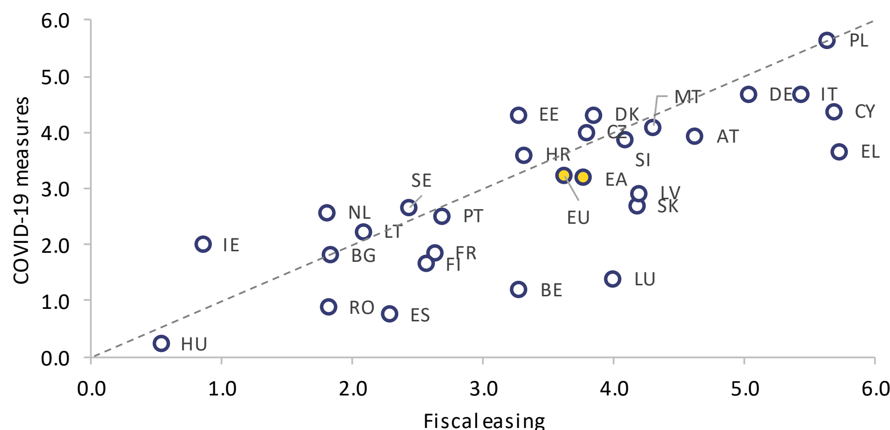
Graph 2.6: **Fiscal effort in 2020 (pps. of potential GDP)**



Note: The graph shows the fiscal effort in 2020 based on the expenditure benchmark methodology and change in the structural balance.
Source: European Commission 2020 spring forecast.

Discretionary measures adopted in response to the pandemic explain most of the fiscal easing in 2020 (Graph 2.7).([15]) The Commission estimates that measures taken in response to the COVID-19 outbreak amount to an average of 3.2% of GDP.([16]) In several Member States the discretionary response to the pandemic exceeds 4% of GDP (Czechia, Denmark, Germany, Estonia, Italy, Cyprus, Malta and Poland). The SCPs suggest an even larger average impact of 4.3% of GDP (Graph 2.8). The differences between the Commission estimates and the SCP data arise from i) classifying some pre-existing schemes as automatic stabilisers as opposed to discretionary measures; ii) different cut-off dates; and iii) different assumptions about the direct budgetary impact of tax deferrals and grants.

Graph 2.7: **Fiscal easing and COVID-19 related discretionary measures in 2020 (% of GDP)**

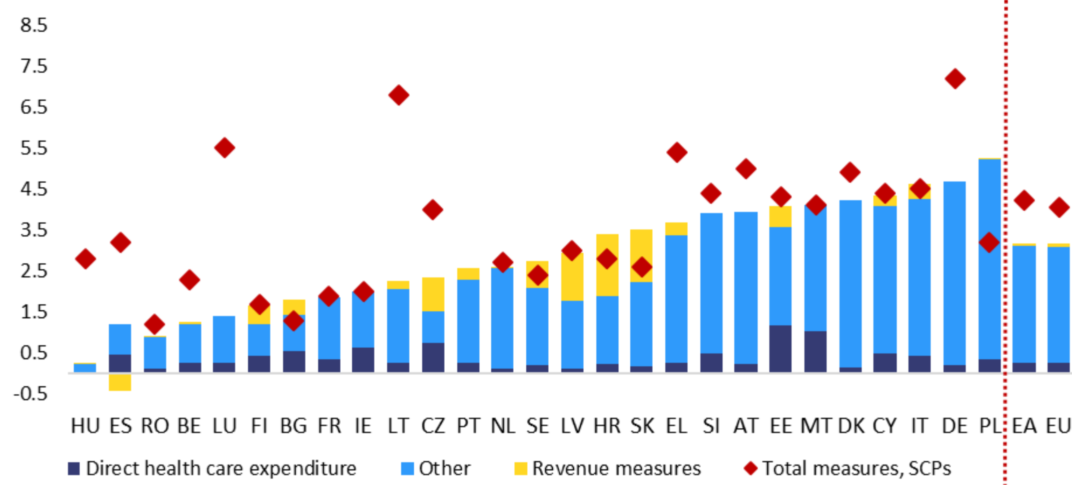


Note: Fiscal easing is measured as the fiscal effort based on the expenditure benchmark methodology.
Source: European Commission 2020 spring forecast.

([15]) Discretionary measures consist of the sum of revenue and expenditure measures as documented in the Commission's spring forecast or SCPs. Fiscal easing on the other hand reflects the negative fiscal effort based on the expenditure benchmark methodology. It includes discretionary measures only on the revenue side (including those taken before the COVID-19 outbreak), while on the expenditure side the fiscal effort is estimated in terms of deviation of primary expenditure growth from the growth of medium-term potential output. That deviation is not necessarily zero in the absence of discretionary expenditure measures, for example due to an autonomous expenditure growth that exceeds (medium-term) potential growth.

([16]) While great efforts have been made to ensure robustness and cross-country consistency of the identification and quantification of COVID-19 measures, this analysis should be considered work-in-progress.

Graph 2.8: **COVID-19 measures with a direct budgetary impact in 2020 (pps. of GDP)**



Note: The graph depicts COVID-19 measures with a direct budgetary impact in 2020, as estimated by the Commission in its 2020 spring forecast (stacked bars) and reported in 2020 SCPs (diamonds). While great efforts have been made to ensure robustness and cross-country consistency of the identification and quantification of COVID-19 measures, this analysis should be considered work-in-progress. Portugal's stability programme reported estimates of the budgetary impacts of COVID-19 measures on an either monthly or annual basis, without providing a projected annual aggregate figure for 2020.
Source: European Commission 2020 spring forecast and 2020 SCPs.

Table 2.1: **COVID-19 measures by beneficiary and budget side (% of GDP)**

		Decomposition by beneficiary					***Decomposition by budget side***	
country	TOT	HOUSEHOLDS		CORPORATIONS		DIRECT GOV. EXP.	EXP	REV
		Exp.	Rev.	Exp.	Rev.			
BE	1.3	0.6	-0.1	0.4	0.0	0.3	1.2	-0.1
CY	4.4	3.6	-0.3	0.0	0.0	0.5	4.1	-0.3
DE	4.7	0.6	0.0	4.0	0.0	0.1	4.7	0.0
EE	4.1	0.8	0.0	1.8	-0.5	1.0	3.6	-0.5
IE	2.0	0.7	0.0	0.7	0.0	0.6	2.0	0.0
EL	3.7	2.3	-0.2	0.9	-0.1	0.2	3.4	-0.3
ES	0.8	0.3	0.5	0.4	-0.1	0.4	1.2	0.4
FR	1.9	1.4	0.0	0.3	0.0	0.2	1.9	0.0
IT	4.5	1.8	0.0	1.9	-0.3	0.5	4.2	-0.4
LV	2.9	0.9	-0.6	0.8	-0.5	0.1	1.8	-1.2
LT	2.2	1.7	-0.1	0.0	-0.1	0.3	2.1	-0.2
LU	1.4	1.2	0.0	0.0	0.0	0.2	1.4	0.0
MT	4.1	0.3	0.0	2.5	0.0	1.3	4.1	0.0
NL	2.6	0.0	0.0	2.6	0.0	0.0	2.6	0.0
AT	3.9	0.2	0.0	3.5	0.0	0.3	3.9	0.0
PT	2.5	0.7	-0.3	1.4	0.0	0.2	2.3	-0.2
SI	3.9	1.2	0.0	2.3	0.0	0.4	3.9	0.0
SK	3.5	1.1	-1.3	1.1	0.0	0.0	2.2	-1.3
FI	1.7	0.2	-0.5	0.6	0.0	0.4	1.2	-0.5
EA	3.1	0.9	0.0	2.0	-0.1	0.2	3.1	0.0
BG	1.8	0.5	0.0	0.9	-0.4	0.0	1.4	-0.4
CZ	2.3	0.5	-0.8	0.7	0.0	0.3	1.5	-0.8
DK	4.2	0.0	0.0	3.8	0.0	0.5	4.2	0.0
HR	3.4	0.0	-1.5	1.9	0.0	0.0	1.9	-1.5
HU	0.2	0.5	-0.2	0.0	0.2	-0.3	0.2	0.0
PL	5.2	0.4	0.0	4.5	0.0	0.3	5.2	0.0
RO	0.9	0.1	0.0	0.6	0.0	0.1	0.9	0.0
SE	2.7	1.4	-0.6	0.1	0.0	0.6	2.1	-0.6
EU	3.2	0.8	0.0	2.0	-0.1	0.3	3.1	-0.1

