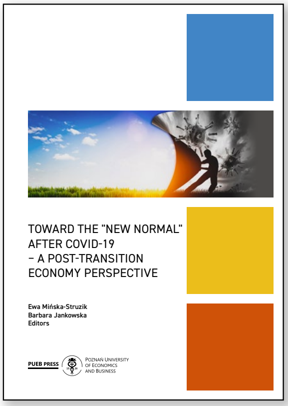

TOWARD THE "NEW NORMAL" AFTER COVID-19 – A POST-TRANSITION ECONOMY PERSPECTIVE

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Editors

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2. How Covid-19 impacted the European integration processes? The case of EU Cohesion Policy and budget

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Abstract

Purpose: The current pandemic crisis caused by Covid-19 significantly impacted the processes of European integration. The European Union decided to act within and beyond existing competences and instruments to support the efforts of its Member States, along with regional and local authorities, in the fight against Covid-19. Our study sheds light on the instruments and solutions proposed within the framework of the cohesion and budget policy to tackle the problems related to Covid-19 in Europe. The analysis focuses on two strands: 1) EU assistance offered through cohesion policy (CP) instruments toward above areas; 2) the future evolution of EU budget, and therefore integration shifts, provoked by the Covid-19 crisis.

Design/methodology/approach: The study analyzes statistical data with regard to the use of instruments of the Cohesion Policy under the Covid-19 pandemic, but also the amendments introduced to legal acts and decision-making processes that refer to the multiannual financial framework (MFF) for 2021–2027.

Findings: We notice a strong shift of priorities regarding environment transformation, digitalization, and health protection, reflected in the MFF. The coordinative role of European institutions and the redirection of different financial instruments to health care follows the neo-

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functionalist paradigm and represents a spillover effect resulting from integration. The crisis analyzed from the institutional perspective is seen as a chance to reform the decision-making process, while on the other hand, as a threat to the inclusive integration of all Member States.

Originality and value: The paper is an original contribution on the overall use of both financial and legislative instruments in the times of unprecedented health and economic crisis caused by Covid-19 in the European Union. The text can be a valuable insight for both researchers and practitioners in the field of broadly understood European studies.

Keywords: EU Cohesion Policy, EU budget, multiannual financial framework, Covid-19, European integration.

2.1. Introduction

The outbreak of the SARS-CoV-2 pandemic was observed in Europe in early Spring of 2020. The most severe consequences appeared in the spring wave in the southern Europe: Italy, Spain, but lately also in other EU Member States (MS). The pandemic showed the shortcomings in the area of health care and a country's available health system have emerged as crucial to the success of the response to the pandemic (Furlong & Hirsch, 2020). In order to protect their health care systems, the governments decided on lockdowns of the economy, which has led to an unprecedented economic crisis compared even to the 1930's global crisis (European Commission, 2020a). The both crises are of different nature but provoked set of policy responses showing necessity to rethink monetary and fiscal policies, instruments to be used to support individuals and businesses and revitalize whole economies, sectors and territories. The pandemic-caused crisis showed the urge need to introduce transborder cooperation between the states.

When we analyze growth rates, we observe drastic contraction forecasts of EU GDP by ca. 7.4% in 2020. The GDP is expected to regain a 4% growth rate in 2021 and 3% in 2022 (the pre-crisis levels). Economic activity is expected to rise again in the first quarter of 2021, but it might be additionally constrained by two factors: 1) virus containment measures and 2) the impact of less beneficial trading relations with the UK (European Commission, 2020a). There is variation in the growth rate and predicted speed of recovery among the Member States, depending on both virus spread and structural economic problems. The structure of regional (subnational) economies is a source of risk of job losses (which vary by more than 20% in the countries), especially in regions whose economy is largely dependent on accommodation and food services, wholesale and retail trade, construction and real estate services, art and entertainment, professional, scientific and technical activities, the manufacture of transport equipment, and air services (OECD, 2020a).

