

STUDY

Requested by the ECON committee



The added value of the Recovery and Resilience Facility

Based on an assessment of the
Recovery and Resilience Plans:
France, Italy, Portugal and Spain



External authors:

Carlos MARTINEZ MONGAY

María Dolores GADEA RIVAS

Beatriz BARRADO

Vanesa AZÓN



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Abstract

This paper assesses the value added of the theRRPs of France, Italy, Spain and Portugal in light of the vulnerabilities limiting their long-term growth, and of some main implementation risks, such as the need to avoid financing recurrent expenditures, the degree of additionality of the RRP, the preference for grants, the lack of EU value added, or insufficient administrative capacity. The paper calls for a political debate on such issues and, in particular, on the role of additionality.

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AUTHORS

Carlos MARTINEZ MONGAY, ECOMOD
María Dolores GADEA RIVAS, University of Zaragoza (Spain)
Beatriz BARRADO, University of León (Spain)
Vanessa AZÓN, University of Zaragoza (Spain)

ADMINISTRATOR RESPONSIBLE

Cristina DIAS
Samuel DE LEMOS PEIXOTO
Kristina GRIGAITĖ

EDITORIAL ASSISTANT

Donella BOLDI

LINGUISTIC VERSIONS

Original: EN

ABOUT THE EDITOR

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To contact Economic Governance Support Unit or to subscribe to its newsletter please write to:
Economic Governance Support Unit
European Parliament
B-1047 Brussels
E-mail: egov@ep.europa.eu

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CONTENTS

LIST OF ABBREVIATIONS	7
LIST OF FIGURES	8
LIST OF TABLES	8
EXECUTIVE SUMMARY	9
1. INTRODUCTION	13
2. SYMMETRIES AND ASYMMETRIES OF THE COVID-19 SHOCK ACROSS FRANCE, ITALY, PORTUGAL AND SPAIN	14
2.1. A global non-economic shock	14
2.2. Asymmetric shocks and recoveries	15
3. MAIN ECONOMIC CHALLENGES OF THE FOUR COUNTRIES. HAS COVID CHANGED ANYTHING?	16
3.1. Labour Market	16
3.2. Budgetary position	17
3.3. Productivity and growth factors	18
4. SOME HORIZONTAL ISSUES: IMPLEMENTATION RISKS, ADDITIONALITY, CONDITIONALITY AND EU PUBLIC GOODS	20
4.1. Horizontal principles in Article 5	20
4.1.1. Not to finance recurrent expenditures	20
4.1.2. Additionality in the narrow sense	21
4.1.3. The 'do no significant harm' principle	21
4.2. The impact of the RRF	22
4.2.1. The results of some simulation exercises on the economic impact of the NGEU	22
4.2.2. The projections in the RRP's and in their Commission assessments	23
4.3. Additionality, a major implementation risk	23
4.4. Other implementation risks	25
4.5. Conditionality	26
4.6. The EU value added	26
5. A COMPARATIVE ANALYSIS OF THE FOUR RRP	27
5.1. Green transition	27
5.2. Digital transition	28
5.3. Country-specific challenges	29
5.3.1. Labour market	29
5.3.2. Public finance	29
5.3.3. Growth factors	30

5.4. Summary assessment	31
6. CONCLUSIONS	32
7. REFERENCES	34
ANNEX 1: TABLES	35
ANNEX 2: FIGURES	37
ANNEX 3: COUNTRY FACTSHEETS.	45
ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: FRANCE	45
ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: ITALY	57
ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: SPAIN	75
ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: PORTUGAL	100

LIST OF ABBREVIATIONS

CFC	Central Fiscal Capacity
CSR	Country Specific Recommendations
DESI	Digital Economy and Society Index
DNSH	Do No Significant Harm (DNSH)
ECB	European Central Bank
EDP	Excessive Deficit Procedure
EIB	European Investment Bank
EIP	Excessive Imbalance Procedure
EMU	European Monetary Union
ESM	European Stability Mechanism
EU	European Union
EUR	Euro
GDP	Gross Domestic Product
MFF	Multiannual Financial Framework
MIP	Macroeconomic Imbalances Procedure
MS	Member States
MTO	Medium Term Objective
NGEU	Next Generation European Union
NRP	National Reform Programmes
PA	Public Administration
PCS	(European Stability Mechanism) Pandemic crisis support instrument
PEPP	Pandemic Emergency Purchase Programme
QUEST	Commission (ECFIN) Macroeconomic model
RRF	Recovery and Resilience Facility
RRP	Recovery and Resilience Plan
SGP	Stability and Growth Pact
SME	Small and medium enterprises
SURE	Support to mitigate Unemployment Risks in an Emergency

LIST OF FIGURES

Figure 2.1: The global economic impact of COVID-19 (Quarter-on-quarter real GDP growth)	37
Figure 2.2: recovery FROM the COVID-19 PANDEMIC (quarter-on-quarter real GDP growth)	37
Figure 3.1: Unemployment rate evolution	38
Figure 3.2: Budgetary position	38
Figure 3.3: Evolution of GDP growth	39
Figure 3.4: Decomposition of productivity	40
Figure 4.1 Comparing the Commission forecasts for GDP (2019=100), public investment (% of GDP) and structural deficit (% of potential growth)	40
Figure 5.1: Distribution of the RRFs funds by source of funding (% total)	42
Figure 5.2: Percentage devoted in RRFs to green and digital transitions	42
Figure 5.3: Total greenhouse gas emissions per GDP in 2019	43
Figure 5.4: Digital Economy and Society Index composite index	43
Figure 5.5: Coverage of the six pillars of the Facility by the RRF components.	44

LIST OF TABLES

Table 2.1: Overview of the COVID-19 impact	35
Table 3.1: Vulnerabilities before COVID-19	35
Table 4.1: The RRF and public investment (% of GDP)	35
Table 4.2: Estimated impacts of the RRFs according to national authorities	36
Table 4.3: Economic Impact of the RRFs (%)	36

EXECUTIVE SUMMARY

The COVID-19 pandemic unleashed an unprecedented economic crisis. The NGEU and its main component, the RRF, were part of the EU response to the shock. This briefing assesses some of the main aspects of the RRFs of France, Italy, Spain and Portugal, also in the light of the vulnerabilities limiting long-term growth in the four countries. The four Member States share similar weaknesses, in particular concerning the functioning of labour markets, low potential growth and risks to the sustainability of public finances. These vulnerabilities represent long-standing structural problems that the pandemic has only magnified.

The NGEU funds represent an opportunity to boost pending reforms to make economies less vulnerable and more resilient, and to accelerate the implementation of policies such as the green and digital transitions, which were already high on the European agenda. Within this context, this briefing has assessed the extent to which the measures put forward in their respective RRFs address the structural challenges faced by the four countries.

The four RRFs have been structured in different ways, which in some cases has made it difficult to establish a direct link between the priorities in the programmes with the six pillars. Nevertheless, the four RRFs comply with the minimum investment requirements concerning the green and digital transition objectives and the investment plans aim to cover specific gaps in both areas.

Many of the measures reinforcing economic and social resilience combine investments and reforms appropriately, although the reforms should be more ambitious overall to reduce the vulnerabilities. NGEU funds provide an opportunity to reduce the social and political costs of the reforms.

All in all, there is both light and shade in the assessment of the RRFs. The light comes firstly from the speed and effectiveness with which the four countries are implementing their programs. Secondly, the volume and composition of investments financed by the funds will undoubtedly have a knock-on and modernising effect on the economies. But we also detect shadows, especially in the area of reforms and whether their ambition will be sufficient to effectively solve entrenched problems, especially those related to the labour market and public finances.

In the case of France, concerns might emerge in the labour market and education, in particular where the most vulnerable groups are concerned. Moreover, the temporary open-ended dualism of the labour market remains unresolved. On the other hand, the impact on sustainability of the RRF will depend on the effectiveness of the proposed expenditure rule and spending reviews, as well as on the containment of pension expenditures, which weigh on sustainability.

In Italy, measures to reduce youth unemployment lack detail. The same can be said about actions to reduce the high regional disparities, a major challenge for the Italian economy. Doubts also arise about the absence of relevant projects in different areas of the green transition. Finally, a medium-term plan to enhance debt sustainability is lacking.

Some vulnerabilities are only partially addressed in Spain. The reform of the labour market, although consensual and on the right track, does not fully address temporariness. Where fiscal sustainability is concerned, there are no concrete measures to effectively correct the high and long-lasting structural gap between revenues and expenditures. The main stumbling blocks are the limited scope of the proposed tax reform and the partial nature of the measures to ensure the future sustainability of the pension system.

In the case of Portugal, the timing for the approval of measures aiming to tackle labour market segmentation is still unclear. The RRF does not sufficiently address the issue of maritime and rail connections, including cross-border coordination to improve communications and reduce transport

costs with the Single Market. In addition, doubts arise about public debt sustainability, especially in a context where inflationary pressures can lead to the reassessment of risk premia.

Enhancing growth potential of the EU economies is a main goal of the RRF. Consequently, the briefing has discussed channels through which the measures in the RRP would maximize their economic impact. At this stage, assessing the impact of the NGEU on activity can only be carried out on the basis of simulation models. Simulation results depend on the set of assumptions framing the model, which allows identifying implementation risks.

Simulations show that GDP impacts depend on the size of the corresponding RRP, which implies that renouncing the loans available reduces its positive impact. This is the case of France and Spain that have not applied for loans and, to a lesser extent, of Portugal, which is only using 20% of the maximum amount of loans. While the economic impact is reduced, it is not surprising that high-debt countries tend to show a preference for grants. Indeed, no Member State is obliged to exhaust the available funds.

The impact of the RRP is greater the faster the money is spent. Administrative capacity is key to ensure that the instalments reach the real economy as quickly as possible, but it is too early to assess possible administrative delays. The administrative machinery may take some time to work at full speed, especially in Italy, Spain and Portugal, given the size of the RRP relative to their respective GDP. While there is no evidence of entrenched, unresolved bottlenecks in any of them, there is a strong case for implementing measures reinforcing the efficiency of public administration.

Significant positive spillovers have been identified thanks to the simultaneous implementation of the RRP in a context of strong trade links within the Single Market. This has some implications. In the first place, it should be a priority of the RRF to preserve and improve the functioning of the Single Market. No RRP seems to include measures undermining the proper functioning of the Single Market in a context of flexible State Aid rules, but ex-post scrutiny should not be weakened. In the second place, *mutatis mutandis*, spillovers from the simultaneous implementation of the RRP would be enhanced by the implementation of cross-border projects. Such projects in the four RRP appear to be well-focused on key enabling technologies such as the production of green hydrogen, the production of electric-car batteries or the development of digital technologies. Yet, the relative weight of genuine cross-border projects in the four programs assessed in this briefing is relatively small, which could be explained by the difficulties of developing this type of project within tight time-scales.

The composition of the RRP also matters. The multipliers of the RRP are much larger for investment projects than for current expenditures. The RRF Regulation rules out the possibility of financing current expenditures and no significant measures involving recurrent expenditures have been included in any of the four RRP. Nevertheless, it should be borne in mind that while the bulk of the RRP funding is devoted to genuine investment projects, the fungibility of the budget might lead to an indirect increase in recurrent expenditures. This would put pressure on public finances once the RRF funding is over. While, according to the Commission's autumn 2021 forecast, the expected instalments over 2021-2023 are matched overall by the projected increase in public investment in France and, to a lesser extent, in Portugal, the amounts to be received by Italy and Spain are more than two and a half times the projected increase in public investment.

The analyses carried out in this report suggest that, especially in Italy and Spain, part of the planned investment would have been substituted by RRF-compliant projects and/or by redesigning old projects to make them compliant with the RRF Regulation. This would not be surprising given the size of the corresponding RRP, especially the Italian one. The growth effects would be ambiguous in either case. On the one hand, new or redesigned projects would have a higher impact on potential growth than

the abandoned ones but, on the other hand, the fiscal impulse would be much lower than in the case of the RRP leading to an equivalent increase in public investment compared, for instance, with the levels observed before the pandemic.

In the framework of the RRF Regulation, additionality is not understood in the broad sense of financing projects that would not have taken place in a non-NGEU context, but in a narrower sense as the obligation to avoid the RRP financing the same projects as other EU funds. This does not seem a major issue in the case of France, Italy and Spain as the funding to be received from other EU funds is dwarfed by the RRP. In the case of Portugal, however, other EU funds are almost as important as the RRP. However, it is still too early to identify possible overlaps.

Concerning additionality, as occurs with loans, high-debt countries can be confronted with a difficult dilemma. While the higher the degree of additionality, the higher the potential growth effect, a lower degree of additionality implies lower debt levels, as certain projects would be financed by NGEU transfers. High-debt countries, as is the case of the four Member States discussed in this report, are confronted with a trade-off between higher potential growth in the long term against lower debt in the short term, which in turn would require a lower fiscal adjustment and a lower negative impact on activity over the medium term.

While there is no evidence of lack of compliance with the RRF Regulation by any of the RRP, this report provides some ideas on possible reforms of the economic governance of the EMU, especially if the NGEU or some form of it would be maintained in the future on a permanent basis which, given recent events, should not be ruled out. The report does not propose possible amendments to the current Regulation, which would not appear realistic given the large amounts already approved. However, the Parliament could extract some lessons for the future, in particular on additionality and debt sustainability.

Although the principle that different EU funds do not finance the same projects should be maintained, the European Parliament could lead a reflection concerning the meaning of additionality within the context of EU fiscal funds.

Full additionality is, no doubt, the best way to underpin both short- and long-term growth but, in the current circumstances, and especially in high-debt countries, full additionality might not be the best strategy in the medium term. In a context of high inflation and tighter financial markets, debt reduction becomes a priority. Nevertheless, past policy mistakes should be avoided and high public investment levels maintained. Debt reduction should not put the recovery in danger.

The economic context in which the NGEU is being implemented is moving from the need to fight against the pandemic in a low inflation and interest rate environment, to a situation of dramatic and exceptional geopolitical tensions, high inflation and tighter financial markets. This new context may justify considering the role of a permanent NGEU, while preserving its fundamental goals, in particular supporting the green and digital transitions.

In this low-additionality scenario it would be paramount that NGEU-compliant projects substitute pre-RRP planned investments, so that EU funds support the transformation of the economy facilitating the green and digital transitions. The financing of projects not fully compliant with the goals of the RRF should be avoided. Similarly, the possibility that, due to the fungibility of the budget, EU funds release domestic money to increase recurrent expenditures should also be avoided. On the contrary, the RRF investments should support fiscal adjustments in order to reduce structural gaps between expenditures and revenues, fully in line with the conditionality principle enshrined in the Regulation.

A lower additionality of the RRP should be accompanied by credible and feasible adjustment plans improving the sustainability of public finances without derailing the recovery. Where necessary, such plans should be accompanied by a package of structural reforms tackling vulnerabilities in labour markets and enhancing long-term productivity growth.

Investment plans funded by the EU should promote the implementation of cross-border projects enhancing their EU value added and their spillovers within the Single Market, which in turn requires avoiding possible distortions of competition by reinforcing State Aid control.

1. INTRODUCTION

The COVID-19 pandemic unleashed an unprecedented economic crisis. Exceptional measures to fight the infection and mitigate the economic impact of COVID-19 caused public deficits and debt levels to soar. Unlike in the past, the EU's reaction to the COVID-19 crisis has been swift and effective.

This time, the fiscal rules have not been an obstacle to supporting the economy. The escape clause of the SGP was activated, which allows automatic stabilisers to operate fully, complemented by sizeable discretionary measures at national level.¹ In parallel, the ECB extended the purchase of bonds through the so-called Pandemic Emergency Purchase Programme (PEPP), amounting to EUR 1.35 tn. While debt levels are at historic levels, interest payments are low and, in some cases, lower than in 2019. The Council adopted a package of measures, including the guarantees of the European unemployment insurance - the so-called instrument for temporary Support to mitigate Unemployment Risks in an Emergency (SURE – amounting EUR 100 billion). The ESM adopted precautionary credit lines -the so-called Pandemic Crisis Support (PCS, amounting to EUR 240 billion)- and the EIB's credit lines to SMEs (EUR 200 billion). The EU budget also contributed with some EUR 70 billion.

This package did not include a mutualised debt fund and, therefore, did not solve the debt problem that some countries were confronting. Given the magnitude of the threat, the Council adopted the "Next Generation EU" (NGEU) on 21 July, 2020. The NGEU is an ambitious recovery programme, totalling EUR 750 bn, which, following the lessons learned from the global financial crisis, breaks the premise of austerity and promotes the active role of the EU budget in the recovery. The NGEU should be financed by borrowing in financial markets until 2026 at the latest, and should be repaid by 2058 at the latest.

The lion's share of the NGEU went to the Recovery and Resilience Facility (RRF, amounting to EUR 672.5 billion, of which EUR 360 billion in loans and EUR 312.5 billion in grants).² 70% of the EUR 312.5 billion will be distributed according to population (size), the inverse of the per capita GDP (GDPpc) and the relative unemployment, and the remaining 30% on the basis of population, (inverse) GDPpc and, in equal proportion, the change in real GDP in 2020 and the change over the period 2020-2021.³ The maximum amounts of loans per MS should not exceed 6.8% of their 2019 GNI in current prices.

To be eligible to receive grants and loans up to such amounts, MS have to submit Recovery and Resilience Plans (RRPs).⁴ The RRP include investment projects to be financed by the RRF and accompanying structural reforms, as well as possible measures to incentivise private investment.⁵

This briefing presents an assessment of the RRP of France, Italy, Spain and Portugal with a view to identifying their EU value added. It should be noted at the outset that the goal of this exercise is not to replicate the work jointly done by the EU institutions and the Member States, but to focus on some dimensions of the EU value added, using as much as possible information in the RRP and in other public sources, including the Commission assessments. In particular, the briefing tries to shed some light on: (1) The extent to which the measures in the RRP are aligned with the EU policy agendas and do not replace programmed national spending; (2) the extent to which RRP develop or implement

¹ Moreover, the Commission flexibilised State Aid frameworks to allow MS to support companies through guarantees and capital when needed.

² The rest of the money went to ReactEU (EUR 47.5 bn), Horizon Europe (EUR 5 bn), InvestEU (EUR 5.6 bn), Rural Development (EUR 7.5 bn), Just Transition Fund (JTF, EUR -10 bn) and RescEU (1.9bn). Council Regulation (EU) 2020/2094 of 14 December 2020 established a European Union Recovery Instrument to support the recovery in the aftermath of the COVID-19 crisis.

³ See annexes I, II and III of Regulation (EU) 2021/241 of 12 February 2021.

⁴ See articles 17 to 21 of Regulation (EU) 2021/241. To be eligible to receive loans, the MS need to justify higher financial needs associated to additional reforms and investment beyond the maximum financial contributions (grants).

⁵ Measures adopted by the MS after 1 February 2020 were eligible as long as they complied with the requirements of the Regulation.

cross-country projects, thus contributing to the deepening of the Single Market; and, (3) the extent to which RRFs create EU positive spillovers, as well as on some other issues that are closely linked to them.

Many of the issues underlying these broad questions can only be assessed on the basis of ex-post information, which will become available in an imprecise future. In the meantime, the available information can only provide more or less indicative and provisional answers to these main questions.

In addition, since one main goal of the RRF is to support recovery and enhance potential growth of the EU economies, this report analyses the RRFs presented by France, Italy, Spain and Portugal, with a view to assessing the extent to which they adequately address the economic challenges faced by the four countries which, in fact, share many commonalities.

The relevance of this group of countries becomes evident when considering their share in the total grants and loans of the RRF. Total maximum grants available for France (EUR 39.4 bn), Italy (EUR 68.9 bn), Spain (EUR 69.5 bn) and Portugal (EUR 13.9 bn) are totalling 191,7 bn, or 57% of the total maximum grants. The share of the four countries in the second 30% tranche of the grants represents 61% of the total, as should correspond to countries having recorded the largest GDP contraction in 2020.

As revealed in this report, the NGEU is not free from risks. In the post-pandemic scenario, the success of the NGEU will likely condition the modernisation of European economies and their capacity to reinforce potential growth, as well as further progress in the EU integration process.

The outline of the report is as follows. Section 2 analyses the impact of Covid-19 on the economies of the four MS. Section 3 identifies their main vulnerabilities. The horizontal principles of the RRF are the subject of section 4. Section 5 carries out a comparative assessment of compliance of the four RRFs with the six pillars. Section 6 concludes proposing main policy recommendations.

2. SYMMETRIES AND ASYMMETRIES OF THE COVID-19 SHOCK ACROSS FRANCE, ITALY, PORTUGAL AND SPAIN

2.1. A global non-economic shock

At the end of 2019, the world economy was still in the expansionary phase that began after the global financial crisis. Although the rhythm was different, there were uncertainties and some signs of a slowdown in the European economies, but nothing foreshadowed the magnitude of the crisis that was unleashed as a result of the COVID-19 pandemic. In early 2020, the world economy experienced one of the deepest—yet shortest—recessions on record, characterised by its global reach, affecting virtually all countries simultaneously. The worldwide adoption of measures to contain the spread of the COVID-19 virus resulted in a sudden stop in economic activity. These measures were generally implemented during the first and the second quarters of 2020.

Lockdown of the population and restrictions on trade in international markets produced one of the deepest dips in real GDP on record. Developed economies recorded a quarter-on-quarter decline of -1.7% in the first quarter of 2020, the economy further contracted by -10.5% in the second quarter. The impact was even more pronounced in Europe, with figures standing at -3.1% and -11.3% of GDP for the EU. From a global perspective, contraction in 2020 was -3.1% for the world economy, -4.5% for advanced economies and -2.1% for emerging and developing markets. Only some emerging countries, such as China with 2.3%, recorded positive growth (see Figure 2.1 in annexe 2). For the four countries under analysis, the drop was particularly sharp with figures standing at -13.5%, -12.9%, -17.7% and -

15.3% in the second quarter of 2020 for France, Italy, Spain and Portugal, respectively (See Figure 2.2 in annexe 2).

As confinement measures were slackened, mobility increased and international markets reopened. The effect was that real GDP growth rebounded strongly in the third quarter of 2020, recording one of the highest quarter-on-quarter growth rates in living memory. This jump during the above mentioned period in economic activity was visible in all developed, developing and emerging economies. OECD data points to 9.4% and in Europe 11.7% and 12.6% for the EU27 and the EA, respectively. These figures increased to 18.5%, 15.6%, 16.8%, and 14.7% for France, Italy, Spain, and Portugal (see Figures 2.1 and 2.2 in annexe 2). However, following this strong initial rebound, the pace of recovery has been different in each country.

2.2. Asymmetric shocks and recoveries

Although the initial shock was fairly symmetric across the four countries, the pace of recovery has somewhat differed. This can be illustrated by some data.

The initial GDP drop was smaller in Portugal than in France, Italy and Spain. During the second quarter, the effects in Portugal were similar to France and Italy, with Spain's being more pronounced. Accumulating the first two quarters of 2020, which constitute the epicentre of the crisis, the total impact in France, Italy and Portugal were quite similar with figures of -18.5%, -17.9% and -18.3%, while in Spain the drop amounted to -25.1% of GDP.

This asymmetry remained when the recovery started in the third quarter of 2020.⁶ The pattern of recovery showed greater dynamism in France, Italy and Portugal. Data from the third quarter of 2021 reveals that all three countries were very close to recovering their pre-COVID-19 GDP levels, with 99.8%, 98.75% and 98.93%, respectively.⁷ Therefore, it is foreseeable that by the end of the year 2021, this objective should have been achieved. In the case of Spain, this figure is 93.4%, so it will not be until 2022 that the pre-pandemic GDP level will be achieved (see Figure 2.2 in annexe 2).⁸

Three elements are crucial to explaining these differences. Firstly, there is the evolution of the pandemic in the four countries. Secondly, the characteristics of their economic structure. Thirdly, the health and economic measures taken.

Although the first known case of COVID-19 was detected in France, Italy was the country where the major outbreak was recorded, where the disease initially spread most rapidly and which was one of the hardest hit in terms of health during the pandemic. By contrast, Portugal was the last western European country where the virus was detected.⁹ The speed of government action and the severity of the

⁶ Both the CEPR (CEPR-EABCN Euro Area Business Cycle Dating Committee) for the euro area as a whole and the FBCDC (French Business Cycle Dating Committee) for France and the SBCDC (Spanish Business Cycle Dating Committee) for Spain have placed the trough in the second quarter of 2020, marking one of the shortest recessions on record.

⁷ As of the closing date of this report, the second data release of q-o-q GDP growth in Q4 is available for Germany (-0.7%) and France (0.7%), while there is just a flash estimate for Spain (2%) and Italy (0.6%).

⁸ It is very illustrative to see the evolution of the forecasts made by the European Commission at different points in time from autumn 2020 and during 2021, taking 2019=100 as the baseline year. Estimates improve successively in France and would be reached in 2022. The same is true for Italy. The cases of Portugal and Spain are somewhat different. In Portugal, the autumn 2021 forecast significantly exceeds the spring forecast. In Spain, something similar occurs, but also pointing to a longer delay in the recovery, which would finally occur in 2023.

It should be noted that the effects of the Ukrainian war are not factored in yet.

⁹ The initial impact (until the end of April 2020) was higher in Italy and Spain with a death toll per million inhabitants of 560 and 616, while in France and Portugal these figures were 275 and 139, respectively. By the end of 2020 the numbers of deaths amounted to 993, 1263, 1160, 701 for France, Italy, Spain and Portugal and in 2021 to 910, 1044, 741 and 1143 (European Centre for Disease Prevention and Control).

restrictive measures adopted were also different. However, by mid-March, all four countries had declared a lockdown.¹⁰

As regards the economic structure of the four countries, productive specialisation explains to a large extent the differences detected in the pandemic economic impact. The weight of activities particularly affected by the lockdown, such as tourism, the retail trade or the aviation industry in the case of France, explain the different economic impact after the implementation of the confinement measures.

Finally, before the European response was articulated, national economic policy measures basically consisted of highly expansionary fiscal policies and employment support measures. Several measures adopted in all four countries addressed issues such as strengthening the health care system and civil protection, efforts to preserve jobs and support the income of laid-off workers and the self-employed, and measures to support businesses (tax deferrals and loan guarantees). All these measures have had an impact on public finances that varies considerably from country to country, depending mainly on the room for manoeuvre allowed by their initial situation (see Alonso et al, 2021, and De Castro et al, 2022).

Table 2.1 in annexe 1 outlines the most relevant aspects of the initial shock of COVID-19 in the four MS. It is difficult to summarise the range of measures that the authorities have been taking to try to curb the spread of the virus. Since most of them directly restricted mobility, a summary index has been compiled from data collected in the COVID-19 Google mobility report that compares mobility trends in six different areas.¹¹ As can be seen in Table 2.1, with data as of 30 April 2020, Spain was the country that adopted the most restrictive policy, followed by France and Italy, with Portugal being the most permissive. With data as of 31 December 2020, the order would be Italy, Spain, Portugal and France.

3. MAIN ECONOMIC CHALLENGES OF THE FOUR COUNTRIES. HAS COVID CHANGED ANYTHING?

The economic situation of the four MS is characterised by a series of vulnerabilities before the outbreak of COVID-19, which have been exacerbated by the pandemic and have amplified its economic consequences. However, they have not been substantially modified in most cases as they represent long-standing structural challenges in all four countries. Although there are notable differences between them, we can identify common patterns, which can be grouped into the following categories: the labour market, the state of public finances, productivity and growth factors. Other issues, such as regional disparities or income distribution, are country-specific and will receive separate attention.¹²

3.1. Labour Market

The unemployment rate in 2019 was 8.4%, 10.0%, 14.1% and 6.5% in France, Italy, Spain and Portugal, respectively (see Figure 3.1 in the annex). These rates reflect the different pace of employment recovery after the global financial crisis. The recession triggered by COVID-19 has not had a major impact on unemployment, with Spain seeing the steepest rise of almost 1.4 percentage points in 2020. This lower incidence, especially compared to that recorded after the Great Recession, is explained by the employment support policies implemented by the four MS. But beyond these figures, the labour markets in the four countries show significant inefficiencies.

¹⁰ See Country factsheets in the Appendix for details of references.

¹¹ The areas are: retail and recreation, grocery and pharmacy, parks, transit stations, workplaces and residential, the latter with a positive trend. The reference value, which is the average value for each day of the week, is calculated over five weeks from 3 January to 6 February 2020.

¹² A detailed description of these vulnerabilities can be found in the country factsheets in the Annex.

In the case of France, unemployment is high, particularly for disadvantaged groups, and the labour market is highly segmented. The COVID-19 shock accentuated the existing structural weaknesses. Although the fall in employment was limited by the unemployment protection measures adopted, the market segmentation and the lack of integration of the most vulnerable groups were aggravated: low-skilled, young people, people with a migrant background (especially women), and persons with disabilities recorded high unemployment rates before 2019 and their situation further deteriorated in 2020.

Something similar has occurred in Italy, a country where, like France, employment not recovered to pre-financial crisis levels by end of 2019. Italy shows significant weaknesses in terms of unemployment among the young and the uneducated population and in the female labour force. The impact of COVID-19 has been severe even if the statistics do not fully reflect this due to the number of workers benefiting from the Wages Guarantee Fund. The loss of employment has particularly penalised the service sector, young people and women, thus accentuating the structural problems existing before 2019.

Although Portugal's unemployment levels are comparatively low, and below the EU average, its labour market also suffers from severe structural weaknesses. These include high segmentation and deficiencies in collective bargaining, resulting in high rates of temporary employment. The inadequate system of social transfers and the low skill level of workers also have significant consequences in terms of inequality and low productivity. Despite the low impact of COVID-19 on unemployment statistics, it has mainly affected young and temporary workers, accentuating the vulnerabilities detected before the pandemic.

Finally, Spain has been characterised for years as having one of the highest unemployment rates in the EU, and for an overreaction of employment adjustment in times of crisis (see Figure 3.1 in annexe 2). A high rate of temporary employment, the duality between insiders and outsiders employees, long-term unemployment and segmentation, penalising young people and women are the main structural problems of the Spanish labour market that successive reforms have failed to correct. As a result of the COVID-19 pandemic, the unemployment rate rose by more than in the other MS under the scope of this briefing, despite the support measures taken, while the structural problems remain.

The almost secular structural problems that shape the labour markets of the four MS have even increased in some cases. It is therefore imperative that these countries seize the opportunity offered by the RRF to make the necessary reforms to correct inefficiencies. These reforms should be based on two pillars. First, redesigning the institutional framework of the labour market requires a major effort to achieve the broadest possible social agreement in the right direction. Secondly, a reform of the education system is needed to provide a suitably qualified active population that meets the needs of the labour demand.¹³

3.2. Budgetary position

The position of public finances and their sustainability is another vulnerability shared by the four MS in their response to the impact of the pandemic, although here, there are clear asymmetries. It should be noted that the delicate situation of public finances is not only the result of the strong impact of COVID-19 but also of a structural problem whose resolution has been delayed over time. The general government fiscal balance over GDP in 2019 was -3.1%, -1.5%, -2.9% and 0.1% in France, Italy, Spain

¹³ This issue is very country specific and is dealt with in detail in the Country Factsheets in the Annex.

and Portugal, respectively, and their public debt-to-GDP ratios were 97.5%, 134.3%, 95.5% and 116.6%.¹⁴

France has had a structural deficit problem since the recovery from the financial crisis. While in 2015-2019, almost all euro area countries reduced their public debt-to-GDP ratios, in France it increased by 1.9%. Starting from a vulnerable situation, the measures adopted to deal with the pandemic further worsened the position of public finances in France, with the headline deficit reaching -9.1% of GDP and debt at 115%. Even before the crisis, the European Commission had recommended France to develop a strategy to gradually reduce public debt given the risks to sustainability. Although it is projected to decrease slightly, the French debt-to-GDP ratio will remain very high and constitutes one of the challenges facing its economy.

In Italy, the debt-to-GDP ratio recorded in 2019 was 134.6%, the second-highest value in the EU. This long-standing problem of the Italian economy, which was accentuated during the sovereign debt crisis, is compounded by an inadequate composition of public spending in terms of productive efficiency. The Italian response to the economic and health crisis and the decline in revenues caused a deterioration in public finances, raising the headline deficit to -9.6% of GDP and the debt to 155.8% of GDP. This situation confronts the Italian economy with high fiscal sustainability risks in the short and medium term. Implementing reforms and investments, where the RRF can play an important role, can boost economic growth and smooth budgetary adjustment. Moreover, reforms included in the RRF can correct the composition of public spending in favour of investment, including on education and R&D.

The Spanish case is characterised by a high structural deficit that has not been reduced despite the sustained economic recovery that started at the end of 2013, causing public debt to reach 95.5% of GDP in 2019. In spite of the limited room for manoeuvre that has conditioned Spain's fiscal response to the COVID-19 crisis, the headline deficit rose to 11% of GDP in 2020, and public debt soared to 120%, the most significant increase since statistics have been available.

Despite the positive Portuguese figure of a balanced budget in 2019, public debt was high, while the ageing of the population puts pressure on the sustainability of the pension system. The impact of Covid-19 has revived the public deficit in Portugal while increasing the public debt-to-GDP ratio until reaching 135.2% in 2020.

To a greater or lesser extent, the budgetary position of the four MS was delicate in the run-up to the pandemic, either because they had not managed to reduce their imbalances after the global financial crisis and accumulated structural deficits during the expansion, as in the case of France and Spain, or because the debt had reached figures above 100% of GDP, as in the case of Italy and Portugal. The fiscal measures taken to soften the effects of the pandemic have only exacerbated the weak public finances position. Nevertheless, it is not only the prominent aggregate indicators that matter but also the composition of expenditure, the sustainability of certain budget items, and the efficiency of the administration that are key elements in ensuring the smooth functioning of the economy. In this context, the weight of ageing-related expenditure should be highlighted, which is pressing the need for pension reforms, as well as some health systems weaknesses, as unveiled by the pandemic.

3.3. Productivity and growth factors

A third vulnerability encompasses a set of elements related to the economy's ability to maintain a sustainable growth rate. Adequate capital accumulation, both physical, knowledge and human capital,

¹⁴ Figure 3.2 shows the evolution of both indicators since 1995. See Country factsheets for a more detailed analysis of the public finance situation in each country.

and the ability to combine them with efficient institutions are the key to success. However, the four MS have some shortcomings in this area.¹⁵

Of the four countries analysed, only France currently maintains a per capita income above the EU average. It is followed by Italy, Spain and Portugal. The corresponding figures in 2021 with respect to the EA were 104.5%, 86.3%, 71.8% and 57.1% for France, Italy, Spain and Portugal, respectively. Particularly noteworthy is Italy's loss of convergence position from 1995 (106.4%) to the present and, to a lesser extent, that of France. Spain and Portugal have maintained a relatively stable position throughout the economic cycle. In all four cases, the per capita income position relative to the EU decreased in 2020 due to the impact of COVID-19.¹⁶

Growth figures also give an idea of the performance of the four economies. Looking at the average growth between 1995Q1 and 2021Q4, Spain has recorded the highest dynamism, above Germany, EU and EA averages, followed by France and Portugal, with Italy lagging behind.¹⁷ The growth factors behind this long-term growth pattern need to be identified.

