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The EU's "SURE Instrument"

# How to assess the EU's Covid-related subsidisation of short-time work schemes

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The SURE instrument enables Member States to receive favourable EU loans to fund COVID-19-related short-time work schemes or similar measures.

- Member States that have built up high levels of debt in recent years, and failed to undertake reforms to increase economic growth, will be the ones that benefit from SURE.
- One argument against financing national short-time work schemes by way of SURE loans is that Member States themselves are responsible how resilient their economies are in the event of a crisis.
- An argument in favour of SURE is the fact that the COVID-19 pandemic represents an exogenous, asymmetric economic shock which Member States are not themselves responsible for. In view of the Corona shock, there was also a need to act in order to prevent sovereign default.
- An alternative option did however exist: using credit lines from the European Stability Mechanism. This would have had the aforementioned advantages without any of the disadvantages. This option was not taken for political reasons.

## Table of Contents

# 1 Introduction

The outbreak of COVID-19 and the extent of its spread has led to a health emergency for the citizens of all the EU Member States. At the same time, the COVID-19 pandemic has sparked a major economic shock across the whole of the EU. In order to provide Member States with financial support in tackling the consequences, the European Parliament and the Council, on a proposal from the Commission, rushed through the SURE Regulation[1] which has been in force since 20 May 2020 and has been used to create the "SURE Instrument". SURE stands for "temporary **S**upport to mitigate **U**nemployment **R**isks in an **E**mergency". With this instrument, the EU can grant Member States, on request, a total of € 100 billion which they can use in particular to supplement their short-time work schemes.

SURE forms part of a support package for the labour market, business and the economy amounting to € 540 billion (see Tab. 1). The package will enable the EU and its Member States to take measures aimed at keeping the economic consequences of the COVID-19 outbreak to an absolute minimum.

**Tab. 1: Support Package**

| EU Support Package | | |
|---|---|---|
| Safety Net 1<br>**SURE** | Safety Net 2<br>**EIB credit package** | Safety Net 3<br>**Precautionary ESM credit line** |
| for labour market and employees | for companies | for Member States |
| EUR 100 billion | EUR 200 billion | EUR 240 billion |
| In total € 540 billion | | |

# 2 The SURE Instrument

## 2.1 Aims, financing and duration

The aim of the SURE instrument is to provide Member States with temporary support in reducing the risk of unemployment in order to mitigate the economic, social and health-related consequences of the COVID-19 outbreak.[2] For this purpose, the Member States will receive "financial assistance" in the form of "favourable"[3] EU loans for short-time work schemes and similar measures. In addition to these immediate objectives, SURE has the long-term aim of preserving the EU's economic structure, prevent long-lasting economic and social damage and favour a swift recovery.[4]

The SURE loans granted by the EU "should" be financed by EU borrowing.[5] For this reason, the SURE Regulation empowers the Commission to issue EU bonds worth up to € 100 billion.[6] The Member States in

[1] Council Regulation (EU) 2020/672 of 19 May 2020 on the establishment of a European instrument for temporary support to mitigate unemployment risks in an emergency (SURE) following the COVID-19 outbreak (hereinafter abbreviated to "SURE-REG").

[2] Cf. Art. 1, 2 and 4 SURE-REG.

[3] Recital 8, SURE REG.

[4] Cf. European Commission (2020): Technical briefing ON-the-record.

[5] Cf. Recital 8, SURE REG.

[6] Cf. Art. 4 et seq. SURE-REG. Thus, like the EFSM Regulation, SURE allows for pre-financing, see in this regard European Commission (2016): Report from the Commission to the European Parliament and the Council on borrowing and lending activities of the EU in 2015, COM(2016) 387, p. 9.

receipt of the loans can thus - insofar as they would have to pay more interest on the financial markets - benefit from the low interest to which the EU is entitled due to its high level of creditworthiness.

Security for the EU bonds is provided by the EU budget[7] supplemented by voluntary guarantees[8] from Member States amounting to at least € 25 billion. The level of the individual guarantee from a Member State depends on the its share of the EU's gross national income (GNI). The guarantees are made available irrevocably, unconditionally and on-demand. They are necessary in order to ensure that any contingent liabilities under the SURE loans are compatible with the own-resources ceiling in the EU's current Multiannual Financial Framework 2014 to 2020.

