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**How to make Next Generation EU a success for the economy?**

The package agreed by European leaders after five days of intense debate is a major step forward for the political integration of the EU. It is the first time that member countries agree on a common fiscal instrument funded from joint debt –an approach which should bring countries closer together.  That said, whether this will also serve as a decisive tool to kick-start an economic recovery and eliminate the risk of cross-country fragmentation depends on a number of added conditions which may or may be met.

Without a doubt, the fact that heads of government managed to agree on a common line of action in the face of the pandemics was path-breaking. We are witnessing a sea change vis-à-vis the years of austerity that marked the financial crisis, when Europe imposed tough conditions on the bail outs of countries which had trouble meeting debt obligations. Acceptance on the need for European-wide macroeconomic action will go hand-in-hand with the pooling of common resources obtained from access to markets (likely on most favorable terms). Moreover, the fact that over half of the funds so collected will be transferred to countries in the form of grants, not loans, is a clear demonstration of solidarity.

Despite these major political gains, however, the economic impact of the agreement can vary from significant to negligible, depending on three key factors. First and foremost, time is of the essence. Projections are for a contraction of the EU economy by nearly €1 trillion in 2020 –this is the "crisis gap" that needs to be overcome. The problem is that any delay in the stimulus measures entails a high probability that the recovery will be incomplete. This is so because a prolonged recession would inexorably multiply the number of enterprise insolvencies and result in massive job losses, thereby eroding the productive basis for a later recovery. By contrast, quick and targeted support efforts will help maintain capacity, paving the way to a strong rebound, including in those countries most affected by the crisis.

The agreed package, worth €750 billion, represents an impressive 75% of the above-mentioned crisis gap. Nevertheless, the fact is that funds will be disbursed over a four-year period, thus diffusing its effect. Moreover, only a portion (€390 billion) is in the form of grants, which carry the largest fiscal impulse. If these grants were disbursed expeditiously as from 2021, the multiplier effects would likely be large. By contrast, any delays will have a disproportionately negative cost in terms of lost output and higher unemployment.

Accelerating the pace of implementation of the programme will be a challenge, as national parliaments will need to approve the necessary changes so that the Commission can issue debt on behalf of member states, which will take time. In

addition, once the funds are available, the process for countries submitting proposals and for Brussels to decide upon disbursements, will also entail delays. It is thus well possible that the funds will not be available until mid-2021.

Secondly, an equally important hurdle lies with the implementation capacity of recipient countries. For instance, the amount of grants and loans potentially available to Italy comes close to €210 billion, more than five times the amount of the budget actually spent on investment by the Italian government in a given year. This could prove quite a daunting task, since much of the funding provided as part of the European recovery programme will have to be used for investment purposes, including in digital technology and green growth, for which the available supply capacity is not necessarily very large. Similar absorption issues arise in large potential recipients like Spain.

Finally, the issue of conditionality may raise some concerns. The agreement reached last night mentions observance of country-specific recommendations as a key criterion for providing the funds. For example, in the case of the Netherlands, the Commission recommends addressing "features of the tax system that facilitate aggressive tax planning" and ensuring "effective supervision and enforcement of the anti-money laundering framework". The extent to which these recommendations will be regarded as pre-conditions for the disbursements of funds will undoubtedly lead to lively debates.

In sum, Next generation EU is an important political achievement. The challenge is now to make it an engine of post-Covid recovery. This will a function on the speed of implementation of the programme and the absorption capacity of recipient countries in managing the funds –two objectives which may be in tension and will require careful policy making.

Eventually, success will depend crucially on whether the EU is able to relax constraints on the detailed economic and social policy choices of each country. And instead focus on common principles and goals that are best pursued by all member countries together, such as the fight against the pandemics and tax evasion, and investing in digital technology and the green economy. Next Generation EU opens a new avenue for achieving this.