Although productivity in France is higher than the EU average, its growth rate has been declining for the past 25 years. However, France still has the highest productivity of the four countries under study. In fact, a more detailed analysis, as shown in Figure 6 in the annexe, illustrates that, long-term growth is concerned, the main problem lies not so much in productivity per worker or per hour worked but in the country's relatively low employment rate. The decline of productivity in France -a phenomenon observed in many other advanced economies- can be explained in particular by tertiarisation, as the service sector recorded smaller productivity increases than the industrial sector, a phenomenon common to all industrialised countries. However, it also reflects elements specific to the French economy, in particular and partially linked to the tertiarisation of the economy, the progressive absorption of low-skilled workers into the labour market as a result of active employment policies.

The Italian economy has been suffering from persistently low labour productivity, which has stagnated over the last twenty years. Combined with high labour costs, this has resulted in a lack of competitiveness. The stagnation in recent years is partly attributable to a lack of flexibility in doing business, excessive bureaucracy, high taxation, inadequate incentives and inefficient labour market management. In addition, Italy is lagging behind in the digital revolution, ranking 25th in the EU.

In the case of Spain, despite its high growth in recent decades, its GDP per capita is still below the EU average. Low productivity and R&D investments are the main obstacles to growth and to accelerate its convergence with the EU. Its low productivity, only slightly above that of Italy's, in both labour and capital factors, is a main vulnerability of the Spanish economy, which has hardly been altered by COVID-19. The more significant presence of companies in sectors directly affected by the lockdown and a business structure based on small and medium-sized enterprises have both conditioned the impact of COVID-19. While the first effect is considered to be transitory until sanitary conditions are definitively normalised, the second represents a structural weakness.

Portugal, the country with the lowest per capita income of the four analysed, has an evident weakness in physical, R&D and human capital accumulation, which limits its growth potential. Nevertheless, the level of total factor productivity is close to that of the euro area, and only surpassed by France. Low

¹⁵ In this section we include data from Germany to improve the perspective of growth factors.

¹⁶ These figures are calculated on the basis of the series of Gross domestic product at 2015 reference levels per head of population facilities por AMECO.

¹⁷ The interquarterly average growth of the four countries from 1995Q1 to 2021Q4 was 0.38, 0.13, 0.45 and 0.32%.

investment in R&D, as well as insufficient capacity of firms to compete in global markets, are some of the country's main vulnerabilities in terms of growth.

In short, the four MS exhibit vulnerabilities limiting their productivity and growth capacity that have not been substantially modified by COVID-19. The RRF represents an opportunity to address these challenges for all of them. In the end, the accumulation of productive factors, physical and human capital and knowledge, and an appropriate institutional design constitutes the recipe for achieving the goal of sustainable growth.

4. SOME HORIZONTAL ISSUES: IMPLEMENTATION RISKS, ADDITIONALITY, CONDITIONALITY AND EU PUBLIC GOODS

The RRF has, simultaneously, a short and long-term vocation. In the short term, the RRF should help MS to put in place expansionary fiscal policies, supporting and accelerating the recovery, so that public investment is not any more the victim of the recession. In the longer term, the RRFs should induce profound structural changes in the economies of the MS, helping them to tackle vulnerabilities that existed before 2020 and that the COVID-19 has only magnified. Assessments of the RRFs should have in mind a possible trade-off between spending as quickly as possible to support the recovery and ensuring that the RRFs fulfil their long-term goals.

Article 3 of the Regulation (EU) 2021/241 of 12 February 2021 - the Regulation thereof - sets up the policy areas supported by the RRF, structured in six pillars, which actually cover almost every possible area of economic policy. These goals are further developed in Article 18, establishing a long list of elements that the RRFs should set out. While the advantage of such a broad scope is to allow MS to include in their RRFs measures to tackle almost every possible relevant investment project and structural reform, the risk is that the RRFs might not be focused enough to maximise their economic impact.

The Regulation incorporates the views of the co-legislators (the European Parliament and the Council) on a series of issues, including additionality, conditionality or the EU value added. This section is organised as follows: we start by reviewing the horizontal principles in Article 5, especially the principle of not financing recurrent expenditures. Then, we focus on the economic impact of the RRFs to discuss some implementation risks. Finally, we try to assess the degree of additionality of the four RRFs. The section ends with the review of the EU value added of the plans.

4.1. Horizontal principles in Article 5

Article 5 establishes three horizontal principles the projects in the RRFs must comply with (1) not substitute recurrent expenditures, (2) respect the additionality of EU funding and (3) respect the 'do no significant harm' principle.

4.1.1. Not to finance recurrent expenditures

The Regulation does not define in an unambiguous way what recurrent expenditures are. The principle of avoiding financing recurrent expenditures could be interpreted in the positive way of financing investment, which is fulfilled by the four RRFs analysed here. Nevertheless, RRF grants and loans are as fungible as any other revenue item. This implies that MS can take advantage of the RRF to finance public investment and use partially or totally the released funds to finance recurrent expenditures. Table 4.1 in annex 1 compares public investment with the amounts received from the RRF over the

period 2021-2023. The table also displays the structural balance, providing a measure of the fiscal impulse as projected in the Commission autumn 2021 forecasts.

Considering 2019 as the baseline, the accumulated increase recorded by public investment is almost matched by the instalments coming from the RRF in the case of France, suggesting that this country would almost fully spend the RRF on non-recurrent expenditures. This would be reinforced by the fact that structural balances strongly decline over time, thus indicating that the fiscal impulses (increases in the structural deficits) in 2020 and 2021 are mainly based on non-recurrent, transitory measures. The expected increase in public investments over 2021-2023 is also broadly matched by the expected RRF instalments flow in Portugal, but the structural balance remains relatively constant. This might indicate that not all the expansionary measures in 2021-2023 are transitory. In the case of Italy, the RRF instalments until 2023 add up to around 2.5 times the cumulative increase in public investment, while the fiscal impulse in 2021 (3% of GDP) fades out in 2023, thus indicating, as in the case of France, that a large part of the fiscal impulse is made of non-recurrent expenditures. In Spain, as in Italy, the RRF instalments flow is much higher than the increase of public investment up to 2023, but the structural balance worsens by half a point of GDP under the no-policy change scenario by that year, which might suggest that a part of the fiscal impulse over the period would consist of recurrent spending.

It should be noted that a RRF instalment flow bigger than the expected increase in public investment does not forcefully imply that the difference is spent on recurrent expenditures. It might mean that the RRF is used to finance public investment projects that would have been carried out anyway. As an alternative, it might mean as well that some projects initially planned have been substituted by genuine RRF investment projects. Both alternatives are two different faces of lack of additionality, as in the end, the increase in public investment with respect to the non-RRF scenario is lower than the funds received from the RRF. Additionality issues will be analysed below in more detail, but we discuss before the narrow concept of additionality applied in the Regulation.

4.1.2. Additionality in the narrow sense

Article 9 establishes that the Facility shall be additional to the support received under other Union programmes and instruments. No other concept of additionality is considered in the Regulation. In particular, the Regulation does not refer to additionality in a broader sense, according to which the Facility should not finance projects that would have been carried out in any case.

The amounts requested in the RRP and those allocated under the main EU funds for the 2021-2027 MFF widely vary across the four MS. According to the European Commission, the amounts allocated to Spain under the MFF at current prices are around EUR 36 bn, compared to EUR 17 bn, EUR 43 bn and EUR 24 bn for, respectively, France, Italy and Portugal. A very rough comparison of these figures with the maximum amounts under the RRP, including grants and loans, would suggest that the relative weight of EU funds other than the NGEU is relatively small, except for Portugal which could receive up to EUR 28 bn from the NGEU and EUR 24 bn from other EU funds.

4.1.3. The 'do no significant harm' principle

The four RRP include systematic assessments of compliance with the do no significant harm (DNSH) principle and the Commission has concluded in the four cases that no measure in the respective RRP is expected to do significant harm in the meaning of the Regulation (DNSH Technical Guidance). This is not surprising as, during the dialogue process, the Commission tried to ensure, as much as possible, compliance with the EU environmental framework, so that most of the projects presented in the RRP are expected a priori to comply with the DNSH principle. In the case of projects for which it is not possible to ensure *a priori* compliance with the DNSH, because it depends on the way they will be

implemented, the four Member States have committed to provide the necessary information in the corresponding milestones associated with each measure to monitor implementation.

4.2. The impact of the RRF

Article 18 envisages that the RRFs have to include a detailed explanation of how they are intended to strengthen growth potential, while article 19 (c) and (g) ask the Commission to assess the effectiveness of the RRF in strengthening growth potential and whether they are expected to have a lasting impact on the MS concerned. Since such assessments cannot be carried out at this stage on the basis of hard, observed data, the assessment can only be based on expert, qualitative judgement, as the Commission has *de facto* done in its assessments of the RRFs, or on *ex ante* simulations on the basis of more or less sophisticated models. In this section, the results of a series of simulation results are analysed. The main concern is not so much to compare quantitative results across different models, but to identify implementation risks, by comparing the hypothesis underlying each model.

4.2.1. The results of some simulation exercises on the economic impact of the NGEU

One of the first simulation results that can be found in the literature was published in the Staff Working Document accompanying the Commission communication of May 2020 (see European Commission, 2020). The Commission services applied the QUEST model to assess the impact of the NGEU (not only the RRF). The simulations consider three groups of countries: High income countries - including France -, high debt countries - including Spain, Italy and Portugal -, and other countries, none of which is under the scope of this briefing. The simulations consider two degrees of additionality in the broad sense. In the first one, 100% of the grants are used in brand new investment projects, but 50% of the loans go to finance expenditures that would have taken place anyway. In the low-additionality scenario, it is assumed that only 50% of the grants finance new projects.

Under the high additionality scenario, the high-debt group records a GDP increase of 4.2% by 2024, while debt is reduced by 5% of GDP. GDP in high-income countries rises by just above 1%. As expected, the impact on the GDP is smaller under lower additionality of grants. However, it is interesting to note that since lower additionality releases resources to finance expenditures that were already programmed, the debt ratio falls by more than in the high-additionality scenario. Therefore, these simulations do not only illustrate the importance of additionality in the broad sense but they also point to a possible trade-off between stabilisation and sustainability; higher growth effects may come at a price of higher debt in the short to medium term.

Codogno and van den Noord (2020) consider the maximum amounts of grants and loans implied by the criteria in the Regulation. The authors conclude that the corresponding fiscal impulse would boost the euro area GDP by 1.5% above the baseline (no NGEU) by 2023. The cumulative growth effect rises to 2.5% by 2027. The impact is estimated to be larger for Portugal (10% by 2027) than in Spain (8%) and Italy (7%), while the impact for France is lower than the euro area average.

Pfeiffer et al (2021) have carried out simulations of the economic impact of the RRF on the basis of the amounts actually requested by the MS in their RRFs. Two different scenarios for the spending speed are considered: A fast one, where the RRF is spent over 2021-2024, and a slow, perhaps more realistic, one, where the RRF is spent over 2021-2026. They are combined with the same low and high-additionality scenarios in European Commission (2020). In the fast-spending scenario, the accumulated impact up to 2024 on the French GDP is about 1.0%, which compares with 2.5% for Spain and close to 3.0% for Italy and Portugal. Unsurprisingly, the GDP effects in the low spending path, up to 2026, are lower than in the fast one -about 0.25% lower in France and 0.5% lower in Italy, Spain and Portugal.

Another interesting feature of this simulation exercise is that it takes into account the synchronising effects of the RRF. Since all the plans are executed over the same period, the RRF represents a simultaneous fiscal stimulus within the EU, which the authors compare with the case that each RRP would be implemented alone. It is important to note that these simulations do not show how the RRF contributes with additional value to the EU and the Internal Market, but they rather show how the existence of open and competitive markets in the EU magnifies the effects of national fiscal responses via intense intra-EU trade flows when they are coordinated at EU level.

The spillovers of the Internal Market via intra-EU trade would represent almost half of a percentage point of additional growth for the EU as a whole. The spillovers for Portugal are slightly above the EU average, while those for Spain and France are close to ½%. In Italy they are just around ¼%. Interestingly, compared with the total impact, spillovers tend to be larger in high income countries. In other words, debt mutualisation would pay off for high-income countries. Part of the resources granted by core countries to the periphery would come back in the form of higher exports and growth.

4.2.2. The projections in the RRP and in their Commission assessments

On top of these simulations, some RRP include *ex-ante* growth projections. This is the case of France and Italy, while it has not been possible to find projections carried out by the Spanish and Portuguese authorities on the specific impact of the RRP. Needless to say, we could consider the projections in the Stability Programs, but they would refer to the total fiscal impulses rather than those specifically associated to the RRF. The projected impacts in the French and Italian RRP are summarised in table 4.2 in annex 1. Although the estimates are not fully comparable, as they have been obtained with two different models and different assumptions, the analysis of which is out of the scope of this briefing, the results in the table seem to be consistent with other simulations showed above.

Such growth projections have been supplemented by the Commission with updated QUEST simulations for the NGEU¹⁸ on the basis of actual RRP over the period 2021-2040. The simulations consider two alternative scenarios, high and low productivity, and include trade effects within the Internal Market (spillovers). The Commission provides as well the 20-year economic impact of implementing structural reforms halving the gap with the best performers.

Unsurprisingly, the Commission simulations are overall in line with other simulations carried out with the QUEST model. Under both the low and high-productivity scenarios, the impacts are larger for Italy and Portugal. The same can be said concerning the permanent effects of the RRP in the very long run. Concerning Single Market spillovers, the largest impact is found in Portugal. Finally, France is the country benefiting most of the implementation of structural reforms.

4.3. Additionality, a major implementation risk

Additionality in the broader economic sense would mean that the RRF is fully spent on projects that would not have been carried out had the NGEU not been adopted. It is pretty obvious that assessing additionality of the RRF requires the identification of a counterfactual. A probably ideal counterfactual would consist of the projects planned in 2019 for the period 2020-2026. Ideal but unrealistic, as no govern prepares a detailed list of all investment projects to be implemented over six years. In addition, one could wonder why the counterfactual should be 2019, as we know that when the pandemic broke out the NGEU did not exist, while MS put in place strong fiscal impulses already in spring 2020.

¹⁸ The RRF is around 90% of the NGEU.

Corti et al (2022) are confronted with both the choice of the counterfactual and the lack of information on the planned investment projects. They start by comparing the public investment levels projected in the Commission autumn forecasts 2021 with the counterfactual represented by the projections in the 2019 Stability Programme. The results are inconclusive, as the maximum correlation between the projected increases in public expenditures and the RRF instalments is of only 17% in the best of the cases. This is not surprising in the light of the data presented in table 4.1 in the annex.

Corti et al (2022) also apply a so-called granular approach, where the counterfactual are the projects included in the National Reform Programmes (NRP) of 2020, complemented with other sources when available. This information is compared with the projects presented in the RRFs. The authors conclude that the degree of additionality is much higher in Italy, where the size in terms of GDP of the RRF is huge, than in Spain, which does not foresee to use the maximum 6.8% of its GNI in loans. On the other hand, the degree of additionality seems to be relatively high in Portugal, where cohesion funds are still sizeable.

To complement this interesting piece of work, we follow here the approach by De Castro et al (2022) and compare, for each one of the four countries, the GDP, public investment and structural deficit projections in five Commission forecasts, including those of autumn 2019 (AF19), spring 2020 (SF20), autumn 2020 (AF20), spring 2021 (SF21) and autumn 2021 (AF21). The results are shown in the three panels of Figure 4.1 in annex 2.

The GDP projections in the AF19 show that, before the pandemic broke out, growth was expected to be relatively mild in France, Spain and Portugal, and almost stagnating in Italy. In terms of GDP, public investment projections remained constant in France (3% of GDP) and Spain (2%), while small increases were projected for Italy and Portugal.

The forecasts of spring 2020, carried out during the lockdown, show the huge impact of the pandemic and suggest that, at the time, it was expected to be relatively transitory. The projections did not include the NGEU, but incorporated the early and strong fiscal response by the MS. Public investment ratios were projected to transitorily rocket, but coming back quickly to pre-pandemic levels.

By October 2020, the NGEU had already been approved, but the Regulation was still under discussion and the RRFs were under preparation in the best of the cases. Therefore, a good candidate for the counterfactual would lie somewhere between the SF20 and the AF20.¹⁹ This counterfactual can be compared with the latest available projections, the AF21, which are based on the execution for at least half of 2021 budget and on the adopted budgetary plans for 2022, already including the corresponding instalments from the RRF.

Public investment significantly increases in the four countries in 2021. In the AF21, 2022 public investment ratios are projected to remain constant at 4.0% and 2.7% in, respectively, France and Spain, while they rise to 3.3% in Italy and 3.0% in Portugal. Compared with the AF20 projections, these ratios represent an increase of ½% in Italy, but ¼% or less in France, Spain and Portugal. These approximations to the investment impact are lower than expected, but consistent with the data in table 4.1.

All in all, this might point to a low degree of additionality, most likely due to the substitution of planned investment projects by those consistent with the RRF principles and goals. This might have mitigated the pressure on public finances in highly indebted countries, while enhancing the magnitude of the fiscal impulse and underpinning the recovery.

¹⁹ It is possible that in their 2021 budgetary plans (included in the AF20) MS had anticipated projects to be financed by the RRF.

A relatively low degree of additionality might perhaps be unavoidable. In the first place, the Regulation itself allowed MS to include projects and reforms in place after 1 February 2020, i.e. before EU governments were fully aware of the magnitude of the shock. After that date, many MS put in place a large fiscal response before knowing the availability of the NGEU. Unsurprisingly, governments would have included measures driving such large fiscal response in the RRP. In the second place, given the short time to put together a coherent plan, high-debt, peripheral countries like Italy, Spain and Portugal, receiving a large chunk of the RRF, might have had no other alternative but to include projects that were in one way or the other in the pipeline. This would not be necessarily bad if the RRF would be limiting the dynamics of public debt without derailing the recovery.

4.4. Other implementation risks²⁰

The discussion above shows that while in qualitative terms the different impact simulations seem to be broadly aligned, the more or less significant divergences in quantitative terms are explained by differences in the assumptions defining the simulation scenarios that help identify implementation risks.

First, MS can consider differently grants and loans, showing a **preference for grants**. Some large countries like France, seem to have renounced so far to the possibility of taking loans. In contrast, Italy has included in its RRP the maximum amounts of both grants and loans, while Portugal envisages to use a relatively small proportion of the maximum loans available. The Spanish RRP, like the French one, does not include any request for loans. This would obviously reduce the growth potential of the RRP, specially in Spain and Portugal, although both Member States could reconsider their choices up to 2023. Leaving loans for the outer years of the RRP might result in back-loaded fiscal stimuli with the concomitant time-inconsistency risks.²¹

Second, growth might be lower than expected due to low **absorption capacity**. It is not possible at this stage to directly determine if the absorption capacity will be an important issue for the RRF implementation. The implication of insufficient administrative capacity is that it would take too much time for the RRF funds to be fully spent, which could undermine the stabilisation role of the NGEU. The priority in the EU should be to ensure that the NGEU is fully and well spent by the Member States in order to maximise its fiscal impulse in the short term and its transformative potential in the longer run.

Looking at the absorption rates in the previous MMF is an indirect (and possibly inconclusive) way to assess absorption capacity issues. For instance, in 2021 the absorption rates for the 2014–2020 MFF were 58% for Portugal, 41% for France, 39% for Italy and 35% for Spain, which compare with 50% for the EU average.

Third, another implementation risk is related to the **composition of the fiscal impulse**. Fiscal multipliers are smaller the larger the proportion of current expenditures. At this stage, it seems that the four RRP will be spent in line with the EU priorities. If fully and correctly implemented, the four RRP should enhance the physical, human and knowledge capital of the MS, unambiguously underpinning inclusive and sustainable growth.

Finally, the simulations carried out by the Commission in its assessment of the RRP clearly show that the longer lasting impacts are produced by the implementation of **structural reforms**. The monitoring

²⁰ See as well Codogno and van den Noord (2020) and Nuñez Ferrer, J. (2021).

²¹ In a Real Time Economic Issues Watch entitled 'Southern Europe will regret not taking EU loans now' released by the Peterson Institute for International Economics on 28 October 2020, Jacob Funk Kirkegaard has floated the idea that should Southern European governments refuse to apply for loans from the NGEU, the ECB would be 'less likely to continue to purchase large amounts of their sovereign bonds, which will in turn cause their rates to rise, resulting in the very budget pressures their fear'. See also Kirkegaard (2020).

of the RRP should pay great attention to the implementation of reforms. All the RRP include a detailed list of reforms. These are discussed in section 5.

4.5. Conditionality

Article 10 of the Regulation introduces conditionality to the implementation of sound economic governance, in particular compliance with the Stability and Growth Pact (SGP) and the Macroeconomic Imbalances Procedure (MIP). It mirrors similar provisions included in other EU funds, where commitments are suspended in case of noncompliance with the recommendations under the excessive deficit procedure (EDP) or with the excessive imbalance procedure (EIP). Although the Regulation devotes almost two pages to spell out the procedure of suspension, it seems that the effectiveness of this article would be rather limited. On the one hand, the escape clause of the SGP has been activated, and the Commission has decided not to open any EDP because it has appreciated the existence of a severe downturn. On the other hand, the EIP has never been applied and it does not seem that the current crisis and its scars in terms of macroeconomic imbalances for the years to come give the most appropriate framework to apply the procedure for the first time. All in all, as was shown during the stepping up the EDP procedure for Spain and Portugal in 2016, this kind of provisions are not easy to apply, as they tend to be pro-cyclical in bad times.

Concerning the **link between the NGEU and EMU governance**, perhaps one key issue is to what extent the NGEU can represent a game changer in the debate on the EMU governance reform. The NGEU represents an unprecedented move by the MS towards debt mutualisation. True, the NGEU is in principle a one-off project, but once a taboo, be it debt mutualisation, has fallen once in the EU, it could fall again. One condition, possibly necessary, albeit surely insufficient, would be that the NGEU is well spent, which is equivalent to say that MS have an interest in minimising implementation risks.

4.6. The EU value added

In the initial Commission proposal²², EUR 190 bn out of the 750 bn of the NGEU were devoted to genuine European funds and instruments, which could have enhanced its EU value added. In turn, in the Council proposal, the amount devoted to up EU funds and instruments fell to EUR 77.5 bn. The difference, around 110 bn, went to increase the available amount in loans in the RRF, which may not be fully spent, as many MS do not envisage to use loans or to use only a fraction of the maximum amount available.

The four RRP include a series of projects with cross-border elements. Dias et al (2021) have scrutinised the RRP to identify cross-border projects. In particular, in Spain and Italy, the bulk of the money allocated to cross-border projects consists of physical infrastructure investments within the framework of the TENs, while the RRP of France and Portugal concentrate their cross-border projects on the area of the digital transition, especially microelectronics. Overall, the amounts allocated to cross-border projects are small compared with the total funds provided by the RRP.

Preserving the Internal Market and improving its functioning is an important way to ensure that the RRF maximises its economic potential. In this context, it is paramount to avoid possible distortionary effects of the Facility by ensuring a smooth enforcement of EU competition policy. Although the firm commitment of MS to avoid incompatible state aid is most welcome and reassuring, the Commission should remain vigilant to avoid that the possible market distortions reduce spillovers effects of the RRF.

²² European Commission (2020).

5. A COMPARATIVE ANALYSIS OF THE FOUR RRP

The Regulation sets up the fundamental pillars of action of the Recovery and Resilience Facility, which should govern national plans. These pillars are six: green transition; digital transformation; smart, sustainable and inclusive growth; social and territorial cohesion; health, and economic, social and institutional resilience; and policies for the next generation, such as education and skills. Therefore, the plans designed in each country should, through investments and reforms, address these general guidelines. The purpose of this section is to compare the RRPs of the four MS, looking at their similarities and differences and analysing the extent to which they meet their objectives.

The first difference lies in the size and financing modalities. While France explicitly opted from the outset not to use its share of loans, Italy decided to use them in their entirety, Portugal a small proportion (20%) and Spain not to use them for the time being but left the door open for 2023 and beyond.

Although the four countries try to address the pillars established by the Regulation, the architecture of their respective RRPs differs both in nomenclature (axes, missions, levers, components) and in the efforts dedicated to the different investment projects as well as in the design of the reforms which address the specific challenges of each country. Undoubtedly, the vulnerabilities of each country, as mentioned above, and the CSRs as stated in the framework of the European Semester, have been very present in the elaboration of the plans. The only requirement imposed by the European Commission on the distribution of the funds was to dedicate at least 37% to ecological transition projects and 20% to digital transformation projects. As shown in Figure 5.2 in annex 2, all countries meet the target with percentages ranging from 46% in the case of France to 38% in Portugal for the green transition and from 28% in Spain to 21% in France for the digital transition.

Since the four MS organised their RRPs keeping a balance between the pillars set out in the Regulation and their specific challenges, the comparison of the plans will first analyse the two areas particularly prioritised in the Regulation, then examine the way countries address their own vulnerabilities, and finally refer to the rest of the pillars.²³

5.1. Green transition

Green transition is a major priority for France, to which it will devote almost 50 per cent of its investment effort. Key measures are the renovation of buildings, sustainable transport (modernisation of the rail network) and the decarbonisation of industrial processes. France also plans to invest heavily in R&D for the development of green technologies, such as hydrogen, and establishing synergies with other EU countries such as Germany. In addition, one main weakness lies in the decarbonising and upgrading of the energy performance of its building stock. To address this problem it is going to launch a comprehensive reform with the "Climate and Resilience Act".

Italy's green transition objectives differ in several respects from France's and focus mainly on three aspects: waste and water management, sustainable mobility and improving buildings' energy efficiency. Although the European Commission has assessed these measures positively and considered that they will make a significant contribution to the green transition, other sources are more critical. In particular, they criticise the absence of relevant projects in key areas such as decarbonisation and all its implications: renewable energies, energy efficiency and e-mobility.²⁴

²³ A detailed analysis of each of the plans, as well as bibliographic references, can be found in the country fiches in annex 3.

²⁴ See factsheets for details.

In Spain, the plan supports the green transition through investments included in nearly all the plan's components. Some fundamental aspects are energy efficiency of public and private buildings, sustainable mobility in urban and long-distance transport, decarbonisation of the energy sector that includes storage techniques and a Renewable Hydrogen Roadmap, and strategies for building renovation. The investment plan is accompanied by the *Law on climate change and energy transition*, establishing the renewable targets for 2030 and the objective of climate neutrality by 2050. Finally, the plan includes measures to increase the resilience of the different ecosystems, especially on the coast, to the effects of climate change.

The green transition target in Portugal, the country with the highest share of emissions per GDP of the four analysed, contemplates a large-scale investment programme to improve the energy efficiency of residential and public buildings, more sustainable transport and the production of renewable hydrogen. Like Italy and Spain, Portugal also includes measures to mitigate the effects of climate change.

In short, all four countries meet the objectives set by the Regulation and have achieved a positive assessment from the European Commission with respect to the green transition. France stands out for its more vigorous commitment and greater innovative ambition.

The three Southern countries share concerns about their particular vulnerability to the effects of climate change and the increased likelihood of extreme events. Consequently, they have included measures to mitigate such effects and preserve their ecosystems, especially in coastal areas.

5.2. Digital transition

Figure 5.4 in annex 2 shows the position of the four countries with respect to digitalisation, one of the aspects privileged in the RRF funds with the objective of boosting EU economic growth. Considering the four items that make up the Digital Economy and Society Index (DISE) as a whole, France and Portugal would be in line with the EU average, while Spain and Italy stand out for their higher and lower digital potential, respectively. Among the 27 EU member states, France, Italy, Spain and Portugal were ranked at positions 15, 20, 9 and 16, respectively, according to the 2021 edition of the DISE.

France will seek to meet its digital challenges with a package of investments to develop and deploy key digital technologies, such as cybersecurity, quantum, cloud and 5G in the private and public sectors. Other investments include the digitalisation of the territory through the extension of fibre optics to improve connectivity, supporting the digitalisation of firms and strengthening key digital capacities. As is the case with the green transition, France will participate in two important European projects in this area.

Italy is lagging behind in most of the items that make up the index, especially in human capital and connectivity. However, thanks to the efforts made in the last few years it has improved in the integration of digital technology. Planned investments and reforms cover the digital transformation of the public administration and justice system and improving digital skills.

Spain's plan concentrates mainly on promoting the digitalisation of companies, especially SMEs, and strengthening the digital skills of the population, its two main weaknesses in the digital field. In connectivity and digitalisation of public services, Spain performs above average.

Portugal intends to focus efforts on the digital transition in education and training in digital skills, the digital transformation of enterprises and the digitalisation of the public administration.

Summarising, Italy, Spain and Portugal share the objective of improving the digitalisation of public services and the digital skills of the population. France, while not neglecting these objectives, shows a greater innovative ambition deploying key digital technologies.

5.3. Country-specific challenges

Unlike the case of the green and digital transitions, the measures to address the main vulnerabilities, "the key macro-economic challenges", of the four countries under study do not come under one specific pillar in the Regulation. They have been addressed in various components within the pillars of the "Smart, sustainable and inclusive growth" and "Health, and economic, social and institutional resilience". The two remaining pillars, "Social & territorial cohesion" and "Policies for next generation", may also include measures of a more specific nature.

5.3.1. Labour market

The aforementioned problems in the French labour market (see Section 3 and annex) are addressed from both an economic and social perspective in its RRP, devoting around 20% of the total funds. The plan proposes investments targeting youth employment, vocational training and the employment of people with disabilities. However, as the Commission's Assessment notes, the measures do not consider other vulnerable groups and do not envisage reforms to reduce temporary employment.

Italy has scheduled two programmes to ensure employment and improve workers' skills. The country seeks to address the main vulnerability of its labour market which is low participation and structural unemployment. The plan combines reforms and investments to increase the supply of childcare facilities, improve women's and youth participation in the labour market and reinforce vocational training.

The key point of the Spanish RRP concerning the labour market is the plan to boost, transform and modernise the vocational training system so that it becomes one of the backbones of a new economic model based on knowledge. The plan also envisages implementing a set of reforms to achieve a more dynamic, resilient and inclusive labour market and to address the problems that have plagued it for decades: temporary employment, market duality, obsolete collective bargaining, high structural and joint unemployment, and increased investment in human capital.

The Portuguese plan also includes investments and reforms to correct the shortcomings of its labour market and seeks to increase the responsiveness of the education and training system, combat social and gender inequalities and increase employment resilience, especially for young people and skilled workers.

5.3.2. Public finance

France proposes two reforms to improve public finances. The first deals with rules to ensure consistency between annual budgets and multi-year objectives, facilitating the adoption and implementation of fiscal policies that guarantee long-term sustainability. The second focuses on assessing the quality of public spending. It is expected to improve the quality and efficiency of public spending, allowing the country to prioritise growth and environmentally-friendly expenditure. An investment package aims to renovate medical centres and residential care homes for elderly people, which will improve access to higher quality care. The question is whether these measures will be adequate or require deeper reforms in certain areas of public finances such as those related to the ageing of the population or the public health system.

Italy's plan calls for a deep modernisation of the public administration through reforms and investments that will remove obstacles to the business environment and competitiveness. Improving

the efficiency of the justice system, cutting red tape and modernising public employment are some of the main objectives. This will be done by identifying the most critical procedures and eliminating redundant ones to simplify administrative processes. In addition, Italy's plan proposes to increase the skills of public sector employees by reviewing career paths and promoting the access of qualified people from the private sector. The digital transition will support these objectives. While all efforts are concentrated on improving the effectiveness of the public administration, no explicit mention is made of any fiscal consolidation plan despite the country's deficit and debt figures. The RRP only mentions some measures for reforming the tax system and a spending review reform.

The Spanish plan proposes consolidating public finances with measures on both the revenue and expenditure sides. Combating tax fraud and reforming the tax system and its administration are among the efforts proposed to increase revenue. The recent proposal reform has limited scope focusing on environmental taxation and the digital transformation of the economy. On the expenditure side, measures are included to make public spending more efficient and sustainable. The objective of the spending review program is to improve Spain's public spending quality and efficiency, allowing the country to reprioritise it towards more growth and environmentally-friendly expenditure. Finally, the plan also recognises the need to reform the pension system to ensure its sustainability in the medium and long term and to guarantee intergenerational equity. However, the design of the reform is strongly conditioned by social and political pressures.

Portugal's RRP provides a comprehensive set of measures to improve the quality and sustainability of public finances. These measures include mechanisms for reviewing public expenditure and broadening the tax base. The plan also consists of reform for modernising and simplifying the public administration.

In sum, all four countries incorporate qualitative measures into their plans to improve the quality and efficiency of public services through a combination of investment and reform. However, a more concrete, detailed and credible fiscal consolidation plan is missing, given the budgetary situation of the four countries. Nevertheless, the Commission welcomes the proposals of the four countries and notes that the measures will ensure sustainable finances in the medium term.

5.3.3. Growth factors

As mentioned in section 3, all four countries present vulnerabilities that affect their potential growth path, especially due to low productivity and low endowment of adequate productive factors or other reasons. Although the pillar "Smart, sustainable and inclusive growth" is the most appropriate to encompass measures to mitigate these vulnerabilities and boost economic growth, the fact is that the individual plans include reforms in different sections. In addition, it should be borne in mind that policy areas, such as the digital transition, the reform of the labour market or the modernisation of the public administration, also have an apparent effect on growth.

For example, in the case of France, the productivity problems have been tackled through labour market measures that would result in a higher employment rate, and with the solid technological commitment in the investments proposed to carry out the green and digital transitions.

Measures to reverse the stagnation of the Italian economy in recent years also rely on labour market reforms and investments, and on the modernisation of its public administration. Significant investments in digitalisation and the green transition are also expected to boost the economy. Italy's plan also includes measures to reduce regional disparities, a severe problem in the country.

The low productivity of the Spanish economy, especially concerning the labour factor, is expected to improve with the labour reform measures, related to the improvement of human capital both in

professional training and digital skills, the boost that will be derived from green investments and, above all, from the digital transition.

Measures related to labour market reform and digital transformation are also featured in the Portuguese case. In addition to investments to improve the infrastructure network, the Portuguese plan also includes a "Business Capitalisation and Innovation" programme aimed at increasing the competitiveness and resilience of the economy.

Summing up, the four countries rely on a set of investments and reforms that are common to them all, affecting the labour market, public administration and actions to impulse the green and digital transitions. Italy and Portugal add measures such as reducing regional disparities or improving private investment to address their specific vulnerabilities.

Another issue not to lose sight of is the social aspects that the Regulation provides in the six pillars, especially "Social & territorial cohesion", "Health, and economic, social and institutional resilience" and "Policies for the next generation". All four plans take these social aspects into account in the measures proposed. For example, they all consider the weaknesses of their health systems or the redistributive or future implications of the programmes. In its assessment reports, the Commission includes a detailed analysis of the contribution of each of the components of the individual plans to the six pillars of the RRF. Figure 5.5 shows a summary of this analysis.