Source: European Commission 2020 spring forecast

COVID-19-related measures with an impact on the deficit consist almost exclusively of additional spending (Graph 2.8).([17]) Member States have focused their emergency spending on the immediate healthcare costs (0.3% of GDP on average), short-time work schemes, extensions of sick pay and unemployment benefits, subsidies to firms and public investment. Some Member States also provide tax relief by outright cancelling certain taxes and social security contributions, though in most cases tax revenues are expected to fall automatically as the output shrinks. On average, COVID-19 related tax relief amounts to only 0.1% of GDP, or less than a half of discretionary revenue measures implemented in 2020, with only Czechia, Croatia, Latvia and Slovakia enacting revenue-side measures in excess of 1% of GDP. However, more revenue-based measures have been taken since the 2020 spring forecast, as the policy focus has slowly started turning from emergency to recovery. In addition to measures with direct budgetary impact, governments alleviate liquidity pressures through tax credit lines and guarantee schemes (Box 2.3). While tax deferrals have no direct impact on government deficits, they could have an impact at a later stage, as some of the postponed tax obligations may never be settled, for example due to corporate bankruptcies.

Member States' efforts have been complemented by actions at the European level (Box 2.4). These actions focus on helping strengthen national health systems, providing emergency lifelines to households and firms, and facilitating a recovery that would make Member States' economies more resilient in the future. A package of €540 billion of loans to support companies, workers and Member States has already been agreed. A new €750 billion recovery instrument (of grants and loans) is under negotiation. This instrument will support reforms and investment based on the priorities identified as part of the European Semester, thereby accelerating the green and digital transitions. These financial packages would come on top of a revamped Multiannual Financial Framework of €1.1 trillion over 2021-2027 period (under negotiations).

([17]) This analysis is based on the Commission 2020 spring forecast only.

Box 2.3: Guarantees and other liquidity support measures in the 2020 SCPs

In addition to direct budgetary support for businesses and households, Member States have provided liquidity support to counter the economic fallout of COVID-19. The most common forms of liquidity support have been tax deferrals (that is, the possibility for delaying tax obligations without penalty) and state guarantees to support existing and new borrowing by businesses and households. The Commission 2020 spring forecast estimates that such liquidity measures have amounted to over 20% of GDP in 2020 in both the EU and the euro area. Due to the heterogeneous nature of the 2020 SCPs, an aggregation of the information provided by Member States is not straightforward.([1]) Instead, this box highlights several measures reported in the programmes.

Deferrals of tax and social security contribution payments amount to around 2% of GDP in 2020 in both the EU and the euro area, according to the Commission estimates. Tax deferrals have no direct impact on government deficit, since taxes are recorded in national accounts in the period when the economic activity generating the tax liability takes place. At the same time, deferrals may temporarily affect debt, should they necessitate additional borrowing by the general government in the deferral period. However, in view of the sizeable economic contraction expected in 2020, some businesses are likely not to survive the crisis and therefore some of the postponed tax obligations may never be settled. The EU statistical framework (European System of Accounts, or ESA 2010) requires that uncollectable taxes and social contributions are not recorded as government revenue; hence, accrued but uncollectable taxes have a deficit-increasing impact. The SCPs rarely provide explicit disclosures of estimated tax-related losses though the tax projections are likely to reflect their impact.

State guarantees are the largest category of COVID-19 related liquidity support measures. The Commission estimates Member States issued guarantees of 20% of GDP in the euro area and 18% of GDP in the EU in 2020. Almost all Member States have issued guarantees, but the size of the programmes and their set-up vary considerably. Some governments are directly guaranteeing loans issued by the banking sector to small and medium business, large companies and households. Other States rely on national promotional institutions to implement liquidity support programmes. The most important role is played in their respective Member States by the Bulga rian Development Bank, ČMZRB and EGAP in Czechia, KfW in Germany, KredEx in Estonia, the Hellenic Development Bank, BPI France, CDP in Italy, Altum in Latvia, INVEGA in Lithuania, the Malta Development Bank, the Polish Development Fund, and Finnvera in Finland.

Comparing the size of the guarantee programmes across countries is challenging. Not all Member States have filled the table on guarantees adopted or announced in response to COVID-19 outbreak (included in the streamlined format of the 2020 SCPs). While most SCPs provided some information on COVID-19 related guarantee programmes, it is not always clear if the amounts reflect the maximum contingent liability for the government or the stock of loans covered by the guarantee. Moreover, the programmes are at different stages of adoption and implementation. For these reasons, the size of the packages discussed below may not be fully comparable.

Several Member States have adopted very sizeable guarantee programmes.([2]) In Germany, the government significantly expanded the loan programmes of the government-owned promotional bank KfW to provide liquidity for companies, self-employed and freelancers. The government also established an Economic Stabilisation Fund to provide assistance, in particular to large companies. The value of these

([1]) For example, national estimates of tax deferrals have not been systematically included in the 2020 SCPs.
([2]) Based on the information provided in the 2020 SCPs and other publicly available documents with the same cut-off date. Some Member States adopted new or extended guarantee programmes after the cut-off date.

(Continued on the next page)

Box (continued)

programmes may reach €820 billion or 25% of GDP according to the stability programme. In Italy, the *Cura Italia* decree adopted in March 2020 enabled state guarantees covering up to €300 billion or 18% of GDP of loans, including for a moratorium of existing loans and for standardised guarantees mainly to small and medium firms. Additional guarantees for a total loan volume up to €400 billion or 24% of GDP were made available through the "Liquidity Decree" in April 2020. Although no indications are provided in the stability programme, the maximum contingent liability for the government from these programmes can be tentatively estimated at around €430 billion or 25% of GDP, based on the assumptions underlying the decrees. In France and Belgium, large-scale guarantee packages exceeding 10% of GDP were adopted to provide state guarantees to new corporate loans. Sizeable guarantee programmes of between 5% and 10% of GDP were adopted in Czechia, Denmark, Estonia, Spain, Luxembourg, Poland, Slovenia, Finland and Sweden. The guarantee programmes countering the economic effects of the pandemic add to the existing stock of government guarantees, which significantly varied between countries, from no guarantees in Ireland and Slovakia to over 30% of GDP in Finland at the end of 2018.([3])

About one-third of Member States expect *ex ante* deficit impact from liquidity measures including guarantees.([4]) These countries are Denmark, Germany, Estonia, Italy, Latvia, Hungary, Netherlands, Poland and Finland.([5]) The impacts vary from marginal in Germany, Hungary and Finland, to around ¼ pps. of GDP in Italy and the Netherlands, and to around ½ pps. of GDP in Denmark, Estonia, Latvia and Poland. In some cases, the impacts seem to relate to standardised guarantees, where previously existing programmes were expanded in response to COVID-19. While firms normally pay fees for the provision of state guarantees – this is also one of the requirements of the Temporary Framework for State Aid measures to support the economy in the COVID-19 outbreak([6]) – information on the revenue expected from guarantees was typically not provided in the 2020 SCPs.