Current pandemic crisis caused by Covid-19 has also had a significant impact on the processes of European integration as such. The European Union drew lessons from the financial and economic crisis from 2008 and decided to act within and beyond the existing competences and instruments to support the efforts of its Member States, and regional and local authorities in the fight against Covid-19. The regional and local levels where the most efficient in providing assistance with regard to e.g. health care and business environment affected by the pandemic. Also actions taken at the EU level can be expected to be efficient in ensuring an effective response to the coronavirus crisis. The challenge the EU is facing now is how to implement a recovery plan designed to counteract the socio-economic downturn and find a proper coordination mechanism in the health care sector. Therefore, our study sheds further light in the debate on the instruments and solutions proposed within the framework of the cohesion and budget policy. The analysis will focus mainly on two strands: 1) EU assistance offered through cohesion policy (CP) instruments towards above-mentioned areas; 2) future evolution of EU budget, and therefore integration shifts, provoked by the pandemic crisis. The paper is based on statistical data with regard to CP and analysis of legal acts and decision-making process referring to multiannual financial framework for 2021–2027. The chapter is structured as follows: the general overview on the EU reactions to the pandemic starts the study (section 2.2), then assistance under the cohesion policy against the Covid-19 is analysed (section 2.3), followed by reflections on the evolution of the EU budget for the years 2021–2027 (section 2.4) and conclusions.

2.2. European Union's reaction to the pandemic

The first reactions and activities were held at national, regional, and local levels. But soon after the numbers of infected have started to rise, the European institutions decided to coordinate efforts and fight against the transborder disease of Covid-19. The joint actions appeared early enough in comparison to the previous financial and economic crisis from 2007/2008, when the European Union learned the lessons how to jointly counteract a crisis.

In March 2020, during a special meeting of the heads of state or government of the 27 EU Member States, the EU identified four priorities for its SARS-CoV-2 response strategy, namely (European Parliamentary Research Service, 2020a):

- limiting the spread of the virus, including assessing the risk and closing external borders, with internal borders possibly open to allow single market functioning;
- ensuring the provision of medical equipment by increasing production of medical devices, issuing calls for production of medical equipment, and negotiating new supplies;

- helping researchers to find a vaccine quicker than in normal conditions, through existing research programs and enhancing cooperation with the private sector and other international organizations;
- aiding EU Member States to manage the social and economic impact of the pandemic.

The EU began to play a coordinating role, complementing national and subnational policies to help countries face common challenges with the use of existing and creation of new instruments (European Parliamentary Research Service, 2020a):

- RescEU (existing instrument newly adapted to the health crisis) stockpiled medical equipment such as ventilators and protective masks, enabling Member States facing equipment shortages to quickly procure the necessary supplies;
- the EU research program Horizon 2020 (existing instrument) was opened for funding of e.g. rapid point-of-care diagnostic tests and the development of vaccines and new treatments; an initial EUR 45 m committed to the project was supplemented in May 2020 with a further EUR 122 m allocated to the program;
- loans and guarantees of overall value of ca. EUR 540 bn under: 1) support to mitigate Unemployment Risks in an Emergency (SURE – new instrument) in order to help protect people at work and jobs affected by the coronavirus pandemic of total value of EUR 90.3 bn divided among MS in the form of loans and guarantees (OJ L 130, 2020.4.24; OJ L 159, 2020.5.20); in order to use it, Member States had to activate short-time work schemes to preserve employment and assist the self-employed; 2) support to businesses by the European Investment Bank and aid to the Member States under the European Stability Mechanism.

What is more, the European Central Bank offered monetary stimulus and temporarily has eased supervision criteria to increase liquidity and access to credit of a value of ca. EUR 1 tn. The European Commission quickly introduced flexibility on EU budgetary and state aid rules (ECOFIN, 2020) to let MS mitigate the effects of the crisis with the amount of ca. EUR 330 bn to activate the general escape clause to use national budgets to support countries' economies, and EUR 2–2.45 tn for the flexible use to support businesses and workers in the MS. The Commission also suspended the limits expressed in the Stability and Growth Pact.