5.4. Summary assessment

In a recent report, the Commission provided the Parliament and the Council on its interim assessment of the Recovery and Resilience Facility implementation after member countries submitted its operational agreement to request its first payment application (European Commission, 2022). This is a very detailed report in which the Commission analyses whether countries have adequately addressed the six pillars of the Regulation. In the case of France, measures to incorporate small businesses in the ecological transition, actions to cope with high youth unemployment and reforms to consolidate public finances stand out. The introduction of the National Programme for Circular Economy, the integration of advanced digital technologies, the "Italy's Transizione 4.0" programme, investments to support the integration of women in the labour market and, finally, measures aiming to achieve a more efficient judicial system, are the actions highlighted in the case of Italy. In Spain, the Climate Change and Energy Transition Law, the reform of the minimum insertion income, the measures to support the digitalisation of SMEs and boost digital skills, and the reforms that strengthen the capacity to carry out and control spending reviews stand out. Finally, in Portugal, the most relevant measures are the capitalisation of its national development bank, the deregulation of regulated professions and insolvency problems, tax reforms to support the transition towards the circular economy, investments to boost digital transformation and other programmes targeting the most vulnerable groups and social and territorial cohesion. In all cases, the detail in the presentation of the actions, the timeline of their implementation, the estimation of costs, the technical aspects and the involvement of the responsible authorities in their performance are also positively valued.

In summary, the implementation of the respective RRFs is expected to have a positive impact on all four economies. But the question behind all these positive elements is whether all these measures are sufficient to solve the structural challenges faced by the countries. In other words, the Commission assesses the implementation of the Regulation but not its design, and the question arises as to whether an automatic application of the regulation's guidelines with identical measures for all member countries is best suited to reduce country-specific vulnerabilities.

For example, in the case of France, concerns might emerge in the labour market and educational proposals. While the program includes a strong target on reducing unemployment among the young, this is not the case in addressing unemployment for other vulnerable groups. Moreover, the dualism problem could remain unresolved. Another concern is the impact of measures aiming to improve public finances, whose success will depend on the expenditure rule's ambition and the evaluation of spending. Moreover, it is essential to note that the plan does not include reforms regarding the pension system, an important and contentious issue that weighs on the sustainability of public finances.

In the Italian case, although its RRP broadly addresses the vulnerabilities of its economy, we can also identify some weaknesses. For example, the general character with which labour market measures aimed at reducing youth unemployment are addressed. Similar is the case for actions to reduce the high regional disparity that Italy suffers from. Finally, doubts also arise about the absence of relevant projects in different areas of the green transition.

Similarly, although the impact of the RRP will undoubtedly be very positive for the Spanish economy, a more critical view suggests that some vulnerabilities are only partially addressed. These include the correction of the structural public deficit, labour market distortions and the efficiency of public administration at different levels of government.

Finally, in the case of Portugal it can be concluded that the reforms and investments envisaged in its RRP adequately cover all the vulnerabilities of its economy, although there is a lack of specifics as to when measures to tackle labour market segmentation and the lack of business financing will be approved. Furthermore, some doubts arise about the future sustainability of its public debt, significantly if EU fiscal rules are relaxed in the future.

There is, therefore, both light and shade in the assessment of the RRP of France, Italy, Spain and Portugal. The light comes firstly from the speed and effectiveness with which the respective member countries are implementing the regulation guidelines in their respective RRRs, as acknowledged by the Commission in its assessment reports. Secondly, the volume and composition of investments financed by the funds will undoubtedly have a knock-on and modernising effect on the economies. But we also detect shadows. These arise from the design of a uniform regulation for all countries that does not vigorously address the specific vulnerabilities of each member state, prioritises investments and does not generate sufficient incentives to address reforms. Doubts arise especially in the area of reforms and whether their ambition will be sufficient to effectively solve entrenched problems, especially those related to the labour market or public finances.

6. CONCLUSIONS

The RRF is part of the EU response to the unprecedented economic crisis unleashed by the COVID-19 pandemic. This briefing has assessed some main aspects of the RRRs of France, Italy, Spain and Portugal, in light of the vulnerabilities limiting long-term growth in the four countries.

Although in different degrees, the four countries share similar weaknesses, in particular concerning the functioning of labour markets, weak potential growth, and risks to the sustainability of public finances. These vulnerabilities represent long-standing structural problems that have not been adequately addressed until now.

The RRRs of the four countries include investment projects and structural reforms addressing the main challenges identified in the CSRs, while *a priori* ensuring compliance with the six pillars enshrined in the Regulation. The RRRs comply with the minimum investment requirements and aim to cover specific

gaps in the green and digital transitions. Many of the measures reinforcing economic and social resilience combine investments and reforms in the appropriate manner.

The analysis in this report has highlighted as a very positive development the speed and effectiveness with which the four countries are implementing their programs. In addition, the volume and composition of investments financed by the funds will undoubtedly have a knock-on and modernising effect on the economies. However, there are doubts in the area of reforms and whether their ambition will be sufficient to effectively solve entrenched problems, especially those related to the labour market and public finances.

There is no evidence of lack of compliance with the RRF Regulation in any of the RRP. The report does not propose possible amendments in the current Regulation, which would not appear realistic given the large amounts already approved. However, the Parliament could extract some lessons for the future and lead a debate on additionality and debt sustainability associated to the EU funds, including permanent fiscal capacity.

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ANNEX 1: TABLES

Table 2.1: Overview of the COVID-19 impact

	First covid case	Fiscal policy	Mobility	Total GDP impact
France	January 24	1.3%	-52.83/-18.00%	-18.45%
Italy	January 30	3.0%	-52.57/-37.67%	-17.87%
Spain	February 25 ²⁵	0.3%	-56.50/-23.00%	-25.05%
Portugal	March 2	0.6%	-47.17/-22.67%	-18.30%

Source: The figures of fiscal policy are calculated as the difference between the structural deficit in 2020 and 2019 (General government structural balance :-Adjustment based on potential GDP Excessive deficit procedure, AMECO). The two Mobility columns summarise the reduction in mobility with respect to the reference period (3 January to 6 February 2020) on 30 April 2020 and 31 December 2020, respectively. Total GDP impact is calculated as the loss of GDP at the end of the second quarter of 2020 compared to the fourth quarter of 2019.1 (OECD).

Table 3.1: Vulnerabilities before COVID-19

	Labour market	Budgetary position	Growth factors
France	High segmentation	High debt-to-GDP ratio	Declining productivity growth for the last 25 years
Italy	High structural unemployment	High and persistent debt-to-GDP ratio	Stagnation of low growth rate
Spain	High unemployment and temporary	High structural deficit and debt-to-GDP ratio	Low labour productivity
Portugal	Severe structural weakness	High debt-to-GDP ratio	Low potential growth

Sources: see the Annex factsheets.

Table 4.1: The RRF and public investment (% of GDP)

		2019	2020	2021	2022	2023
France	Pub. Invest.	3.7	3.7	4	4	4
	RRF	0	0	0.2	0.6	0.3

²⁵ The first case of coronavirus infection was detected on 31 January 2020 on the island of La Gomera, but it was not until 25 February that the virus spread to the Peninsula.

	St. Balance	-3.3	-4.6	-6.7	-5.2	-3.9
Italy	Pub. Invest.	2.3	2.6	2.8	3.2	3.2
	RRF	0	0	1.4	2.6	2.0
	St. Balance	-2.4	-5.0	-8.0	-5.9	-4.9
Spain I	Pub. Invest.	2.1	2.6	2.7	2.7	2.6
	RRF	0	0	1.6	1.6	1.5
	St. Balance	-4.1	-4.5	-4.7	-4.1	-4.6
Portugal	Pub. Invest.	1.8	2.2	2.5	3.0	3.5
	RRF	0	0	1.0	1.1	1.6
	St. Balance	-1.4	-1.9	-3.0	-3.2	-3.1

Source: AMECO (DG ECFIN) European Commission. Autumn 2021 forecasts.

Table 4.2: Estimated impacts of the RRFs according to national authorities

	2021	2022	2023	2024	2025	2026
FR	1,1	1,0	0,6	0,6	0,5	-
IT	0,5	1,1	1,6	2,0	2,4	2,7

Source:

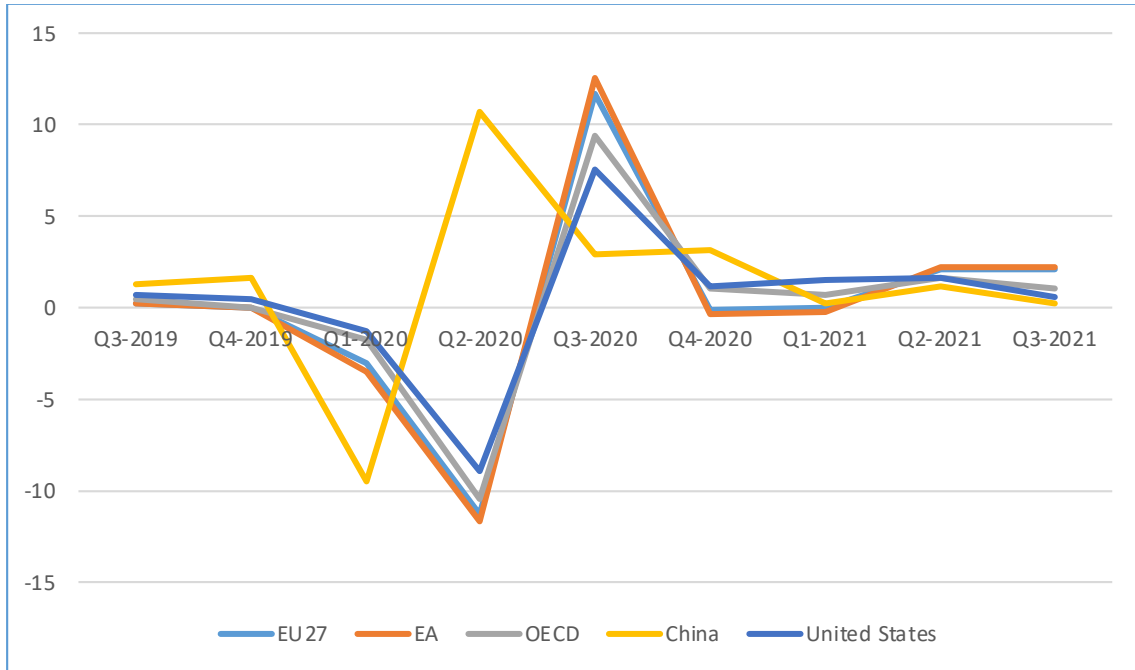
Table 4.3: Economic Impact of the RRFs (%)

	France	Italy	Spain	Portugal
Low productivity by 2026	0.2	1.5	0.4	1.5
Hig productivity by 2026	0.5	2.5	1.2	2.4
Hig productivity by 2040	0.1	1.1	0.8	0.9
Spillovers	0.2	0.3	0.3	0.5
Reforms by 2040	12	17	10	10

Source: Commissio's assessments of the RRFs.

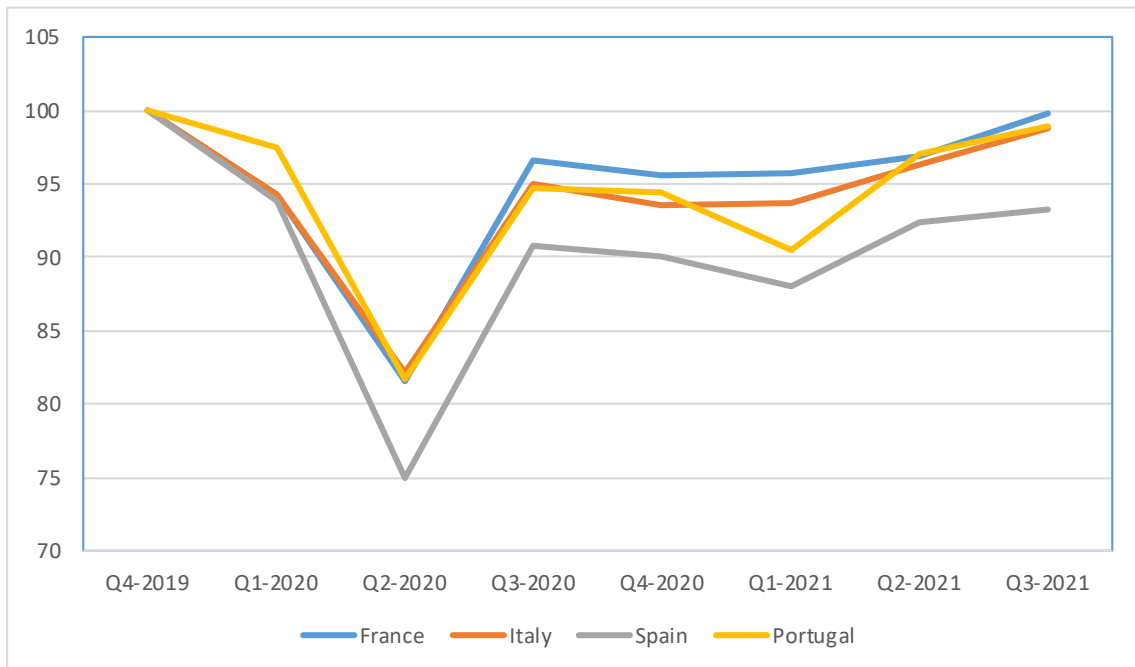
ANNEX 2: FIGURES

Figure 2.1: The global economic impact of COVID-19 (Quarter-on-quarter real GDP growth)



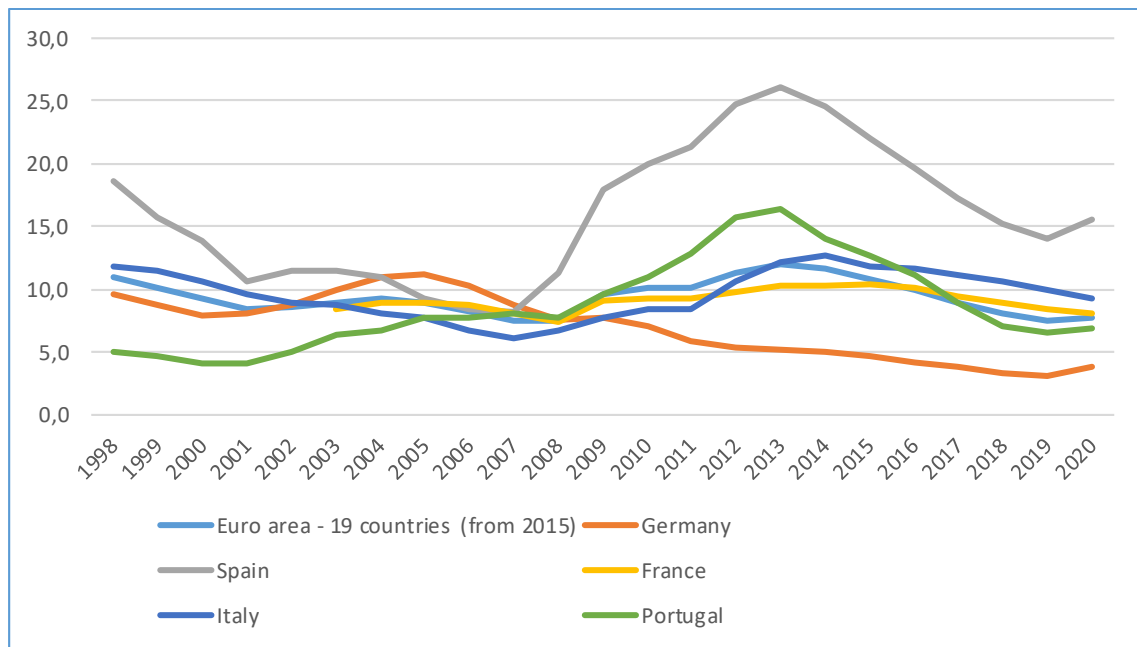
Source: OECD, Economic Outlook, December 2021.

Figure 2.2: recovery FROM the COVID-19 PANDEMIC (quarter-on-quarter real GDP growth)



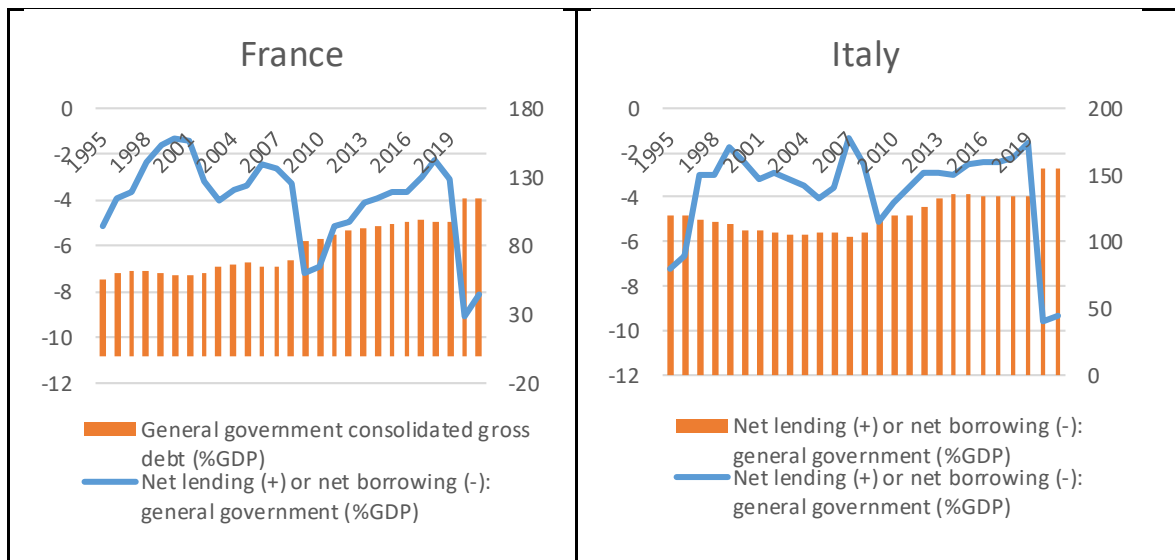
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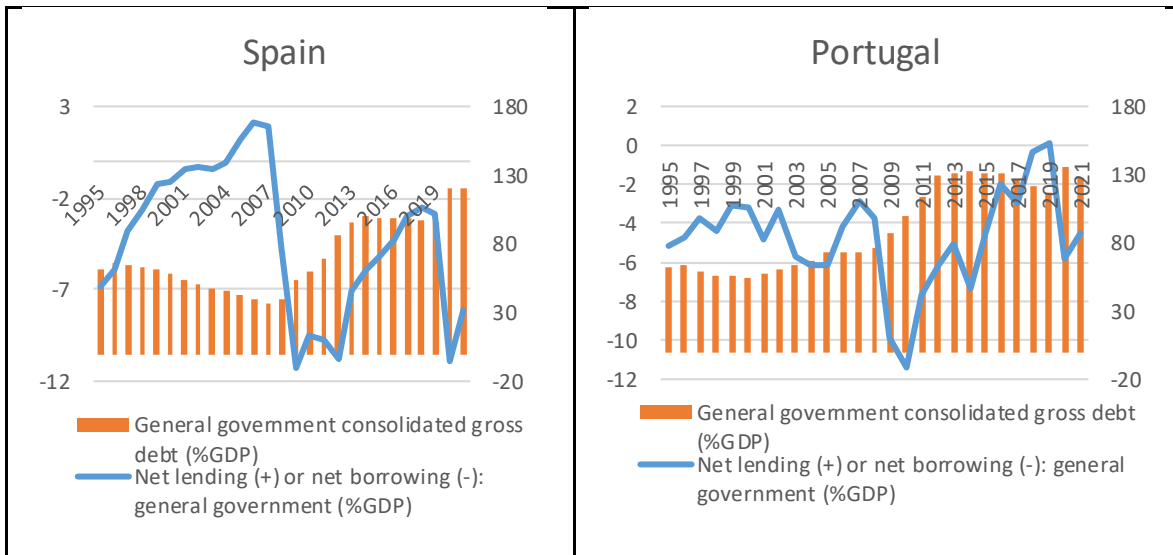
Figure 3.1: Unemployment rate evolution



Source: Eurostat.

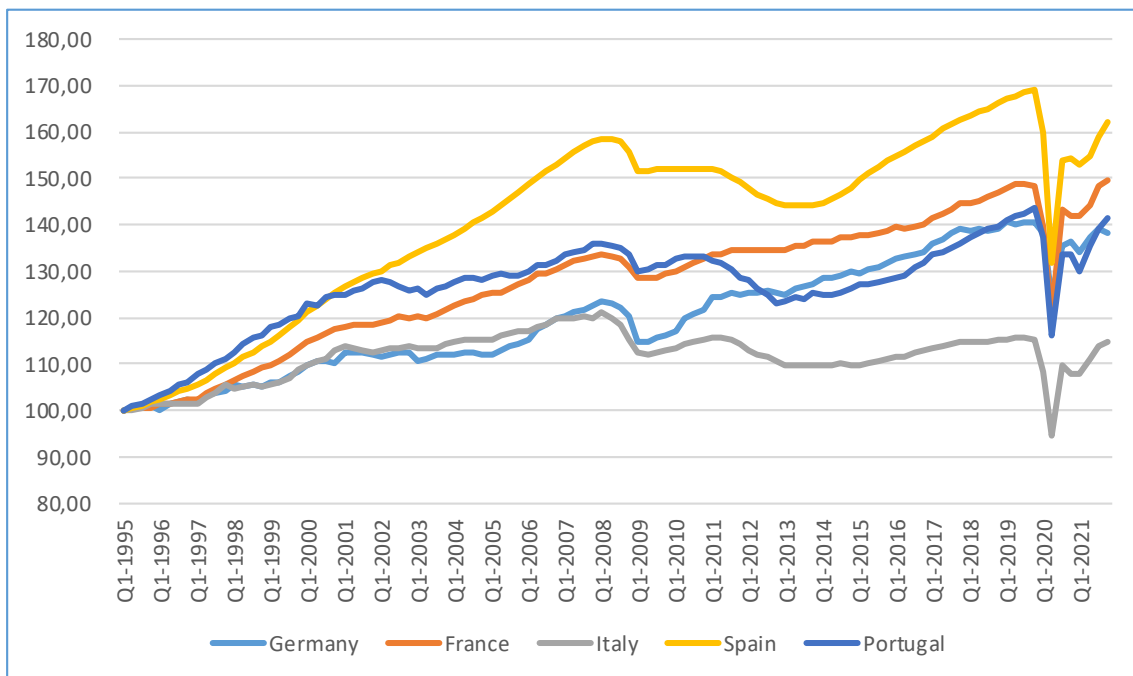
Figure 3.2: Budgetary position





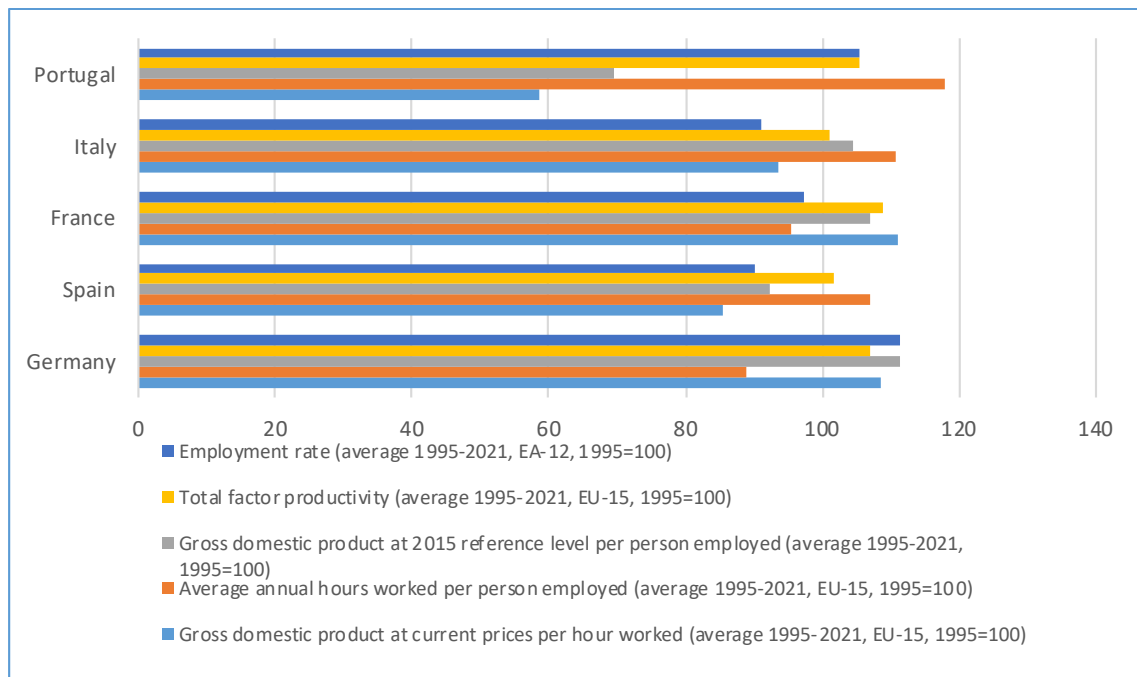
Source: AMECO.

Figure 3.3: Evolution of GDP growth



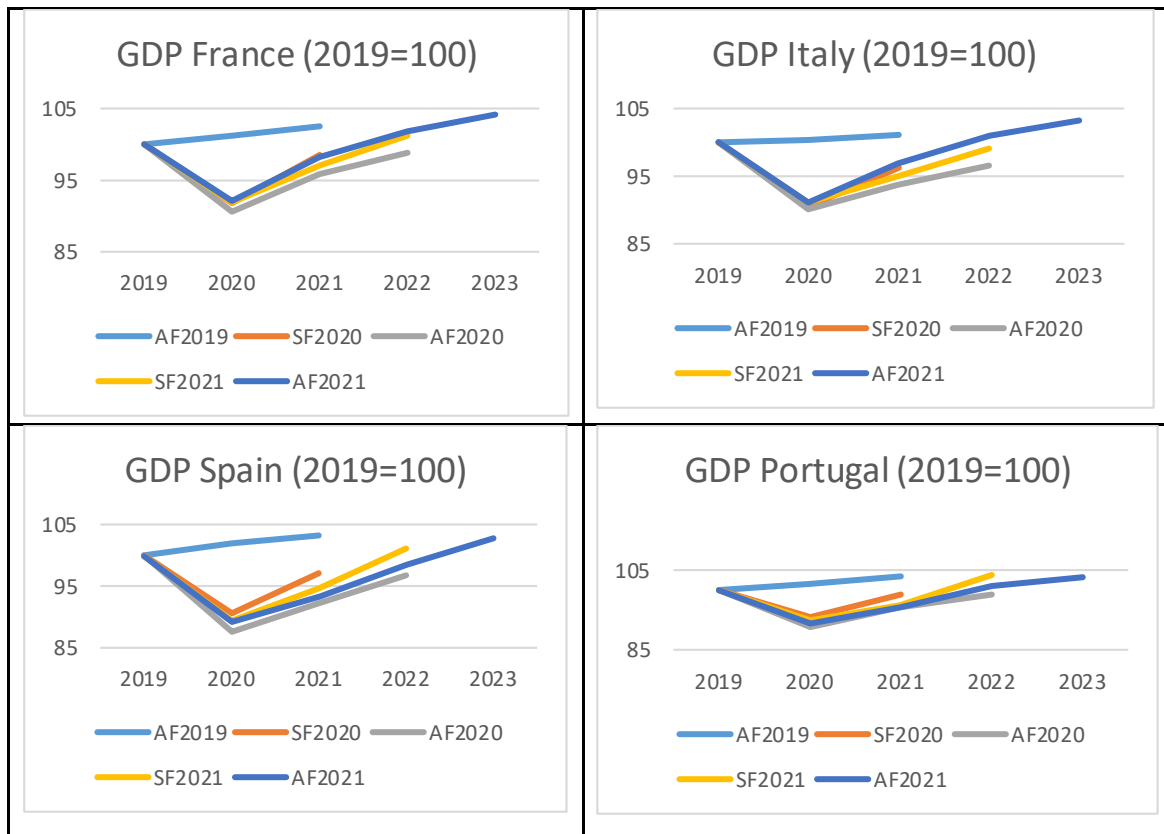
Source: OECD, Economic Outlook, December 2021.

Figure 3.4: Decomposition of productivity



Source: AMECO.

Figure 4.1 Comparing the Commission forecasts for GDP (2019=100), public investment (% of GDP) and structural deficit (% of potential growth)



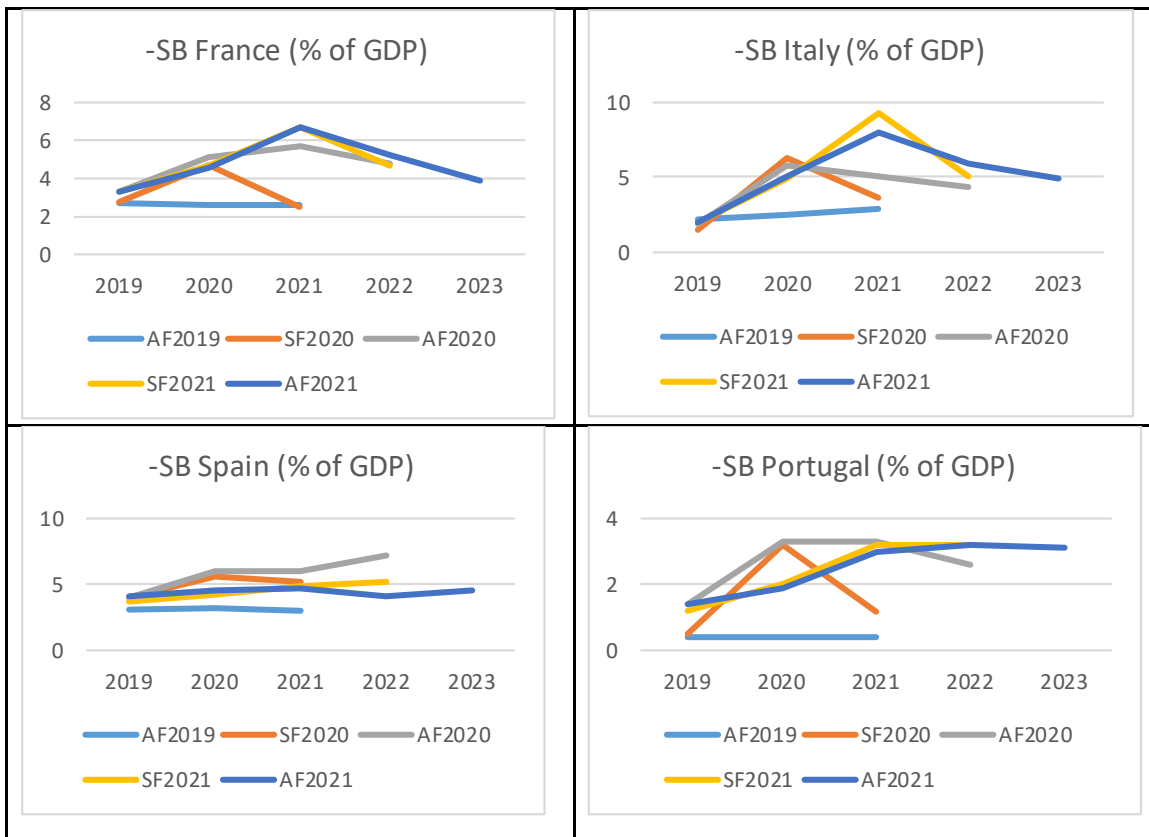
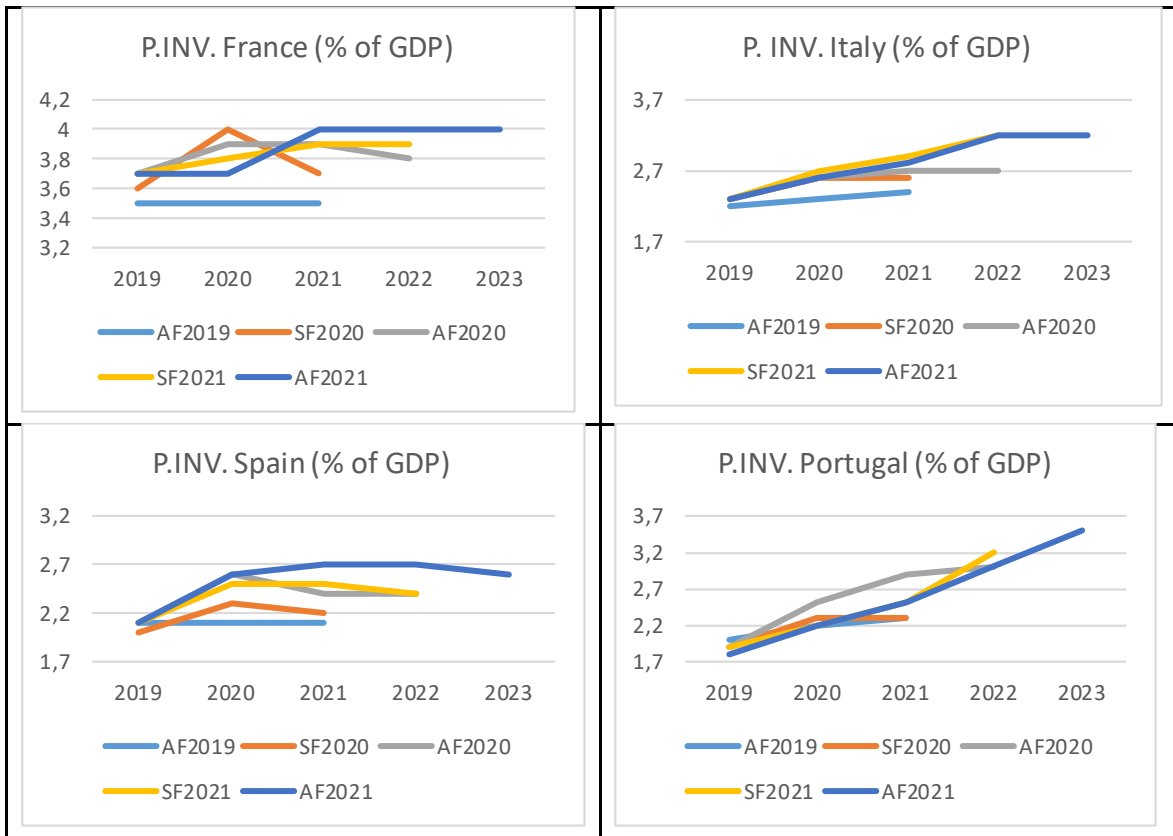
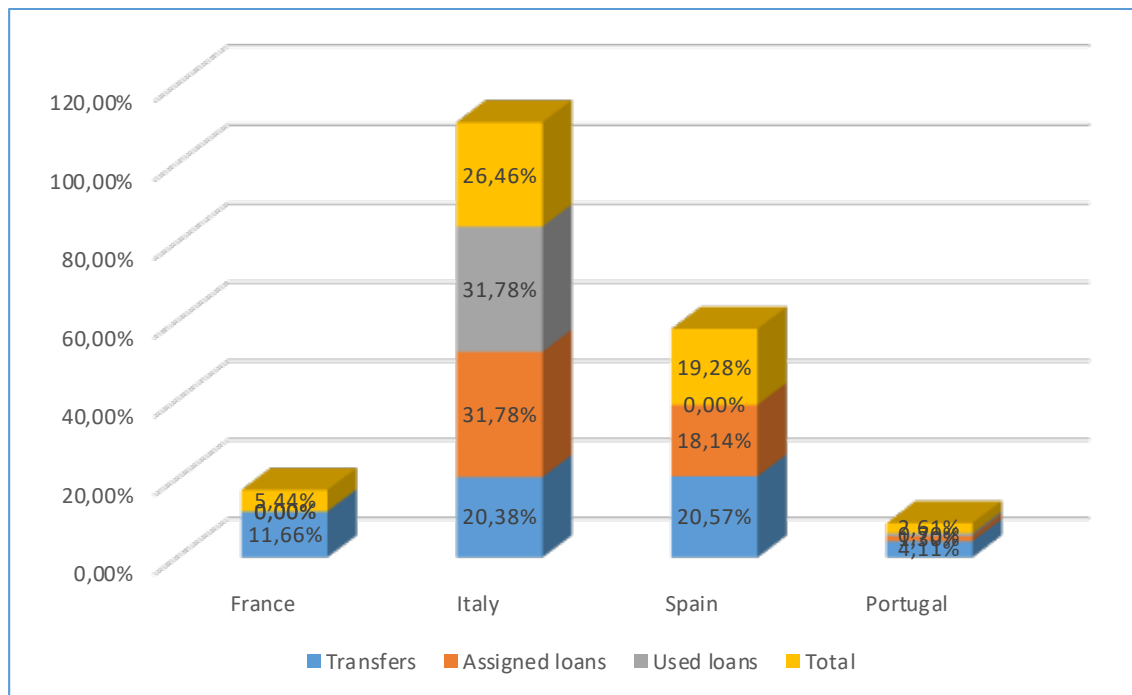
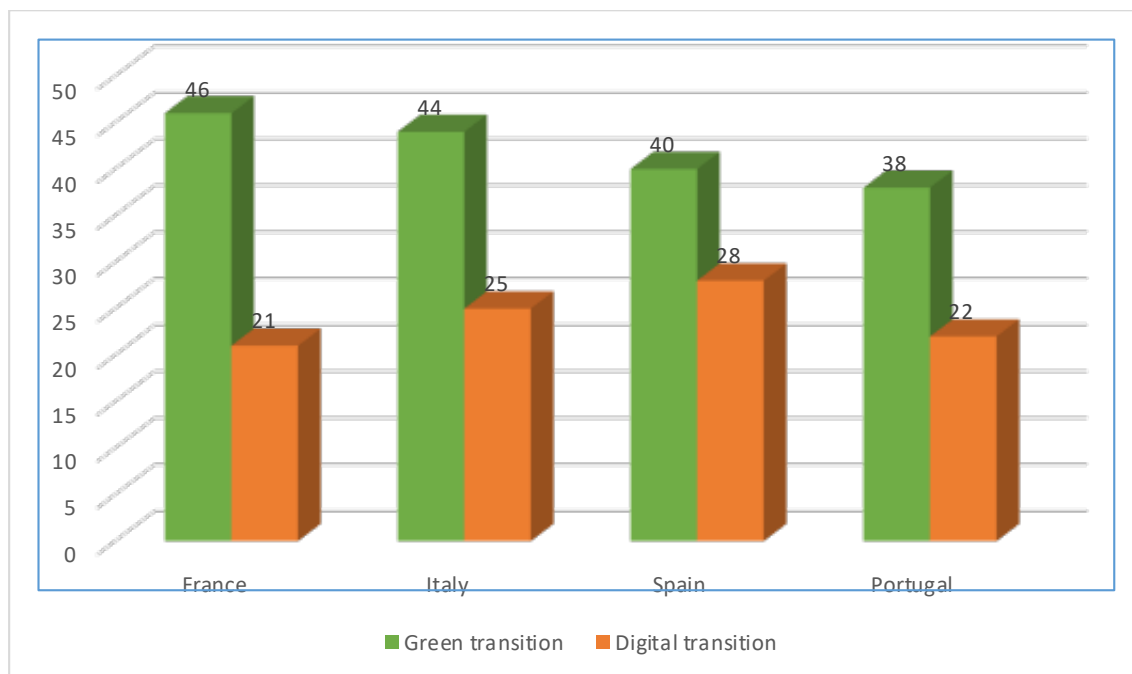