([3]) https://ec.europa.eu/eurostat/documents/1015035/10401885/Contingent-liabilities-news-release.pdf
([4]) By analogy to guarantees, it is also possible to have *ex ante* deficit and debt impact stemming from other liquidity measures (such as loans by government agencies), although, as a rule they are recorded as financial transactions.
([5]) For the Netherlands, this information is available from the 2020 Spring Budget Memorandum.
([6]) https://ec.europa.eu/competition/state_aid/what_is_new/sa_covid19_temporary-framework.pdf

Box 2.4: **Measures adopted at the European level to cushion the impact of COVID-19**

Member States' efforts to tackle the economic consequences of the COVID-19 pandemic are supported at the European level. A number of measures were quickly agreed, in particular maximum flexibility in the use of EU funds and a package of €540 billion of loans to support companies, workers and Member States. Furthermore, the Commission has proposed a new recovery instrument worth €750 billion and a revamped Multiannual Financial Framework of €1.1 trillion over 2021-2027 period, which are under negotiation.

a. Immediate response

Mobilising the EU structural funds for most pressing needs: The Corona Response Investment Initiative will allow Member States to mobilise all the non-utilised structural funds, promoting an expenditure of up to €37 billion of EU funds. Furthermore, under the Coronavirus Response Investment Initiative Plus, exceptional additional flexibility to reprogram and transfer resources among funds and categories of regions will facilitate the use of uncommitted funding on fighting the crisis. EU funds will not need to be matched by national co-financing before they can be unlocked.

Protecting jobs and people at work: The new instrument for temporary Support to mitigate Unemployment Risks in an Emergency (SURE) will provide up to €100 billion in loans to Member States to address sudden increases in public expenditure for the preservation of employment. It will help Member States to finance the cost of short-time working schemes allowing firms experiencing economic difficulties to temporarily reduce the hours worked by their employees. Workers are provided with public income support for the hours not worked. It will also fund similar schemes providing income replacement for the self-employed. The instrument can also support, as ancillary, the financing of some health-related measures, in particular at the workplace. The Commission will finance the loans by issuing bonds, backed by a system of voluntary guarantees provided by Member States.

Supporting companies: The European Commission has unlocked €1 billion from the European Fund for Strategic Investments (EFSI) that will serve as a guarantee to the European Investment Fund (EIF), part of the European Investment Bank Group. This will allow the EIF to issue special guarantees to incentivise banks and other lenders to provide liquidity to at least 100.000 European small and medium-sized business and small mid-cap companies hit by the economic impact of the pandemic, for an estimated available financing of €8 billion. In addition, a new Pan-European Guarantee Fund, created by the EIB Group, aims at providing finance to hard-hit companies that are viable in the long-term (in particular small and medium-sized companies). The fund is based on guarantees from the Member States and is expected to mobilise up to €200 billion of additional financing. The EIB Group is also repurposing existing instruments to support companies affected by the crisis and to finance urgent infrastructure improvements and equipment needs in the health sector.

Easing financing of healthcare spending in euro area Member States: The Pandemic Crisis Support, established by the European Stability Mechanism, will provide loans of up to €240 billion. The loans are available to all euro area Member States, with an access of 2% of the respective Member State's gross domestic product as of end-2019 as a benchmark. To access the Pandemic Crisis Support Member States have only to commit to use this credit line to support domestic financing of direct and indirect healthcare, cure and prevention related costs due to the COVID-19 crisis.

b. Investment and financial support in the first years of recovery (under negotiations)

Sustainable and fair recovery: The Commission presented a recovery plan, which targets the sectors and geographical parts of Europe most affected by the current crisis, on 27 May 2020. The funding would be composed of two parts: i) a revamped Multiannual Financial Framework of €1.1 trillion for 2021-2027; and (ii) an emergency recovery instrument, called Next Generation EU, funded through the Commission's borrowing on the capital markets. Under the Commission proposal, Next Generation EU would be worth

(Continued on the next page)

Box (continued)

€750 billion (about 5½% of the annual EU GDP): up to €500 billion would be distributed as grants (of which €67 billion in provisioning for guarantees) and €250 billion would be made available in the form of loans. [1] The funding will be channelled through the European budget and will reinforce financial programmes key to the recovery, with an end date of 31 December 2024. The package will support Member States' efforts to recover from the crisis, boost private investment and help ailing companies, and accelerate the green and digital transitions. It will be spent across three pillars:

- The first pillar will support investment and reforms that are essential for a sustainable recovery. This pillar will include a new Recovery and Resilience Facility with a budget of €560 billion (distributed in grants and loans) and specifically designed to fund investments and reforms aligned with European priorities. It will also include a new REACT-EU initiative of €55 billion (€50 billion through Next Generation EU) to help Member States tackle the most pressing economic and social needs, including the immediate crisis repair measures such as job retention and creation schemes and health infrastructure spending. This initiative will become operational in 2020, according to the Commission's proposal. Finally, this pillar will bring in additional funding for the Just Transition Fund (€30 billion through Next Generation EU) and for the European Agricultural Fund for Rural Development (€15 billion through Next Generation EU) to support the green transition.

- The second pillar will incentivise private investment. It will include a new Solvency Support Instrument that will mobilise private resources for viable companies that are struggling due to the crisis. This instrument will have a budget of €31 billion (€26 billion through Next Generation EU), for provisioning for guarantees aiming to unlock more than €300 billion in solvency support, and will become operational in 2020. The capacity of InvestEU will be further raised with an overall budget contribution through Next Generation EU of €30.3 billion, including a new Strategic Investment Facility, for provisioning for guarantees aiming at mobilising €150 billion of investment.

- The third pillar will group new and topped-up instruments now deemed indispensable given the lessons learned from the health crisis. Among them is a new health programme, EU4Health, with an overall budget of €9.4 billion (€7.7 billion through Next Generation EU), aiming at investing in prevention, crisis preparedness, procurement of medicines and equipment, as well as improving long-term health outcomes. Moreover, RescEU - the Union Civil Protection Mechanism – will be increased and reach €3.1 billion (€2 through Next Generation EU), while EU funds related to external actions will be raised by €15.5 billion (Humanitarian Aid by €5 and Neighbourhood, Development and International Cooperation by €10.5 in the form of provisioning for guarantees). Finally, Horizon Europe will be reinforced and reach €94.4 billion (€13.5 billion through Next Generation EU) in order to fund vital research in health, resilience and the green and digital transitions.

The Commission will borrow up to €850 billion (€100 billion for SURE and €750 billion for Next Generation EU) on the financial markets. Member States will have to reimburse in the medium/long term only the €350 billion of loans (€100 billion for SURE and €250 billion for Next Generation EU) while €500 billion will be repaid according to a formula through future EU budgets. This could imply either an increase in national contributions to future EU budgets, or the setting-up of new own resources. For the latter, a number of new revenue streams have been mentioned, including an own resource based on operations of large companies, a carbon border adjustment mechanism, revenues from emission trading system, or a digital tax.

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(1) Amounts are expressed in 2018 prices.

3. ASSESSMENT OF THE EURO AREA FISCAL STANCE

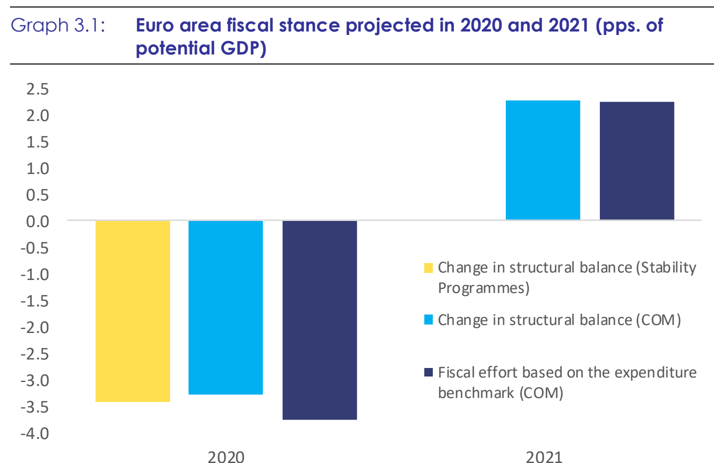
This section discusses the policy mix in the euro area, that is, the interplay of the fiscal policy stance with the monetary policy stance in 2020 and 2021. ([18])

3.1. FISCAL POLICY STANCE

Unprecedentedly large uncertainty surrounds the assessment of the fiscal stance for 2020 and even more so for 2021. The key unknowns are the scale and duration of the pandemic, the duration and scope of containment measures, the shape of the rebound and the potential growth of the euro area economy after the crisis. This uncertainty influences both the Commission 2020 spring forecast and the 2020 stability programmes. Even though the pandemic affected all Member States, the economic impact is uneven. The actual impact will depend on Member States' economic structures and their capacity to respond, including through buffers in public finances. This asymmetric response to a common shock makes it essential to have an EU central level support, including through the Next Generation EU initiatives proposed by the Commission (Box 2.4).