Moreover, cohesion policy funds from the 2014–2020 financial perspective were re-allocated to help regional and local authorities fight against Covid-19 (see section 3.). The authorities were at the front line, while the pandemic has been testing multilevel governance strength (OECD, 2020b), but it also showed institutional limitations of the EU during the first and second wave of the pandemic (Pazos-Vidal, 2020).

2.3. Cohesion policy support to the fight against the pandemic

In April 2020, the European Commission adopted two packages of measures (OJ L 130, 2020.04.24) – namely the Coronavirus Response Investment Initiative (CRII) and the Coronavirus Response Investment Initiative Plus (CRII+) – in order to mobilize EU cohesion policy allocations to respond to the pandemic. The CRII package (OJ L 130, 2020.4.24):

1) provides flexibility to use existing unspent resources and redirect them to where they are most needed;
2) allows for transferring unallocated EU funding between funds and categories of regions;
3) gives an opportunity to increase EU pre-financing to improve cash flow;
4) creates an option to increase the EU co-financing rate to 100% for the 2020–21 accounting year.

The CRII/CRII+ initiatives were linked and prolonged on May 27, 2020, with the presentation of the REACT-EU (Recovery Assistance for Cohesion and the Territories of Europe) package as part of the new additional recovery and resilience facility (see section 2.4). Both initiatives were focused on three areas, and the implementation of CRII/ CRII+ was based on reprogramming of already adopted operational programs in MS (European Commission Cohesion Data, 2020):

- health care: in order to secure personal protective equipment, finance testing and support hospitals by purchasing additional medical equipment (see section 2.3.1.);
- businesses: with regard to providing working capital to SMEs, facilitating digitalization and setting up or redesigning financial instruments (see section 2.3.2.);
- persons: by implementing employment retention schemes and supporting vulnerable groups (see section 2.3.3.).

Until November 19, 2020, EUR 7.6 bn in additional EU pre-financing was provided, 129 cohesion policy programs have opted for 100% EU co-financing and EUR 3.3 bn has been transferred between funds and/or between categories of regions (EC Cohesion Data, 2020).

2.3.1. Change in the EU allocation to health actions

In response to the urgent need for adopting EU cohesion policy to the Covid-19-related challenges, the CRII/CRII+ packages provided for the possibility to redirect EU financial resources in particular to health actions. Eighteen out of 27 Member

States made use of the implemented provisions to reallocate appropriations in the framework of the funds granted to measures relating to the protection of public health and safety. In comparison to the originally planned financial support earmarked for the health care systems in the 2014–2020 programs, transfers of resources within the existing and still unallocated EU funding have resulted in an increase of ca. EUR 6.7 bn. The main target of the additional means in this field focus on securing personal protective equipment, compensating financially Covid-19 testing and financing purchases of medical equipment made by hospitals. The health sector falls within the shared competence between the UE and MS. Hence, the measures conducted with financing from the European Structural and Investment Funds (ESIF) are often programed within the framework of various priority axes in the operational programs (OP) managed by EU regions and MS. In order to see the reprogramming of financial support, it is necessary to analyze financial data in OP that are structured into categories of intervention (CoI) with precisely defined intervention fields. Figure 1 reports the reallocation of the EU funds in planned support to health care since the beginning of the Covid-19 pandemic. Figure 1 summarizes the aggregative values of health investments coded under the intervention fields as follows: health infrastructure, e-health, active and healthy ageing, access to social and health services.