Figure 5.1: Distribution of the RRFs funds by source of funding (% total)



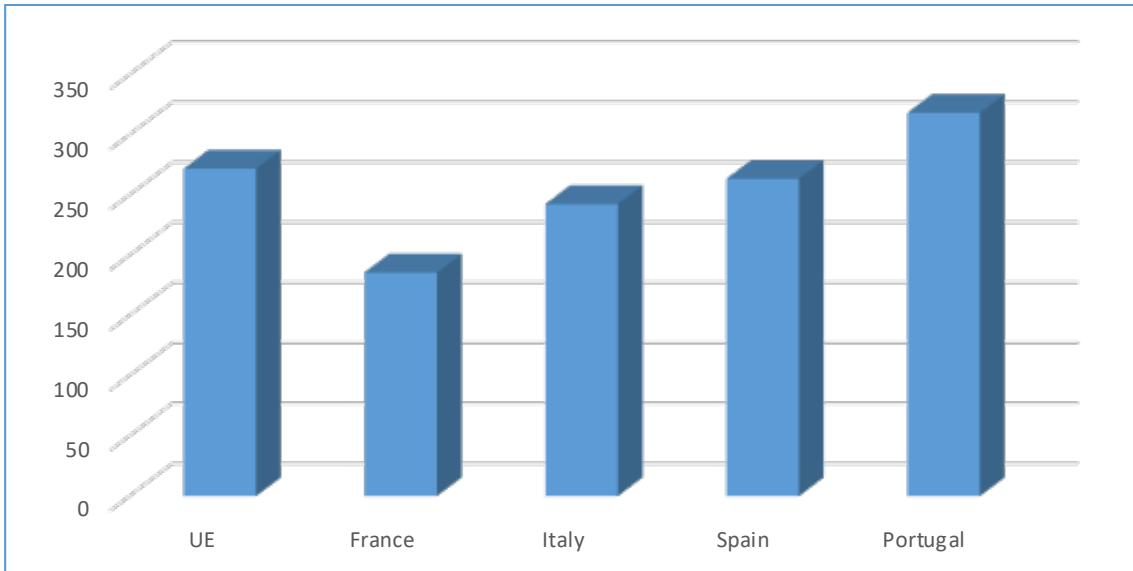
Source: European Commission.

Figure 5.2: Percentage devoted in RRFs to green and digital transitions



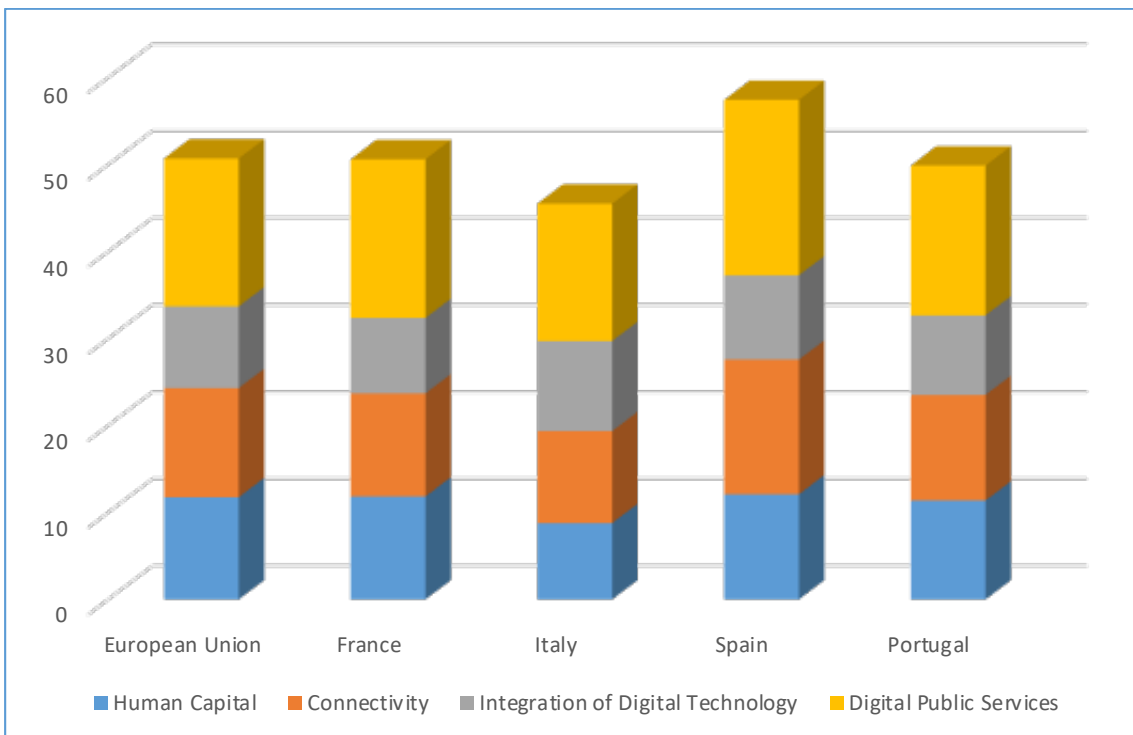
Source: European Commission, Assessment of the recovery and resilience plans.

Figure 5.3: Total greenhouse gas emissions per GDP in 2019



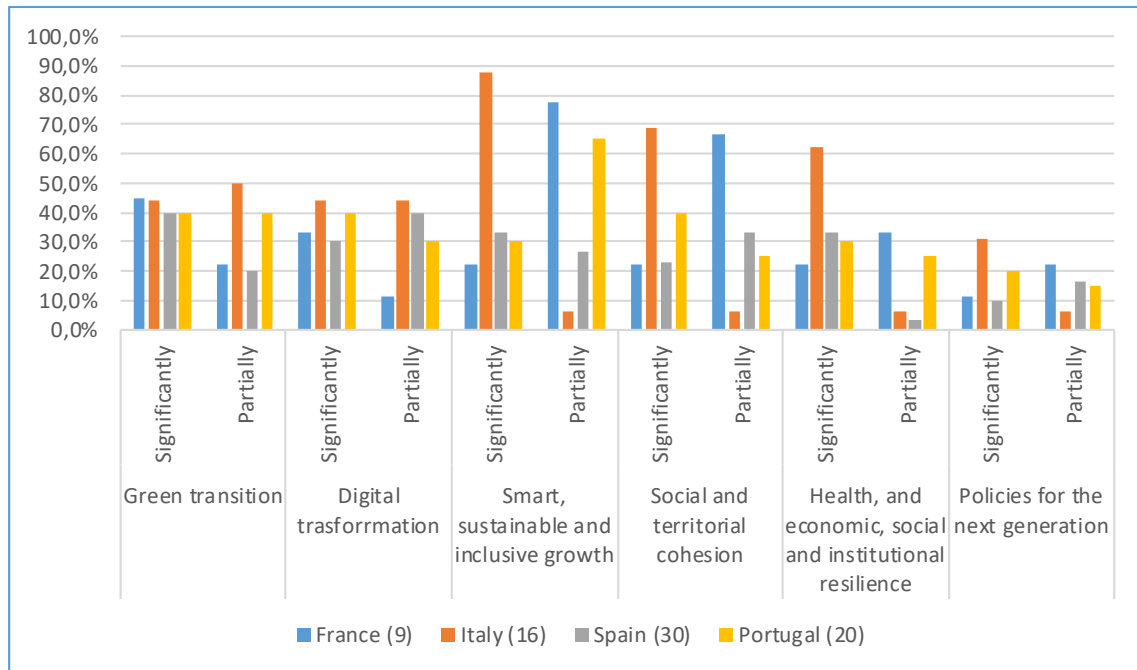
Source: United Nations framework convention on climate change and EU Greenhouse Gas Monitoring Mechanism (EU Member States).

Figure 5.4: Digital Economy and Society Index composite index



Source: DESI composite index.

Figure 5.5: Coverage of the six pillars of the Facility by the RRP components.



Source: Commission Staff Working Document. Analysis of the recovery and resilience plan of France, Italy, Spain and Portugal.

ANNEX 3: COUNTRY FACTSHEETS.

ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: FRANCE

	2017	2018	2019	2020	2021	2022
GDP growth	2.3	1.8	1.5	-7.9	7.0	3.6
Consumer price index (harmonised)	1.2	2.1	1.3	0.5	2.1	2.8
Unemployment rate	9.4	9.0	8.4	8.0	8.0	8.0
General government gross debt (% of GDP)	98.1	97.8	97.5	115.0	114.6	113.7
General government fiscal balance (% of GDP)	-3.0	-2.3	-3.1	-9.1	-8.1	-5.3

Source: Own elaboration based on Eurostat, the European Commission Autumn 2021 Economic Forecast, and the Winter 2022 European Economic Forecast.

Structural challenges

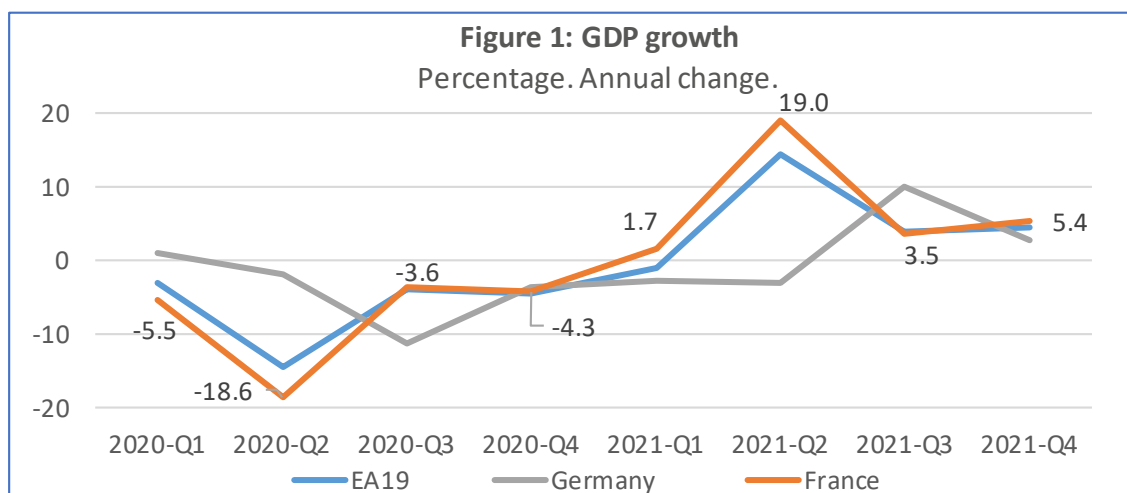
- Unemployment is high, particularly for disadvantaged groups, and the labour market remains highly segmented.
- The high government debt-to-GDP ratio poses significant fiscal sustainability risks for France.
- Although France's productivity is higher than the EU average, productivity growth has been declining for the past 25 years.

The French economy has been hit severely by the COVID-19 pandemic, both in terms of health and economic impact.²⁶ The first case was confirmed on 24 January 2020²⁷. The virus spread quickly. To avoid the spread of the virus, the French government implemented containment measures, including several strict and lengthy national lockdowns. The crisis led to a GDP contraction of 8.9% in 2020 (6.4% in the euro area), the sharpest since the end of the Second World War. France's specialisation in aeronautics and international tourism was disadvantageous given that these two sectors were particularly affected in the context of a global crisis (Banque de France, 2021). During the first and second quarters of 2020, the French GDP contracted by 5.5% and 18.6%, respectively (See Figure 1). A recovery accompanied the reopening of the economy in the third quarter (3.6% in year-on-year terms) and then it again contracted in the last quarter by 4.3%, resulting in an average growth in

²⁶ At the closing date of this report (20/02/2022), France has 32,959 cumulative total cases and 205 deaths per 100,000 population. See <https://covid19.who.int/table>

²⁷ See: <https://solidarites-sante.gouv.fr/actualites/presse/communiques-de-presse/article/trois-cas-d-infection-par-le-coronavirus-2019-ncov-en-france-429100>

2020 of -7.97.0%. In 2021, the French economy grew 7.0%. The easing of COVID-19 restrictions and the vaccination campaign helped to the recovery of pre-crisis levels activity. The growth was specially remarkable in the second quarter (+19.0% in year-on-year terms).. According to the Winter 2022 European Economic Forecast, GDP growth is projected to remain slightly positive in the first quarter of 2022 (+0.1%) and to increase as of the second quarter (+0.6%) in the second half of the year, the improvements in international trade, the recovery of tourism, and the deceleration in inflation could accelerate the economic activity. Annual GDP is forecast to increase by 3.6% in 2022 and 2.1% in 2023.²⁸



Source: Own elaboration based on Eurostat database.

To cushion the effect of the fall in activity on the labour market, the French government implemented strong public support measures, including an expansion of the short-time work scheme, grants for small firms and the self-employed, and public guarantees for bank loans to firms. The budgetary impact of the fiscal package amounts to 3.3% of GDP (European Commission, 2021a).

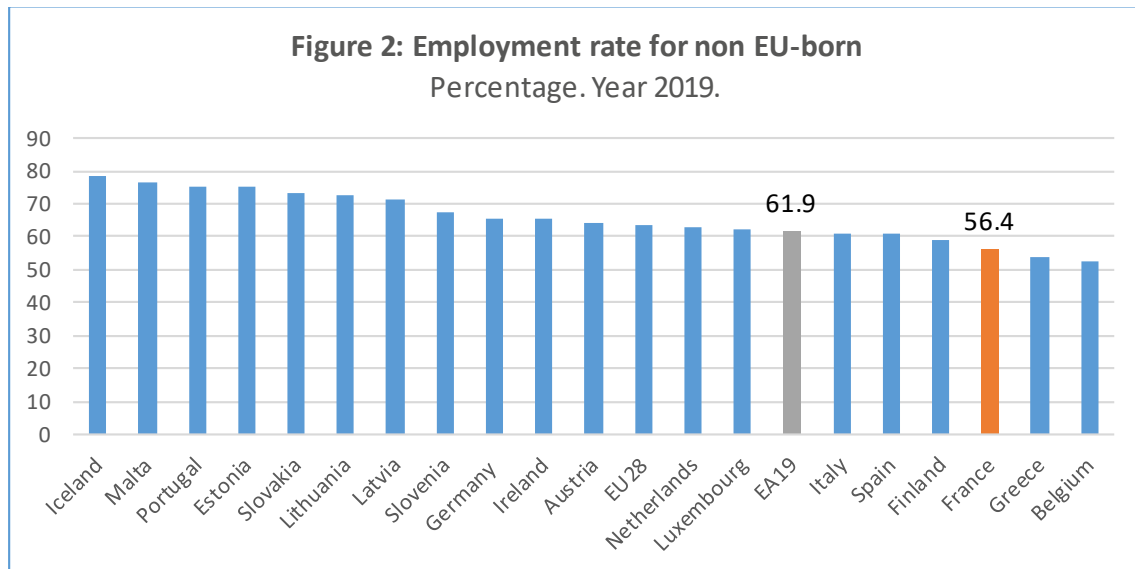
The COVID-19 crisis risks worsening some structural weaknesses of the French economy. Before the pandemic, France was experiencing moderate economic growth. The country faces structural challenges, especially high levels of public debt, a highly segmented labour market and low productivity growth. This is hindering improvements in material living standards. Despite the growth in real wages, both GDP per capita and household purchasing power per unit of consumption have stagnated over the past ten years (OECD, 2019a).

French structural challenges

Unemployment remains high, particularly for disadvantaged groups, and the labour market remains highly segmented. Although labour market developments have been positive in recent years, France faces a structurally high unemployment rate and a strong segmentation of the labour market. These two issues represent historical weaknesses of the French economy. The unemployment rate remained above the EU average, in particular among vulnerable groups such as the low-skilled, young people, people with a migrant background and persons with disabilities (European Commission, 2021a; OECD, 2019). The employment rate for the non-EU born, 56.4% in 2019 (61.9% in the EA), is one of the lowest in the EU (see Figure 2). Furthermore, its labour market is highly segmented: flexibility in the labour market relies mainly on fixed-term and temporary workers. Employees with temporary contracts are less well paid, receive less training and find it difficult to obtain permanent employment

²⁸ Needless to say, due to the change in the geopolitical landscape and the worsening of the energy crisis, such forecasts are subject to significant downside risks and most likely have become obsolete.

(Banque de France, 2017). The transition rate between temporary and permanent contracts, at 11.7%, is also one of the lowest in the EU. This duality between employees on permanent contracts, which has increased in recent years, and temporary employees has a significant economic and social cost. Low-skilled workers, young people, migrants and workers in low- and medium-skilled service sector occupations are disproportionately affected by temporary employment (Eichhorst et al., 2018). Workers employed under fixed-term and temporary contracts experience frequent periods of unemployment. Furthermore, the worse economic conditions could be felt in housing market due, for example, to difficulties in obtaining housing or credit (Banque de France, 2017).



Source: Own elaboration based on Eurostat database.

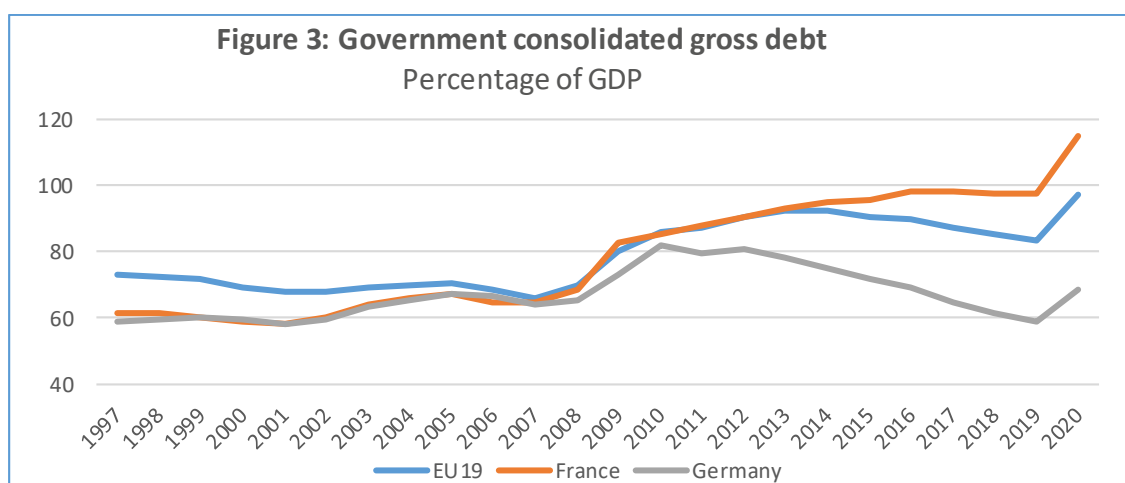
The significant inequalities of opportunities in accessing the labour market can be explained partially by inequalities observed in the educational system. As the European Commission (2021b) highlights, France is facing challenges in improving educational outcomes for vulnerable groups, such as those from lower socio-economic or migrant backgrounds. Educational outcomes are excessively impacted by the socio-economic background of students in France and intergenerational mobility is low in comparison with its peer countries. According to the latest results of the Programme for International Student Assessment (PISA), the variance in students' reading performance explained by their socio-economic and cultural status is 17.5%, the second-highest behind Hungary (12.0% is the OECD average). According to the OECD (2017, 2019a), more disadvantaged children continue to show weaker educational outcomes. Moreover, as the reports highlight schools in poor neighbourhoods have a higher proportion of inexperienced teachers and staff turnover is larger.

Despite positive recent developments, the COVID-19 shock is accentuating the existing structural weaknesses in the French labour market. 284,000 jobs were destroyed between the end of 2019 and the end of 2020 (the first annual decrease since 2012) with a significant drop concentrated in services (French RRP, 2021). Although the measures of temporary short-time schemes largely protected employment the COVID-19 pandemic is aggravating the divide in the labour market, namely, the integration of the most vulnerable groups who yet face numerous obstacles, such as limited work experience, care obligations, low skills or health limitations (European Commission, 2021a; OECD, 2021). The low-skilled, young people, people with a migrant background (especially women), and persons with disabilities had high unemployment rates and their situation further deteriorated in 2020.

The pandemic also increased the dualism of the labour market. Workers on temporary contracts, particularly interim contracts, as well as the self-employed have been particularly affected by the ravages of the crisis. According to the Commission's autumn 2021 forecast, unemployment is projected to stabilise in 2022 at 8.0% of the labour force.

The high government debt-to-GDP ratio poses significant fiscal sustainability risks for France.

Before the outbreak of the COVID-19 crisis, France showed macroeconomic imbalances in the area of public finances. In 2019, France registered a public deficit of -3.1% of GDP (compared to -0.6% of GDP on average in the euro area). France's public debt-to-GDP was 97.5%, one of the highest values before the COVID-19 crisis and noticeably higher than the euro-area average (83.6%). This higher value is not an isolated case. Since 2007, France has registered higher public debt ratios than its peer countries (see Figure 3). While over the period 2015-2019, almost all euro area countries reduced their public debt-to-GDP, in France it increased from 95.6% in 2015 to 97.5% in 2019. Furthermore, France also has a high structural general government deficit. In 2019 the Commission invited France to develop a strategy to gradually reduce its public debt, especially in a context where private debt is also high, public pension spending is among the highest in Europe (14% of GDP) and ageing-related expenditures are expected to increase. According to the Debt Sustainability Monitor (2020), France faces sustainability risks in both the short and the medium term.



The interventions adopted to mitigate the pandemic have had a large impact on French public finances. From a deficit of 3.1% of GDP in 2019, the budget balance of France worsened, turning into a 9.1% deficit of GDP in 2020. According to the European Commission Autumn Forecast, underpinned by the projected strong recovery of the economy, the deficit is predicted to improve moderately in 2022 (5.3%) and 2023 (3.5%). Similarly, public debt has increased markedly during the crisis due to the combined effect of the severe contraction of GDP, large automatic stabilisers and the fiscal stimulus package. The debt-to-GDP ratio increased from 97.5% in 2019 to 115.0% in 2020. It is expected to decrease slightly to 114.6% of GDP in 2021 and 113.7% in 2022. However, the debt-to-GDP ratio will remain high, and the country faces a high fiscal sustainability risk both in the short and medium-term (European Commission, 2021e).

Although France's productivity is higher than the EU average, productivity growth has been declining for the past 25 years. Aggregate productivity in France is higher than the OECD and EU averages. However, since the beginning of the 2000s productivity growth has decreased as in most advanced economies (Bergeaud et al., 2016; OECD 2018, 2019a). The slowdown can be partially explained by structural factors such as the tertiarisation of the economy. While productivity has grown in the manufacturing industry, it has stagnated in service sector (OECD, 2019b). The stabilisation of the contribution of information and communication technologies (ICTs) to potential growth has been

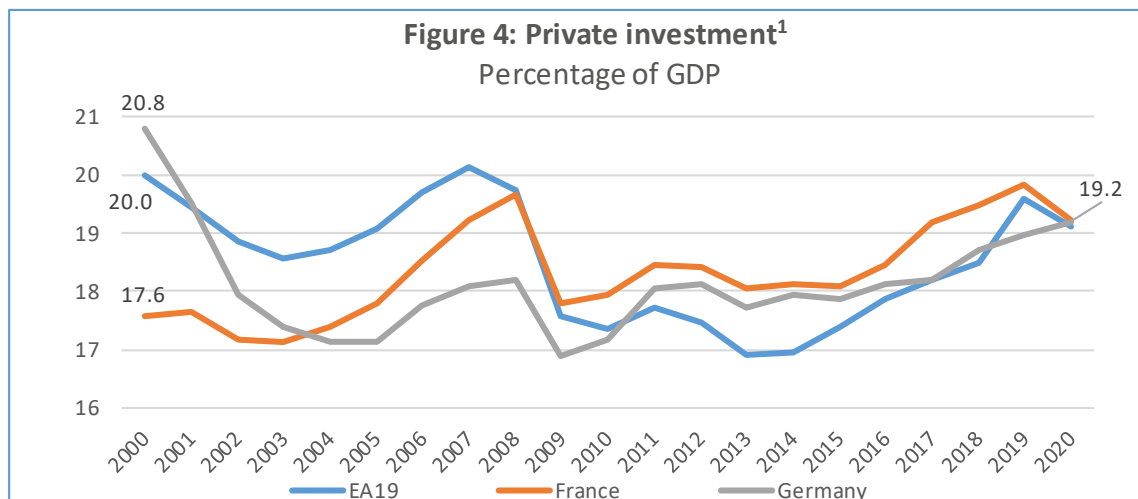
identified as a determinant of the decrease (Cette et al, 2015). According to the OECD (2019), the slowdown also reflects the specificities of the French economy, particularly the progressive absorption of low-skilled workers in the labour market resulting from active employment policies. Moreover, as the report points out, weak competition, the complexity of the tax system, the rigidity of the labour market, and skills mismatch are hindering productivity growth.

The pandemic and the associated containment measures have had effects on aggregate labour productivity growth. COVID-19 has been an unprecedented shock. In France, as in most countries, it has induced a large contraction in GDP with asymmetric effects across sectors of the economy, with those sectors characterised by relatively low labour productivity and which involve face-to-face contact (such as hospitality, tourism, personal and domestic services) being the most affected. In 2020, the average growth in annual real GDP per hour worked rose to 0.3% (1.3% in the euro area) during this period, while real GDP and total hours worked declined by annual averages of 8.9% (-6.5 in the euro area) and 8.1% (-7.8 in the euro area) respectively. This increase in average productivity²⁹ could be explained by a “composition effect” as low-productivity sectors are more heavily affected. Labour markets and firms were asymmetrically damaged by the crisis, with small firms and their workers bearing the brunt of the fallout from the pandemic. However, this composition effect is not expected to be permanent (NPB, 2021). The shock has also led to a reorganisation of production processes. This could result in increased intermediate costs and higher unit costs. For example, some firms (especially in face-to-face activities) have had to reduce the production capacity in order to keep the social distancing rules.

While French investment is high compared to other European and OECD countries, the trend over at least the last few years is not favourable (Cerniglia & Saraceno, 2020). Since the crisis of 2008, France like other European countries has registered a stagnation in investment rates. While shares have started to increase again in 2015, the country has not yet reached pre-financial crisis levels. Between 2007 and 2019, the total investment ratio on GDP declined by 0.30 percentage points (-1.0 in the euro area). Weak investment could hurt growth and competitiveness (Baldi et al., 2014) and have a substantial impact on the capital stock, hindering growth potential, productivity, employment levels, and job creation.

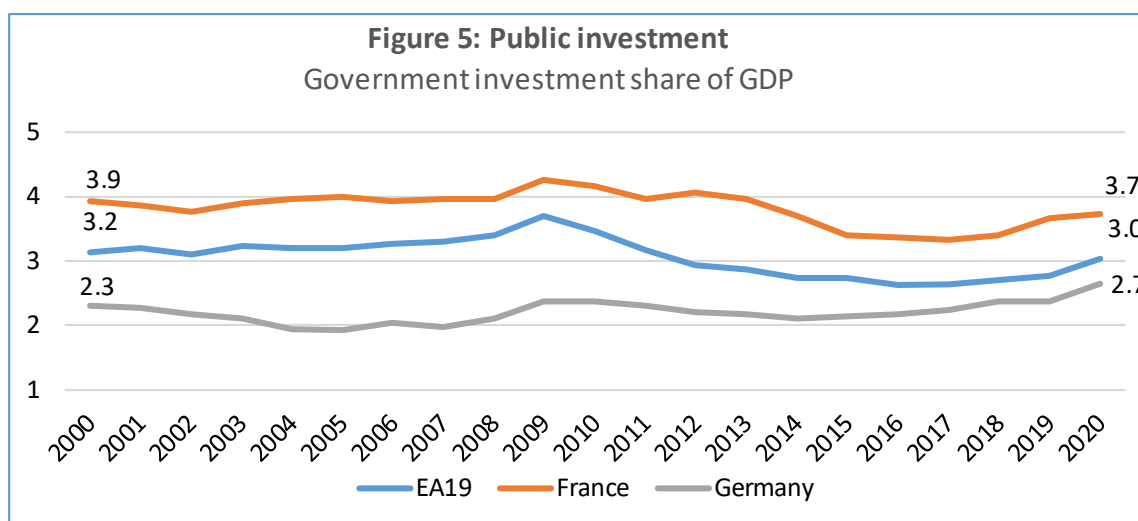
While the COVID-19 pandemic led to a drop in the total investment share of GDP, the French government has taken measures to support the recovery. The implementation of the France Relance recovery plan (EUR 100 billion, EUR 41 billion of which is financed with funds from the Recovery and Resilience Facility) is expected to boost private and public investment. Higher public investment in infrastructure, digitalisation, and training programs could improve productivity and resource reallocation (OECD, 2019a).

²⁹ This productivity growth is also observed in the euro area and developed economies. For an analysis of the effect of the COVID-19 pandemic on productivity growth, see the article entitled “The impact of the COVID-19 pandemic on labour productivity growth” Economic Bulletin, Issue 7, ECB, 2021. “https://www.ecb.europa.eu/pub/economic-bulletin/focus/2021/html/ecb.ebbox202107_04~c9050e1d70.en.html”,



Source: Own

elaboration based on Eurostat database. ¹Private investment is calculated as the total investment of all sectors minus public investment.