SURE loans can only be granted when all Member States have submitted their guarantee commitments. This took place on 22 September 2020.[9] Where a Member State has received a SURE loan and is unable to make its repayments to the EU, the Commission may draw on the Member States' guarantees, in proportion to the relative share of each Member State in EU GNI. Before the Commission does so, however, it must check how far it can afford to make repayments from the EU budget. In addition, the need for the guarantees from Member States can be examined if an agreement is reached on changing the own-resources ceiling. If a Member State fails to comply with the Commission's call for funds under the guarantee, the guarantees of all the other Member States will be drawn upon on a pro rata basis - up to the total amount of the guarantee provided by each Member State. The Member State that fails to comply with the call for funds nevertheless remains obliged to do so.

SURE loans are only available temporarily: The Council can adopt implementing decisions up until 31 December 2022 for granting SURE loans.[10] It may decide, however, on a proposal by the Commission, to extend the period of availability of SURE, each time for an additional period of six months, if the severe economic disturbance caused by the COVID-19 outbreak continues to exist and continues to affect the financing of measures eligible for support.[11]

## 2.2 Measures by Member States that are eligible for support and SURE procedure

Under the SURE instrument, Member States may apply for loans for the following labour-market policy measures[12] which they have taken or are planning to take:[13]

- short-time working schemes,
- or "similar" measures aimed at protecting employees and the self-employed thereby reducing the incidence of unemployment and loss of income, e.g. income replacement for the self-employed,[14] and
- "relevant health-related measures"[15], particularly in the workplace. This may mean measures aimed at reducing occupational hazards and ensuring the protection of workers and the self-employed in the workplace.

[7] This arises from Art. 4 ("to borrow on the capital markets or with financial institutions on behalf of the Union") and from Recital 9 ("loans from the Union budget") of the SURE-REG.
[8] Cf. Art. 11 et seq. SURE-REG
[9] Cf. European Commission in Germany (2020): Press release dated 22 September 2020.
[10] Cf. Art. 12 (3) SURE-REG.
[11] Cf. Art. 12 (4) SURE-REG.
[12] Cf. Recital 9, SURE REG..
[13] Cf. Art. 1 (2) and Art. 3 (2) and Recital 7 SURE-VO.
[14] Cf. Art. 1 (2) and Art. 3 (2) and Recital 7 SURE-VO.

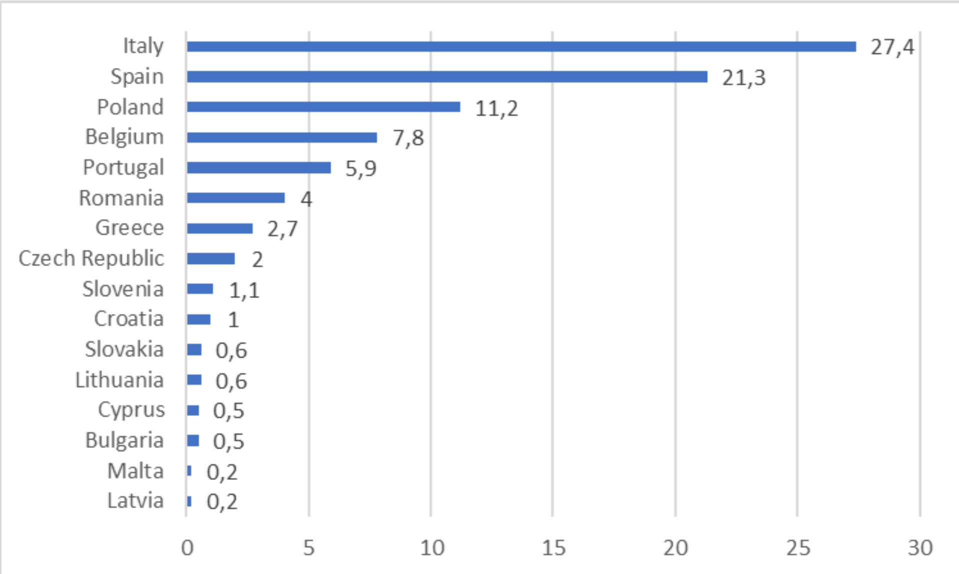
The procedure for granting loans involves six steps:

| | | |
|---|---|---|
| 1 | Member State requests a loan | Art. 3 (1) SURE-REG |
| 2 | Commission consults the Member State and checks the request. | Art. 6 (2) SURE-REG |
| 3 | Commission submits to the Council a proposal for granting a loan. | Art. 6 (1) SURE-REG |
| 4 | Council adopts an implementing decision | Art. 6 (1) SURE-REG |
| 5 | Commission and Member State conclude the loan agreement | Art. 8 (2) SURE-REG |
| 6 | Commission disburses the loan in instalments | Art. 7 SURE REG. |