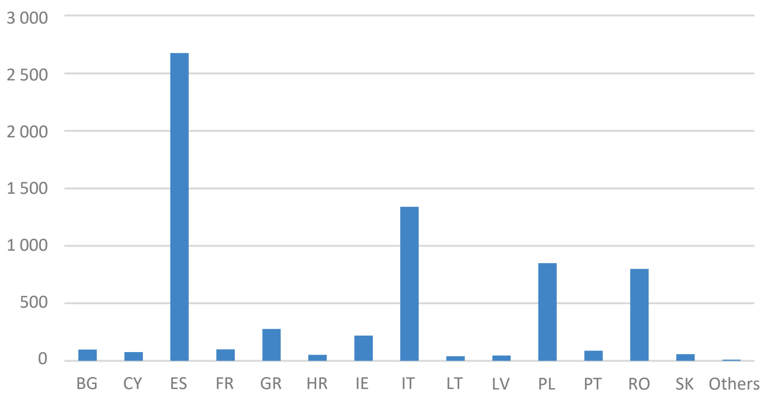

Figure 1. Reallocations of the EU funds in planned support to health care in EUR m*

* The financial data show the value of total transfers proposed in the national and regional programs to support the public-health measures in the fight against Covid-19 since 1 February 2020 up to now.
Source: Own work based on (European Commission Cohesion Data, 2020).

The finding emerging from this figure is that the highest values of changes are observed in those MS which, on the one hand, have been the largest beneficiary of

EU cohesion policy funds (e.g. Poland, Italy), and on the other – were most affected by the coronavirus crisis (e.g. Italy, Spain). More than 80% of total reallocations for Covid-19 actions were made by four MS: Poland, Italy, Spain, and Romania. The southern European countries in particular had to tackle the rapidly increasing number of Covid-19 infection cases. The outbreak of a novel coronavirus disease highlighted the limited capabilities of health care facilities to ensure the adequate protection of the health and safety of people being in need of medical attention. This also refers to health care workers and care providers who are vital to the functioning of health care, and – like the rest of the population – they face the same challenges when implementing infection prevention measures. Thus, health care staff had to be suddenly fitted out with huge quantities of personal protective equipment to avoid the transmission of infection and maintain a high standard of care and safety.

According to the financial data reported so far to the Commission by MS, approximately EUR 2.5 bn (37.5% of total reallocations) was already spent on the health sector to combat and counteract the Covid-19 pandemic. However, given that the data are provided with a delay, the total amount of EU financial support mobilized for such purposes is likely to be significantly higher. In view of this, the highest share in current spending is noticed in the purchases of personal protective equipment, medical equipment, and medicines linked to Covid-19 (close to 80%). It should be noted, however, that approximately EUR 1.1 bn out of this amount were spent on providing health care staff with necessary personal protective equipment. To state it explicitly, the reallocated funds have been devoted to furnishing among other items of personal protective equipment (e.g. gloves, gowns, shoe and head covers, masks, face shields, body suits etc.), ventilators, ambulances and vehicles for emergency response, hospital beds for additional space to accommodate Covid-19 patients requiring critical care.

2.3.2. Change in the EU allocation to business support

Many European countries have implemented strict quarantine measures or various forms of lockdown across their territories to slow the spread of the coronavirus. Those different types of unprecedented restrictions have been imposed on all areas of socioeconomic life, ranging from school closures through suspensions of cultural events to temporary prohibitions of certain business activities (e.g. shopping centers, hotel and restaurants, hair and beauty salons, sport and leisure centers). Economic ramifications of the coronavirus crisis quickly became evident and brought many businesses to a near-standstill. Small and medium-sized enterprises (SMEs) on the front lines have been particularly affected by the pandemic. Suspensions of certain commercial, industrial, or artistic activities by lockdowns have not only directly affected those types of businesses but also indirectly affected affiliates or business partners and even companies in other countries. Therefore, business expected a rapid response to address current disruptions and to increase its resilience to the economic slowdown.

Being aware of the fact that SMEs act as a lynchpin linking the pandemic to a broader economic recession, MS were allowed from the very beginning to introduce reallocations of funding aimed at supporting business. Most transfers relied on shifting financial resources from one type of activity with larger unallocated means to another that currently showed a higher potential and opportunities to emerge from the downturn. As a result of changes made by countries and regions in the allocations at their disposal, EUR 9.8 bn were reprogrammed in order to relaunch the economy and deny the crisis. As can be seen from Figure 2, the largest changes in operational programs in favor of enterprises were adopted by Southern countries and Poland as an exception in this group. The value of business-oriented reallocations introduced by these countries accounts for 65% of the total reprogramming amount. What is striking about the data in this figure is that countries not rated among the major beneficiaries of EU cohesion policy spent relatively considerable funds on the measures focused on enhancing enterprises' resilience strategies. This finding suggests that the EU cohesion policy funds have been involved in large-scale activities directed at enterprises in various areas affected by the pandemic in many countries.

