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Emergency Measures in Europe During the COVID-19 Crisis

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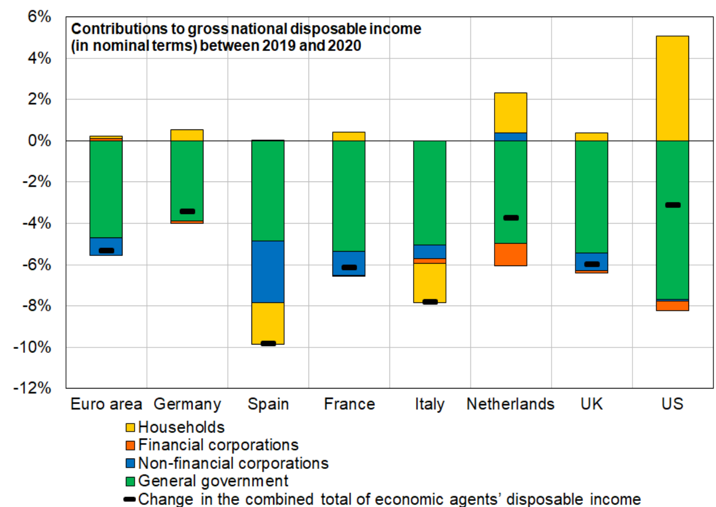
- Compared to previous crises, Europe's response to the COVID-19 crisis was unprecedented. In terms of the size of fiscal response, the emergency measures announced by France for 2020 and 2021 are close to the euro area average (5.7% of 2019 GDP, excluding deferrals of taxes and social security contributions and loan guarantees, vs 6.7%).
- Taking the euro area as a whole, governments absorbed 88% of the shock suffered by private agents. Country by country, however, there were differences depending on the size of the shock and the scope of the measures taken in response.
- Disposable household income was largely preserved by short-time working schemes, which on average accounted for a quarter of all emergency measure expenditure in the euro area. Italy, Spain and Austria saw a slight decline in disposable household income, whereas emergency measures gave rise to increases in France, Portugal, the Czech Republic and Belgium, despite significant economic shocks. While disposable household income also rose in Germany, Denmark, Sweden, Finland and the Netherlands, this was primarily because these countries were less severely impacted by the pandemic.
- Even though similar private-sector support measures were introduced across the continent, the final impact of the pandemic on firms has been more uneven across European countries. Firms reported lower 2020 revenue in Italy, Belgium, France and Spain, whereas firms in Germany, Denmark, the Czech Republic and Sweden were not as hard it, due to the lower severity of the shock experienced in these countries. Dutch firms even saw increased profits, thanks to transfers to businesses
- Now that the initial period of emergency is over, the recovery plans being implemented by European countries will supplement the fiscal response and help support the recovery.

Final distribution of the economic shock to gross national disposable income in 2020



Source: Eurostat, national accounts; DG Trésor calculations.
How to read this chart: Gross national disposable income is the sum of the disposable incomes of all economic agents (firms, households, government). An agent's disposable income is income resulting directly from its participation in the production process, net of current transfers with other agents (therefore taking government intervention measures, for example, into account). It is commonly used in relation to households, but the concept is also valid for other economic agents: for firms, their main source of income is their gross operating surplus; for government, gross disposable income includes tax and social security revenue, minus transfers to other agents. For France, the figures are adjusted for the effect of converting the Competitiveness and Employment Tax Credit (CICE) into a permanent reduction in employer social security contributions.

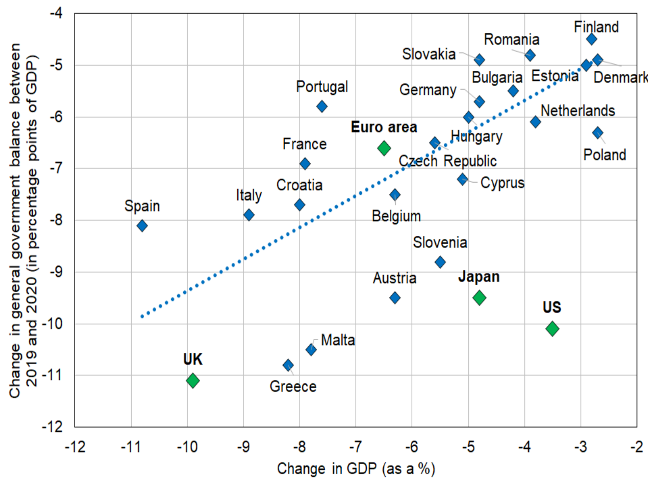
1. European countries responded to the crisis with massive fiscal support

1.1 Overall, the European fiscal response to the crisis was proportional to the economic shock

In 2020, the euro area's public deficit grew by 6.6 percentage points of GDP (from –0.6% of GDP in 2019 to –7.2% in 2020).