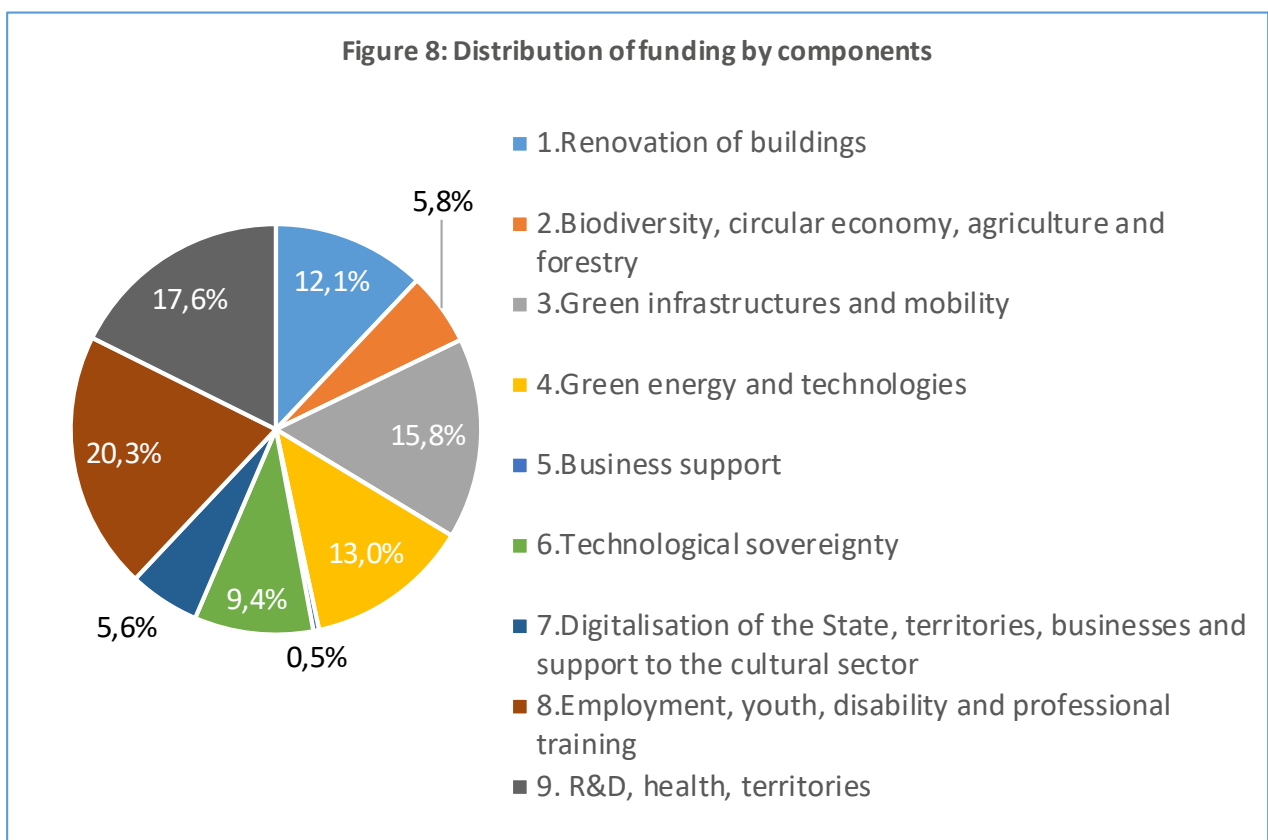
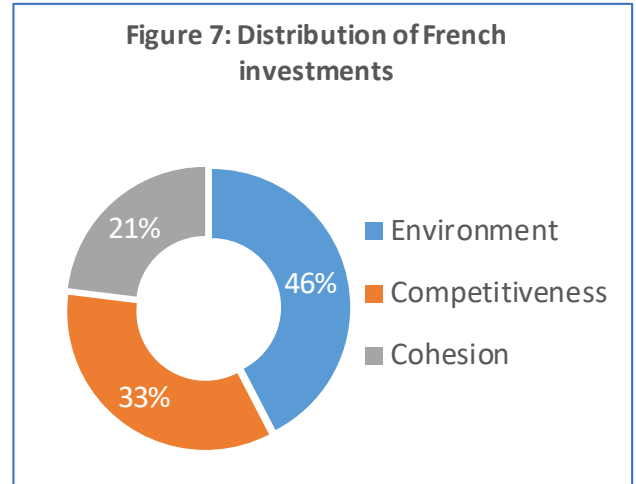
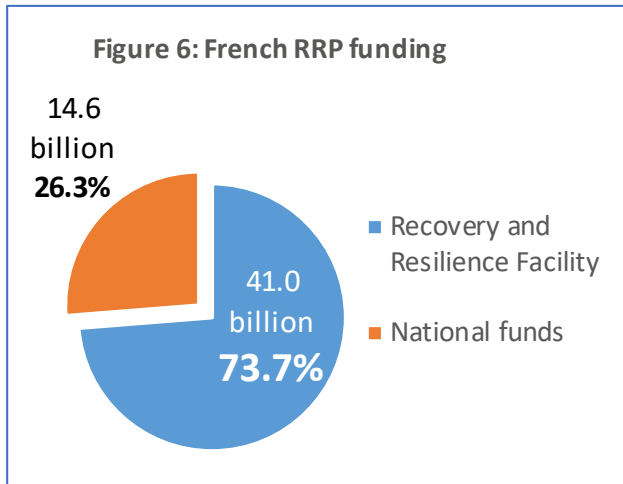


THE FRENCH NATIONAL RECOVERY AND RESILIENCE PLAN

The recovery plan's structure

The French Recovery and Resilience Plan amounts to EUR 55.6 billion. The financial contribution allocated to France under the Recovery and Resilience Facility is EUR 41.0 billion in non-repayable financial support (6.1% of a total of EUR 672.5 billion). France has not yet requested any loans.

The Plan primarily covers the six pillars structuring the scope of applications to the Facility (European Commission, 2021a): i) green transition, (ii) digital transformation, (iii) smart, sustainable and inclusive growth, (iv) social and territorial cohesion, (v) health and economic, social and institutional resilience, and (vi) policies for the next generation. The measures to cover these pillars are organised into nine components, which include 70 investment projects and 22 reforms.



Source: Own elaboration based on French RRP and European Commission.

The plan's governance

The implementation and monitoring of the measures of the French RRP are carried out at the highest level, with the support of all the services involved. To ensure its appropriate implementation, the recovery and resilience plan has been put into practice under the dual authority of the Prime Minister and the Minister of Economy, Finance and Recovery (European Commission, 2021a). They will monitor the implementation of each measure in close contact with the prefects of the regions and the officials of each ministry. The Directorate-General for the Treasury, the Budget Directorate, the Directorate-General for Public Finance and the Social Security Directorate will also monitor the plan. Specific reforms will be monitored by each of the ministries concerned. At a regional level, monitoring committees are in charge of monitoring progress on projects in the regions. Information on the

progress of each measure must be submitted on a monthly basis to the “General Secretariat in charge of the Recovery Plan” (the “Recovery Secretariat”).

The Plan’s impact on the GDP

According to estimations of the French RRP based on the Mésange Model, the economic impact of the Next Generation EU in France could lead to an increase in GDP of between 1.1% and 0.6% by 2024 (See Table 1).³⁰ Cross border (GDP) spillovers account for 0.4% in 2024, showing the value-added of synchronised expenditure across the Member States. Even assuming that half of the expenditure is not productive, the RRP would still lead to a significant impact. By 2030, GDP could be 0.8% higher. As indicated in the Plan, in the short term the public investment effort will accelerate the recovery, returning to the pre-crisis level of activity in 2022. (In the short and medium-term, supply-side measures should increase the pace of potential growth through an increase in the stock of physical capital, human capital and productivity - (Gouvernement Français, 2021).

Table 1: Annual impact on GDP of the Recovery Plan (in %). Differences compared to a scenario without Recovery Plan.

	2021	2022	2023	2024	2025	2030
Baseline scenario	1.1	1.0	0.6	0.6	0.5	0.8

Source: French RRP

ASSESSMENT OF THE MEASURES IN THE FRENCH PLAN TO ADDRESS STRUCTURAL CHALLENGES

Assessment of the measures to address high unemployment and labour market segmentation

Employment and social interventions are included in component 8. The plan allocates EUR 11.3 billion to this component, 20.3% of the total RRP.

The Plan proposes investments targeting youth employment (EUR 4.5 billion), professional training (EUR 1.7 billion) and the employment of persons with disabilities (EUR 58 million). Apart from projects to promote apprenticeship programs and the training of employees in short-time work schemes, the RRP envisages measures to support workers through access to training, in line with pre-identified skills needs, thus increasing their mobility in the labour market. In the case of youth, the plan includes subsidies for companies hiring young people under 26 years old. To address inequalities in education the Plan proposes different measures: renovation and creation of further places in boarding schools for excellence, creation of places for the continuation of studies for young baccalaureate holders, assistance to mobilize employers to hire disabled workers, an exceptional extension of the supported employment scheme, the prevention of early school leaving and the provision of academic guidance. To help alleviate the financial constraints on higher education students, the plan includes an increase in State-guaranteed student loans. Regarding the measures to reduce the dualisation of labour market, the unemployment insurance reform introduces a modulation of the contributions (called “bonus-malus”) to fight against the excessive use of short contracts. This measure gives employers a bonus if they hire on a permanent basis and incurs a malus if they hire on a temporary contract basis.

The RRP presents the investments in detail, including terms of implementation, cost estimation, technical description of the measures, the timeline, and the authorities responsible for its performance.

³⁰ These results cannot be directly compared to the numbers reported in the European Commission Assessment of the French plan given that there are differences in the assumptions and methodology. For more details about the different estimations on the impact of the RRP, see section 4.2.1. “The results of some simulation exercises on the economic impact of the NGEU” of this report.

They are appropriate for the objectives targeted and consistent with the recommendations carried out by the European Commission. However, as the Commission's Assessment notes, while the program includes a strong target on reducing unemployment among the young, concerns might emerge over addressing unemployment for other vulnerable groups such as people with a migrant background, women, low-work intensity or single-parent households. Moreover, concerns also emerge regarding the dualism issue. The intervention proposed may not be sufficient to solve the problem. Moreover, concerns also emerge regarding the dualism issue. The intervention proposed may not be sufficient to solve the problem.

Assessment of the measures to improve public finances

The RRP presents two reforms to improve public finances (Gouvernement Français, 2021). They are included in component 7. The first reform introduces a multiannual expenditure rule to ensure consistency between the annual budget bills and the multi-year objectives. It aims to facilitate the adoption and implementation of fiscal policies ensuring long-term sustainability. The expected date of completion of the measure is 2023. The second reform focuses on the evaluation of the quality of public expenditure to achieve savings and efficiency gains. According to the plan, the intervention will include stock-taking of the outcome of the reforms on the effectiveness of public action over the Presidential term, the publication of an audit report on public finances by the Court of Audit, and the inclusion of the evaluation of public expenditure in upcoming budgetary laws. The assessment of the quality of public spending will be made a regular practice and will be assessed annually. The expected date of completion of the measure is 2025.

The RRP describes the two reforms in detail, which are appropriate for the objectives targeted and consistent with the recommendations set out in the CSRs. The plan includes the objectives, technical description, and the expected implementation of the reforms, and the related indicators. However, as the assessment of the European Commission points out, the contribution of these reforms to debt reduction in the medium to long term will depend on the ambition of the expenditure rule and of the evaluation of spending. If they are implemented successfully, these reforms should provide a larger fiscal margin. However, the plan does not include any reform of the French pension system, which is an important and contentious issue that weighs on the sustainability of public finances.

Assessment of the measures to face the green transition

Despite all the efforts made in recent years, France is still falling short of its targets for reducing greenhouse gases. Even though it is one of the countries with the lowest greenhouse gas emissions - due mainly to its predominantly nuclear electricity generation capacity and relatively strong electrification - the pace of the reduction of greenhouse gas emissions is concerning. With the new European commitments for 2030, the European Commission has proposed a target for France of -47,7% compared with 1990 (OECD, 2021). Neither is the current pace of renewable energy deployment enough to meet 2030 targets. In 2019, the share of renewable energy consumption was 11.33% while the target for 2020 was fixed at 23% and for 2030 at 33%. Household waste volume in France is high, while its recovery rate remains lower than in its peer countries. France also faces major challenges in decarbonising and upgrading the energy performance of its building stock, which represents 45% of final energy consumption and 25% of greenhouse gas emissions (European Commission, 2021).

In this context, the French plan allocates a significant portion of the budget to the green transition. In particular, the French plan's contribution amounts to 46% (EUR 20.2 billion) with four components dedicated to environmental and climate action. This exceeds the minimum of 37% required by the RRF Regulation, being one of the plans with the highest climate content (Bruegel, 2021). Most of the

measures included under the environment priority of the *France Relance* plan are included in the French RRP.

Among the various green measures proposed, the plan highlights the measures related to supporting biodiversity protection and decarbonisation. In particular, the “Climate and Resilience law” aims to contribute to the greenhouse gas emissions reduction target for 2030, the law on circular economy and the renovation of buildings reforms to promote energy efficiency. Moreover, the plan presents an investment proposal to support the SNCF (the biggest measure with EUR 4.39 billion), the body which administers the railway infrastructure, to modernise the French railway network. The plan also includes a specific focus on decarbonised hydrogen, promoting the production of hydrogen from renewable energy or low-carbon hydrogen from the electricity grid. Moreover, the RRP highlights the plan’s compatibility with other European initiatives and funds, such as industrial decarbonisation projects and the hydrogen strategy. Cooperation between the other Member States is also identified (for example the Important Project of Common European Interest (IPCEI) on hydrogen between France and Germany).

According to the European Commission Assessment of the RRP (2021a), the green pillar is well covered by the Plan. The proposed actions are in line with the orientations set by the European Green Deal and most measures are expected to have a lasting impact on the green transition. The green Pillar has received an A rating. However, as Berghmans (2021) notes, the plan only covers the investments over the next two years. Therefore, the extent to which the French NRPP contributes to climate objectives will depend on investments over the long term.

Assessment of the measures to face the digital transition

France ranks 15th of the 27 Member States in the 2021 edition of the European Commission’s Digital Economy and Society Index (DESI). Although the country is in line with the EU average in most areas of the DESI (see Table 2), the gap with the EU front runners persists (European Commission, 2021e). The area where France performs worse is connectivity. Although the country has registered a significant improvement in recent years, fixed high-capacity networks and fast broadband (next-generation access) are still below the EU average and rural coverage remains low (18.4% against the 27.8% EU average).

Table 2: France in the 2021 edition of the European Commission’s Digital Economy and Society Index (DESI). Relative performance by dimension.

	France Rank	France Score	UE Score
Overview	15	50.6	50.7
Human capital	14	47.4	47.1
Connectivity	17	47.4	50.2
Integration of Digital Technology	19	34.8	37.6
Digital Public Services	13	73.0	68.1

Source: Own elaboration based on European Commission (2021e) report.

In this context, the French RRP assigns 21.32% of the plan’s total, exceeding the target of 20% (European Commission, 2021). Digital transition measures will also be complemented by national resources as part of the *France Relance* plan. Among the measures, it highlights the digitalisation of the health system, the support for key digital technologies such as cybersecurity, the cloud, quantum and 5G in the private and public sectors, and the territory’s digitalisation. Measures to extend optic fibre

should improve connectivity, especially in rural areas and the outermost regions. The plan also provides investments supporting the digitalisation of firms (in particular SMEs) and strengthening key digital capacities. According to the plan, the country will also participate in two Important Projects of Common European Interest (IPCEIs). One involves the areas of cloud and edge computing and the other covers microelectronics and communication technologies.

The RRP presents most of the investments, the timeline of the different projects and reforms, and the authorities responsible for their implementation. According to the European Commission Assessment, the Plan addresses the main digital challenges and has the potential to contribute to the attainment of the Digital Decade targets and the digital government commitments under the Berlin Declaration on Digital Society and Value-based Digital Government. In this area, France has received a rating of A as defined in the NGEU regulations.

Summary assessment

According to the Commission's Report to the European Parliament and the Council on implementing the Recovery and Resilience Mechanism, France submitted its operational agreement to request its first payment application on 26 January 2022 (European Commission, 2022). The French RRP received the Commission's positive opinion on 21 February 2022. The report considers that the French government addresses the six pillars adequately to be considered for the Recovery and Resilience Facility. The most relevant contributions mentioned in the report include, among others, the proposals to accompany small and very small enterprises in the ecological transition and energy renovation (pillar 3: smart, sustainable and inclusive growth), the measures to deal with youth unemployment (pillar 4: social and territorial cohesion) and the reforms to improve the public finances such as the reform aims to establish a multi-annual expenditure rule and the assessment of the quality of public expenditure (pillar 5: health, and economic, social and institutional resilience).

The French RRP addresses the French challenges with broad measures and targeted investments. The plan presents the actions in detail, including implementation, cost estimation, technical description, the timeline, and the authorities responsible for its performance. The proposed interventions can be expected to be implemented with a positive impact on the French economy. Of particular relevance are the measures presented to support the green transition, which represents a significant proportion of the funds. However, we observe that some structural challenges could remain unresolved. In particular, some doubts arise in the labour market and educational proposals. They are appropriate for the objectives targeted and consistent with the recommendations carried out by the CSRs. However, while the program includes a strong target on reducing unemployment among the young, concerns might emerge over addressing unemployment for other vulnerable groups such as people with a migrant background, women, low-work intensity, or single-parent households.

Another concern is the impact of measures aiming to improve public finances. The RRP describes the two reforms (multiannual expenditure rule and the reform targets to enhance the evaluation of the quality of public expenditure) in detail, which are in line with the recommendations set out in the CSRs. However, as the assessment of the plan carried out by European Commission points out, the contribution of these reforms to debt reduction in the medium to long term will depend on the ambition of the expenditure rule and of the evaluation of spending. Moreover, it is important to note that the plan does not include reforms regarding the French pension system (an important and contentious issue that weighs on the sustainability of public finances).

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ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: ITALY

	2017	2018	2019	2020	2021	2022
GDP growth	1.7	0.9	0.4	-8.9	6.5	4.1
Consumer price index (harmonised)	1.3	1.2	0.6	-0.1	1.9	3.8
Unemployment rate	11.2	10.6	10.0	9.2	9.8	9.3
General government gross debt	134.2	134.4	134.6	155.6	154.4	151.4
Government deficit/surplus	-2.4	-2.2	-1.5	-9.6	-9.4	-5.8

Source: Own elaboration based on Eurostat, the European Commission Autumn 2021 Economic Forecast and Winter 2022 Economic Forecast.

Structural challenges

- Low productivity and high-debt GDP are constraining Italian growth.
- High structural unemployment and low market participation remain serious concerns, especially for young people and women.
- Social and regional disparities persist and remain among the highest in Europe.
- Despite recent reforms, the public administration and justice system's performance and effectiveness are less efficient than in peer countries.

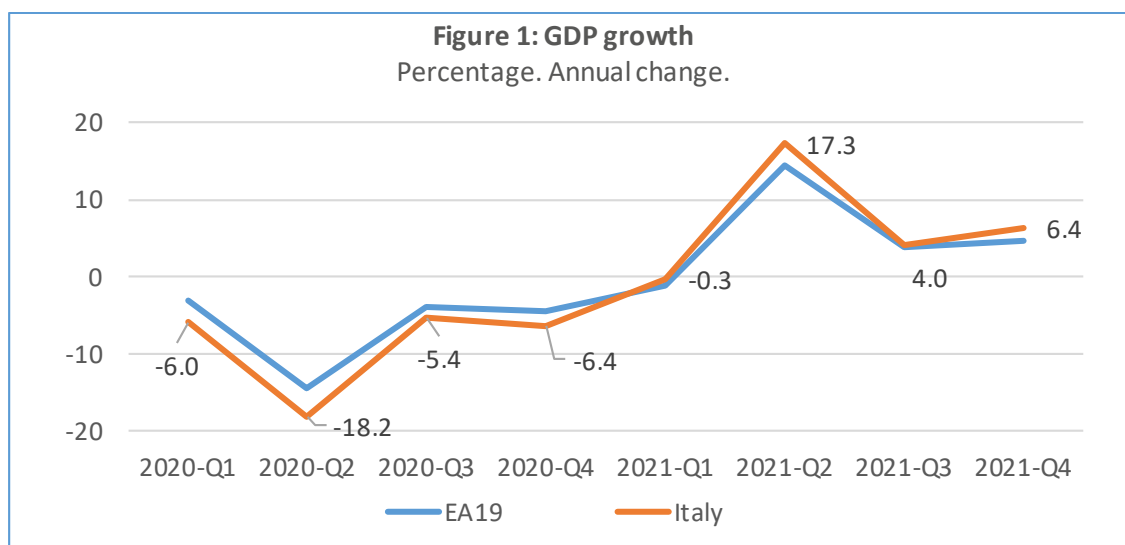
Italy is one of the euro area countries worst affected by the COVID-19 pandemic in health and economic terms.³¹ The first COVID-19 case was confirmed on 30 January 2020.³² On 20 February 2020, an outbreak of COVID-19 infections was detected in Codogno (Lombardia). Within 15 days, cases had been confirmed in most of the Italian provinces and the epidemic quickly started to emerge in the rest of Europe. In response to the COVID-19 pandemic, and the absence of medical and pharmacological solutions, on 9th March the Italian government imposed severe mobility restrictions across the entire country in an attempt to stop the spread of the coronavirus.³³ The impact of the first and subsequent lockdowns (one of the strictest in Europe) was severe (see Figure 1) and was manifested through various channels: the reduction in global economic activity, exports and tourist flows; the decline of consumption; and the effect of uncertainty on investment by companies (Banca d'Italia, 2021). In 2020,

³¹ At the closing date of this report (20/02/2022), Italy has 20,662 cumulative total cases and 255 deaths per 100,000 population. See <https://covid19.who.int/table>

³² See: <https://www.salute.gov.it/portale/nuovocoronavirus/dettaqlioNotizieNuovoCoronavirus.jsp?lingua=italiano&menu=notizie&p=dalministero&id=4035>

³³ Decree of the President of the Council of Ministers 9 March 2020, "Further implementing provisions of the decree-law 23 February 2020, n. 6, containing urgent measures regarding the containment and management of the COVID-19 epidemiological emergency, applicable throughout the national territory". Available at: www.gazzettaufficiale.it/eli/id/2020/03/09/20A01558/sg

Italy's GDP dropped 8.9% (6.4% in the euro area). The Italian GDP composition can partially explain such a pronounced impact: contact-intensive services, the most affected activities during the lockdowns³⁴, account for a relatively large proportion of the economy compared to other large European countries (the share of highly constrained activities in terms of total output in 2019 in Italy was 39% and in EU27 was 33.4%). Moreover, tourism (one of the most seriously affected activities) accounts directly for about 6% of GDP and indirectly 13% of GDP (OECD, 2021:16).



Source: Own elaboration based on Eurostat.

The Italian fiscal response to the consequences of the pandemic was substantial.³⁵ The impact of these policies on the public budget amounted to 4.5 % of GDP in 2020 (European Commission, 2021). Key measures adopted included, among others, funds to strengthen the Italian health care system and civil protection, measures to preserve jobs and support the incomes of laid-off workers and the self-employed, and measures to support businesses (tax deferrals and loan guarantees).

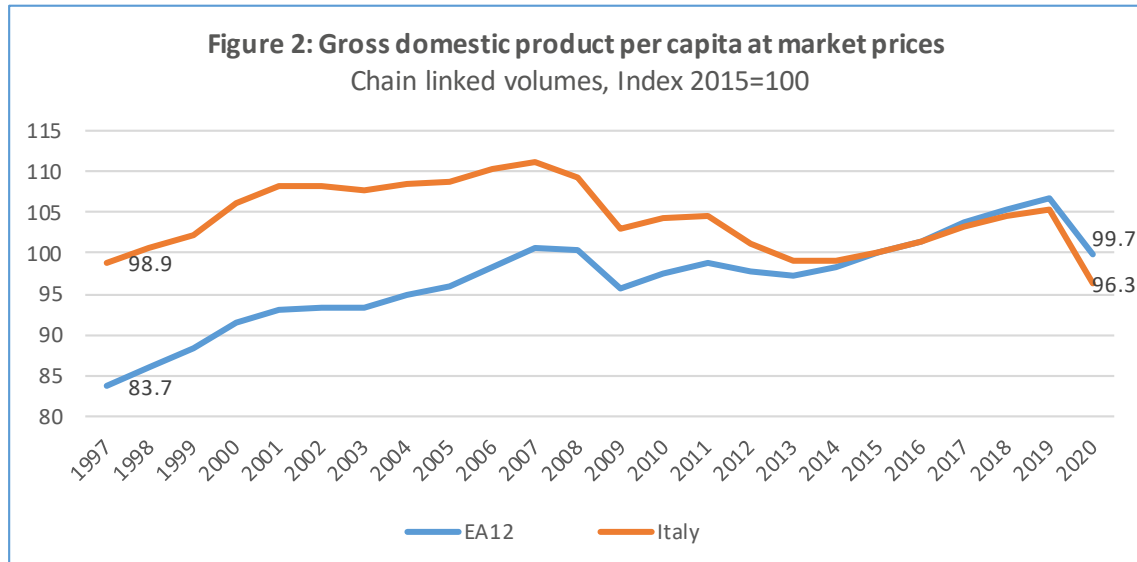
Although the fiscal response has been significant, the current crisis has hit a country that was still fragile from an economic, social, and environmental point of view (Banca d'Italia, 2021). Over the last decade, the Italian economy was characterised by weak growth. In recent years, supportive global economic conditions, expansionary monetary policy, and an extensive program of structural reforms (institutional, public administration, banking sector, and labour market, among others) helped Italy's gradual economic recovery (OECD, 2019a:3). However, after solid real GDP growth in 2017 at 1.6 %, the recovery lost momentum during 2018 (0.8%) and slowed further in 2019 when Italy recorded a growth rate of 0.3%, its worst result since 2014 (European Commission, 2020).

The structural reforms brought a recovery in fiscal and trade accounts, but the results have been modest in other areas. Structural problems persist and Italy continues in a vulnerable situation with excessive macroeconomic imbalances (European Commission, 2019). For over 20 years, Italy has been experiencing output and productivity growth rates that are significantly lower than its peer economies.

³⁴ For an analysis of the effect of containment measures in the EU during the COVID-19 pandemic, see the article entitled "The impact of containment measures across sectors and countries during the COVID-19 pandemic", Economic Bulletin, Issue 2, ECB, 2021. Available in: https://www.ecb.europa.eu/pub/economic-bulletin/focus/2021/html/ecb.ebbox202102_04~eef0a56145.en.html

³⁵ For detailed information in English about the Italian measures see: <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#>

In 2019, the total production of goods and services was approximately the same as it was 15 years earlier. GDP per capita income is roughly the same as 20 years ago (see Figure 2).

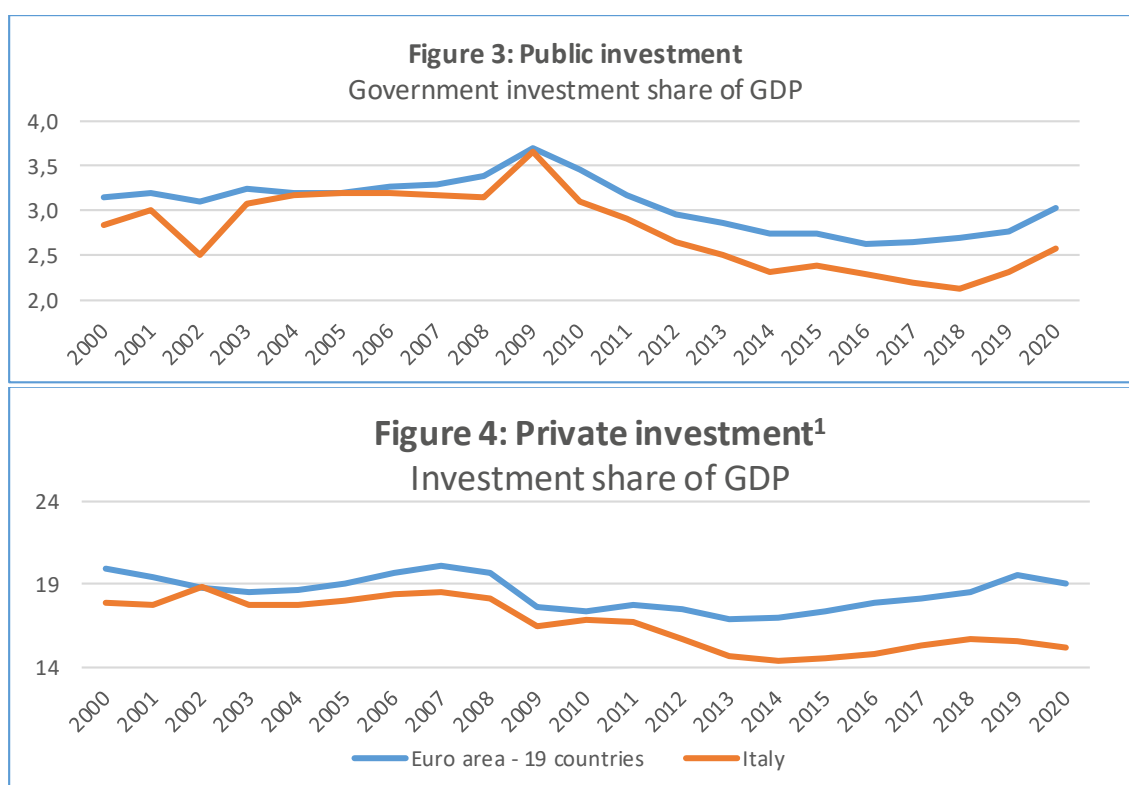


Source: Own elaboration based on Eurostat.

ITALIAN STRUCTURAL CHALLENGES

The GDP growth has been limited by persistently low labour productivity compared with the EU average, which has not increased visibly for the past 20 years (OECD 2019b:2). From 1999 to 2019, GDP per hour worked in Italy grew by 4.2%, compared with 21.2% in France and 21.3% in Germany. Total factor productivity decreased by 6.2 per cent between 2001 and 2019, compared with a general increase at the European level (Governo d'Italia, 2021). The weak productivity, especially in the South, and the high labour costs in comparison with the EU average has resulted in a loss of competitiveness. These problems are partly attributable to the lack of flexibility for companies, excessive bureaucratic procedures, high levels of taxation, inadequate work incentives, and an ineffective labour administration (Schrader and Ulivelli, 2017; OECD, 2019a). Moreover, Italy lags in the digital revolution. According to the Digital Economy and Society Index³⁶ 2021 edition, Italy ranked 25th out of the 27 EU countries: only 42% of people aged 16-74 years have at least basic digital skills (56% in the EU) and only 22% have above basic digital skills (31% in the EU). Regarding the integration of digital technology in the business sector, Italy ranked in 22nd place. The lack of adequate infrastructures combined with a productive structure with a prevalence of small and medium enterprises (SMEs) represents an obstacle to adopting new technologies and productive strategies. In the South, these structural factors are more pronounced and productivity is particularly low (European Commission, 2020).

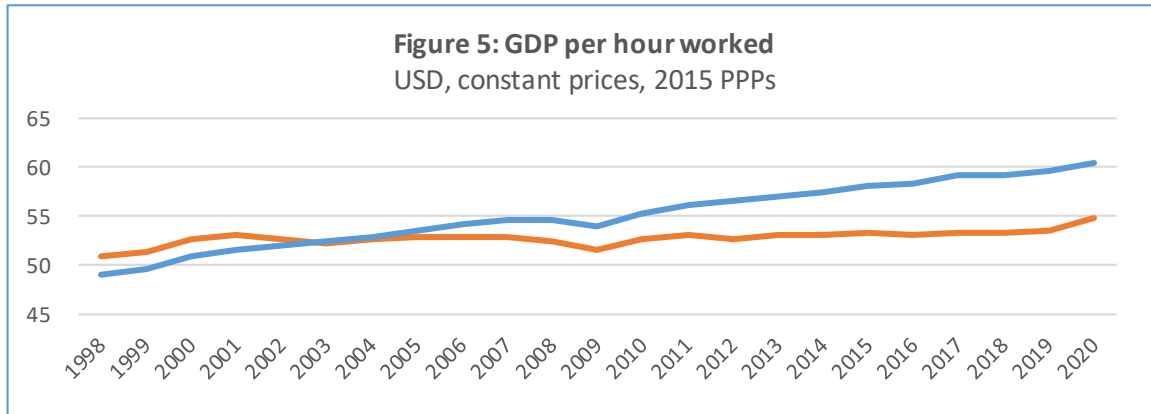
³⁶ The Digital Economy and Society Index (DESI) published by the European Commission annually summarises indicators of Europe's digital performance and tracks the progress of EU countries. It focuses on five key areas: Human capital, connectivity, integration of digital technology, digital public services and Research & Development in ICT.



Source: Own elaboration based on Eurostat. ¹Private investment is calculated as the total investment of all sectors excluding public investment.

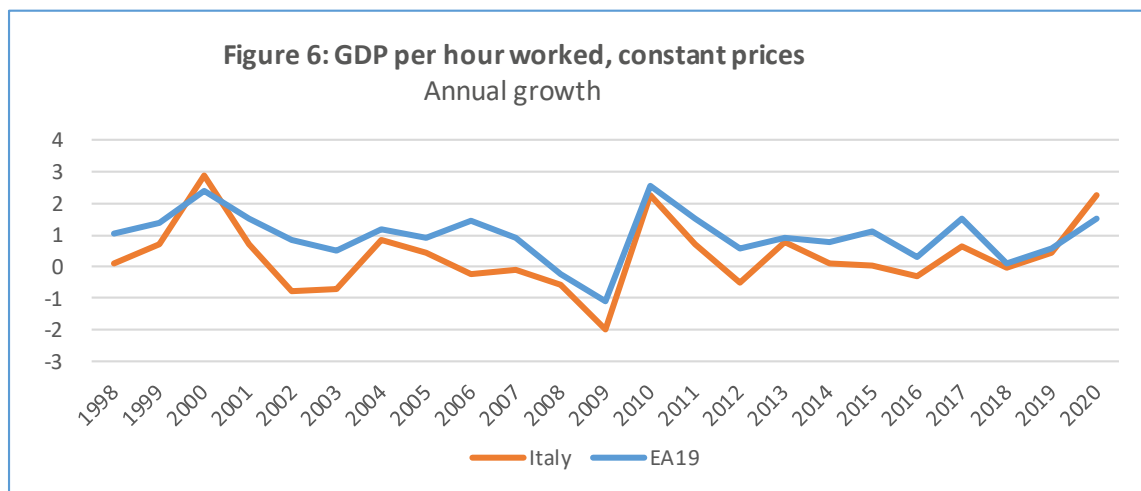
These shortcomings are partly linked to the decline in public and private investments. In the last 20 years, total investments in Italy grew by 66 per cent compared to 118 per cent in the euro area (Governo d'Italia, 2021). In Italy, private investment fell significantly in the 2008 crisis compared to peer countries and public investment also dropped. Recovery was weak (European Commission, 2018). In 2019 total investment as a share of GDP was only 17.9% in Italy compared to 22.4% in the euro area, against 21.7% and 23.4% in 2007, respectively. Moreover, its economy is characterised by an inefficient public administration, a high debt to GDP-ratio, and high regional differences in income and well-being (OECD, 2020;2021; European Commission, 2020;2021a).

Unemployment remains a serious concern in Italy. The high rate of unemployment recorded during the crisis of 2008 has not reduced significantly in recent years, remaining above 10%. In 2019, the unemployment rate in Italy was 10.0% (7.3% in European Union), with the highest values for young and women, especially in the southern regions. Of particular concern is the high level of young Italians neither in employment nor in education and training (NEET). In 2019, 22.1% of young people (between 15 and 29 years old) were in this situation, almost double that in the European Union (12.5%). This high unemployment among the young can hinder their acquisition of skills and their future employability (European Commission, 2018). While the employment rate has increased, it is still one of the lowest rates among developed countries with rates for youth and women noticeably below the EU average (European Commission, 2019; OECD 2019a). The low employment among women is partly attributable to caring responsibilities. Moreover, most of the new jobs created in the country are temporary, job quality is low and there are high divergences between people's jobs and their skills (Cazes et al., 2015; OECD, 2019).



Source: Own elaboration based on OECD.

Source: Own elaboration based on OECD.



The crisis has had a significant impact on the labour market. In 2020, the number of employees decreased by 2.1 per cent (525,000 people fewer); the total hours worked fell more markedly, by 11.0 per cent, to the lowest level in the last four decades (Banca d'Italia, 2021). The unemployment rate decreased by -0.8 percentage points (from 10.0% in 2020 to 9.2% in 2019) as a large number of persons exited the labour market (the labour market participation rate fell by 1.6 per cent in 2020). Moreover, beneficiaries of the Wages Guarantee Fund (*Cassa Integrazione Guadagni*) continue to be statistically counted as employed. The negative effects have been especially severe for workers with a fixed-term contract and self-employed workers. The employment level in the service sector, with a larger proportion of high-contact activities, has decreased considerably, particularly in tourism. Job losses penalised in particular young people and women, and especially young women resident in the South (Bank of Italy, 2021; European Commission, 2021).