In step 2 of the procedure, the Commission examines, in particular, whether there has been a "sudden and severe" increase in actual or planned expenditure by the Member State related to short-time work schemes or similar measures. The increase must have occurred due to the COVID-19 outbreak.

On 24 and 25 August, the Commission submitted to the Council proposals for granting SURE loans to 16 Member States as provided for in step 2 of the procedure (see Fig. 1).[16]

**Fig. 1: Amount of the SURE loans to be received by the individual Member States according to the Commission proposal (in € billion)[17]**




Graph: cep.

The Council's implementing decision - step 4 - must contain the conditions of the loan, such as the amount and term. In addition, it must also contain a description of the national measures for which the loan is being granted. The loan agreement referred to in Step 5 must provide for a regular review of whether the money is being put to proper use.

## 3 Economic assessment of the SURE instrument

The SURE instrument enables Member States to receive favourable EU loans to fund short-time work schemes or similar measures. Short-time work schemes are effective instruments for reducing worker lay-

[15] Recital 5, SURE REG.
[16] In addition to these 16 Member States, Hungary also submitted a request for a SURE loan.
[17] Cf. European Commission (2020): Commission proposals.

offs during an unexpected economic crisis.[18] During such a crisis, they help to stabilise the income of private households and reduce the wage or lay-off costs of companies. In addition, once the crisis is over, companies can resume or increase their production more quickly as they do not have to recruit new employees. Companies thus save the costs of recruitment and induction training. Employees also benefit during and after the crisis because they do not lose their jobs. During the COVID-19 pandemic, therefore, many Member States have introduced short-time work schemes or extended existing schemes.[19] In most Member States, the costs of short-time work have risen sharply.

Irrespective of the good reasons for national short-time work schemes, the question arises as to whether there is really a need for SURE because the interest-rate advantage to Member States resulting from the SURE loans is small. This is due to the fact that the yields on national government bonds have so far hardly reacted to the COVID-19 pandemic and remain well below the yields existing at the time of the euro crisis (see Tab. 2). As far as the eurozone countries are concerned, this is principally due to the ECB programmes for buying up government bonds.

**Tab. 2: Yields on government bonds with a 10-year maturity for selected Member States (in %)**

| | December 2011 | September 2020 |
|---|---|---|
| France | 3.13% | -0.23% |
| Greece | 35.49% | 1.07% |
| Italy | 7.04% | 0.97% |
| Portugal | 13.56% | 0.30% |
| Spain | 5.09% | 0.28% |

Source: Our own graph based on Investing.com.

The remaining yield differentials which currently exist between the Member States are principally the result of varying levels of public debt and the varying expectations for economic growth in the different Member States. Bonds from Member States with a high level of debt and where economic growth is expected to be low, generally have a higher default risk and thus a higher yield than bonds from Member States with a low level of debt and high expected economic growth. Since the former profit more from the low-interest SURE loans than the latter, SURE will be rewarding Member States that have built up high levels of debt in previous years and have failed to undertake reforms to increase economic growth. Member States with a low level of debt and high expected economic growth, on the other hand, will profit little from SURE loans or even profit not at all. In the latter case, these are Member States that are able to obtain loans at better conditions than the Commission. For instance, the interest that Germany has to pay for newly issued bonds is lower than the interest which the Commission has to pay.[20] Currently, the yield differential between an EU bond with a 10-year residual maturity and an equivalent German government bond is about 0.3 percentage points.

[18] Cf. Adams-Prassl, A. et al. (2020): Inequality in the Impact of the Coronavirus Shock: Evidence from Real Time Surveys, IZA DP No. 13183.
[19] Cf. European Central Bank (2020): Short-time work schemes and their effects on wages and disposable income.
[20] Cf. EU Commission (2020): Investor Presentation July 2020, p. 18.