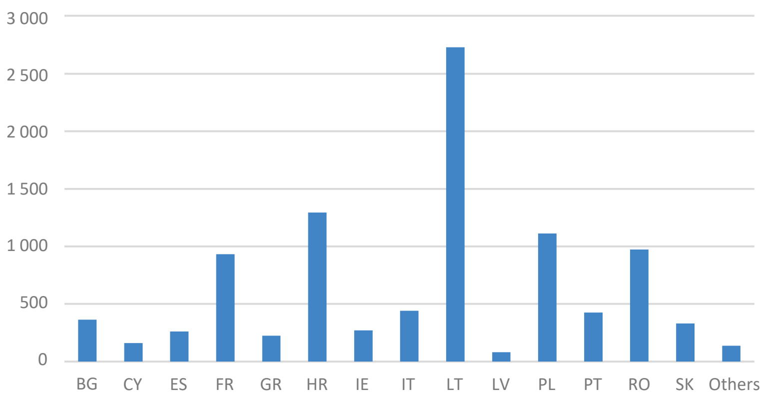

Figure 2. Reprogramming of the EU funds in planned support to enterprises in EUR m*

* The financial data show the value of total transfers proposed in the national and regional programs to support the function of the business activities best address the Covid-19 crises since February 1, 2020, up to now.

Source: Own work based on (European Commission Cohesion Data, 2020).

Member States proposed different measures to help enterprises cope with short-term financial risks and long-term business implications. It means that the support actions were designed to maintain temporarily the company's financial liquidity and provide incentives that will allow it to resume business activity fully later. Among priority measures offered by reprogramed funds the highest shares fall on generic productive investments in SMEs (55.1% of total reallocated amount), SMEs business development, entrepreneurship, and incubation, including support to spin-offs and spin-outs (respectively 15.2%). In addition, SMEs could benefit from support for investments (implementing R&I activities) such as liquidity needed to cover additional costs or risks. The value of funding earmarked for this support amounted to over EUR 0.5 bn which constitutes approximately 5.5% of the total reallocated amount to enterprises. As a consequence, nearly 400,000 European enterprises could benefit from grants supporting their working capital. It can thus be suggested that reprogramed funds have significantly contributed to preventing bankruptcy, encouraging investment and, most importantly, reducing layoffs.

2.3.3. Change in the EU allocation to support individuals

The implementation of mandatory mass quarantines by almost all European countries to prevent coronavirus spread resulted in the fact that many citizens were put on various forms of social isolation. However, they were affected by the coronavirus crises in different way, often deprived of employment and earning opportunities. Thus, the funding available under the European Social Fund (ESF) was also opened to reprograming at the level of national and regional operational programs so as to counteract the negative effects of the Covid-19 crisis. The total volume of the reallocated resources in ESF to support people directly amounted to EUR 2.9 bn. The financial assistance was used to combat the pandemic in such forms as supplementary wage for health care personnel, PPE and services for vulnerable groups, special support to short-time work arrangements, and IT equipment. Figure 3 shows an overview of the funds reprogramed to combat the effects of the pandemic among societies. General inspection of the data indicates that three countries dominate in regard to the amount of the reallocated funds, i.e. Italy, Poland, and Slovakia: they redirected ca. 87% of the total reprogramming amount.