The Commission 2020 spring forecast projects the euro area fiscal stance to be strongly supportive in 2020 (Graph 3.1). It amounts to 3¾ pps. of GDP based on the expenditure benchmark methodology and 3¼ pps. of GDP according to the change in the structural balance—levels not seen in the past 20 years (Box 3.1). The aggregation of the 2020 stability programmes points to a similar fiscal stance for the euro area. The supportive stance in 2020 is essentially the result of the sizeable fiscal measures taken by Member States in response to the COVID-19 pandemic.

Graph 3.1: **Euro area fiscal stance projected in 2020 and 2021 (pps. of potential GDP)**



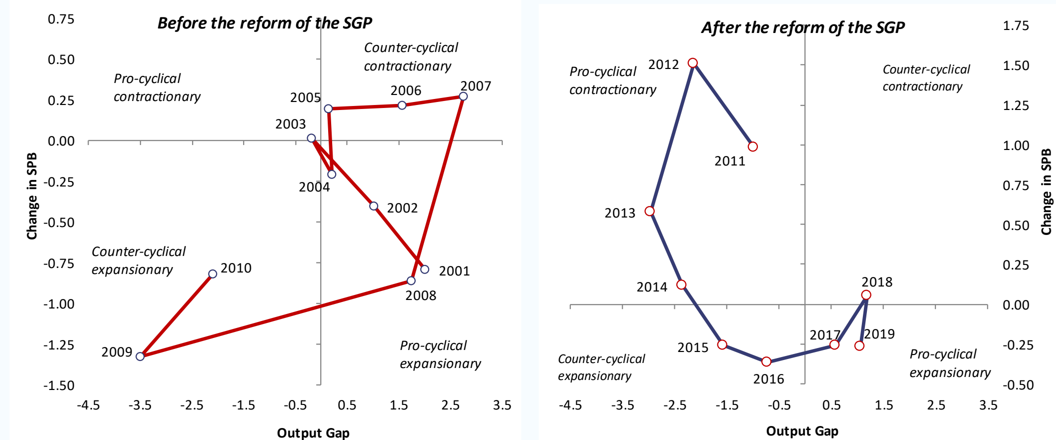
Note: The fiscal stance for 2020, measured by the change in the structural balance based on Member States plans, does not include Belgium, Cyprus, Luxembourg and Portugal because of missing data. Germany's potential growth and France's one-offs are based on the Commission forecast.
The fiscal stance for 2021 based on Member States' plans is not presented due to the large number missing data.
Source: European Commission 2020 spring forecast and 2020 Stability Programmes.

([18]) Because of lack of data in the SCPs, the fiscal stance analysis for 2021 is based exclusively on the Commission 2020 spring forecast.

Box 3.1: A retrospective view of the euro area fiscal stance

Engineering an appropriate euro area fiscal stance is challenging. The aggregate fiscal stance in the euro area is the sum of national fiscal policies, which are subject to common rules focused on ensuring the sustainability of national public debt. This implies contractionary national fiscal policy in almost all cyclical conditions as long as the medium-term budgetary objective (MTO) has not been achieved. Building buffers and achieving the MTO in good times is meant to allow Member States to make full use of automatic stabilisers when needed. As long as the medium-term budgetary objective (MTO) has not been achieved, sizeable counter-cyclical expansionary policies to support the stabilization are allowed only in extraordinary circumstances, such as the current crisis, through the activation of the general escape clause (see Section 2.1).

Graph 1: **Euro area fiscal stance in 2001-2019, change in the structural primary balance (pps. of potential GDP)**



Source: European Commission 2020 Spring forecast

Note: The fiscal stance up to 2011 is represented by the change in cyclically adjusted primary balance (CAPB).

Following a sharp contraction in 2011-2013, the euro area fiscal stance has been broadly neutral since 2014.([1]) Using the change in structural primary balance as a metric (Graph 1), the euro area fiscal stance appears to have been pro-cyclical in 6 out of the last 19 years, expansionary in 3 years (2001-2002, 2008) and contractionary in the 3 years following the sovereign debt crisis (2011-2013). The fiscal stance was counter-cyclical expansionary only in the immediate aftermath of the financial crisis (2009-2010), in part due to the implementation of the European Economic Recovery Plan.([2]) Since the strengthening of the Stability and Growth Pact in 2011, the euro area fiscal stance has never been clearly counter-cyclical. It has been broadly neutral since 2014 (defined as within an interval between -0.25 and +0.25 pps. of potential GDP), with the exception of 2016, when it was slightly counter-cyclical expansionary. Other metrics of the fiscal stance, namely fiscal effort measured according to the expenditure benchmark methodology and the structural balance change, confirm these results for the last 9 years (Graph 2, left panel).([3])

Discretionary revenue measures and lower interest expenditure gave the main contributions to the fiscal contraction recorded since 2011 (Graph 2, right panel). On average, discretionary revenue measures contributed 0.2 pps. of GDP to fiscal consolidation each year in 2011-2019, with the entire revenue hike occurring in 2011-2013. At the same time, structural primary expenditure grew overall in line with nominal

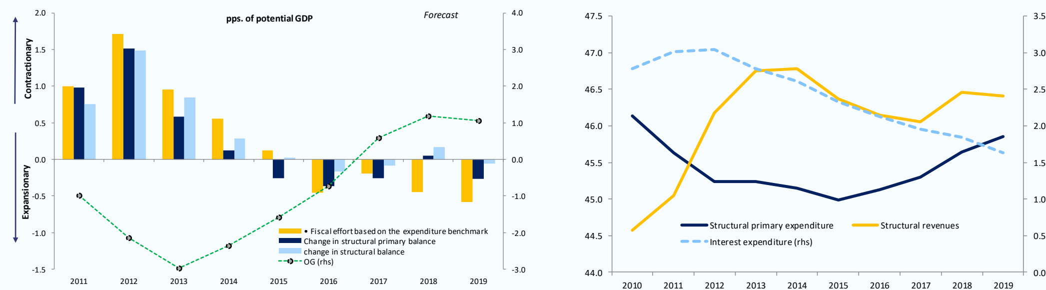
([1]) Real time output gap estimates might have provided a different picture.
([2]) https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52008DC0800&from=EN.
([3]) The effort based on the expenditure benchmark approach cannot be computed for the entire horizon 2001-2019 because of missing data in the series of the one-offs and discretionary revenue measures.

(Continued on the next page)

Box (continued)

potential growth, while lower interest expenditure contributed by 0.1 pps. of GDP, on average, to the fiscal contraction. The effort was concentrated in the first three years of the covered horizon (2011-2013), with an annual consolidation of 0.7 pps. of the GDP on average. By contrast, the aggregate the fiscal stance was broadly neutral in 2014-2019.