Overall, the extent to which each country's public deficit grew is proportional to the shock it experienced (see Chart 1). This increase stems from both the discretionary economic measures introduced by governments in response to the crisis and the effects of automatic stabilisers responding to the economic downturn, with country-by-country differences depending on the scope of their social safety nets.

Chart 1: 2020 variations in GDP and general government balance



Source: Eurostat; DG Trésor calculations.
Note: For France, the increase in the public deficit between 2019 and 2020 has been adjusted for the effect of converting the Competitiveness and Employment Tax Credit (CICE) into a permanent reduction in employer social security contributions.

Compared to the euro area, other major advanced economies saw their deficits grow more substantially in relation to the economic shock they suffered: the United States and Japan recorded larger public deficit increases (–10.1 and –9.5 percentage points of GDP, respectively), even though the economic shocks they experienced were less severe. The United States in particular had to introduce a vast programme of emergency measures to reach segments of the population typically not covered (or insufficiently covered) by social safety nets. While the UK also saw a sharp increase in its public deficit (–11.1 percentage points of GDP), it was in relation to a more substantial economic shock.

1.2 The shock to economic activity and income was largely absorbed by public finances

Thanks to government responses, a significant portion of the income lost by households and firms in 2020 was absorbed (less significant losses of disposable income, see chart on cover page). For the euro area as a whole, governments absorbed 88% of the income shock in 2020. Firms saw only a moderate decline in their disposable income, and household disposable income was protected.

The breakdown of the shock between economic agents is uneven across the EU, due to differences in the economic shocks suffered by individual countries and their respective fiscal responses, whether in terms of scope or the nature of their policy measures.

- In Spain and Italy, the emergency fiscal response only managed to partially offset the effects of the economic shock on the income of firms and households: the Spanish government only absorbed 49% of lost income, and Italy's 65%. Firms consequently shouldered 30% of the shock in Spain and 7% in Italy, with households shouldering 21% in Spain and 24% in Italy.
- In France and the UK, the final shock was almost fully borne by the government and households saw an increase in disposable income, with the support measures that were introduced having overcompensated for the primary income shock. As for firms, they saw a slight decline in disposable income in both countries.
- In the Netherlands, and Germany to a lesser extent, the government response overcompensated for the shock of the crisis (133% in the Netherlands and 113% in Germany) and disposable income increased for both non-financial corporations and households.
- In the US, extensive government support measures for households gave rise to a 246% overcompensation and a significant increase in household income.

Box 1: Evaluating the impact of the economic shock on economic agents' disposable income

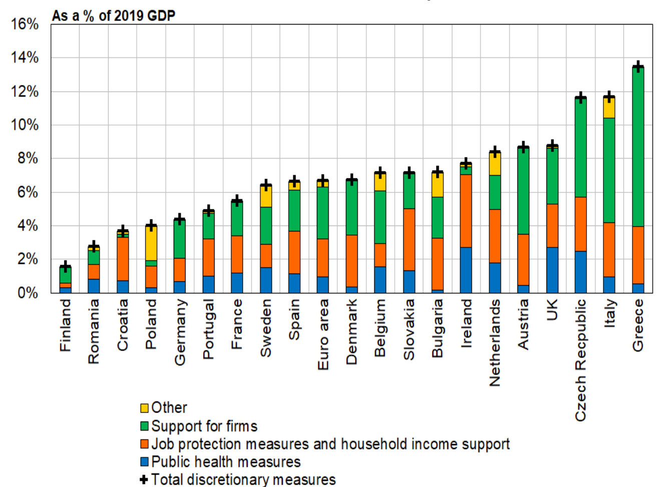
The analysis put forward in this paper draws a connection between the decline in GDP between 2019 and 2020 and the variation in gross disposable income of different categories of economic agents (firms, households including sole traders, and general government). By focusing on income, we are able to study the effect of the economic shock on agents and the distribution of the effects of the shock, taking into account the effects of automatic stabilisers and agents' reactions, particularly firms as regards labour and use of value-added. In terms of public policy, it reveals to what extent the transfers that were made protected the income of private agents and their ability to invest and consume.