Social and regional disparities persist and remain one of the highest in Europe. The gap between the wealthy regions of Northern Italy and the poorer areas in the South is larger in Italy than in most other OECD countries (Veneri and Murtin, 2016; OECD, 2019a). The regional disparities are observed in terms of income (the fourth-highest among OECD countries), employment, productivity, infrastructures, and well-being. As the OECD (2019a) points out, territorial differences in GDP per capita in Italy primarily reflect disparities in employment rates, especially among women. This is not observed in its peer countries where productivity differences are key in explaining GDP per capita gaps. Female employment rates vary widely among Italy's regions. While Bolzano, Trento, and Emilia-Romagna record female employment rates above 60%, in regions such as Calabria, Sicilia, they do not reach 30%.

Young people's employment rates and skills are also a serious concern in the South. In these regions, 25.1% of Italians between 15 and 29 years old are neither in employment nor in education and training (13.3% in Nord-ovest regions). A high proportion of workers earn some income from informal work. These jobs are often associated with lower productivity, bad working conditions, and lower-income (OECD,2019b). While disposable household income in Piemonte was EUR 21,300 in 2018, in Calabria it was EUR 12,000. In terms of health, the difference in life expectancy is up to 10 years between the poorest social groups in the South and the richest in the North. Regional disparities are also observed in the public administration (PA) and investment. All the southern regions are placed at the bottom of the European Quality of Government Index 2021 (Charron et al.,2021). Moreover, on the digital front, the South is characterised by a greater backwardness.³⁷

The asymmetric socio-economic impact of the COVID-19 is aggravating the regional disparities (European Commission, 2021). The pandemic has affected the country overall, but the most vulnerable have suffered more. Resilient regions could seize the opportunities offered by digitalisation. In Italy, the South and rural areas are still lagging in terms of access to high-speed broadband,³⁸ have a lower share of jobs amenable to remote working, and the workforce has a lower level of education (OECD, 2021).

Despite recent reforms,³⁹ the public administration performance is less efficient than in peer countries (European Commission 2018; 2019). The integrity and effectiveness of Italian public institutions is among the weakest across developed countries (OECD, 2020; European Commission, Directorate-General for Structural Reform Support,2021). Investors and households report lower trust in public institutions and public services (education, security and crime prevention, and environmental protection) than in other OECD countries. The inefficiency of the public sector is hindering competition and the effectiveness of public investment, and adding administrative burdens to the private sector (European Commission, 2019; OECD, 2019; IMF, 2020). Some sectors are still over-regulated, especially in regulated professions. Furthermore, Italy's tax system is also complex. The time necessary to comply with tax laws is considerably longer in Italy (238 hours) than in peer countries (e.g. 140 in France), according to World Bank estimations (OECD, 2020). Trial length in civil justice remains worrying despite the progress made in recent years: on average it takes more than 500 days to conclude a civil process in the first instance (Governo d'Italia, 2021).

Although the pandemic has accentuated some existing problems (suspension of administrative deadlines or time to complete procedures, for example), during the pandemic there was a sharp acceleration in the digitalisation of the public administration. The most relevant measures include: the simplification of procedures (through the use of digital technology and the decentralisation of offices), the implementation of remote working, and the simplification measures for administrative procedures initiated concerning the emergency. During 2020 and 2021, there was a sharp acceleration in the adoption of major enabling platforms for digital public services (DESI, 2021). The legislative initiatives to boost digitalisation include the "Rilancio" Decree,⁴⁰ which establishes a fund for innovation and digitalisation of public administration services for citizens and business, and the Simplification and

³⁷ According to the DESI, at a regional level, while Lombardy obtains 72.9 out of 100, Calabria ranked the last, with a score of 18.8, significantly below the Italian average (53.8) (Osservatorio Agenda Digitale, 2020).

³⁸ According to the OECD (2020), while 90% of total households in Italy benefit from access to high-speed broadband, only 43% of rural households do so. Moreover, in some regions, one-fourth or more of the population either does not use the Internet or does not have a computer.

³⁹ For more details about the recent reforms and Italian administration performance see the article: "Bulman, T. (2021), *Strengthening Italy's public sector effectiveness*, OECD Economics Department Working Papers, No. 1690, OECD Publishing, Paris,

⁴⁰ Legislative Decree No 34 of 19 May 2020

Innovation Decree⁴¹ which established the adoption of the main e-government platforms by all areas of the public administration. Moreover, a political strategy for the national cloud⁴² was released. During the pandemic, improvements were seen in the use of digital public services with significant increases in the number of digital identities issued (SPID), the public administrations using SPID, and the users registered in the IO app (a user-centric digital app for public services). Despite these improvements, the use of digital public services and the availability of pre-filled forms remain relatively low. Italy ranked 18th in the EU in digital public services in 2020 (European Commission, 2021c). Although the share of Italian online users who resort to e-government services increased notably from 30% in 2019 to 36% in 2020, it remains well below the EU average of 64%.

Public finances are another vulnerable point of the economy. Italy has been one of the most indebted countries in the world in most years during the past decade. In 2019, Italy's public debt-to-GDP was 134.6% (EUR 2.4 billion), the second-highest in Europe. The high public debt is an old problem in the Italian economy. Already before the introduction of the Euro, the country had not met the Maastricht criteria. Following the Great Recession in 2008, Italy experienced a sudden stop in private capital inflows. Government gross debt as a share of GDP increased from 103.9% in 2007 (66.0% in the euro area) to 155.6% in 2019 (97.3% in the euro Area). The rise in the real interest rate on debt, observed after the Great Recession (2008-2012) as a consequence of the sovereign debt crisis, and the low GDP growth rates have been identified as the main causes of the high debt ratio in recent years (Antonin et al., 2019). Moreover, the composition of public spending has hindered other public investments. While government expenditure is concentrated on old-age pensions, R&D and tertiary education spending remain low (European Commission, 2021). According to the Debt Sustainability Monitor (2021), Italy faces medium fiscal sustainability risks in the long term.

Public and corporate debt have been severely hit by the COVID-19 crisis. The policy response to the consequences of the pandemic and the decline in revenues caused a deterioration in the already weak public finances. The government debt-to-GDP ratio rose from 134.6% in 2019 to 155.8% in 2020. The general government deficit increased from 1.6% of GDP (the lowest level since 2007) to 9.4% of GDP in 2021. Government financing needs are expected to decrease in 2022 (5.8%) according to the Autumn European Commission Forecast. The additional policy response is expected to increase more than the projected economic growth. Moreover, ageing-related costs are projected to increase substantially in the medium term. The European Commission (2021) points out that Italy's economy could face high fiscal sustainability risks in the short and medium-term. However, it is also pointed out that the implementation of reforms and investments as part of the Italian RRP is expected to have a substantial positive and persistent impact on GDP growth, which could improve debt sustainability in the long term.

THE ITALIAN NATIONAL RECOVERY AND RESILIENCE PLAN

The recovery plan's structure

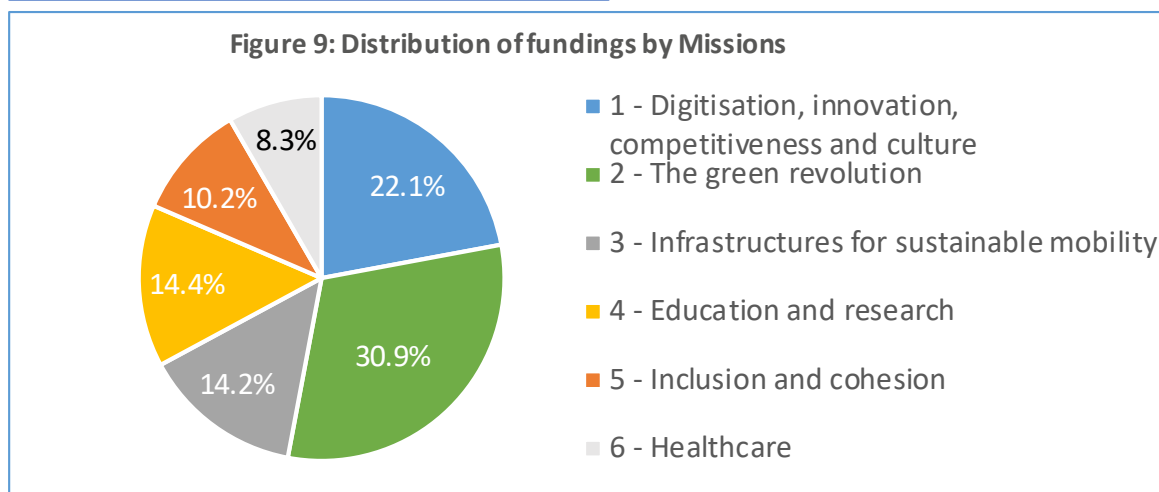
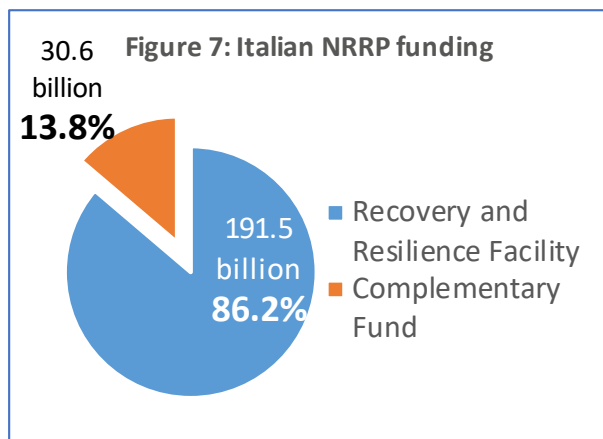
The Italian Recovery Plan amounts to EUR 222.1 billion. Of that total amount, EUR 191.5 billion comes from the Recovery and Resilience Facility (EUR 68.9 billion in non-repayable financial support and EUR 122.6 billion in loans). In absolute terms, Italy has the largest share of EU funds (28% of the entire rescue fund of EUR 750 billion). Italy is supplementing that amount with an additional EUR 30.6 billion through the Complementary Fund, financed directly by the State.

⁴¹ Legislative Decree No 76 of 16 July 2020

⁴² 7 September 2021. Available at: <https://cloud.italia.it/strategia-cloud-pa>

The Plan is structured around 6 areas of interventions ("Missions"): digitalisation, innovation, competitiveness, and culture; green revolution and ecological transition; infrastructure for sustainable mobility; education and research; cohesion and inclusion; health. They are divided into 16 Components that address specific challenges and are structured under investments and reforms (horizontal reforms, enabling reforms, and sectoral reforms). Moreover, three cross-cutting priorities underpin the investments, reforms, and projects: reducing disparities among regions, generations, and genders.

Source: Authors' elaboration based on Italian RRP and European Commission.



The

Plan's governance

A dedicated multi-level governance framework has been created to guarantee the effective implementation and monitoring of the plan (European Commission, 2021). The Plan's governance follows the principles for RRP Governance established by the Recovery Fund and the governance and administrative simplification Decrees adopted by the Italian Government (Decree-Law of 31 May 2021, n. 77 and Decree-Law of 9 June 2021, n. 80).

Italy's Ministries and local authorities have the direct responsibility of carrying out the investments and reforms within the agreed timeframe and effective management of resources. The Italian plan's governance focuses on the establishment of a "Control Room" ("*Cabina di Regia*"), chaired by the President of the Council of Ministers, and composed of the relevant Ministers and Undersecretaries. The Control Room will meet periodically, to ensure the assigned functions are being correctly carried out. Its main duties include the verification of the implementation of the Plan, the monitoring of the effectiveness of the administrative capacity available, the transmission to Parliament of a report on the Plan's implementation every six months, and the provision of other useful information to guarantee

the correct monitoring. A significant role will be played by local authorities, which are responsible for investments amounting to over 45% of the Italian plan (Leonardi and Bellisai, 2021). When the issues concern several regions, the President of the Conference of Autonomous Regions and Provinces, the President of the Association of Italian Municipalities and the President of the Association of Italian Provinces take part in the control room. Finally, through a special structure, the Italian Ministry of Economy and Finance will monitor the progress of the implementation of the Plan and will be the intermediary figure with the European Commission.

The Plan's impact on GDP

According to the Italian estimations using the QUEST model of the European Commission,⁴³ the RRP should lead to uniform growth along the entire horizon of the Plan. In the best scenario, it is estimated that GDP will be 3.6 percentage points higher than in the baseline scenario without the Plan (See Table 1).⁴⁴ As the Plan points out, in the short term, the demand effect prevails, triggered, for example, by higher costs for the construction and implementation of public investments. In the medium term, greater investments could increase the stock of public capital with persistent positive effects on potential and actual GDP. Moreover, as the Plan highlights, the efficiency of public investments also plays an important role in the medium term: the difference in the level of real GDP in the final year of the simulation compared to the baseline scenario is 1.8 percentage points in the low scenario compared to 3.6 percentage points if high-efficiency investments are assumed (Governo d'Italia, 2021). However, as the European Commission (2021) notes, although this high efficiency could be achieved, it requires effective implementation and high productivity of the investment stimulus. Therefore, these simulations are subject to downside risks.

Table 1: Estimated impact of the Italian RRP on national GDP.

	2021	2022	2023	2024	2025	2026
Best scenario	0.5	1.2	1.9	2.4	3.1	3.6
Medium scenario	0.5	1.1	1.6	2.0	2.4	2.7
Low scenario	0.5	0.9	1.4	1.5	1.7	1.8

Source: Italian RRP

ASSESSMENT OF THE MEASURES OF THE ITALIAN PLAN TO ADDRESS STRUCTURAL CHALLENGES

Assessment of the measures focused on the labour market and educational outcomes

Labour market reforms are included in mission 5 of the RRP. Two main reforms are proposed: a national programme for an employability guarantee ("Programa nazionale per la Garanzia Occupabilità dei Lavoratori") and a national new skills plan ("Piano Nazionale Nuove Competenze"). The budget for

⁴³ The impact assessment addressed the impacts not only of the RRF, but also of the other components of the NGEU, starting with REACT-EU. In addition, consistently with the RRP setup outlined in this document, it has been assumed that more than 70% of the additional NGEU funds will be used to finance public investment. The model also assumes that the stock of public capital can be considered a factor of production and at the same time a catalyst for the productivity of private firms.

⁴⁴ These results cannot be directly compared to the numbers reported in the European Commission Assessment of the Italian plan given that there are differences in the assumptions and methodology. For more details about the different estimations on the impact of the NRRPs, see section 4.2.1. of this report: "The results of some simulation exercises on the economic impact of the NGEU".

these two programs amounts to 4.4 billion and both reforms will have been adopted by the end of 2021.

The national program for employability guarantees intends to reduce the excessive heterogeneity of the services provided at the local level. The program will be adopted via an interministerial decree, after agreement in the state-regions conference. The national new skills plan aims to improve the training of workers in transition and the unemployed. To do so, the Plan intends to strengthen the vocational training system and set essential quality levels for upskilling and reskilling activities in favour of the beneficiaries of income support, short-time workschemes, or the Citizenship Income.

In line with the Country-Specific Recommendations (CSRs), reforms are proposed to support women's entry into the labour market, such as better provision of care facilities and reform of the support for the non-self-sufficient elderly. Moreover, the RRP also proposes to include initiatives to enhance female entrepreneurship (for example, the "Women's Enterprise Fund"). To promote wage transparency, the RRP also introduces a national system of certification of gender equality which is expected to start in spring 2022.

Regarding youth unemployment, the Plan addresses young people's integration in the labour market enhancing the "strengthening the dual system" and "Universal Civil Service" initiative. With the first program, the NRPP intends to strengthen the dual system to set up training paths that meet the needs of companies, provide the productive fabric with the range of competencies it needs to reduce the mismatch between skills required in the labour market and those provided by the education system, and enable the country to emerge from the crisis and ensure recovery. The Universal Civil Service initiative aims to increase the quality of the projects and the number of young people involved in activities that contribute to the improvement of the country's social cohesion and to promote the acquisition of soft skills together with personal and social competencies.

The proposed labour market reforms are relevant and in line with the CSRs highlighted in recent years. However, the Plan does not cover sufficiently all the structural problems. Initiatives to reduce the high unemployment among the youth are too generic. The proposal to strengthen the dual system does not establish specific strategies. Moreover, it does not offer details on the timeline for the implementation by the responsible authority for all the measures. While there is a significant amount (EUR 4.4 billion) of the budget allocated to two main programs (Employability Guarantee and a National New Skills Plan), the Plan does not specify how this money will be distributed.

Part of the labor market structural problems can be explained by persistent challenges affecting the Italian education system. Before the pandemic, early childcare and education were characterised by low coverage, hindering female participation. Moreover, the percentage of people with tertiary education was below the EU average. Training, adult learning participation, and digital skills are also low.

The Plan addresses these challenges with various reforms and initiatives. It presents investments to increase the supply of educational services for all levels, to support the school-to-university transition, and to promote tertiary education.

The proposed education and skills reforms appear to address the educational and social challenges faced by Italy. According to the European Commission Assessment of the Italian RRP, it addresses the vulnerabilities identified by the Social Scoreboard and contributes to the European Pillar of Social Rights. Moreover, the Plan represents to *"a large extent a comprehensive and adequately balanced response to the economic and social situation thereby contributing appropriately to all six pillars of the RRF Regulation"*. Although the assessment of the European Commission is positive, we note that some proposals are not covered sufficiently. The Plan details how the investments in childcare and the

increase of the tertiary education supply will be implemented. However, other key reforms are mentioned with significantly less detail. In the case of the proposed improving of digital skills, the measures are too vague. For example, the Italian RRP establishes that new curricular programs will include a new subject ("coding") but it does not mention the implementation date of this measure. It also fails to mention how the money will be distributed among the different projects (for instance, how much money will be spent on improving infrastructure or teaching subjects related to digital skills?). The same is observed for the proposed strategies to address the "skills mismatch". While the Plan points out the relevance of increasing the supply of Higher Technical Studies and "create greater osmosis between ITS and university courses", it does not specify in detail how this will be implemented.

Assessment of the reforms regarding the public administration and the justice system

Public administration (PA) reforms are included in mission 1 of the RRP. The package includes EUR 7.1 billion. The Plan proposes a radical modernisation of the public administration focusing on four areas: a) accessibility; b) good administration; c) skills; and d) digitalisation. In economic terms, the latter is the most important area (EUR 6.1 billion).

To improve accessibility, a single recruitment platform will be created with detailed information of potential candidates. Moreover, agreements will be signed with institutions and universities to facilitate the selection of high and specific profiles. To simplify the procedures, the Italian government has introduced a set of reforms (Article 15 of Legislative Decree no. 76 of 2020) which intends to identify the most critical procedures and eliminate administrative authorisations not justified by the public interest. To increase the skills of public employees, the plan intends to invest in two lines of intervention. On the one hand, a revision of the career paths of the PA. On the other hand, promoting the access of qualified people from the private sector. Finally, the PA digitalisation represents the most important area. In particular, it centers around the creation of a national cloud-based hybrid infrastructure (PSN), extending the supply of citizen-oriented digital services to both central and local administrations, strengthening the defense against cybercrime, and the creation of a "transformation office".

Reforms and investments to increase the efficiency of the justice system amount EUR 2.3 billion. The main goal is to reduce the length of civil and criminal proceedings and the backlog of cases. To this end, significant temporary investment is envisaged in human resources, strengthening the hiring of young human capital and creating new technical and administrative positions. Moreover, the measures to reduce the costs and the duration of the procedures of the justice system also include a substantial expansion of digital services, including digitalised tools both for civil and criminal proceedings, and the creation of systems for the digital collection of procedural information and data. In addition, the package also proposes interventions to improve regulations in specific sectors and to remove several barriers to competition including, among others, measures to improve tax compliance or the simplification of the public procurement framework.

The RRP presents in detail the investments, the timeline of the different projects and reforms, and the authorities responsible for its implementation. The implementation of reforms should produce a positive and persistent impact on public administration. In the case of the reforms in the justice system, they are appropriate for the objectives targeted and consistent with the recommendations specified in the CSRs. However, the timelines and steps for the implementation of the various projects are less detailed than in the case of the reforms aimed at modernising the PA. According to the European Commission Assessment of the Italian RRP, the country-specific recommendations on public administration and the justice system are substantially addressed. These measures will also support the implementation and monitoring of the Plan and raise the quality and supply of public services.

Assessment of the reforms regarding social and regional disparities

The Italian RRP, through an integrated horizontal approach and in line with the 2030 Plan for Southern Italy, aims to reduce the citizenship gap between the North and the South of Italy. In line with the CSRs (2019,2020), this priority has been identified as a cross-cutting priority that affects all the RRP's missions.

The Plan allocates to the South 40% of the territorialisable resources of the NPRR (approximately EUR 82 billion out of 206 billion), for the eight regions of Southern Italy (above the 34% envisaged by current legislation in favor of the South⁴⁵). These interventions have been integrated with the European and national cohesion policies. Thus, the Plan includes, in addition to RRF support, additional EUR 8.4 billion from the React-EU (relating to the period 2021-23), EUR 54 billion from the European Structural and Investment Funds (relating to the period 2021-27), EUR 58 billion from the Development and Cohesion Fund (until 2030) and about one billion from the Just Transition Fund. Consistently with the additionality principle of the RRF Regulation, the Italian government points out that *"all these funds are complementary: they add up and do not overlap"*.⁴⁶

Regarding its territorial distribution, the Italian RRP does not provide the necessary information to define the portion of the overall expenditure that will be allocated to the individual regions of the South. However, the Italian government website publishes a table with the distribution of resources for the South among the six Missions.

Table 2: Distribution of investments allocated to the South in RRP Missions.

	EUR (Billion)	%
1. Digitalisation, innovation, competitiveness, and culture	14.6	36.1%
2. The green revolution and ecological transition	23.0	34.3%
3. Infrastructures for sustainable mobility	14.5	53.2%
4. Education and research	14.6	45.7%
5. Inclusion and cohesion	8.8	39.4%
6. Healthcare	6	35-37%
TOTAL	81.6	

Source: Government of Italy website: https://www.governo.it/sites/governo.it/files/PNRR_Mezzogiorno.pdf

Note: The Plan makes available to the South a complex of resources equal to 40 per cent of the territorialisable resources of the PNRR (81.6 billion out of 206 billion, including the complementary fund)⁴⁷.

⁴⁵ "The clause, introduced during the conversion of the decree-law n. 243/2016 and subsequent amendments in law no. 18/2017, provides that the central administrations of the state must allocate 34% of ordinary capital resources to the regions of the South, therefore proportional to the percentage share of the reference population". For more details see: <https://politichecoesione.governo.it/it/strategie-tematiche-e-territoriali/strategie-territoriali/lausola-34-investimenti-ordinari-al-mezzogiorno/>

⁴⁶ For more details about the different funds allocated to the South see: <https://www.ministropersud.gov.it/it/approfondimenti/schede/quali-sono-i-fondi-destinati-al-sud-nei-prossimi-anni/>

⁴⁷ For more details about the resources allocated to the South and its distribution see: <https://temi.camera.it/leg18/temi/il-mezzogiorno-nel-pnrr.html>

Among the measures proposed, particular attention is paid to digital infrastructures, with 45% of the RRP resources for ultra-broadband connectivity destined for Southern regions. Relating to the green transition, there are interventions intended to reduce the territorial gap in waste management, with about 60 per cent of projects destined for municipalities located in the Center-South. The plan presents also projects to reduce the dispersion of water resources, which in the South is equal to 51% (the national average is 41%). Moreover, the plan proposes to allocate projects for the dissemination of renewable energy and sustainable transport (for example, the projects to convert trains from diesel to hydrogen will be more concentrated in the southern regions). Regarding sustainable mobility, the Plan highlights the strengthening of the regional railway lines⁴⁸ (the plan refers especially to the Salerno-Reggio Calabria, Naples-Bari, Palermo-Catania-Messina, and Taranto-Potenza-Battipaglia routes). In the educational area, the Plan proposes to increase the availability of places in kindergartens and preschools, especially low in the southern regions⁴⁹. The main social cohesion measures focus on strengthening essential services and increasing the attractiveness of the areas at greatest risk of depopulation in the Special Economic Zones (SEZ), located in the South.⁵⁰ Moreover, the Plan presents measures to improve health systems through the reorganisation of health policies with reforms and investments based on care needs.

According to the Italian RRP, *“the South will contribute by one percentage point to the variance in national GDP in the final year of the Plan”*. The European Commission Assessment of the Italian RRP affirms that the proposed projects and interventions are consistent with the CSRs and address the vulnerabilities identified by the Social Scoreboard. The measures support the strengthening of social and territorial cohesion and contribute to the European Pillar of Social Rights. However, we note that the lack of detail makes it difficult to assess their effectiveness. The South will receive a substantial quantity of resources (40%). While the objectives of the reforms are relevant, no details are provided on the territorial distribution. Some questions emerge: How will the resources be distributed among the different southern regions? Under what criteria will this distribution be made? Some concerns also emerge regarding the ability to spend the funds and carry out the projects. The completion of works takes on average almost a year longer than in the Center-North. Moreover, the southern regions also have the highest rates of non-use of European funds assigned and of unfinished works (Galli and Liaci, 2021).

Assessment of the reforms aiming at the sustainability of public finances.

The plan includes some relevant fiscal-structural reforms aimed to improve the sustainability of public finances. Three reforms should be highlighted:⁵¹ i) The Italian tax system reform; ii) the spending review process reform; and iii) the completion of the fiscal federalism reform.

The reform of the tax system is key and aims at reducing tax evasion, including strengthening the capacity of the tax authority in terms of staff, analytical infrastructure and data access, the deployment

⁴⁸ Currently, there are fewer and slower trains in the southern regions, as well as the largest number of single-track and non-electrified lines (Pendolaria, 2021).

⁴⁹ Despite the increase in recent years, the coverage rate for children aged 0-2 is still below the national average and the target of 33% required by the EU.

⁵⁰ Special Economic Zones (“SEZs”) are geographical areas in which a governmental authority offers incentives (fiscal advantages and simplified procedures) for the development of businesses in order to attract investment (in particular from foreign investors). The SEZs are allowed in six regions in the South: Campania, Basilicata, Puglia, Calabria, Sicily and Sardinia.

⁵¹ The plan also mentions a reform to reduce effective rates on labor income, be it on employees or the self-employed, particularly for low and medium-low income taxpayers. With this measure, it is expected to increase the employment rate and reduce non-declared work. The Government has already taken some steps (with the 2021 Budget Law) to reduce the tax wedge on labor. This reform is not included as a measure in the Plan. Therefore, the plan does not mention milestones or targets and the lack of detail makes it difficult to assess its effectiveness.

of pre-filled VAT tax returns, as well as the introduction of effective sanctions for the refusal of electronic payments.

The spending review reform is expected to strengthen the existing national legislation in order to increase the effectiveness and support the better monitoring of public finances. In particular, it aims to strengthen the existing structures and the implementation of new phases of monitoring: (i) before the proposals; (ii) monitoring their effective implementation; (iii) post-evaluation of the results actually achieved. Moreover, the plan includes a commitment to implement three yearly spending reviews over 2023-2025.

Finally, the completion of the fiscal federalism reform⁵² has three main objectives: to improve the transparency of tax relations between the different levels of government; to allocate resources to local administrations on the basis of objective loads; and to encourage the efficient use of resources. In particular, the reform will have to define the applicable parameters and implement fiscal federalism for the regions with ordinary statute, the provinces and the metropolitan cities.

The RRP presents in detail the reforms, the objectives pursued, the timeline, the different steps, and the authorities responsible for their implementation. They are appropriate for the objectives targeted and consistent with the CSRs. According to the European Commission Assessment of the Italian RRP, the measures are expected to reduce the revenue loss from tax evasion and to improve the efficiency of public expenditure in the medium term, contributing to improving fiscal sustainability.

Assessment of the measures to support the green transition

Italy faces challenges due to the green transition. Due to its geography, Italy is particularly vulnerable to the consequences of climate change, especially to droughts. Moreover, coastal areas, deltas, and floodplains will probably suffer the effects of rising sea levels and intense rainfall (European Commission, 2019; Governo d'Italia, 2021). Per capita emissions remained substantially unchanged until 2019 with hardly any reductions in the previous five years (OECD, 2021). Moreover, waste management and water infrastructure need substantial investments, particularly in the southern regions. Recent progress in both renewable energy and energy efficiency is also modest and building energy efficiency is still low (European Commission, 2018; Governo d'Italia, 2021).

Within this context, the Italian RRP allocates 37.5% to face the green transition (European Commission, 2021a). Climate proposals and measures are included in five out of the six missions, Missions 2 and 3 being the core of the climate budget.

Among the investments included in the plan, the following stand out: the investments and reforms for the circular economy and waste management, the development of the bio-methane sector, and the production of energy from renewable sources. Resources are also allocated for the renewal of local public transport, with the purchase of low-emission buses, and for the renewal of part of the fleet of trains for regional transport. The plan also proposes renovations for energy efficiency and measures to support the widespread use of hydrogen. These investments are accompanied by reforms aimed at simplifying the bureaucratic process that slows down the development of the green sector.

According to the European Commission Assessment of the Italian plan, the "Green Transition" pillar is well covered and the measures proposed to address the challenges are expected to make a significant contribution to the green transition. In this sense, Italy has received an A rating as defined in the NGEU regulation. However, environmental organisations and climate think tanks have pointed out that

⁵² Decree-Law n. 68/2011 (articles 1-15)

resources are insufficient for transformative and innovative projects and they have limited effectiveness in the achievement of national climate targets. Leonardo and Bellisai (2021) report that the main criticisms relate to the absence of relevant projects in the three key decarbonisation dimensions (renewable energies, energy efficiency, and e-mobility). For example, the plan directs resources to marginal areas of the energy transition. Regarding the renovation of buildings, the “ecobonus”⁵³ has a high cost and it seems that it does not have a long-term energy efficiency impact. E-mobility focuses on a medium and long-distance train, while urban transport has a marginal role. In this sense, organisations have pointed out the absence of a strategy for developing electric mobility, a crucial measure for the decarbonisation of transport.

Assessment of the measures to face the digital transition

Improving the digital skills of the population and workforce is a priority for Italy (European Commission, 2021). In the DESI 2021 edition, Italy ranks 20th out of 27 EU Member States. The country lags in all the areas of the DESI, performing particularly poorly in human capital where Italy ranks 25th out of 27. Only 42% of people aged 16-74 years have at least basic digital skills (56% in the EU) and only 22% have above basic digital skills (31% in the EU). Regarding connectivity, Italy ranks 23rd. However, Italy does not lag behind in all the areas. The efforts made in the last years through legislative interventions have had an impact on digital intensity. Italy ranks 10th in integration of digital technology: 69% of Italian SMEs have at least a basic level (60% in the EU). Moreover, almost the totality of Italian enterprises uses electronic invoices (95% of them, almost three times the EU average). Although the COVID pandemic prompted a sharp acceleration in the digitalisation of the public administration, the use of digital public services remains low. Italy ranked 18th in the EU in digital public services in 2020. Only 36% of Italian online users use e-government (64% in EU).

In this context, the Italian RRP places great emphasis on digital transformation, assigning 25.1 % of the plan’s total allocation in grants and loans to this goal (European Commission, 2021). Mission 1 is the core of digital strategy, but structural and sectoral reforms are present in almost every component of the plan.

The reforms and investments contributing to the digital transition cover the digital transformation of the PA and justice system. Among the projects allocated to the modernisation of the PA, the cloud-first approach has prominent focus, together with the improvement of interoperability of databases and digital identity technologies. Measures are also included to envisage the digitalisation of the private sector (Transition 4.0), improving connectivity, and internationalisation, particularly in small and medium-sized enterprises. Finally, measures related to making tourism and culture more digitally accessible are also included. The Plan also presents measures aimed at improving both basic and advanced digital skills.

The RRP presents in detail most of the investments, the timeline of the different projects and reforms, and the authorities responsible for its implementation. They are appropriate for the objectives targeted and consistent with the recommendations specified in the CSRs. According to the European Assessment of the Italian plan, the measures proposed to address the main digital challenges are aligned with the objectives of the Digital Strategy of the Union and the priorities identified in the 2021 Annual Sustainable Growth Strategy. Italy has received an A rating as defined in the RRF regulations in this area.

Summary assessment

⁵³ The Ecobonus offers a deduction of 110% on certain expenses for house renovations related to energy efficiency or other anti-seismic improvements.

According to the Commission's Report to the European Parliament and the Council on implementing the Recovery and Resilience Mechanism (European Commission, 2022), Italy submitted its operational agreement to request its first payment application on 30 December 2021. The Italian RRP received the Commission's preliminary positive assessment on 28 February 2022. The report considers that the Italian government addresses the six pillars adequately to be considered for the Recovery and Resilience Mechanism. The most relevant contributions mentioned in the report include, among others, the introduction of the National Programme for Circular Economy (pillar 1: green transition), the integration of advanced digital technologies, and investments to improve connectivity across the national territory (pillar 2: digital transition). The report also highlights "Italy's Transizione 4.0" (pillar 3: smart, sustainable, and inclusive growth), the investment to support women's participation in the labour market (pillar 4: social and territorial cohesion). The report also highlights the measures aiming to make the judicial system more efficient (pillar 5: health, economic, social, and institutional resilience).

The Italian RRP is broad and addresses, as a whole, the vulnerabilities of its economy. The plan includes a series of reforms and investments in line with the priorities identified in the CSRs and the RRF Regulations' objectives. However, we note that not all proposals could solve the vulnerabilities in the long term. Measures to promote digital transition, improve the situation of public finances, and the efficiency of public administration present specified strategies and details. Nevertheless, some concerns emerge. For example, the proposed labour market reforms are relevant and in line with the CSRs highlighted in recent years. However, while initiatives to promote women's participation are well specified, the measures to reduce unemployment among the youth are, in some cases, generic. In the case of the efforts aiming to address regional disparities, the Plan follows an integrated horizontal approach, including measures across all Pillars. The South will receive a substantial quantity of resources (40%). The objectives of the reforms are relevant, but no details are provided on the territorial distribution among the different southern regions, making it difficult to assess their effects. Finally, in the case of green transition, environmental organisations and climate think tanks have pointed out the absence of relevant projects in the three key decarbonisation areas (renewable energies, energy efficiency, and e-mobility).

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ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: SPAIN

	2017	2018	2019	2020	2021*	2022*
GDP growth	3.0	2.4	2.0	-10.8	5.9	6.8
Consumer price index (harmonised)	2.0	1.7	0.8	-0.3	1.4	1.1
Unemployment rate	17.2	15.3	14.1	15.5	15.7	14.4
General government gross debt (% of GDP)	98.6	97.4	95.5	120.0	119.6	116.9
General government fiscal balance (% of GDP)	-3.0	-2.5	-2.9	-11.0	-7.6	-5.2

Source: AMECO.