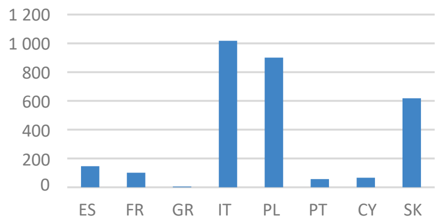

Figure 3. Reallocation of the EU funds in planned support of individuals in EUR m*

* The financial data show the value of total transfers proposed in the national and regional programs to support social services, retention of employment, support to vulnerable groups and others since February 1, 2020, up to now.

Source: Own work based on (European Commission Cohesion Data, 2020).

2.4. Multiannual financial framework and resilience and recovery facility: Next Generation EU

The times of pandemic has affected negotiations on multiannual financial framework that should provide financing of EU policies for the forthcoming years 2021–2027. In order to help its MS to recover from the coronavirus crisis the European Commission proposed in May 2020 an additional EUR 750 bn fiscal stimulus to MFF (EUR 390 bn in grants and EUR 360 bn in loans) and other flexibility measures and monetary stimuli. This is an unprecedented, new, yet temporary instrument (resilience and recovery facility) for the future development of the EU, on which the heads of governments and states (the European Council) primarily agreed in July 2020. On November 10, 2020, the European Parliament and the EU Council reached an agreement on the next budget and this new instrument named the Next Generation EU (NGEU), finally approved at the December EU Council summit. Unexpectedly, the Polish and Hungarian governments opposition to the linking of EU budget with the rule of law conditionality made them tried to veto the agreement and break solidarity with all other EU MS waiting for the adoption of MFF and NGEU.

Most resources under the new MFF will go to the following budget headings: Cohesion, Resilience and Values, Natural Resources and Environment followed by Single Market, Innovation and Digital (Table 1, Figure 4). This distribution of resources reflects the shift of EU priorities to deal with environment protection and stresses the necessity to implement the European Green Deal, resilience building, innovation and digitalization in post-Covid-19 times. Additionally, the crisis that is affecting health care systems brought an impetus to launch a new EU4Health initiative worth EUR 5.07 bn that will help in e.g. the coordination of future risks related to the next pandemic, and provide necessary supplies of medicine, access to health care, diagnostics etc. The designed initiative does not give more room for maneuver under European treaties. The importance of research in the program Horizon Europe and education and mobility within the Erasmus+ program was additionally underlined by the increase of allocations to them, but also by the creation of the Just Transition Fund to transform coal-based regions.

Table 1. MFF and NGEU for 2021–2027 (EUR bn)

Heading	MFF	NGEU	Total
Single Market, Innovation and Digital	132.8	10.6	143.4
Cohesion, Resilience and Values	377.8	721.9	1 099.7
Natural Resources and Environment	356.4	17.5	373.9
Migration and Border Management	22.7	–	22.7
Security and Defense	13.2	–	13.2
Neighbourhood and the World	98.4	–	98.4
European Public Administration	73.1	–	73.1.
Total	1 074.3	750.0	1 824.3

Source: (European Commission, 2020b).

The use of NGEU requires that each Member State will prepare recovery and resilience plans presenting a coherent package of reforms and public investment projects that should be implemented by 2026. The plans should be linked to challenges of the European Semester, country-specific recommendations, and actions related to the green and digital transition, namely correspond to the 2021 Annual Sustainable Growth Strategy; which has four dimensions of environmental sustainability, productivity, fairness, and macroeconomic stability (COM/2020/575, European Commission, 2020c). The Commission is preparing the ground for the disbursement of NGEU and the mechanisms implemented under SURE instrument are proposed as a model.

The new MFF initiated a discussion on revenues and a basket of new own resources and its ceiling (e.g. Dobreva, 2018, Dachrenberg, 2020), along with a new dimension to the European fiscal policy regarding loans and guarantees, which form the core of new instruments such as SURE and NGEU. This might signify further deepening of integration processes, but also reveal challenges to future economic policy of increased public expenditure.