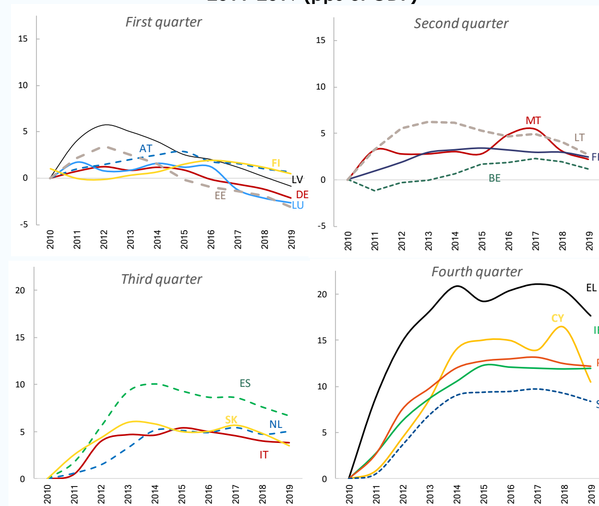
Graph 2: **Euro area fiscal stance in 2001-2019, different metrics and budgetary components (pps. of potential GDP)**



Source: European Commission 2020 Spring forecast.

Almost all countries show a positive cumulative fiscal effort in 2011-2019 but magnitudes varied (Graph 3). Greece and Ireland undertook the largest fiscal effort of 18 and 16 pps. of GDP, respectively. In contrast, Germany, Estonia Latvia and Luxembourg had an expansionary cumulative fiscal stance during this period. In most countries, the annual stance became neutral or expansionary in 2015.

Graph 3: **Overview of the cumulative fiscal effort (measured with the expenditure benchmark) in the euro area in 2011-2019 (pps of GDP)**



Note: The graph represents clusters of countries as identified by the quartiles of the distribution of the total effort measured according to the expenditure benchmark methodology. For Germany and Luxembourg the stance according to other metrics is distorted by sizeable revenue windfalls (cumulatively equal to 3½% and 3% respectively). Moreover, between 2010 and 2019 fiscal consolidation in all Member States has benefited from lower interest expenditure, the effect of which is captured in the structural balance metric (e.g. -3% for Greece, -1¾% for Germany and Luxembourg and -1½% for Belgium, Ireland and Austria). In 2019, for Cyprus, the fiscal effort based on the expenditure benchmark is largely affected by sizeable one-offs that increased Gross Fixed Capital Formation (GFCF) in 2018. In the expenditure benchmark GFCF is smoothed over four years which, in this case, implies lower expenditure net of one-offs in 2018 and higher in 2019.

Source: European Commission 2020 Spring forecast.

The euro area fiscal stance is forecast to turn contractionary by around 2¼ pps. of potential GDP in 2021. This forecast is based on a no-policy-change assumption and reflects the expected withdrawal of most of the crisis-related temporary measures. This aggregate stance does not yet include the possible support measures financed by grants under the Next Generation EU initiative (Box 2.4). An autonomous recovery in aggregate demand is projected to reduce the very large negative output gap by some 5 pps. (from -7¼% of potential GDP in 2020 to -2½% in 2021).

3.2. MONETARY POLICY STANCE

The European Central Bank (ECB) has deployed a broad range of monetary policy measures to mitigate the adverse economic effects of the COVID-19 pandemic. The measures, which are complementary and reinforce each other, can be grouped in three broad areas: the provision of additional liquidity to banks, an easing of collateral requirements and substantial additional purchases of public and private sector assets.

- The additional liquidity-providing operations aim at upholding the banking sector capacity to issue loans throughout the crisis. They include targeted (that is, conditional on achieving lending benchmarks) operations with long maturities (TLTRO III) and non-targeted, temporary, short-term operations (PELTRO).

- The collateral easing measures enhance banks’ access to ECB liquidity. These measures expand the pool of assets that banks can pledge with the Eurosystem in return for central bank loans and reduce the haircuts applied on this collateral.([19]) These measures will reduce risks that collateral shortages hamper banks’ access to central bank loans.

- Asset purchase programmes aim to dampen excess volatility in important segments of the euro area financial markets while further easing the general monetary policy stance in response to the downward effect of the pandemic on the euro area inflation outlook. The ECB has announced substantial additional purchases of public and private sector assets, which will amount to €1.470 trillion under the Asset Purchase Programme (€120 billion until the end of 2020) and the Pandemic Emergency Purchase Programme (€1.350 trillion until at least mid-2021).

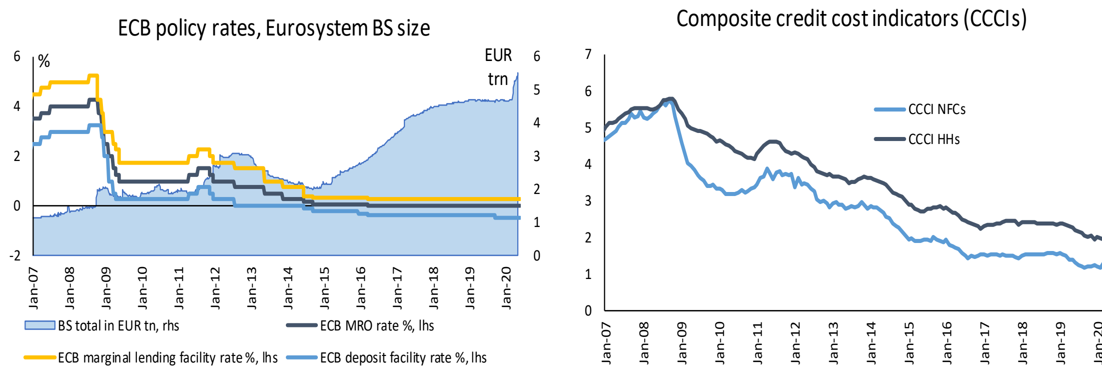
The Single Supervisory Mechanism complemented these actions by relaxing regulatory requirements on banks in a countercyclical way. These bank supervision measures will provide temporary capital and operational relief to euro area banks, which could be used to absorb losses or to provide loans to the real economy.

Financing conditions have remained overall favourable for the real economy (Graph 3.2). Developments in credit costs before the COVID-19 outbreak were indicative of improved financing conditions for the real economy, with the composite credit cost indicators ([20]) for households and non-financial corporations declining to record low levels at the euro area aggregate level. While the credit costs for non-financial corporations increased somewhat in March 2020, the deterioration in the financing costs of non-financial corporation came mainly on the back of increased risk premia that pushed higher corporate bond yields in the context of the financial market tensions related to the COVID-19 outbreak. Overall, the composite credit cost indicators for non-financial corporations still stood in March 2020 some 20 bps lower than one year ago. The credit costs for households reached a record low in March 2020, standing some 40 bps lower than at the same period last year.

([19]) The Eurosystem applies a discount, known as the valuation haircut, to provide a buffer against potential changes in the value of collateral.

([20]) The composite credit cost indicators are calculated as weighted averages of interest rates on different types of bank loans and corporate bonds (in case of non-financial corporations).

Graph 3.2: **Euro area monetary policy and credit cost indicators**



Note: The CCCIs are calculated as weighted averages of interest rates on different types of bank loans and corporate bonds (in case of non-financial corporations).
Source: Macrobond, ECB, European Commission, Bloomberg, BofA ML.

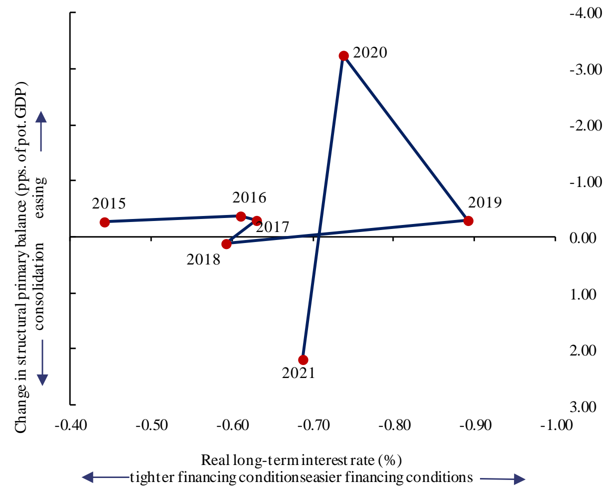
3.3. POLICY MIX

The policy mix is expected to strongly support economic activity in 2020. The monetary policy measures taken by the ECB have exerted significant downward pressure on nominal long-term rates since the end of 2014 (Graph 3.3). However, monetary easing has been only partially transmitted to real rates as long-term inflation expectations also declined over the same period. As a result, average real long-term rates for 2020 (derived from the 10-year swap rate deflated by inflation expectations) are expected to be somewhat higher than in the previous year. Nonetheless, they remain in negative territory and financing conditions should thus remain very supportive of growth. Also, the fiscal policy stance is expected to strongly support economic activity in 2020 and is projected to retreat in 2021.