There are two main types of transfers at play, between the initial economic shock and the loss of income suffered by the different categories of agents: private transfers (between firms and households) and public transfers (involving governments). Private transfers include wages and property income payments (e.g. dividends). Public transfers include taxes and social security contributions, benefit payments, and emergency support measures introduced by the government. Furthermore, from a national accounting perspective, short-time working schemes resulted in a transfer from the government to households (benefit payments) in lieu of wages normally paid by firms.

2. Between European countries, emergency measures varied more in terms of scope than substance

To better understand the differences in how governments absorbed the losses of firms and households, we analysed the discretionary emergency measures adopted across Europe in more detail. There are three categories of measures: (i) fiscal measures with a direct impact on the general government balance; (ii) deferrals of taxes and social security contributions and similar measures; and (iii) loan guarantees and similar measures. According to our estimates,[1] the amounts represented by the discretionary emergency measures that were announced (although not necessarily spent) with a direct impact on the general government balance account for 6.7% of euro area GDP for the period from March 2020 to June 2021 (on a country-by-country basis, the median of the available estimates stands at 7.2% of GDP). However, the number and diversity of support measures has made it difficult to compile a definitive list. Furthermore, there are many countries that have not provided a detailed overview of all their measures and the corresponding expenditure.[2]

Chart 2: Total emergency measures (announced figures for 2020 and 2021)



Source: DG Trésor estimates.
Note: At 1 July 2021. Amounts correspond to what has so far been announced (but not necessarily spent) for 2020 and 2021.

(1) Direction générale du Trésor (2021), "Étude comparative internationale sur les mesures d'urgence mises en place face à la crise en Europe", April 21, available on www.tresor.economie.gouv.fr.
(2) In many cases, the results of analyses by international institutions therefore differ significantly.

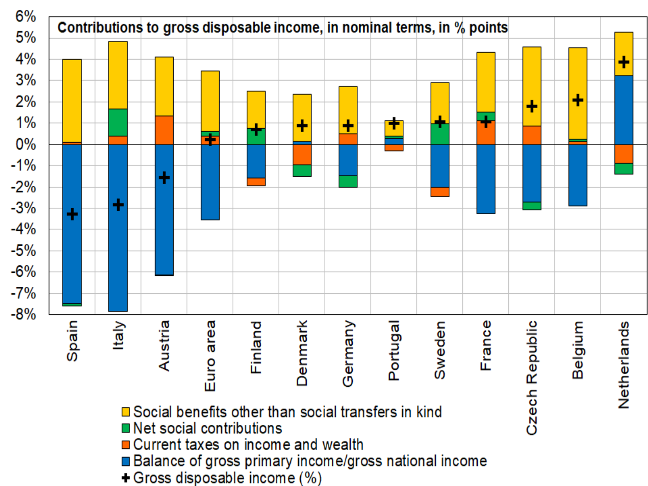
There are significant differences between countries, with the scope of the direct measures that were announced varying between 1.6% and 13.5% of GDP. France falls somewhere in the middle, at 5.7% of GDP. Also, in some countries, the amounts that were announced are significantly higher than what was actually spent, whether due to the economic shock being less severe than expected or low uptake of support measures (e.g. for being overly complex or insufficiently attractive). In particular, the amount of direct aid paid out to firms was lower than what was announced in Germany, Sweden and Denmark. In contrast, these amounts were particularly high in France and Spain.

2.1 Measures for households and their impact on disposable income

Short-time working schemes, which account for more than 25% of emergency measure expenditure in the euro area, were vital in stabilising household income during the pandemic and safeguarding jobs. Such schemes were widely used in Austria, the Netherlands, the UK, Denmark, Spain, Italy and France, with the specifics varying country by country. Some offered more generous wage replacement benefits, such as France (where it was 84% of net hourly wages), the UK, Austria and the Netherlands, compared to others such as Germany (67% of net wages), Belgium, Denmark, Spain, Portugal and Sweden.

