Post Covid Recovery and Ecological Transition in Europe

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A Green Recovery to the Pandemic Meltdown

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A European Public Investment Outlook

- Public Investment in EU declined from 2008 to 2016. In 2018 still 15% lower than in 2008 (2.9% vs 3.4%)
- Fiscal consolidation identified as the main driver of the drop
- Infrastructure were particularly hit (-25%). No saturation. The gap increased
- The German case
  - Severe deterioration of public capital stock since 2000
  - Demographic change, decarbonization and digitalization \(\rightarrow\) Additional investment needs
  - Sector by sector analysis leads to the estimation of €450bn over the next decade.
  - Positive impact on potential growth and compatible with 60% debt target
Lessons from the past – volatility, multipliers and impact of fiscal consolidation on investment

- Government investment very volatile through the cycle
  - A surprise drop in GDP by 1% reduces government investment cumulatively by about 3-4% over the following years (change in government investment on surprise decline GDP)
- Public sector stimulus most effective through investment – IMF (2020) → Impact on debt sustainability
- Government investment response to fiscal consolidations is large and long lasting.
  - After 10 years, cumulative decline in government investment is 2pp of GDP
  - Forthcoming EIB Investment Report 2020-2021
Investment and public investment – the Global Financial Crisis vs the Covid Crisis

Real investment and contributions by institutional sector
(% change over the same quarter of previous year)

Corporate
Government
Households
Residuals
Total economy

SLIDES COURTESY OF D. REVOLTELLA, EIB
Source: Eurostat Sector accounts and EIB staff calculations.
Notes: Investment aggregates in current prices, NSA. Deflated using 2015 CLV deflator for GFCF, NSA.
The European Green Deal: Next Generation EU

• Large borrowing by the Commission (€ 750bn). Repaid in 2028-2058
• A complement to the MFF (€1050bn)
• Distributed to countries in grants (€390bn) and loans (€360bn)
• Main instrument, Recovery and Resilience Facility (€672.5bn)
• Three priorities
  ▪ Ecological transition
  ▪ Digitalization
  ▪ Cohesion
• Climate action is the main item
  ▪ 37% of National Recovery and Resilience plans investment
  ▪ Just transition Fund, created in 2020 to boost investments in low-carbon energy. (€10bn)
The National Recovery and Resilience Plans


• Allocation to countries based on need (impact of crises)  
  ➔ Limited risk sharing

• Italy plans to use both loans and grants. Spain might in the future
What green investment?

- Green infrastructure and mobility
  - Germany: electric mobility (cars, buses rail)
  - France and Italy, about 50% in railway system (Italy’s choice to focus on high speed trains has been criticized)

- Green energy investments
  - Germany and France: strong emphasis on hydrogen (decarbonized or not)
  - Spain and Italy: wider range of investment in renewable energy and smart grids, in addition to support for hydrogen projects.

- One explanation of the differences is in the amount of resources available: Germany (and France) having less resources have diversified less
The Green component of National Plans

Source: Bruegel base on national plans submitted between 25-28 April 2021.
How to Spend it

• The Next Generation EU is a financing scheme for national investment plans

• In a recent policy brief, we tried to shift the focus on a large truly European investment plan

- We propose a 10-year, €2tn investment programme mostly devoted to finance genuinely European projects, where there is an EU value added (€1.5tn)
  - A single European Health agency in charge of 2 objectives:
    - A European Ultra Rapid Train Network
    - Energy/decarbonisation – electrify the Green Deal!
      ‣ Boost fundamental research (> foreseen expansion Horizon Europe, was €100bn weakened by frugals)
      ‣ Accelerate construction of smart, integrated electricity grid (RES e-highway)
       Total cost estimated to 2050 ~€500 bn
Changing the EU Rules

• A Golden Rule
  ▪ Formalize the preferential treatment for investment that is in the new Commission «flexibility» doctrine
  ▪ Extensive definition of public investment (“augmented” golden rule, Dervis and Saraceno 2014)

• Coordination of public investment choices: Public investment as one arm of industrial policy?
  ▪ Transnational aspects of infrastructure investment
  ▪ Joint definition (European Semester?) of what is «growth-oriented expenditure»
  ▪ EU budget and co-financing by EIB: a permanent Next Generation?

• Do not waste the occasion given by the Commission rule revision process