Vulnerabilities

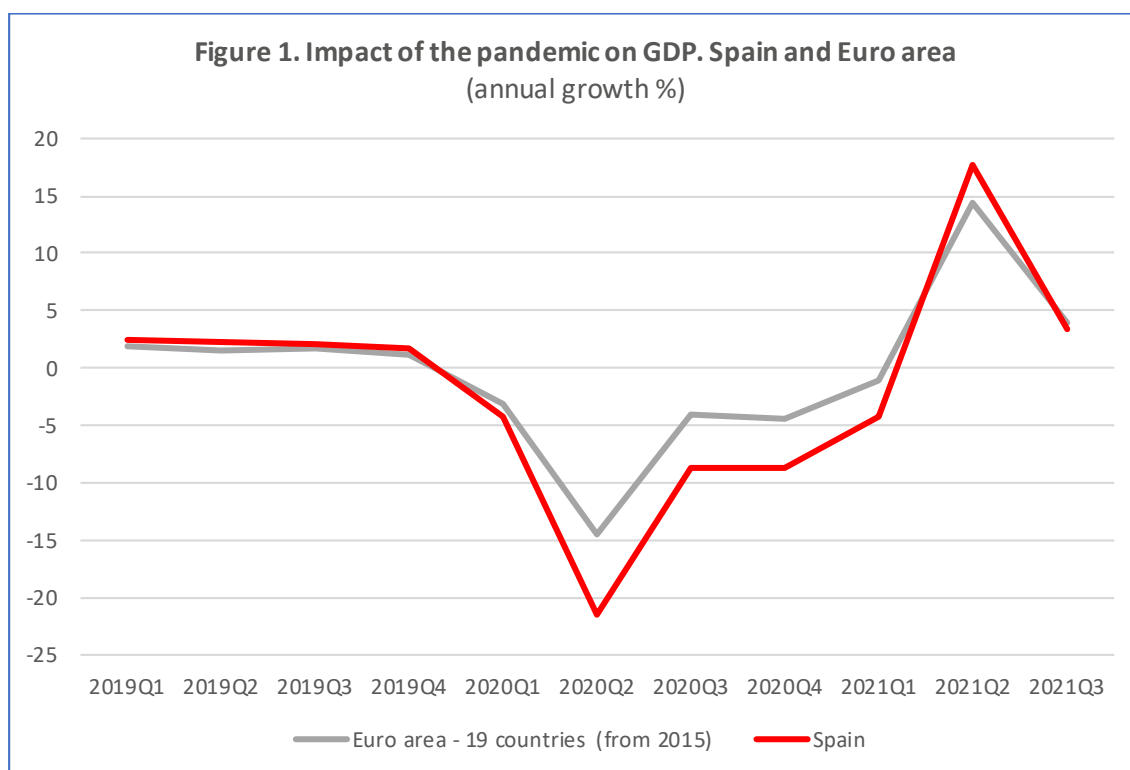
- High public debt and deficit-to-GDP ratio
- Concerns about the sustainability of the pension system
- A labour market that suffers from severe structural weaknesses
- Low productivity growth
- Low investment in Research and Development
- Energy inefficiency and lagging in the ecological transition.

Spain is one of the countries most affected in both health and economic terms by the COVID-19 pandemic, having recorded among the highest number of infections despite establishing one of the strictest lockdowns in the European Union.

In Spain, the first case of coronavirus infection was detected on 31 January 2020 in La Gomera in the Canary Islands, but it was not until 25 February that the virus spread across the entire Spanish peninsula. Faced with the rapid spread of the pandemic, the Spanish government decreed a state of alarm throughout the national territory on 14 March, extending it until 21 June, limiting the free movement of citizens to essential acts only, i.e., the purchase of food and medicines and seeking medical care, and from 30 March to 9 April all non-essential economic activity was suspended.

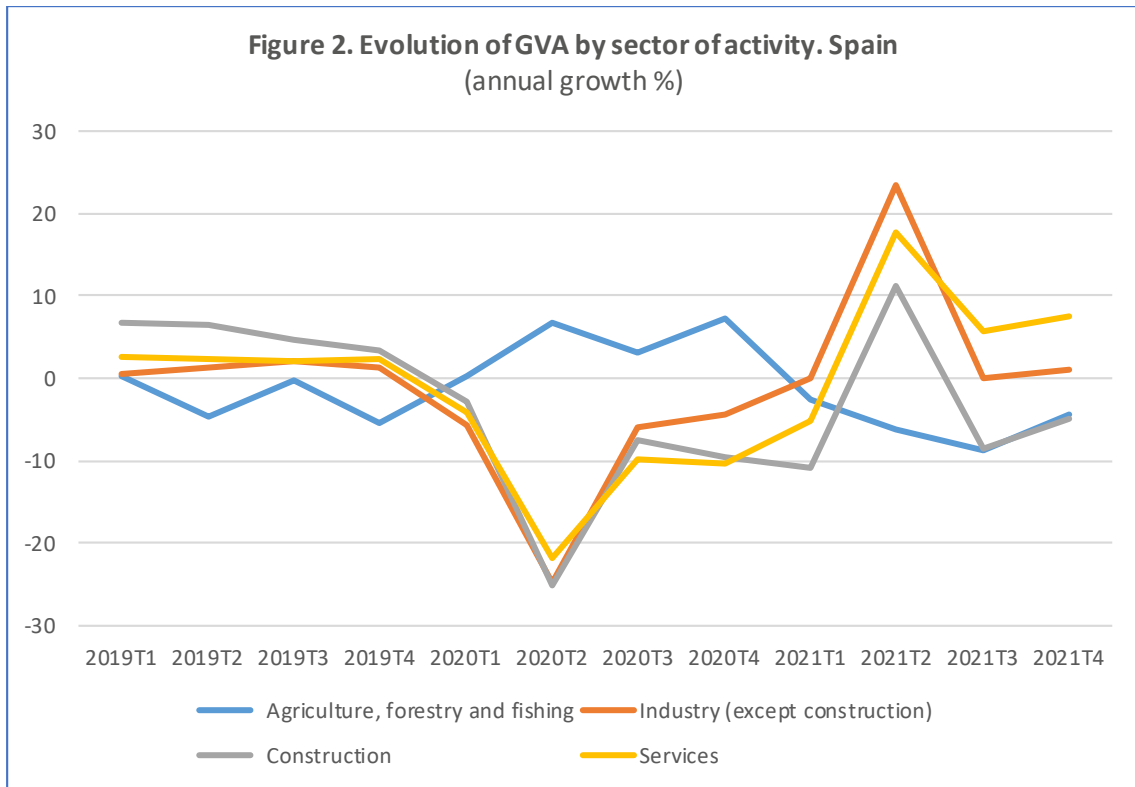
The economic impact of the crisis on the Spanish economy has been one of the most intense among developed countries, not only because of the high intensity of the pandemic and the strict confinement established but also because of some peculiarities of the Spanish economy, related to its productive structure. Those sectors, companies and workers that have significant importance in the economy have been most affected by the pandemic. (Banco de España, 2021). Thus, after maintaining sustained growth over the last six years, according to European Commission (Eurostat) estimates, GDP fell by 10.8% in 2020, the strongest fall recorded in the European Union as a whole (-5.9%), the euro area (-6.4%) and the leading developed economies.

Although the effects of the pandemic were already apparent at the end of 2019 the Spanish economy did not start to fall in year-on-year terms until the first quarter of 2020 – by 4.3% – and then declined by an exceptional 21.5% in the second quarter of the year and by nearly 9% in the third and fourth quarters. Thus, in 2020, the fall in GDP was 10.8%. However, in the first quarter of 2021, it continued to fall by 4.3%. This sharp decline in the Spanish economy is due to the greater weight of "social" activities, such as hospitality sector, and the composition of Spain's productive fabric which has a high percentage of SMEs (Arce, 2021).

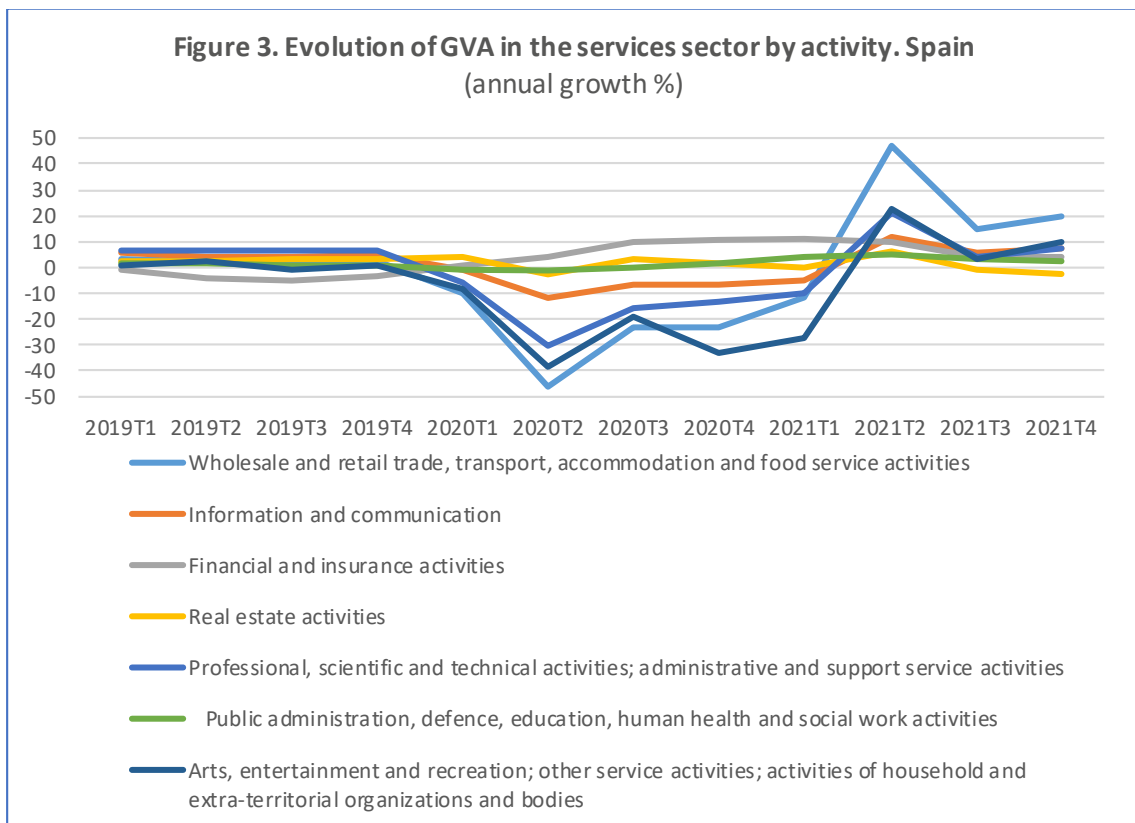


Source: Eurostat.

The initial impact of the pandemic was very severe in both industry and services, but not in the agricultural sector. However, the intensity and persistence of the decline in services - especially in hospitality, leisure, commerce and transport - contrasts with the more rapid recovery of the industrial sector (see Figures 2 and 3). Geographically, the fall in activity was particularly intense in the more touristic regions such as the Mediterranean coast and the islands. The most severely affected groups were young workers and those with temporary contracts in the labour market. The smallest firms have suffered the most significant contraction in turnover (Banco de España, 2021).



Source: Eurostat.



Source:

Eurostat.

The Spanish government's fiscal response to the pandemic has been substantial. However, the high initial public debt-to-GDP ratio has not allowed it to be as intensive as in other euro area countries. The impact of the measures adopted amounted to 5.5% of GDP in 2020 (European Commission, 2020a).

The main measures adopted were aimed at strengthening the health system to increase the capacity to care for the sick as well as promoting scientific research; protecting the most vulnerable people through direct transfers; protecting workers and the self-employed, facilitating teleworking, and making the conditions for accessing Temporary Redundancy Programmes (ERTEs) more flexible; and preventing company bankruptcies, by deferring the payment of taxes for SMEs, subsidising the Social Security contributions of workers affected by ERTEs and making a line of guarantees available to companies and the self-employed to safeguard their liquidity, among others.⁵⁴

The period of economic growth recorded by the Spanish economy since the end of 2013 has allowed it to correct some critical macroeconomic imbalances: in recent years, there have been recurrent surpluses in the current account balance, household and corporate indebtedness have fallen significantly, and the construction sector and the financial system have undergone a significant restructuring that has led to a substantial reduction in their size and fragility. However, significant imbalances remain, such as the general government balance, which has been running deficits since 2008 - and especially the structural deficit, which has been increasing since 2015 - the high public debt to GDP ratio, which has been rising since 2007, and the high segmentation of the labour market (Banco de España, 2020).

However, the Spanish economy continued to show large imbalances -high public debt and deficit, a highly segmented and more rigid labour market than in other neighbouring countries, low productivity growth, low public and private investment- together with weak, albeit sustained, growth, so that the shock of the pandemic hit the Spanish economy particularly hard. Thus, Spanish GDP per capita in 2020 was still at levels well below those of 2017, i.e. levels close to those of before the 2008 crisis.

⁵⁴ You can consult the following web pages for all the measures adopted as a result of the pandemic in relation to:

Tax measures: https://www.boe.es/biblioteca_juridica/codigos/codigo.php?id=360&modo=2¬a=0&tab=2

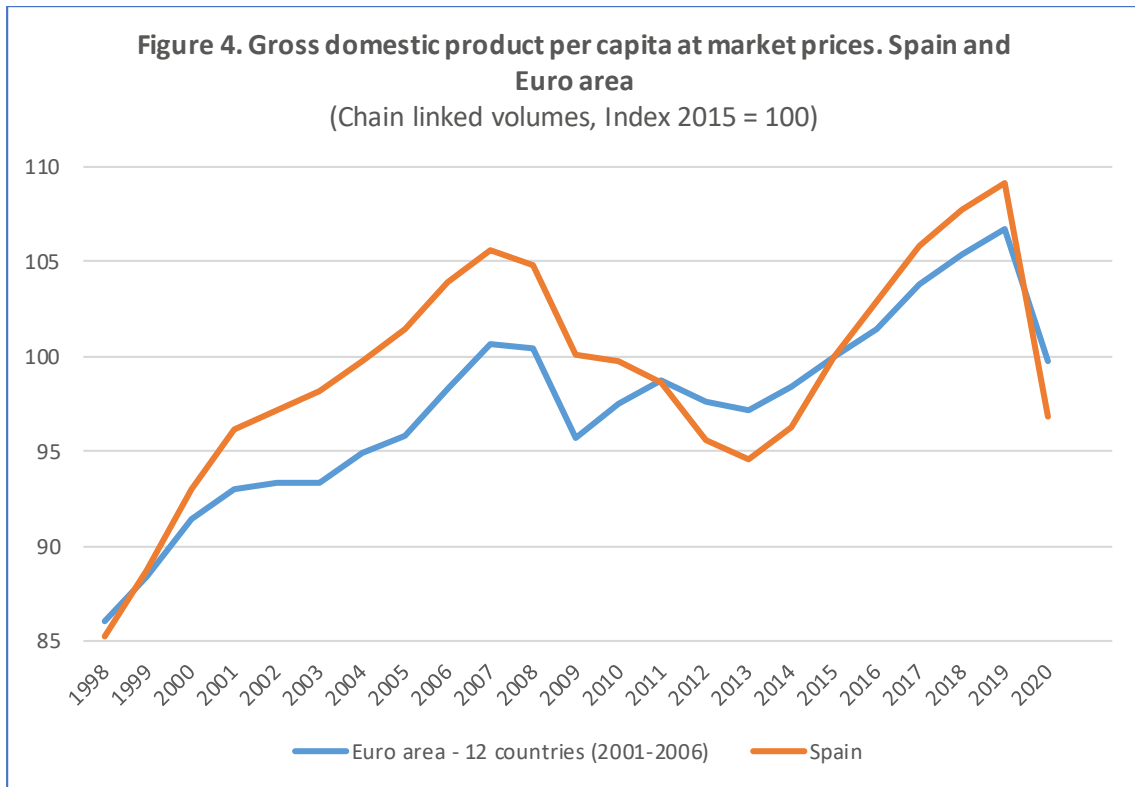
Self-employed workers: https://www.boe.es/biblioteca_juridica/codigos/codigo.php?id=358_COVID-19_Trabajadores_Autonomos&modo=2

Vulnerable groups: https://www.boe.es/biblioteca_juridica/codigos/codigo.php?id=359_COVID-19_Colectivos_Vulnerables&modo=2

Leasing of dwellings and commercial premises: https://www.boe.es/biblioteca_juridica/codigos/codigo.php?id=361_COVID-19_Arendamiento_de_vivienda_y_locales_comerciales&modo=2

European and State law: https://www.boe.es/biblioteca_juridica/codigos/codigo.php?id=355_COVID-19_Derecho_Europeo_y_Estatal__&modo=2

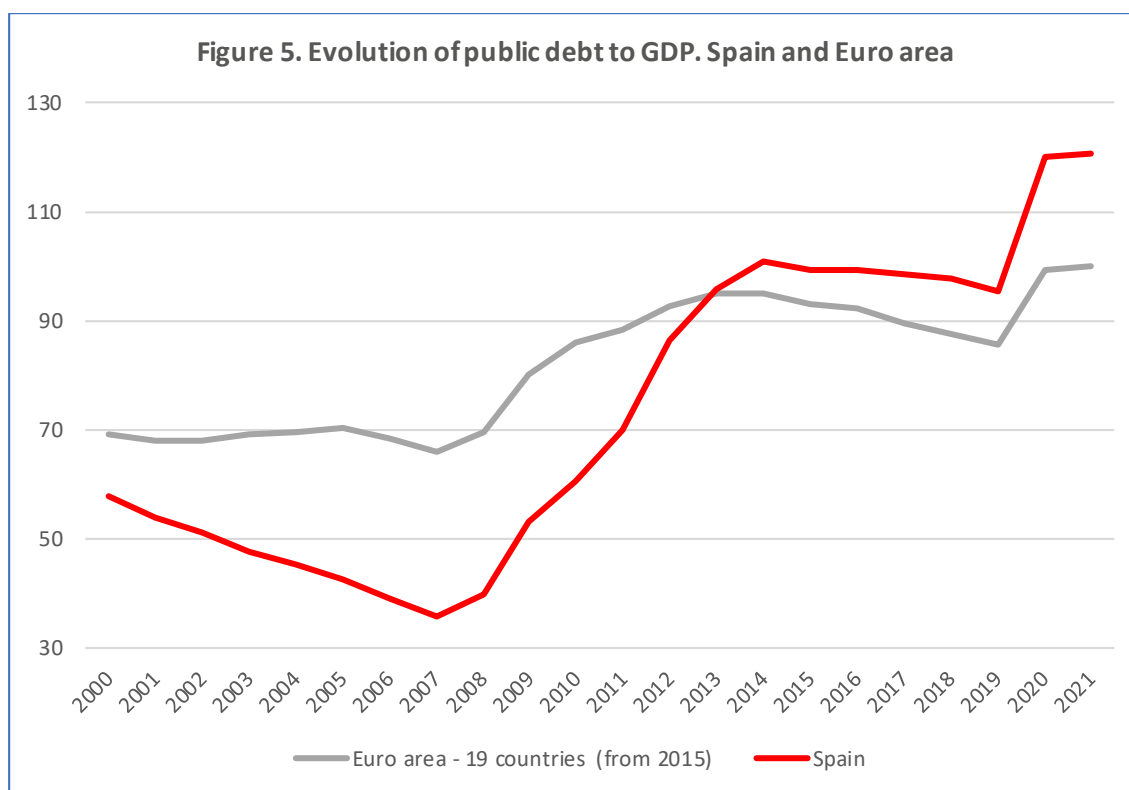
Autonomous Community Law: https://www.boe.es/biblioteca_juridica/codigos/codigo.php?id=396_COVID-19_Derecho_Autonómico&modo=2



Source: Eurostat.

SPANISH VULNERABILITIES

High public debt and deficit: The Spanish general government has been running a deficit since 2008, despite the slow but sustained economic recovery since late 2013, which caused public debt to rise progressively to 95.5% of GDP in 2019 (78.5% and 85.5% the EU and the euro area, respectively), far from the 35.8% recorded before the financial crisis.

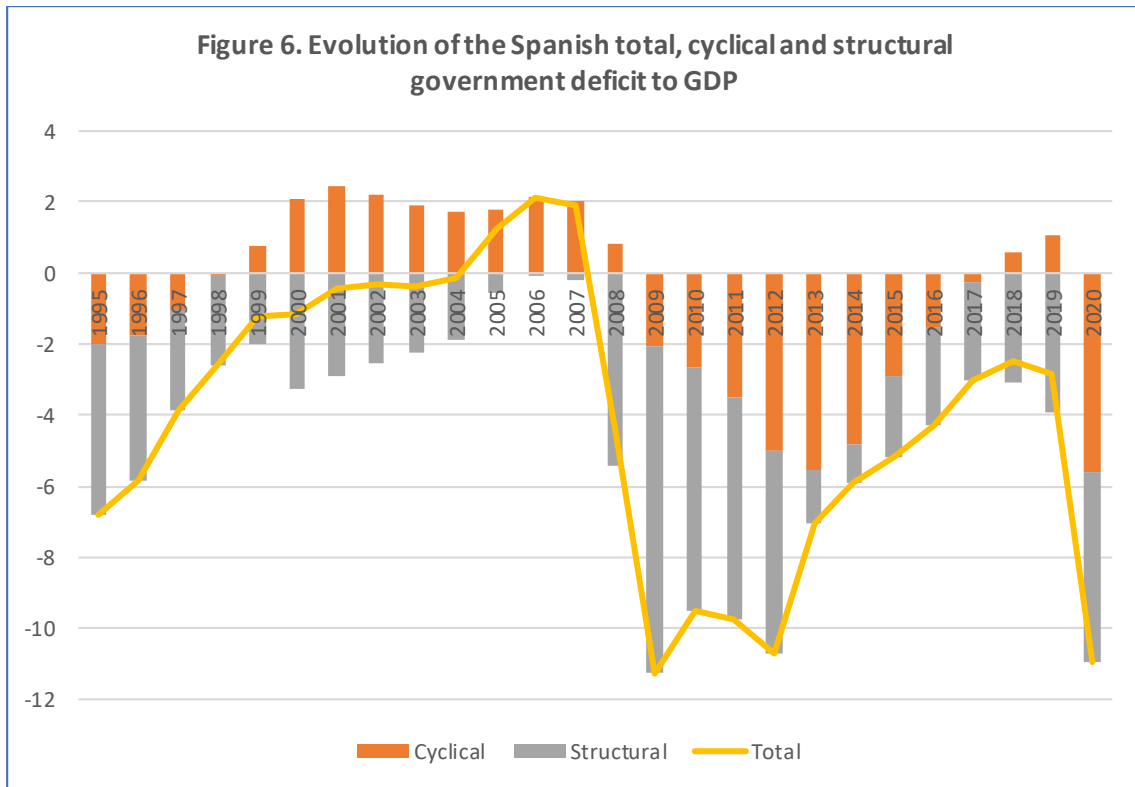


Source: AMECO.

Moreover, the Spanish public deficit is largely structural. In fact, in 2019 the general government balance (-2.9% of GDP) was due exclusively to structural factors (-3.9%)⁵⁵ as cyclical factors resulted in surpluses (1%), and since 2015 the structural deficit of the Spanish economy has not stopped increasing.

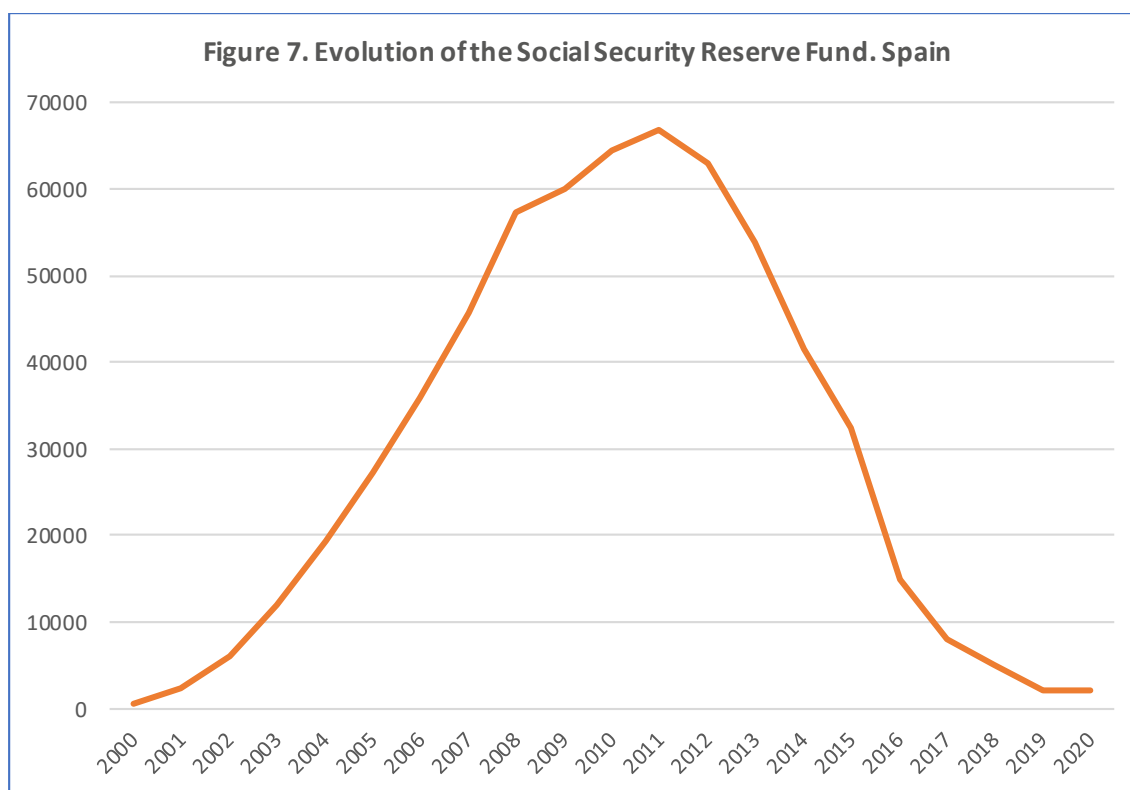
The public deficit to GDP rose by 11% in 2020, half of it a. As a result, public debt soared to 120% of GDP, increasing 24.5 percentage points, the highest increase recorded since statistical information has been available (AIReF, 2021).

⁵⁵ Spain's high structural deficit is mainly due to Social Security (which accounts for about 40% of consolidated expenditure), and more specifically due to high pension expenditure.



Source: AMECO.

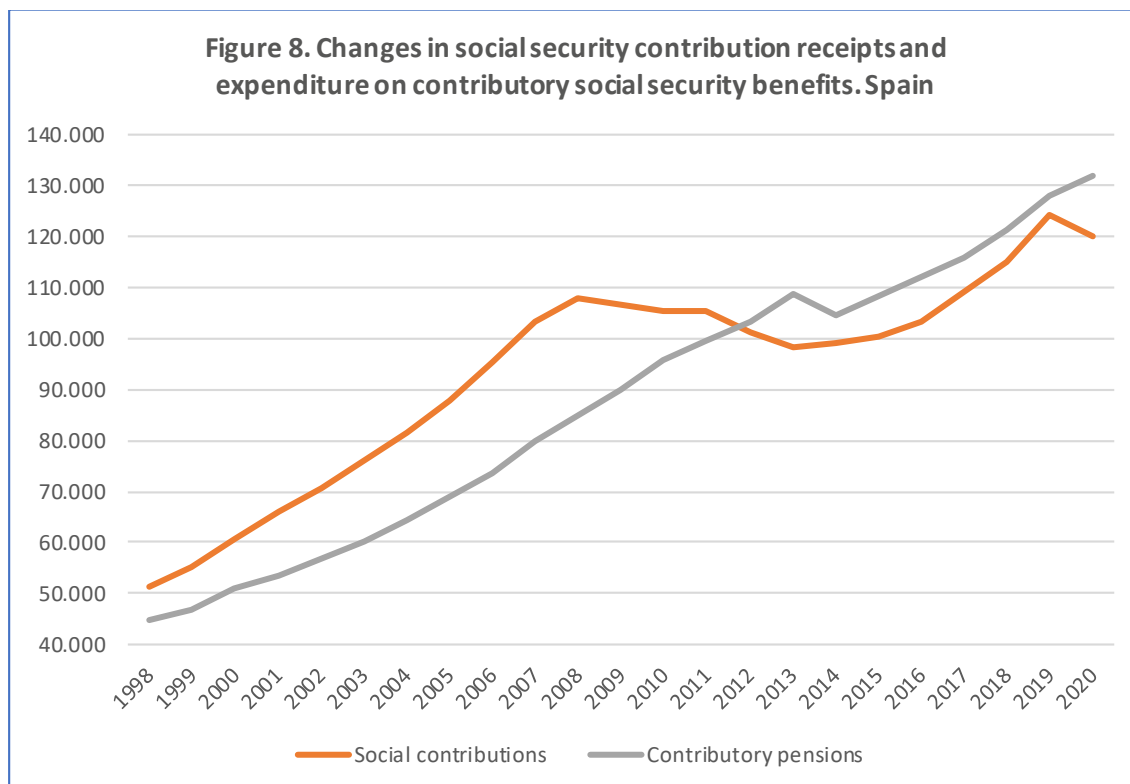
Concerns about the pension system's sustainability: Since 2008, the social security system has shown a substantial imbalance in its non-financial balance. Thus, since 2007, when the system was running a surplus, the deterioration of its balance reached 2.8 percentage points of GDP by 2019, representing a deficit of 1.3% of GDP, i.e. the equivalent of around EUR 17 billion. This permanent budgetary imbalance has led to the social security reserve fund falling from €66.8 billion in 2011 to just over €2 billion by the end of 2019.



Note: EUR million

Source: General Treasury of the Social Security.

The deterioration in the social security balance responds to the accelerated increase in spending on contributory pensions compared to the much more modest growth in revenues from Social Security contributions (see Figure 7), due to both an increasingly ageing population, rising life expectancy, and progressively higher pensions (Hernández de Cos, 2021).

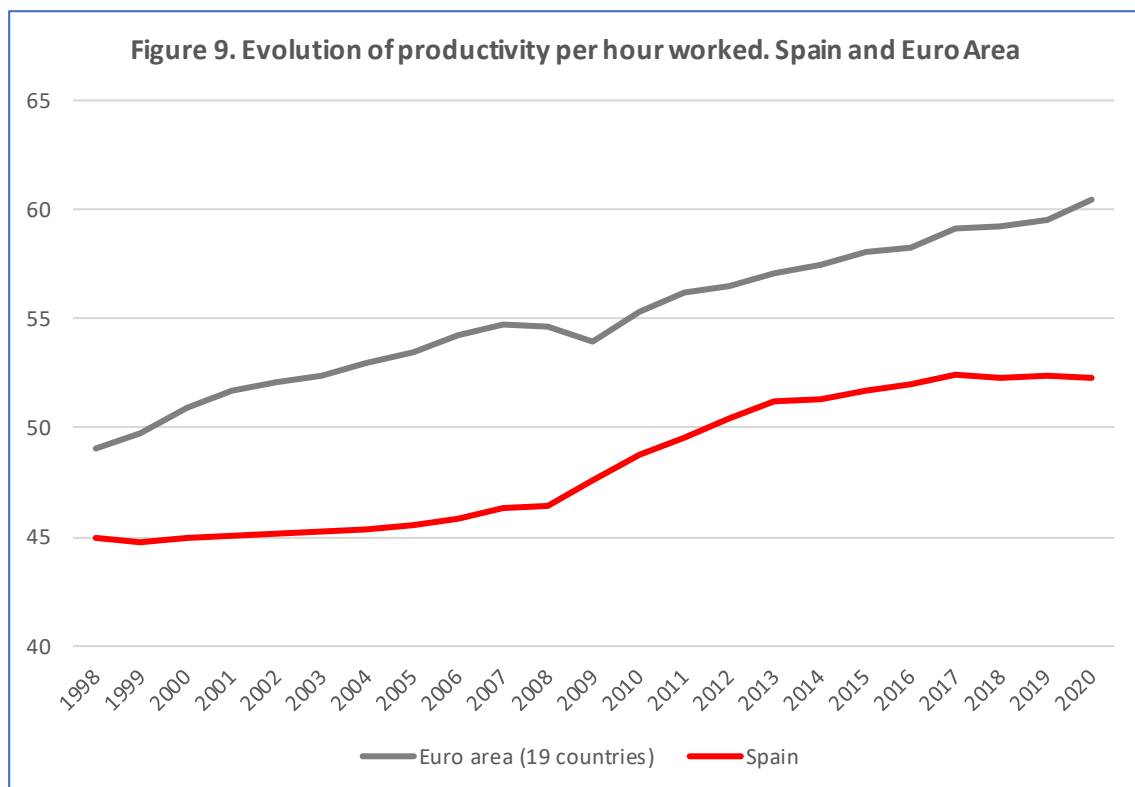


Note: EUR million

Source: General Treasury of the Social Security.

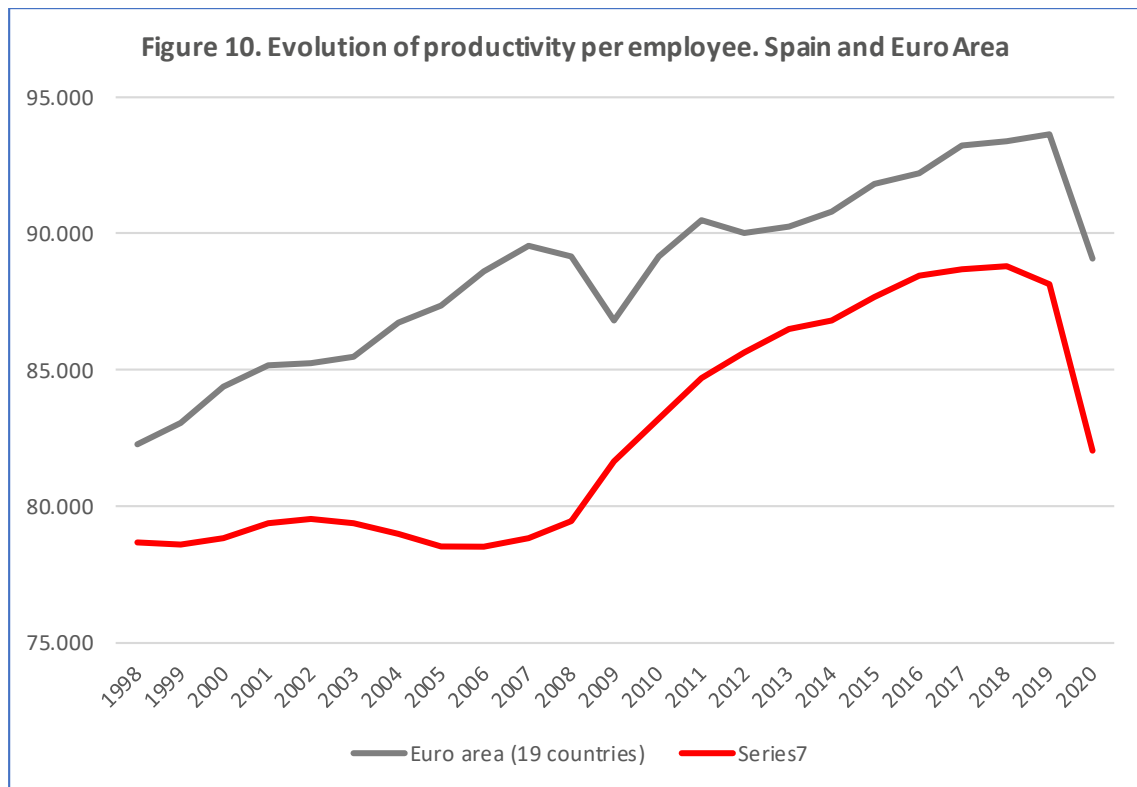
Deficiencies in the public health system: Spain's public health system is today one of the most advanced in the world, both in terms of the quality and accessibility of its services and its efficiency, as well as its universal nature. In the last two decades, public health spending as a percentage of GDP has increased by more than two percentage points, standing at 9.1% of GDP in 2019. However, the pandemic has revealed a public health system with a shortage of permanent staff and a structure that pays too little attention to mental health (OECD 2021, 2021b). In addition, the system must adapt to the new needs of an ageing population, whose expenditure in the health system is higher - more frequent visits to general and specialised medical consultations and higher consumption of medicines - as has been demonstrated with the pandemic.