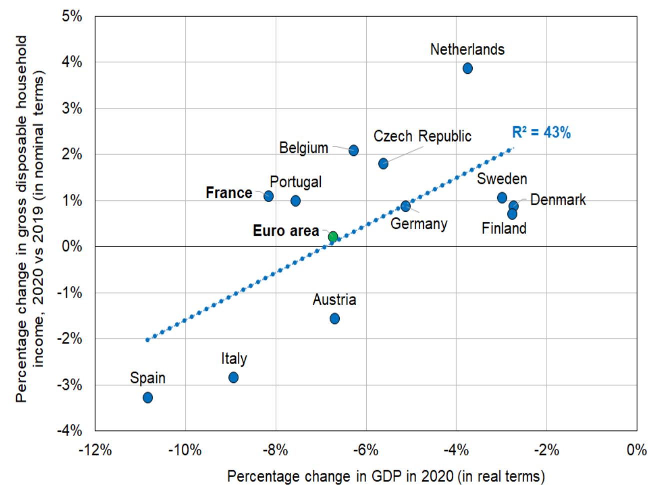
Short-time working schemes were rounded out by household income support measures, with a particular increase in direct transfers[3] and, in some countries, cuts to taxes or social contributions (Czech Republic, Greece and some parts of Italy). With some exceptions, there were not many direct incentives to encourage consumer spending, as the effectiveness of any measures designed to support private demand would have been hampered by public health restrictions.[4]

Chart 3: Impact on disposable household income (nominal terms) in 2020



Source: Eurostat, national accounts; DG Trésor calculations.
How to read this chart: This chart shows the variation (in nominal terms) in disposable household income between 2019 and 2020, and the contributions of individual sub-components of disposable income from a national accounting perspective. It therefore provides an "accounting" breakdown of the variation in disposable income.

Chart 4: Change in GDP (real) and disposable household income (nominal) in 2020



Source: Eurostat, national accounts; DG Trésor calculations.

(3) Some countries increased family allowances (a per-child benefit in Germany and Austria, for example). Other countries, such as France, Spain and Italy, introduced measures in the form of transfers targeted to low-income households.
(4) Notable exceptions included countries that introduced incentives to encourage spending in specific sectors, such as a holiday voucher scheme in Italy or a program to subsidise restaurant meals in the UK.

The pandemic caused a sharp drop in household primary income,[5] which was sharper the more severe the country's economic shock. On the whole, support measures worked to preserve disposable household income in 2020. Three groups of countries emerge from our analysis (see Charts 3 and 4):

- One group where disposable household income declined in 2020, by between 2% and 3%, despite government support measures (Italy, Spain, Austria).
- Another group where disposable household income grew slightly in 2020, and where transfers and social benefits more than offset the drop in primary income:
  - In France, Portugal, the Czech Republic and Belgium, despite a significant economic shock, household income increased (by 1.1% in France) as a result of the support measures that were introduced.
  - Germany, Denmark, Sweden and Finland, disposable household income also grew, but mainly because their economies were less affected by the crisis.
- The Netherlands, which saw a strong increase (4%) in disposable household income for the year.[6] The social benefits introduced in the Netherlands appear to have overcompensated for the impact of the crisis, in addition to which wages rose substantially in 2020.

Overall, short-time working schemes worked to protect jobs in European countries. Euro area employment fell by 1.6% in 2020, against a 6.6% drop in GDP, and the variation in employment rates across Europe was much less uneven than the variation in economic activity. Since short-time working schemes meant that people remained employed even if they were not actively at work or working full hours, employment rates as measured by the number of people holding jobs declined much less than the total number of hours worked in European economies.