The fiscal stance in 2020 can be assessed as appropriate based on the current macroeconomic projections. A supportive policy mix is needed to preserve as much as possible of the potential growth capacity and to protect businesses and workers. Moreover, active fiscal policy is particularly relevant and efficient to support macroeconomic stabilisation in the short term when interest rates are very low. Therefore, given the weak demand and disrupted supply, the accommodative monetary policy needs to be complemented by a supportive fiscal stance in the euro area. Overall, the Commission 2020 spring forecast estimates that the fiscal policy action taken in response to the COVID-19 outbreak will have a positive impact on real GDP of around 5 pps. in 2020. It aims to keep workers and business afloat and to limit hysteresis effects and thus a more permanent impact on potential GDP prospects.

Given the high uncertainty surrounding the forecast for 2021, it is premature to assess the fiscal stance for 2021. The appropriate fiscal stance for 2021 will depend crucially on the macroeconomic outlook. The Commission forecast assumes an autonomous recovery in demand in 2021, but the economic outlook remains exceptionally uncertain. At the same time, while a supportive fiscal stance is currently warranted in all Member States in order to facilitate the recovery, fiscal sustainability in the medium term should continue to be safeguarded. In particular, it should be ensured that, when economic conditions will allow, Member States pursue fiscal policies to achieve prudent medium-term fiscal positions and ensure debt sustainability, while enhancing investment. Debt sustainability is analysed in the next chapter.

Graph 3.3: **Euro area real long-term interest rates and change in structural primary balance, 2015-2021**



Source: European Commission 2020 Spring forecast.

4. SUSTAINABILITY

The Commission has recently updated its debt sustainability analysis (DSA) for all euro area Member States([21]) and all non-euro area Member States with Maastricht debt-to-GDP ratio expected to be higher than 60% of GDP in 2020 (Croatia and Hungary).([22]) The assessment includes two scenarios – a baseline and an adverse scenario – for government debt and gross financing needs projections.([23]) The baseline scenario is based on the Commission 2020 spring forecast and assumes a gradual adjustment of fiscal policy beyond 2021, consistent with the EU economic and fiscal coordination and surveillance frameworks.([24]) The adverse scenario assumes higher interest rates (by 50 bps.) and lower GDP growth (by -0.5 pp.) compared to the baseline scenario throughout the entire projection horizon of 10 years.

Under the baseline scenario, the debt-to-GDP ratios would gradually decline in nearly all Member States over the medium term (Graph 4.1). This downward path from the peak levels would be driven by a fiscal adjustment in line with the commitment of euro area Member States to strengthen economic and financial fundamentals, consistent with the EU economic and fiscal coordination and surveillance frameworks. The favourable interest - growth rate differential would also support the projected debt-to-GDP reduction path. The magnitude of this decline would vary across countries depending on the initial fiscal deficit as well as the sign and the magnitude of the interest - growth rate differential (snowball effect).

The debt-to-GDP ratios would be on stable or declining paths in most euro area Member States also under the adverse scenario. A combination of less dynamic economic recovery and adverse financial conditions would entail upward pressures to the debt-to-GDP ratio. However, they would remain broadly stable, with declines projected for the outer years only in some countries.

Government gross financing needs are also expected to decrease over the medium-term but would remain high in several high-debt countries. Gross financing needs are expected to reach values close to their pre-crisis levels by 2030 under the baseline scenario (Table 4.1), as primary balances improve and

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([21]) The assessment for euro area Member States was carried out in the context of the eligibility assessment to the Pandemic Crisis Support provided by the European Stability Mechanism (ESM). The fiscal policy assumptions are consistent with the EU economic and fiscal coordination and surveillance frameworks, as described in Annex II of the eligibility assessment report for the Pandemic Crisis Support provided by the ESM. The baseline assumptions for Greece reflect the post-programme commitments, in line with the methodology used in the context of Enhanced Surveillance. Since the activation of Enhanced Surveillance for Greece in July 2018, the assessments for Greece use the methodology established in the Compliance Reports, ESM Stability Support Programme for Greece, Third and Fourth Reviews, March 2018 and June 2018, respectively.
https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-financial-assistance/loan-programmes/european-stability-mechanism-esm_en

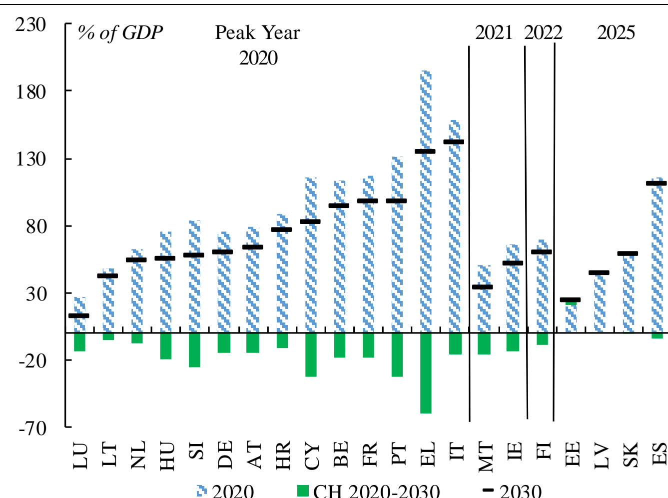
([22]) The assessment for non-euro area Member States with an expected debt ratio in 2020 above 60% of GDP (Croatia and Hungary) was carried out in the context of the Article 126(3) reports for these countries
https://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/30_edps/126-03_commission/com-2020-547-hr_en.pdf
https://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/30_edps/126-03_commission/com-2020-552-hu_en.pdf.

([23]) Government gross financing needs are defined as the sum of the budgetary deficit, debt amortizations (including debt securities and loans) and other debt creating/ reducing flows (stock-flow adjustments).

([24]) Real GDP growth is projected in line with the so-called T+10 methodology agreed upon by the Economic Policy Committee's Output Gap Working Group (EPC-OGWG) and affected by any additional fiscal adjustment considered over the medium term (through the fiscal multiplier, set at 0.75 in line with the Commission regular DSA framework). After the output gap closure, real GDP growth is driven by potential. Inflation is assumed to converge gradually to 3% in Hungary and 2% elsewhere. Interest rates assumptions are set in line with financial market expectations, based on forward rates as of March 2020 (in line with the Commission regular DSA framework). The fiscal policy assumptions are consistent with the EU economic and fiscal coordination and surveillance frameworks, as described in Annex II of the eligibility assessment report for the Pandemic Crisis Support provided by the ESM. The baseline assumptions for Greece reflect the post-programme commitments, in line with the methodology used in the context of Enhanced Surveillance. Since the activation of Enhanced Surveillance in July 2018, the assessments for Greece use the methodology established in the Compliance Reports, ESM Stability Support Programme for Greece, Third and Fourth Review, March, and respectively, June 2018.
https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-financial-assistance/loan-programmes/european-stability-mechanism-esm_en

debt-servicing costs decline. However, gross financing needs would remain high in the short- to medium-term in Belgium, Spain, France, Italy, Hungary and Portugal. In these countries, between 2020 and 2024, gross financing needs are expected to remain at higher levels than pre-crisis levels, with a significant decline expected only in the outer forecast years. However, no significant tightening in financing conditions is expected. Despite fragile market sentiment, European sovereign debt markets are expected to remain stable notably thanks to the EU level support, including the ECB Pandemic Emergency Purchase Programme, the Pandemic Crisis Support, and the Commission's proposal for a European Recovery Fund.