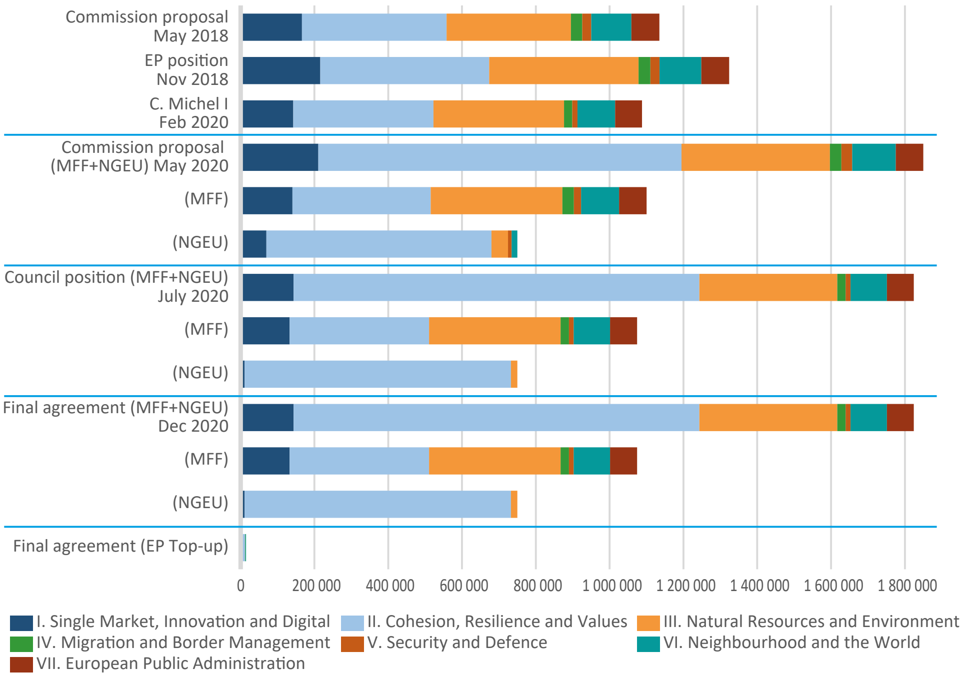

Figure 4. The evolution of MFF and NGEU 2021–2027 in negotiation processes, May 2018–November 2020 (in constant 2018 prices) in EUR m
Source: European Parliamentary Research Service, 2020b.

2.5. Conclusions

The Covid-19-caused crisis reveals serious implications for European integration process.

First, we notice a strong shift of priorities regarding environment transformation, digitalization, and health protection, reflected in MFF. The coordinative role of European institutions and the redirection of different financial instruments to health care follows Haas' neofunctionalist paradigm (1968) and represents a spillover effect resulting from integration (Pazos-Vidal, 2020). Second, the EU reacted relatively fast to counteract the crisis by using existing legal and financial instruments, not to mention creating new ones. Third, as Fabbrini (2020) argues, the crisis immediate health cost and its socioeconomic implications expose the institutional and substantive shortcomings of the current EU system of governance and show the need to reform the EU and 1) enforce it in the areas of health and 2) redesign the system of own resources without merely relying on financial transfers from its Member States. The EU decision-making process requires further shifts from an inter-governmental mode that sometimes creates a bottleneck to timely response from the European level toward e.g. a Conference on the Future of Europe that could make the EU system of governance more effective and democratic. This motion requires changes in treaties as well, which is a challenge because the unanimity of all MS would be required to do so (Pazos-Vidal 2020, Fabbrini, 2020). Fourth, the last crises that affected the EU in the near past led to the use of international agreements outside the EU legal order e.g. in the European debt crisis (Fabbrini, 2020). If a veto to MFF were to appear, one of the solutions to save the implementation of Next Generation EU would be to use a similar legal instrument. Such a solution might have led to further divisions among MS and the strengthening of a multi-speed Europe, in which some countries would deepen the integration process "in the club" while others concentrate on existing/selected policies and are left behind the integration process. The crisis analyzed from the institutional perspective appears as a chance to reform the decision-making process but, on the other hand, as a threat to the inclusive integration of all Member States.

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Part III
CHALLENGES FOR COMPANIES