2.2 Measures for firms and how they affected gross operating surpluses

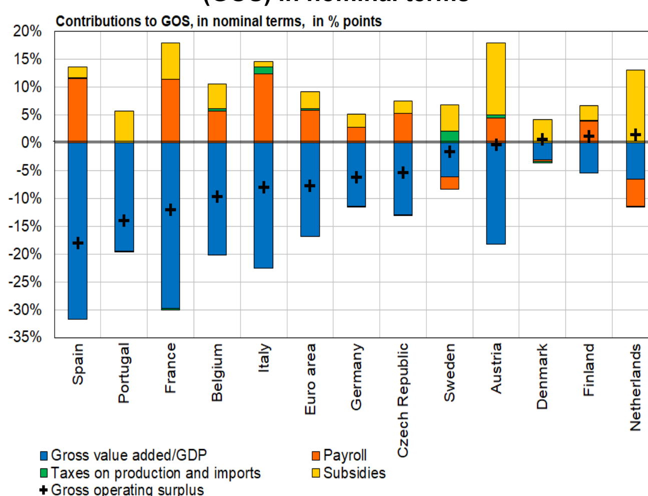
Measures designed to protect firms were relatively consistent across European countries in terms of the types of instruments used:

(i) Most countries introduced direct subsidies for firms, generally targeted to SMEs, VSEs and self-employed workers. Generally speaking, these were not sector-specific measures but were based on the shock experienced by the firm, to ensure funds went where they were needed and to limit windfall effects.

(ii) Sector-specific measures were introduced in some cases to support the hardest hit industries (e.g. tourism, transportation), for instance in Poland, Italy, the UK and Denmark.

(iii) Taxes and social security contributions were waived or lowered in some countries, such as the Czech Republic, Spain, Italy and France.

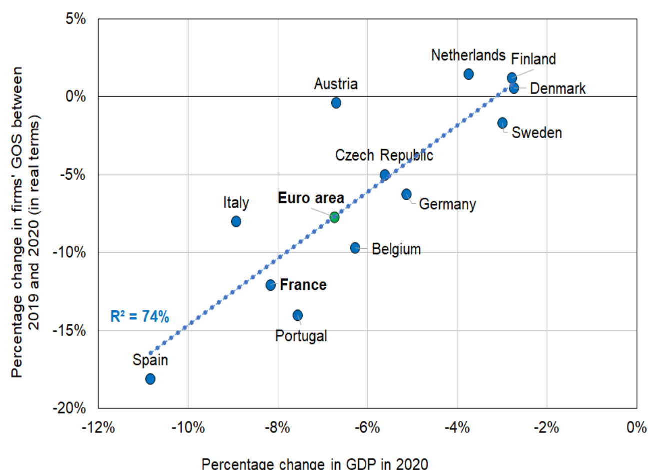
Chart 5: Impact on firms' 2020 gross operating surplus (GOS) in nominal terms



Source: Eurostat, quarterly national accounts; DG Trésor calculations.
How to read this chart: The chart shows the change in gross operating surplus (GOS) for non-financial corporations in nominal terms between 2019 and 2020, and the contributions of individual GOS sub-components from a national accounting perspective. It therefore provides an "accounting" breakdown of the variation in firms' GOS.

(5) Primary income includes income resulting directly from participation in the production process. The majority of household primary income is made up of wages and property income.
(6) The differences noted between countries are partly attributable to statistical decisions. In France's national accounts and as defined by Eurostat, short-time working is considered a cash benefit (D.623) paid to households by the government. As a result, the short-time working scheme resulted in, on the one hand, a decrease in payroll in firms' accounts, thereby supporting their bottom line, and on the other hand, a social benefit in households' accounts, partially offsetting the decline in their earned income and supporting their purchasing power. In the Netherlands, the short-time working scheme took the form of a direct government subsidy to firms and therefore did not result in a decrease in their payroll. And since households continued receiving the same wages, even for those who were on short-time working, from a national accounting perspective, there was no decline in primary income in households' accounts in 2020. A similar statistical treatment appears to have been used in Portugal and Sweden.

Chart 6: Change in GDP (real) and GOS (nominal) in 2020



Source: Eurostat, quarterly national accounts; DG Trésor calculations.

Overall, the support measures that were introduced worked to limit the decline in firms' gross operating surpluses in 2020 (see Charts 5 and 6). Four groups of countries emerge from our analysis:

- Despite government support, there were sharp declines in firms' gross operating surpluses in Italy (–8%), Belgium (–10%), France (–12%), Portugal (–14%) and Spain (–18%). These countries were more heavily impacted relative to other European countries, which largely explains the sharp decline in GOS (see Chart 6).
- Germany, the Czech Republic and Sweden experienced less significant declines in GOS, largely because their economies were not as severely affected by the crisis.
- In Austria, despite an initially strong economic shock, similar to what was experienced by the most heavily hit countries (see above), extensive government support, in the form of large subsidies, worked to preserve firms' GOS in 2020.
- The Netherlands, Finland and Denmark experienced a smaller initial shock on primary income, which, combined with support measures for firms, resulted in a slight increase in gross operating surplus (+1% in 2020).