Graph 4.1: **Change in public debt-to GDP ratios between 2020 and 2030; baseline scenario (% of GDP)**



Source: European Commission 2020 spring forecast.

The composition of government debt mitigates debt vulnerabilities. Euro area governments have increased the average maturity of their debt over the past years,([25]) and a large share of their liabilities is issued at fixed rates. These developments allow dampening the effect of potential rises in financing costs and reducing rollover risks. Moreover, in most Member States, a significant share of government debt is held by residents, contributing to the resilience of the debt position to global market fluctuations. In countries where the share of non-residents is higher, holdings by official lenders and/ or the Eurosystem also constitute stable financing sources. In some countries, positive net international investment positions also highlight how the private sector's strong net creditor position more than compensates the government's debtor position.([26])

However, risks related to the unprecedented nature of the crisis exist. Large uncertainties surround the current set of projections, notably related to the strength of the recovery. Relatedly, contingent liability risks may arise from the private sector, via the possible materialisation of government guarantees put in place to support firms and self-employed. Government guarantees announced through 23 April 2020 average above 15% of GDP. While these additional contingent liabilities reflect necessary measures adopted by governments in order to support the economy, they represent a potentially significant risk for public finances. Even though banks' balance sheets have considerably strengthened over the last decade, implicit contingent liabilities from latent financial sector vulnerabilities exist. Conversely, upward risks also exist. First, the European and national recovery plans could bring a faster recovery with favourable impacts on potential growth of stronger-than-expected investment dynamics. Second, the stepping-up of structural reforms could yield larger positive impacts on potential growth.

([25]) See for example, ECB, Debt securities and service by EU governments, monthly, February 2020.
([26]) See European Commission *Debt Sustainability Monitor 2019* for more detailed information on the debt profile. See European Commission *2020 Alert Mechanism Report* for more detailed information on net external positions.

Overall, the debt sustainability assessment indicates that, notwithstanding risks, the debt positions remain sustainable over the medium-term in all Member States considered in the DSA, also given important mitigating factors. Even if the government debt positions deteriorate due to the COVID-19 crisis, the baseline debt-to-GDP ratios are expected to be on a sustainable trajectory over the medium term in all Member States, consistent with EU Member States remaining subject to the EU's economic and fiscal co-ordination and surveillance frameworks. Government financing needs are also projected to reduce, after the peak foreseen for 2020. Delayed economic recovery and adverse financial conditions would however entail upward pressures to the debt-to-GDP ratio, with only late declines projected in some countries. Contingent liabilities, arising from the government guarantees to firms and self-employed put in place in response to the crisis, although necessary to support the economy, also represent tangible risks. Nonetheless, the profile of government debt mitigates debt vulnerabilities in the euro area Member States, thanks to the lengthening of maturities over the past years and relatively stable financing sources. The historically low level of borrowing costs is another important mitigating factor.

Table 4.1: **Gross financing needs (2020 – 2024), % of GDP, baseline scenario**

	2019	2020	2021	2022	2023	2024	2030
BE	16.1	24.8	20.7	19.6	19.1	18.5	15
DE	10.7	24.7	14.7	14.1	13.7	13.4	12
EE	0.8	12	3.6	3.2	2.7	2.4	1.1
IE	5.9	12.1	13.5	9.6	9.1	7.9	5.1
EL	15.9	13.2	11	10.3	12.3	12.8	13.1
ES	16.6	27.7	24.2	23.9	23.6	23.3	19.3
FR	17.7	27.7	21.5	20.4	19.9	19.2	16.1
HR	14.7	22.1	16.4	16.4	16	15.7	14.3
IT	20	31.7	26.5	25.7	25.2	24.6	20.4
CY	14.9	24.7	6.4	10.4	10.3	10.1	12.3
LV	4.6	7.6	7.7	7.8	7.4	7	5.3
LT	6.1	11.9	7	5.1	4.8	4.7	5.1
LU	3.1	8.2	2.6	0.9	0.7	0.4	0.1
HU	18.6	23.6	22.7	21.5	20.6	19.7	15.2
MT	5.3	10.8	8.8	7.3	6.7	6	3.6
NL	7	19	9	11.9	11.6	11.1	9.6
AT	8.1	14.3	10.5	9.9	9.2	8.7	6.3
PT	11.7	19.2	14.2	14.2	13.4	13	11.9
SI	6.9	22.2	11.3	10.5	9.9	9.4	7.7
SK	3.3	11.7	7.8	6.8	6.4	6	4.2
FI	8.7	15.2	12.3	11.3	10.6	9.9	8

Source: European Commission 2020 spring forecast

ANNEX 1

Table A1.1: **Real GDP growth (%)([27])**

	2020 Stability and Convergence Programmes			2020 Spring forecast			Difference compared to forecast (red means higher in programme)		
	2019	2020	2021	2019	2020	2021	2019	2020	2021
BE	1.4	-8.0	8.6	1.4	-7.2	6.7	0.0	-0.8	1.9
CY	3.2	-7.0	6.0	3.2	-7.4	6.1	0.0	0.4	-0.1
DE	2/4	-6	n.a.	0.6	-6.5	5.9	0.0	0.5	n.a.
EE	4.3	-8.0	8.0	4.3	-6.9	5.9	0.0	-1.1	2.1
EL	1.9	-4.7	5.1	1.9	-9.7	7.9	0.0	5.0	-2.8
IE	5.6	-10.5	6.0	5.5	-7.9	6.1	0.0	-2.5	0.0
ES	2.0	-9.2	6.8	2.0	-9.4	7.0	0.0	0.2	-0.2
FR	1.3	-8.0	n.a.	1.3	-8.2	7.4	0.0	0.2	n.a.
IT	0.3	-8.0	4.7	0.3	-9.5	6.5	0.0	1.5	-1.8
LV	2.2	-7.0	1.0	2.2	-7.0	6.4	0.0	0.0	-5.4
LT	3.9	-7.3	6.6	3.9	-7.9	7.4	0.0	0.6	-0.8
LU	2.3	-6.0	7.0	2.3	-5.4	5.7	0.0	-0.6	1.3
MT	4.4	-5.4	3.9	4.4	-5.8	6.0	0.0	0.4	-2.1
NL	1.8	1.4	1.6	1.8	-6.8	5.0	0.0	8.2	-3.4
AT	1.6	-5.2	3.5	1.6	-5.5	5.0	0.0	0.3	-1.5
PT	n.a.	n.a.	n.a.	2.2	-6.8	5.8	n.a.	n.a.	n.a.
SI	2.4	-8.1	3.5	2.4	-7.0	6.7	0.0	-1.1	-3.2
SK	2.3	-7.2	6.8	2.3	-6.7	6.6	0.0	-0.5	0.2
FI	1.0	-5.5	1.3	1.0	-6.3	3.7	0.0	0.8	-2.4
EA-19	1.2	-6.6	n.a.	1.2	-7.7	6.3	0.0	1.1	n.a.
BG	3.4	-3.0	n.a.	3.4	-7.2	6.0	0.0	4.2	n.a.
CZ	2.6	-5.6	3.1	2.6	-6.2	5.0	0.0	0.6	-1.9
DK	2.4	-4.4	4.8	2.4	-5.9	5.1	0.0	1.5	-0.3
HR	2.9	-9.4	6.1	2.9	-9.1	7.5	0.0	-0.3	-1.4
HU	4.9	-3.0	4.8	4.9	-7.0	6.0	0.0	4.0	-1.2
RO	4.1	-1.9	n.a.	4.1	-6.0	4.2	0.0	4.1	n.a.
PL	4.1	-3.4	n.a.	4.1	-4.3	4.1	0.0	0.9	n.a.
SE	1.2	-4.0	3.5	1.2	-6.1	4.3	0.0	2.1	-0.8
EU-27	1.5	-6.2	n.a.	1.5	-7.4	6.1	0.0	1.3	n.a.
p.m. UK[1]	1.4	1.1	1.8	1.4	-8.3	6.0	0.0	9.4	-4.2

Note: Fiscal year data are reported for the UK.
Source: European Commission 2020 spring forecast and 2020 SCPs.

