A small step forward

Grégory Claeys argues that the EU's SURE plan to safeguard employment is too modest to have a significant impact the COVID-19 crisis

The European Union's new instrument, the so-called temporary Support to mitigate Unemployment Risks in an Emergency (SURE), will provide temporary support of up to €100 billion in loans to EU countries that request financial assistance to fund job-saving initiatives. While the creation of the instrument has generated a lot of interest, its main benefit is to show that, if needed, the EU can create a borrowing capacity and issue a common safe asset.

In terms of having a significant impact on the EU's fiscal response to the COVID-19 crisis, however, SURE is too modest, and should be evaluated as only a part of a more complete recovery plan.

What is SURE?

The EU has been making back-to-back loans to its member states since the 1970s, but SURE has two original features. First, its stated objective is to ensure that countries can easily and cheaply finance the short-term work schemes heavily used since the beginning of the COVID-19 lockdowns.

Second, to protect the EU's AAA rating, the money raised by issuing bonds on international financial markets will be guaranteed by the so-called 'headroom' of the EU budget (ie. the additional resources the Commission can call on from member countries to service its debt, principal and interest, if a debtor defaults), but also by an additional €25 billion in direct irrevocable callable guarantees from EU countries.

The Commission portrayed SURE as a *"tangible expression of Union solidarity."* But how generous is it, and what impact can it have in the context of the COVID-19 crisis?

The three main advantages of SURE

- SURE will provide an extra source of financing for EU countries on top of market financing and potential credit lines from the European Stability Mechanism (ESM). Its loans could be cheaper and possibly longer-term than what some countries, including Greece, Cyprus, Italy, Portugal and Spain, can currently obtain from the market, because the EU should currently be able to borrow on the market at around 0% and pass this rate to member states.

- SURE offers a lighter and more agile governance framework than other EU financial assistance programmes, particularly the ESM credit lines, even under the simplified procedures of its new 'Pandemic Crisis Support' facility. To access the SURE funds, EU countries would only need to show that the money is deployed for short-term work schemes. Approval just requires a qualified majority in the Council, and there will be no need

SURE is too modest to have a significant impact on the EU's fiscal response to the COVID-19 crisis, and should be evaluated as only a part of a more complete recovery plan to consult each national parliament for every request. Given its novelty, SURE might also be less politically toxic than the ESM in some countries, such as Italy.

- Finally, SURE provides an additional incentive for countries to put in place short-term work schemes and use them during future possible lockdowns. Short-term work schemes help avoid the break-up of labour relationships, which is very costly for workers and companies. They have been used extensively in the past two months and have proved crucial to ensure the survival of European firms and to prevent a very quick rise in unemployment.

  However, these schemes are very different in different EU countries: countries including Germany, Italy, France and Belgium have well-established schemes; others including Cyprus, Greece, Estonia and Latvia entered the crisis without such schemes and had to improvise. The fact that SURE emphasises the need to have such schemes in place and encourages member states to use them is good in itself. If it were to be prolonged, SURE could also be used to share national best practices on short-term work schemes, for example using workers' idle time for online training to improve their skills.

Four limits of SURE

- SURE's effect on public finances will be very marginal as the programme is too small (€100 billion) to lead to significant savings in interest costs. Imagine for example that Italy were to borrow from SURE €20 billion at 0% for 10 years, instead of the 1.8% it would pay the markets, at the time of writing. Italy would then save around €360 million per year. Considering its forecast deficit of 11.1% of GDP in 2020, ie. around €200 billion, SURE would cover 10% of the new debt incurred this year, and thus reduce borrowing costs on this new debt by 10%. Given the relatively low level of the spread between the two, this would only represent savings equivalent to 0.02% of Italy's GDP.

- There is a risk that a stigma will be attached to the use of the programme. There are not yet studies on stigma effects from EU financial assistance programmes, but (even if they are not fully comparable) there is some empirical evidence that the announcement of IMF programmes can increase yields. Markets could interpret a request as a sign of weakness and therefore ask for higher rates when countries issue new bonds, thus erasing savings generated by the lower cost of SURE loans.

  In addition, unlike an ESM credit line, a loan from SURE would not make a country eligible for the ECB's Outright Monetary Transactions scheme (OMT). One solution to avoid any 'first-mover' stigma would be for a large number of countries, ideally all of them, to use SURE at the same time.

  However, there would be two limits to that solution: first, SURE is not financially advantageous for countries that already enjoy interest rates at a similar or lower level to what they could secure using SURE (eg. Germany, France, the Netherlands, Austria). Second, if many countries use it, the relatively small amount of money available would have to be divided between them, reducing the already small savings on interest costs made by each country.

- The main limitation of SURE is that it solves the wrong problem. Access to finance is not an issue for euro area countries at this stage, thanks in particular to the massive intervention by the European Central Bank since mid-March. If access to finance were to become a real problem for some countries, SURE would then be too small.

  This was already an issue for one of its predecessors, the European Financial Stabilisation Mechanism (EFSM), which was limited to €60 billion. The European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM) were created to address this very problem.

- Finally, SURE is not a significant and permanent EU borrowing capacity to be used as a stabilisation tool. Nor is it an *"emergency operationalisation of a European Unemployment Reinsurance Scheme",* as the Commission put it when it was announced. At the request of some EU countries, SURE will be temporary and will be dismantled in a couple of years. SURE is also not an insurance mechanism, as it does not involve any ex-post transfers following the materialisation of a risk. As a lending facility, SURE only involves mutualisation of borrowing costs.

Conclusions

The Commission's quick proposal and negotiations with member states, establishing SURE within a few weeks, should be commended. SURE also rightly highlights the importance of short-term work schemes and gives EU members an incentive to use them in the current crisis, and maybe also to improve them in the future.

However, the facility will have a small impact on the EU's fiscal response to the COVID-19 crisis. Its merits should be measured as part of the complete recovery initiative that will be presented by the Commission by the end of the month.

The main advantage of SURE is to show that, if needed, the EU can create a borrowing capacity and issue a common safe asset using the community method, instead of using intergovernmental agreements, as was done with the ESM and the EFSF.

Undeniably, a common debt-management office issuing a common safe asset at large enough scale would be very useful to the euro area in a crisis. In particular, such an EU debt instrument would help the ECB fulfil its mandate – politically, it would be easier for the ECB to buy European debt than to buy national debts.

However, such a facility would need to be much bigger than SURE. The 18 May Franco-German 'Recovery Fund' proposal to issue €500 billion of EU debt to increase the size of EU programmes in the next few years goes in this direction. Issuing such a large amount of EU debt should be possible by increasing drastically the headroom of the EU budget. What is needed now is support from the other 25 EU countries. ■

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This article was originally published on Bruegel