The advantage of SURE loans for Member States with high yields is however limited by the fact that the scale of the SURE instrument is limited to € 100 billion. The Italian government, for instance, is expecting to make savings from the SURE loans only of € 5.5 billion over a period of 15 years.[21]

In addition to the issue of whether SURE loans are currently actually necessary, there is also the basic question of whether they are justified. One argument against financing national short-time work schemes by way of European bonds is that Member States themselves are basically responsible for how resilient their economies are in the event of a crisis, since economic policy and fiscal policy still fall, not within the European, but the national area of competence. Resilience is influenced in particular by the country's fiscal capability during a crisis, the flexibility of its labour market and the effectiveness of public administration.[22]

An argument in favour of the use of SURE loans is the fact that the COVID-19 pandemic represents an exogenous economic shock which Member States are not themselves responsible for. And, although it hit all Member States at about the same time, it did so to very varying degrees, so the shock was asymmetric. In such a case, it makes sense to share the costs of fiscal stabilisation between the Member States.[23] Member States that are unaffected or less affected by the pandemic support the Member States that are particularly severely affected. In this way, SURE acts like an insurance. The SURE instrument is also supported by the fact that, in view of the Corona shock, there was a need for action in order to prevent sovereign default. Thus, at the end of 2019, Greek debt stood at 177% of GDP, Italian at 135% and Portuguese at 111% of GDP. An insolvency, especially in the case of Italy, would – at least in the short term – have been much more costly than providing the country with financial support. This is the comeback for past failures to enforce the Stability and Growth Pact.

An argument against SURE, on the other hand, is the fact that the loans reduce the Member States' responsibility for making their own provisions for the event of a crisis. This undermines the Stability and Growth Pact. By supporting the Member States in a crisis, SURE reduces the incentives for Member States to bring in reforms. And it is often in times of crisis that reforms can be introduced which at other times would not be possible such as greater labour market flexibility or streamlining the civil service.

The negative incentive for reforms is further increased because SURE also reduces the Member States' aversion to a programme under the European Stability Mechanism (ESM). This is due to the fact that SURE loans reduce the strain on the public finances of the Member States. Their effect is thus similar to that of ESM loans but, unlike these, they do not come with reform requirements. Although the SURE loans must be used for specific purposes, the purposes are very broadly worded. Thus, it is ultimately unclear what is meant by measures that are "similar" to short-time work schemes, or by "relevant health-related measures".[24]

Irrespective of these basic aspects, it is doubtful whether the actual or planned increase in expenditure for short-time work schemes by Member States is a good indication of how severely a Member State has been affected by the COVID-19 pandemic. The European Central Bank, for instance, estimates that 23% of employees in Spain were on short-time work due to the COVID-19 pandemic.[25] In France, on the other hand, it was 47%. At the same time, Spain's -22.1% fall in GDP for the second quarter of 2020 was sharper

[21] Cf. Italian Finance Ministry.
[22] Cf. Heinemann F. (2020): "Next Generation EU" und das drohende Risiko einer verpassten Chance, p.8.
[23] Cf. Vandenbroucke, F. et al. (2020): The European Commission's SURE initiative and euro area unemployment re-insurance.
[24] Cf. Asatryan, Z. et al. (2015): Reforming the Public Administration, ZEW-Discussion Paper No. 15-049, p. 19.
[25] Cf. European Central Bank (2020): Short-time work schemes and their effects on wages and disposable income.

than France’s -19,0% drop.[26] The increase in expenditure for short-time work is also distorted by the fact that the design of short-time work schemes varies between Member States and that they have been expanded in different ways during the course of the pandemic, such as regarding the maximum eligibility period or level of income support.[27] A Member State that has been generous in scaling up its short-time work scheme during the COVID-19 crisis may report a larger increase in expenditure on short-time work than a Member State that has not scaled up its short-time work scheme.

An alternative option did however exist: claiming credit lines from the ESM. This would have had the aforementioned advantages without any of the indicated disadvantages and problems: The asymmetric shock and risk of insolvency would have been dealt with by measures at EU level; attaching a certain level of conditionality to the granting of loans would have created incentives for reform and the provision of funds would not have had to be bound up with the level of short-time work. This option was not taken for political reasons.

[26] Eurostat (2020): Press release 121/2020.

[27] For a summary see cepCorona Briefing No. 9/2020.

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