Table A1.2: **General government balance (% of GDP)**

	2020 Stability and Convergence Programmes			2020 Spring forecast			Difference compared to forecast (red means higher in programme)		
	2019	2020	2021	2019	2020	2021	2019	2020	2021
BE	-1.9	-7.5	n.a.	-1.9	-8.9	-4.2	0.0	1.4	n.a.
CY	2.7	-4.3	-0.4	1.7	-7.0	-1.8	1.0	2.7	1.3
DE	1 2/4	-7 1/4	n.a.	1.4	-7.0	-1.5	0.0	-0.2	n.a.
EE	-0.3	-10.1	-3.8	-0.3	-8.3	-3.4	0.0	-1.8	-0.5
EL	1.5	-4.7	-0.2	1.5	-6.4	-2.1	0.0	1.7	1.9
IE	0.4	-7.4	-4.1	0.4	-5.6	-2.9	0.0	-1.8	-1.2
ES	-2.8	-10.3	n.a.	-2.8	-10.1	-6.7	0.0	-0.2	n.a.
FR	-3.0	-9.0	n.a.	-3.0	-9.9	-4.0	0.0	0.9	n.a.
IT	-1.6	-10.4	-5.7	-1.6	-11.1	-5.6	0.0	0.7	-0.1
LV	-0.2	-9.4	-5.0	-0.2	-7.3	-4.5	0.0	-2.1	-0.5
LT	0.3	-11.4	-3.9	0.3	-6.9	-2.7	0.0	-4.5	-1.2
LU	2.2	-8.5	-3.0	2.2	-4.8	0.1	0.0	-3.7	-3.1
MT	0.5	-7.5	-3.6	0.5	-6.7	-2.5	0.0	-0.8	-1.1
NL	1.7	1.1	0.1	1.7	-6.3	-3.5	0.0	7.4	3.6
AT	0.7	-8.0	-1.9	0.7	-6.1	-1.9	0.0	-1.9	0.0
PT	n.a.	n.a.	n.a.	0.2	-6.5	-1.8	n.a.	n.a.	n.a.
SI	0.5	-8.1	n.a.	0.5	-7.2	-2.1	0.0	-0.9	n.a.
SK	-1.3	-8.4	-4.9	-1.3	-8.5	-4.2	0.0	0.1	-0.7
FI	-1.1	-7.2	-4.0	-1.1	-7.4	-3.4	0.0	0.2	-0.6
EA-19	-0.7	-7.8	n.a.	-0.6	-8.5	-3.5	0.0	0.7	n.a.
BG	2.1	-3.1	n.a.	2.1	-2.8	-1.8	0.0	-0.3	
CZ	0.3	-5.1	-4.1	0.3	-6.7	-4.0	0.0	1.6	-0.1
DK	3.7	-8.0	-2.4	3.7	-7.2	-2.3	0.0	-0.8	-0.1
HR	0.4	-6.8	-2.4	0.4	-7.1	-2.2	0.0	0.3	-0.2
HU	-2.0	-3.8	-2.7	-2.0	-5.2	-4.0	0.0	1.4	1.3
RO	-4.3	-6.7	n.a.	-4.3	-9.2	-11.4	0.0	2.5	n.a.
PL	-0.7	-8.4	n.a.	-0.7	-9.5	-3.8	0.0	1.1	n.a.
SE	0.4	-3.8	-1.4	0.5	-5.6	-2.2	-0.1	1.8	0.8
EU-27	-0.6	-7.5	n.a.	-0.6	-8.3	-3.6	0.0	0.7	n.a.
p.m. UK[1]	-2.2	-2.5	-3.1	-2.5	-10.7	-6.2	0.3	8.2	3.1

Note: Fiscal year data are reported for the UK.
Source: European Commission 2020 spring forecast and 2020 SCPs.

Table A1.3: **General government total debt (% of GDP)**

	2020 Stability and Convergence Programmes			2020 Spring forecast			Difference compared to forecast (red means higher in programme)		
	2019	2020	2021	2019	2020	2021	2019	2020	2021
BE	98.9	115.0	n.a.	98.6	113.8	110.0	0.3	1.2	n.a.
CY	95.5	116.8	103.2	95.5	115.7	105.0	0.0	1.1	-1.8
DE	n.a.	n.a.	n.a.	59.8	75.6	71.8	n.a.	n.a.	n.a.
EE	8.4	21.9	23.4	8.4	20.7	22.6	0.0	1.2	0.8
EL	176.6	188.8	176.8	176.6	196.4	182.6	0.0	-7.6	-5.8
IE	58.8	69.1	68.4	58.8	66.4	66.7	0.0	2.7	1.7
ES	95.5	115.5	n.a.	95.5	115.6	113.7	0.0	-0.1	n.a.
FR	98.1	115.2	n.a.	98.1	116.5	111.9	0.0	-1.3	n.a.
IT	134.8	155.7	152.7	134.8	158.9	153.6	0.0	-3.2	-0.9
LV	36.9	51.7	52.2	36.9	43.1	43.7	0.0	8.6	8.5
LT	36.3	50.6	52.7	36.3	48.5	48.4	0.0	2.1	4.3
LU	22.1	28.7	29.6	22.1	26.4	25.7	0.0	2.3	3.9
MT	43.1	54.5	55.5	43.1	50.7	50.8	0.0	3.8	4.7
NL	48.6	46.3	45.2	48.6	62.1	57.6	0.0	-15.8	-12.4
AT	70.4	81.4	79.3	70.4	78.8	75.8	0.0	2.6	3.5
PT	n.a.	n.a.	n.a.	117.7	131.6	124.4	n.a.	n.a.	n.a.
SI	66.1	82.4	n.a.	66.1	83.7	79.9	0.0	-1.3	n.a.
SK	48.0	61.3	62.0	48.0	59.5	59.9	0.0	1.8	2.0
FI	59.4	69.1	71.5	59.4	69.4	69.6	0.0	-0.3	1.9
EA-19	96.2	110.8	n.a.	86.0	102.7	98.8	10.1	8.1	n.a.
BG	n.a.	n.a.	n.a.	20.4	25.5	25.4	n.a.	n.a.	n.a.
CZ	30.8	37.0	40.0	30.8	38.7	39.9	0.0	-1.7	0.1
DK	33.2	40.7	41.2	33.2	44.7	44.6	0.0	-4.0	-3.4
HR	73.2	86.7	83.2	73.2	88.6	83.4	0.0	-1.9	-0.2
HU	66.3	72.6	69.3	66.3	75.0	73.5	0.0	-2.4	-4.2
RO	35.2	40.9	n.a.	35.2	46.2	54.7	0.0	-5.3	n.a.
PL	n.a.	n.a.	n.a.	46.0	58.5	58.3	n.a.	n.a.	n.a.
SE	35.1	39.9	38.3	35.1	42.6	42.5	0.0	-2.7	-4.2
EU-27	82.7	94.6	n.a.	79.4	95.1	92.0	n.a.	n.a.	n.a.
p.m. UK[1]	83.2	82.9	83.2	85.2	102.5	100.2	-2.0	-19.6	-17.0

Note: Fiscal year data are reported for the UK.
Source: European Commission 2020 spring forecast and 2020 SCPs.

[1]The United Kingdom withdrew from the European Union as of 1 February 2020. The Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and European Atomic Energy Community (OJ L 29, 31.1.2020, p. 7) entered into force on the same date. It provides for a transition period during which Union law, with a few exceptions, is applicable to and in the United Kingdom. For the purposes of Union law applicable to it during the transition period, the United Kingdom is treated as an EU Member State, but will not participate in EU decision-making and decision-shaping.

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