2.3 Cash support measures and guarantees also helped firms weather cash-flow challenges during the crisis

Deferrals of taxes and social security contributions and loan guarantees were not included in the preceding estimates, but should be taken into account in the overall analysis of the crisis response, since they did help firms cope with cash-flow challenges, even if they did not directly impact disposable income. In particular:

- From March, many countries deferred tax payments for heavily hit firms and accelerated tax credit refunds. These measures represented particularly substantial amounts in Denmark and Sweden and, to a lesser degree, France (representing 3.1% of GDP in 2020) and Germany. Since taxes and social security contributions were only deferred and are due to be paid eventually (the situation for all but a small fraction of firms), these measures will not have any real impact on firms' income or the public deficit from a national accounting perspective. That said, it is helpful to take these measures into account to understand the reality of the cash-flow shock firms experienced during the crisis.
- Government guarantee programs were also introduced for new loans to help ensure firms had access to credit. The amounts announced by some countries to help firms cover their needs were particularly high (13.5% of GDP in France, 22.9% in Germany, 13.3% in Spain and 19.5% in Italy). In many cases, the actual amounts ultimately used fell below what was offered by the government: as of mid-2021, uptake of government loan guarantees only represented half of what was on offer in France and Italy, and one-tenth in Germany.

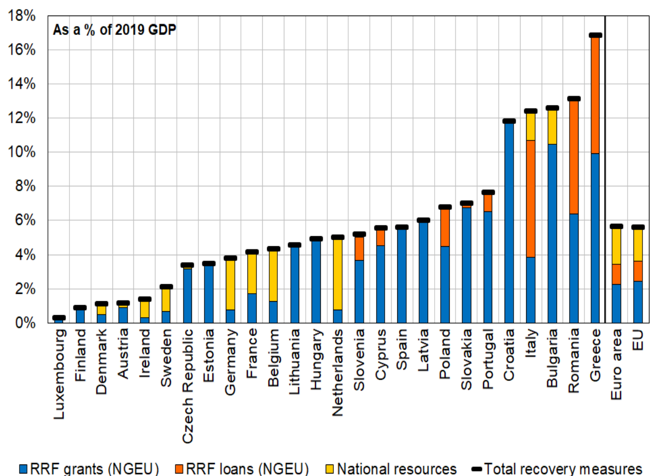
3. Recovery plans will round out emergency measures and help drive the recovery

As Europe moves beyond the emergency period of the crisis, the recovery plans being rolled out by Member States will supplement the fiscal response and support the economic recovery. In particular, the deployment of the Next Generation EU (NGEU) program will provide recovery support. The Recovery and Resilience Facility (RRF), the centrepiece of the NGEU program, includes €728bn (5.2% of the EU's GDP) in the form of loans and grants to support the reforms and investments made by EU countries. Each country put together a National Recovery and Resilience Plan (NRRP) detailing how it plans to use the funds, with some

countries opting to chip in national funds to round out their recovery efforts. To date, recovery plans (including both EU funding under NRRPs and direct expenditure by Member States) represent 5.6% of EU and euro area GDP (see Chart 7). However, comparison of the plans is complicated by the different time horizons over which countries plan to use the funds. Germany, for instance, plans to frontload the majority of its recovery plan funding in 2020-2021, whereas Spain and Italy plan to spread out their investments through to 2026.

The fact that the national recovery plans have been embedded in the European Semester – and that an eligibility criterion for RRF funding is that plans address the Semester's recommendations – could stimulate growth potential via reforms that do not necessarily require funding.

Chart 7: Recovery plans across Europe, by funding type



Source: Individual governments; DG Trésor economic teams.
How to read this chart: Amounts excluding REACT-EU and MFF funds. The Netherlands and Bulgaria are yet to officially submit their NRRPs to solicit funding under the RRF, which means RRF amounts may change for these countries. Some countries may also solicit loans under the RRF at a later date (e.g. Spain, Portugal).

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