Low productivity growth: Low productivity growth is compromising the country's economic development, as well as being strongly linked to low wages, long working hours and the lack of competitiveness of many firms. In recent decades productivity growth has been very modest, measured by both total factor productivity and by productivity per hours worked and per worker, due both to the greater weight in the Spanish economy of activities with lower productivity growth and to lower productivity in all productive sectors (Fernández Cerezo & Montero, 2021). The fact is that low productivity growth cannot only be blamed on the production structure but there are four other factors of a cross-cutting nature that limit the efficiency of the economy (Oficina Nacional de Prospectiva y Estrategia del Gobierno de España, 2021).

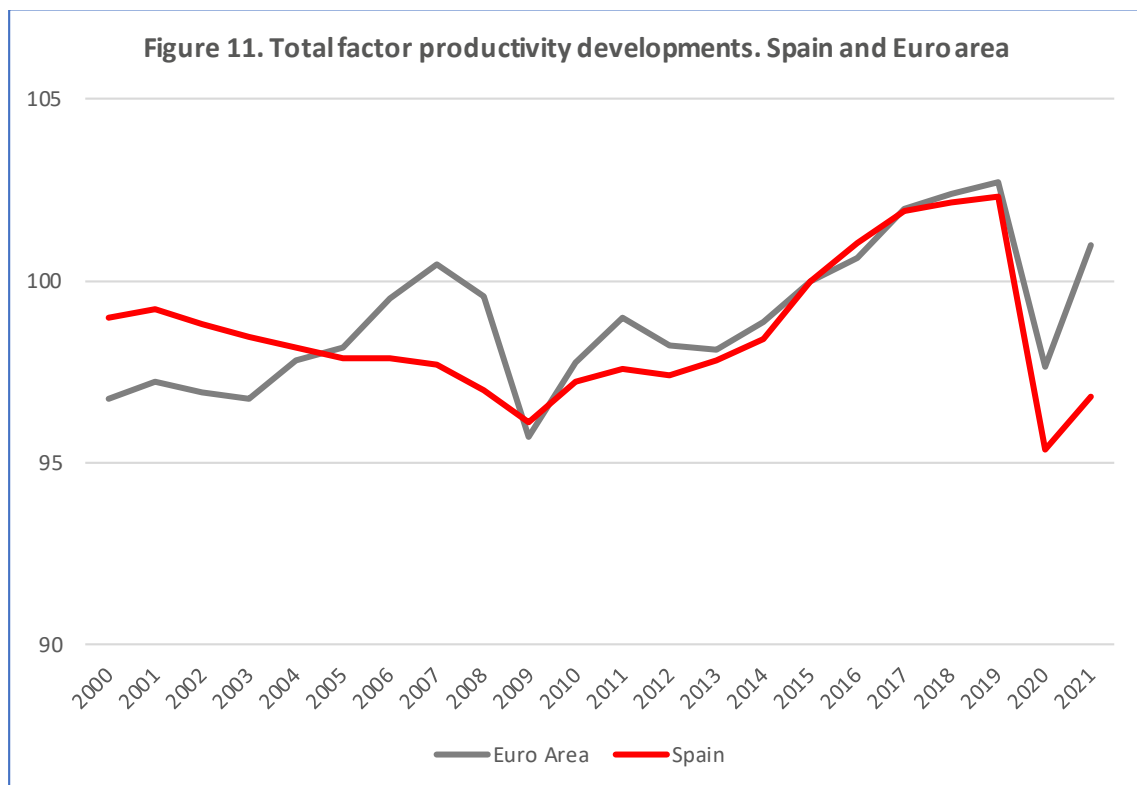


Note: USD, constant prices, 2015 PPPs.

Source: OECD.



Note: USD, constant prices, 2015 PPPs.
Source: OECD.



Note: Index 2015 = 100.
Source: AMECO.

Firstly, human capital. Despite the progress made in recent decades, Spain still has a lower level of human capital than the most advanced economies (OECD, 2018), and there is still much room for improvement in terms of the development of managerial skills, business leadership and human resource management, especially in small businesses and among the self-employed (OECD, 2021).

Secondly, innovative capacity. Although Spain has greatly strengthened its capacity to innovate, improving its human resources, expanding its technological infrastructures and increasing the share of more knowledge-intensive sectors and firms in its economy (European Commission, 2021a), the country still lags behind the EU27 average in global innovation rankings (European Commission, 2021a). Moreover, Spain invests less in intellectual property, its R&D expenditure relative to GDP is lower and its number of patents is lower than that of the leading European and world powers. This reduced innovation deficit is particularly concentrated in the business sector due to the predominance of SMEs in the productive fabric, the lower relative weight of more capital-intensive sectors, the scarce connection between universities and companies, and the reduced presence of bonds, shares or venture capital in Spanish business financing. However, the Spanish public administration also contributes to low innovation: state aid is scarce and involves a lot of bureaucracy, it is often granted in the form of loans, which discourages applications, and much of the aid is not implemented. Finally, research and higher education centres in Spain still have lower levels of research, innovation, scientific and digital transfer, and business creation than the most advanced countries in Europe (Fundación COTEC, 2021) (Oficina Nacional de Prospectiva y Estrategia del Gobierno de España, 2021).

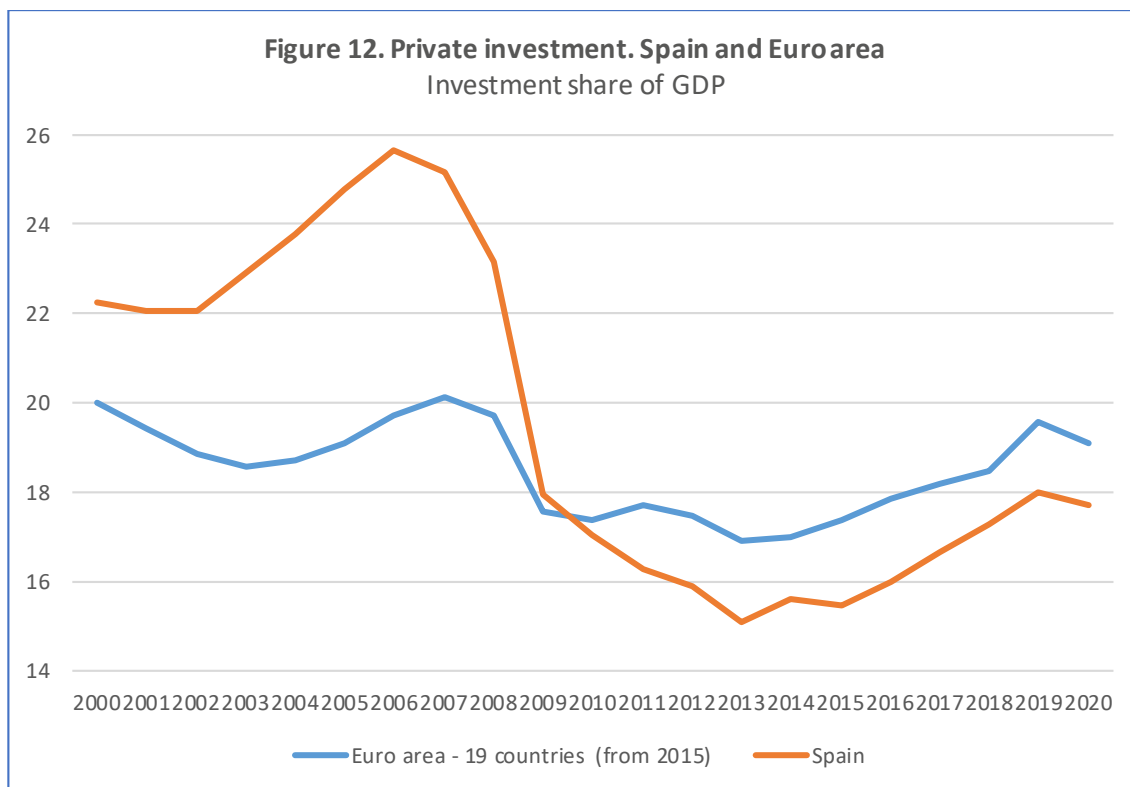
Thirdly, the implementation of digital technology (to which we devote a later section). Spain has made great progress in recent decades, although it still lags behind in the availability of digital skills among the population or the integration of digital technology in companies (European Commission, 2020b). However, the pandemic has had a positive impact on this vulnerability, increasing the number of companies using big data, increasing the use of e-commerce and significantly increasing the percentage of the working population that teleworks (Oficina Nacional de Prospectiva y Estrategia del Gobierno de España, 2021).

Fourth, regulation. Productivity is also strongly conditioned by the quality of the institutional and regulatory framework. Spain now appears in all rankings as a fully-fledged state with freedoms and guarantees as extensive as those of the most advanced countries. However, there is still room for improvement in such essential aspects as accountability, control of corruption, and government effectiveness, where Spain performs worse than its peers (World Justice Project, 2021). Reforms carried out in recent years have also helped to increase competition and reduce market fragmentation (OECD, 2019), although there are still legal and administrative obstacles that hinder innovation and business growth, such as some restrictions on starting a business (World Bank, 2021), some barriers to business start-ups (World Bank, 2021), certain barriers to entry in the services sector (Alonso-Borrego, 2010), the heterogeneity of procedures for doing business at regional level or linked to business size (Almunia & López-Rodríguez, 2018; Fariñas & Huergo, 2015) and the low efficiency of insolvency procedures (García-Posada Gómez, 2020). Finally, productivity progress has also been conditioned by labour regulations (to which we devote a later section) as well as the public procurement system, which tends to benefit consolidated firms (European Commission, 2020c), and the large size of the shadow economy (Kelmanson & al., 2019).

Reduced public and private investment: Since the outbreak of the international financial crisis, Spain's investment effort ⁵⁶ has recorded much more modest growth than its neighbouring countries.

⁵⁶ This is calculated as the ratio between the investment made and the GDP generated in the corresponding year.

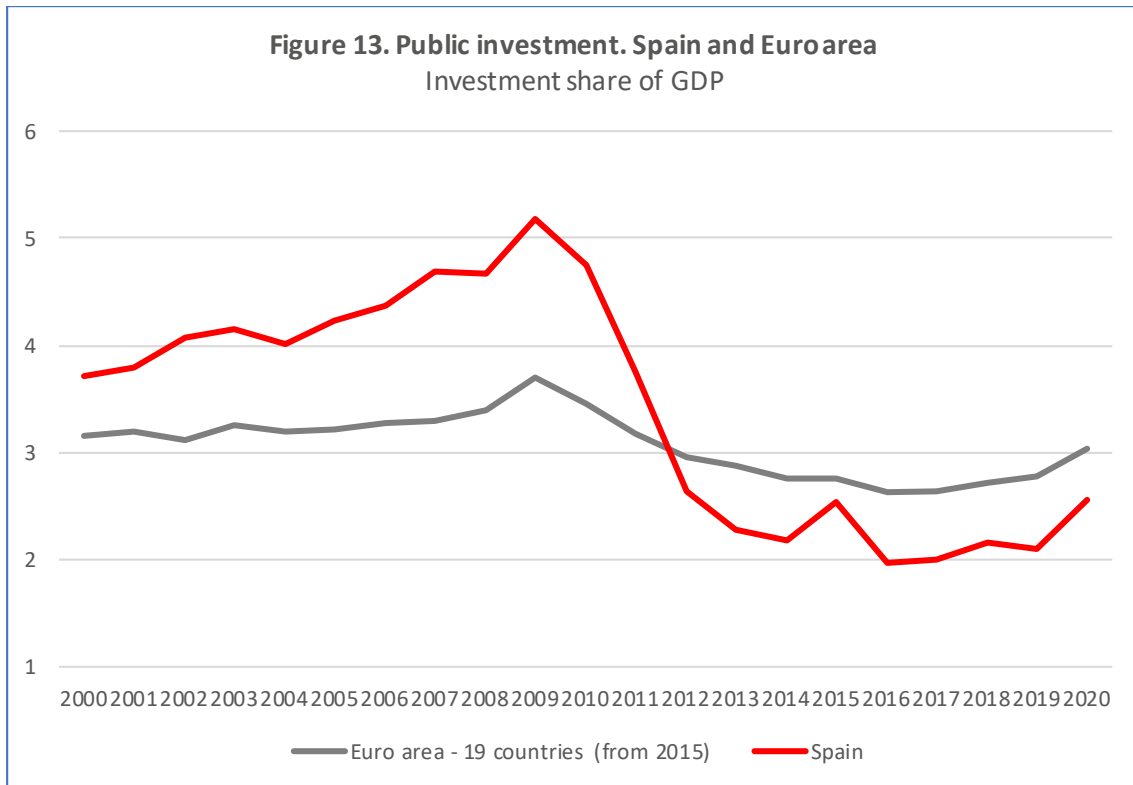
Spanish private investment as a percentage of GDP grew at a very high rate between 1995 and 2007, so that in 2007 it was more than twice as high as in 1995. Following the outbreak of the crisis, it plummeted, reaching a minimum in 2013. Since then, it has shown slow but sustained growth, although it has remained below the average of the eurozone countries, and the pandemic has triggered a new relapse, albeit lower than in the eurozone countries as a whole.



Note: Private investment is calculated as the total investment of all sectors excluding public investment.

Source: Eurostat.

Unlike private investment, Spanish public investment as a percentage of GDP maintained high growth until 2010, due to the expansionary fiscal policy implemented by the government after the outbreak of the financial crisis in 2008. However, from that date onwards it fell drastically and since 2013 it has remained at levels similar to those of 1995, which has been detrimental to health, education and public infrastructure. The pandemic also caused public investment in Spain to fall more than in the eurozone as a whole in 2020 (Mas Ivars & Pérez García, 2021).

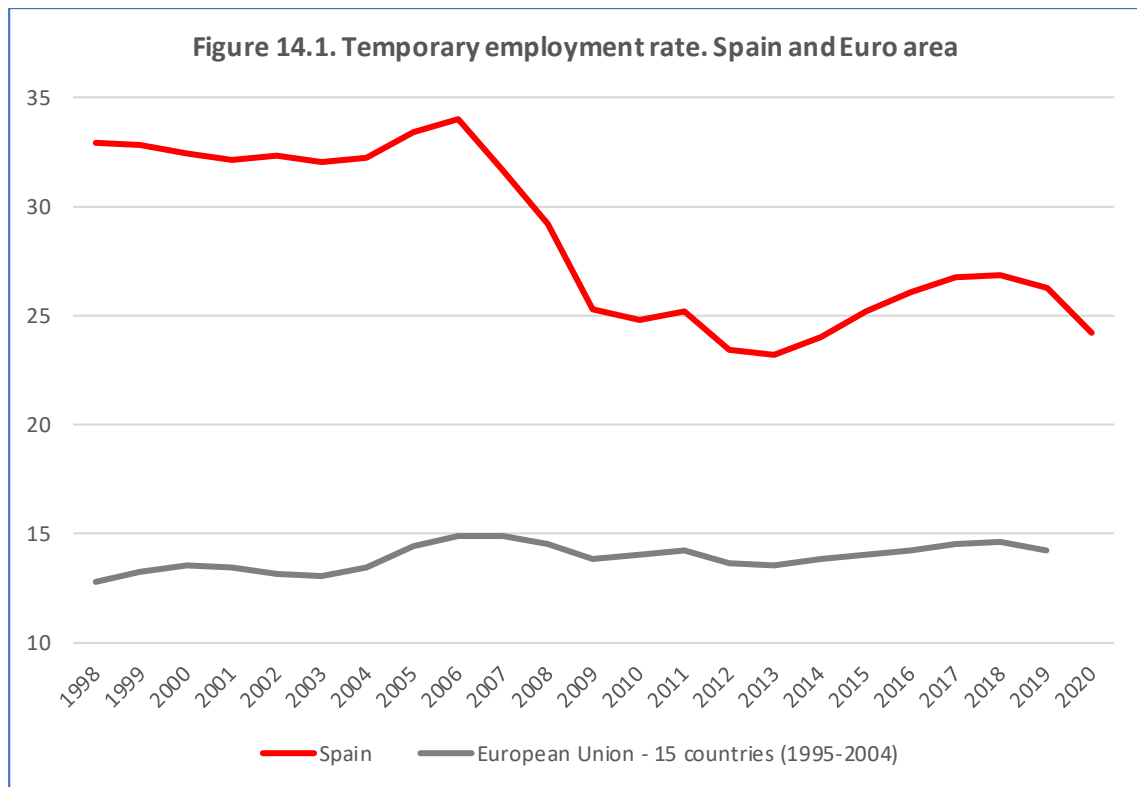


Source: Eurostat.

A labour market that suffers from severe structural weaknesses: The Spanish labour market is characterised by a high rate of temporary employment, higher unemployment rates, especially among young people and women, and a high rate of long-term unemployment compared to the average of EU and Eurozone countries, despite the 2012 labour reform which made the Spanish labour market more flexible. Moreover, there is currently a severe mismatch between the skill levels required by the productive sectors and the training of the labour force, as well as a mismatch between the average skill levels in Spain and the rest of the European Union countries (Gobierno de España, 2021) and (Servicio Público de Empleo Estatal, 2020).

During the pandemic, these imbalances have become more pronounced. Job losses have been concentrated among young workers, temporary workers and women, accentuating social inequalities (OECD (2021)). Indeed, after growing steadily since 2014, the temporary employment rate fell by five-tenths of a percentage point in 2019 and by 1.6 percentage points in 2020. In turn, the youth unemployment rate rose by 5.8 percentage points, to 38.3% in 2020, and the female unemployment rate by 1.4 percentage points, to 17.4% - a far cry from the 13.9% for men.

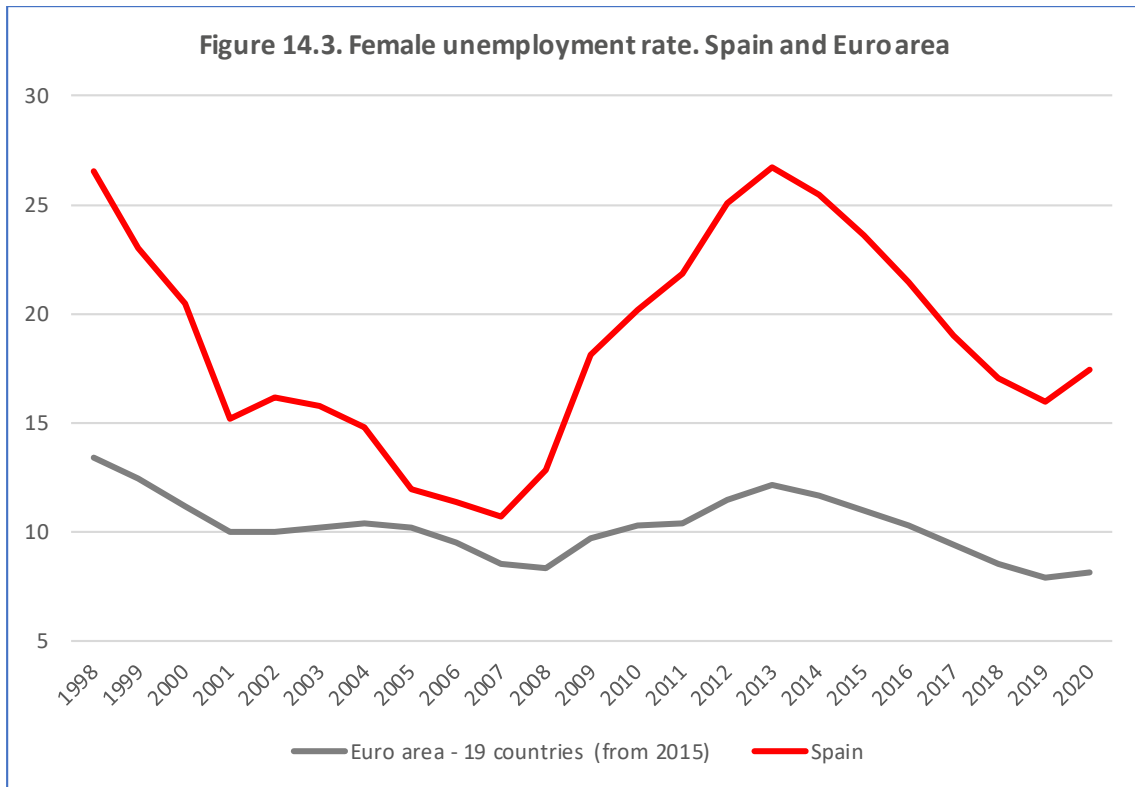
Figure 14. Labour market indicators



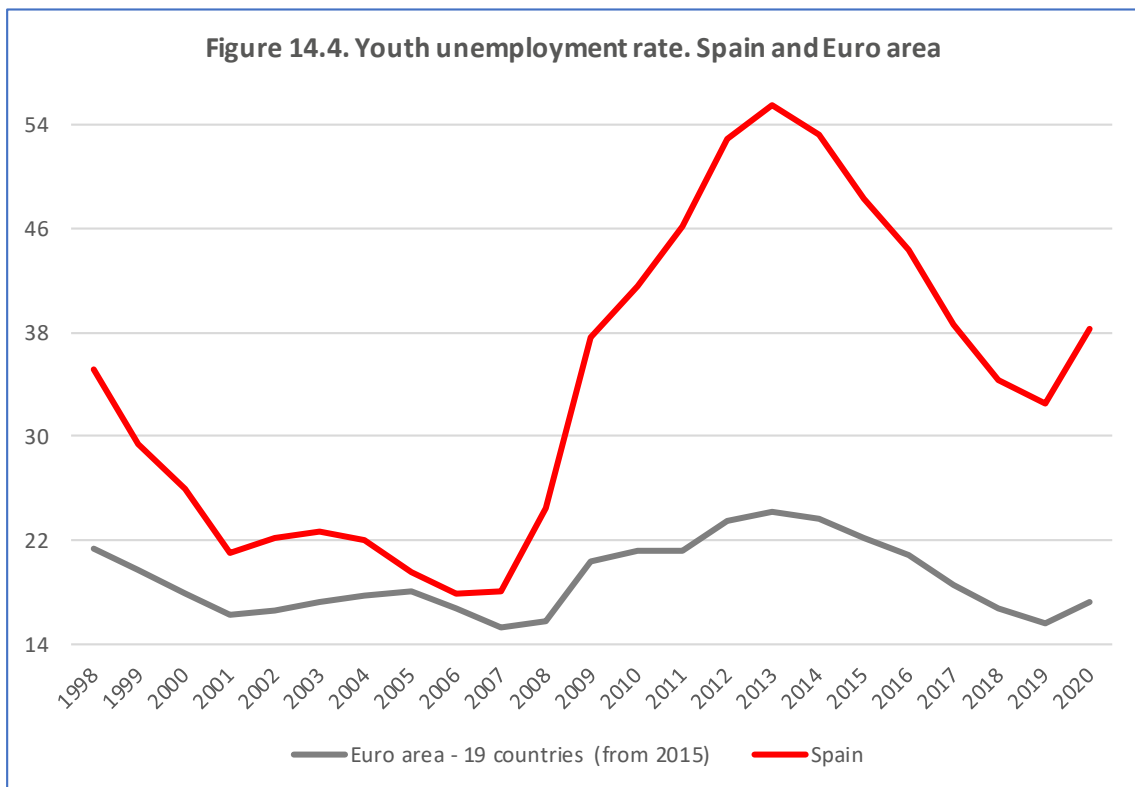
Source: Eurostat.



Source: Eurostat.

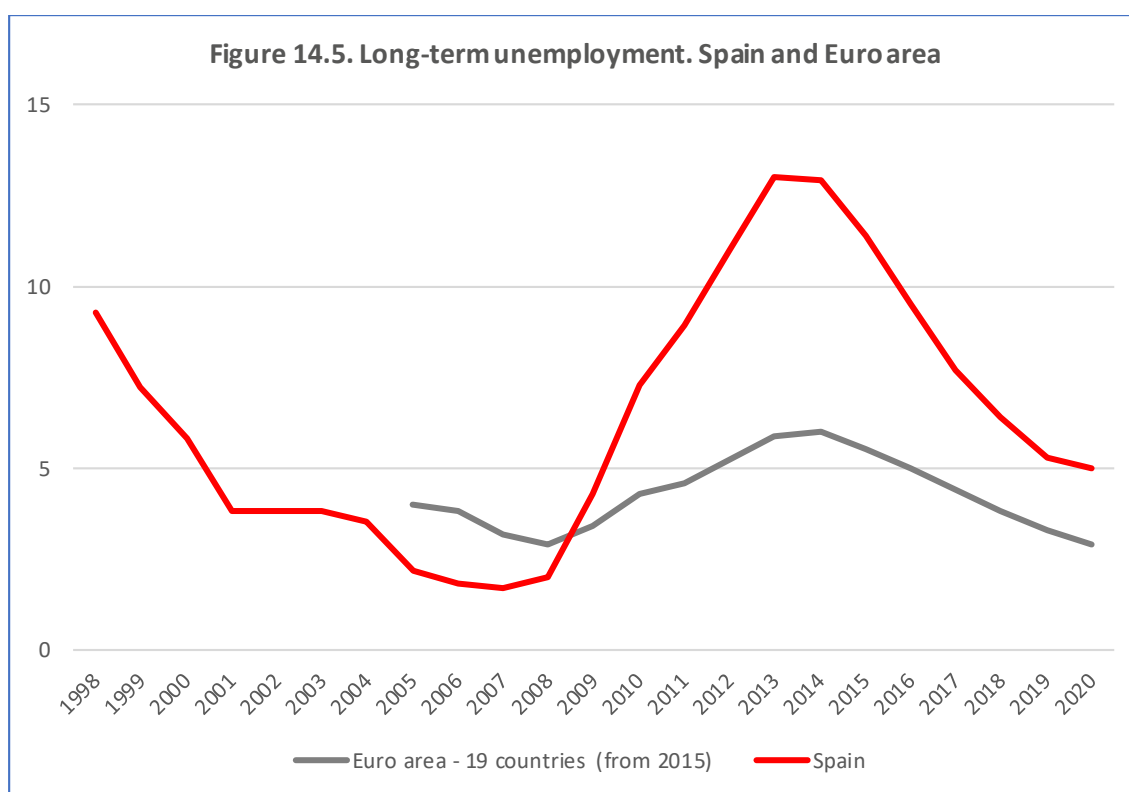


Source: Eurostat.



Note: Population aged 15-24.

Source: Eurostat.



Note: Population aged 15-74.

Source: Eurostat: Eurostat.

Lack of coordination between the different levels of Spanish public administrations: The pandemic has highlighted the lack of coordination between the different levels of government: central government and autonomous regions - those with devolved powers in health and education-, including the lack of reliable and homogeneous data from the National Public Health Surveillance Network. (Otero-Iglesias, Molina, & Martinez, 2020).

THE SPANISH NATIONAL RECOVERY AND RESILIENCE PLAN⁵⁷

The recovery plan's structure

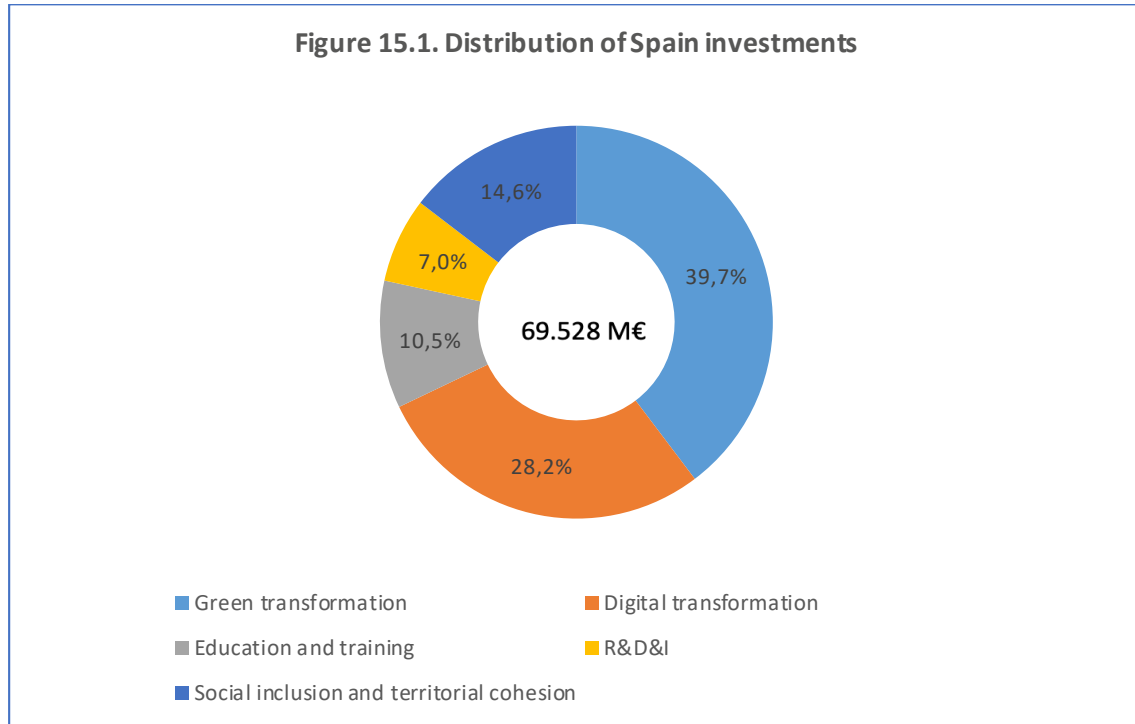
The Spanish Recovery and Resilience Mechanism amounts to 140 billion euros until 2026, of which around 69.5 billion euros correspond to non-refundable transfers and the rest in loans (although at the time of writing, Spain has not applied for any loans). In addition, Spain will receive from the REACT-EU Fund just over 12 billion euros for implementation in the period 2021-2022.

"Spain Can" Plan, drawn up by the Spanish government and approved by the European institutions, includes reforms and investments to be implemented between 2021 and 2023. Over this period, almost 69.5 billion euros will be allocated, which will be directed mainly to the areas of green transformation (39.1%) and digital transformation (29%), education and training (10.5%) and Research and Development and Innovation (7%), in addition to the strengthening of social inclusion and territorial cohesion.

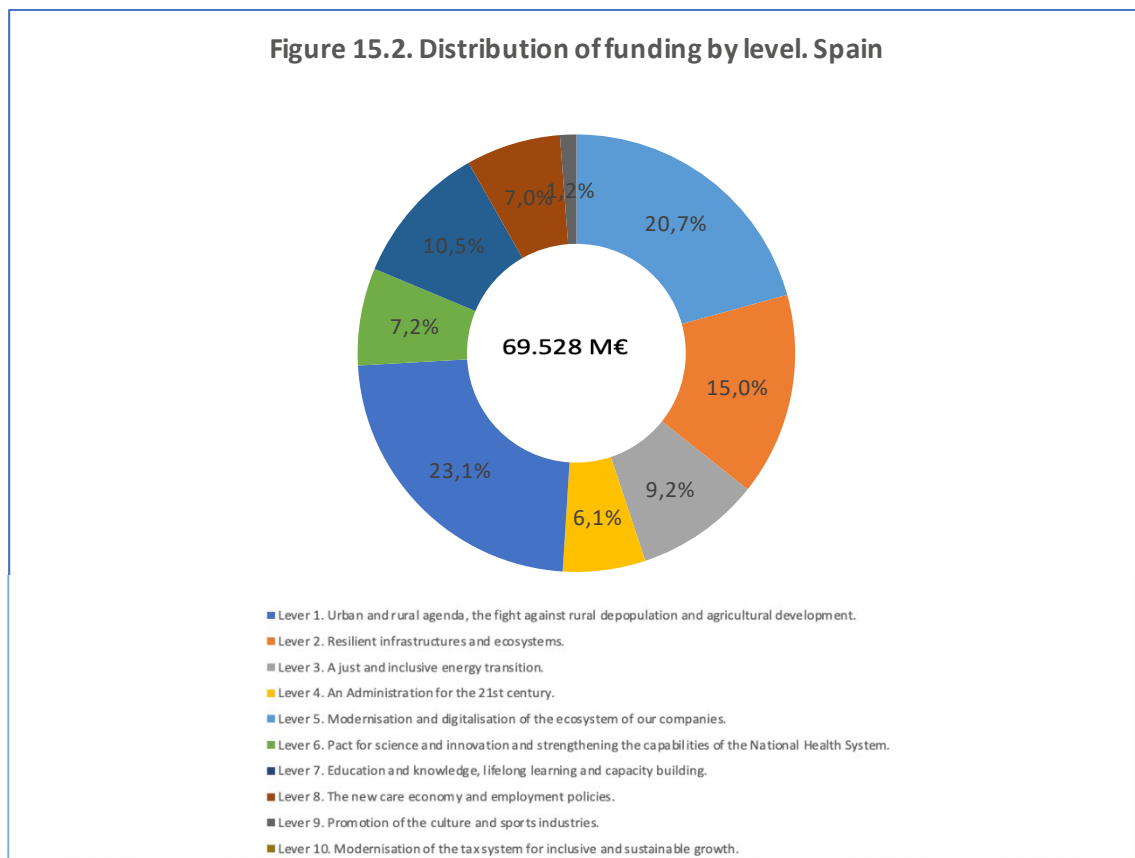
⁵⁷ Puede consultar de forma detallada el PRR español en la siguiente página web: <https://planderecuperacion.gob.es>

The Spanish Plan has four cross-cutting axes: ecological transition, digital transformation, social and territorial cohesion and gender equality, and is organised around ten levers that bring together the 30 components and reforms to modernise the country. The Plan includes 212 measures, of which 110 are investments and 102 reforms, for the period 2021-2023.

Figure 15. Destination of Spanish Recovery and Resilience Plan funds



Source: Own elaboration based on the Spanish RRP "Spain Can".



Governance: To establish a governance model that achieves an agile and efficient deployment of the investments and reforms of the Recovery and Resilience Plan and that guarantees transparency, coherence and continuity of actions, the Spanish government has implemented a specific regulatory, financial, budgetary and governance framework with the adoption of Royal Decree-Law 36/2020 of 30 December. The governance model is organised as follows:

- A Commission for Recovery, Transformation and Resilience has been set up, to be chaired by the President of the Government and composed of all Ministers, the Secretaries of State for the Economy and Enterprise Support, Finance, Budget and Expenditure, Social Rights, the General Secretariat for European Funds and the Secretary-General for Economic and G20 Affairs of the President's Office. This Commission has established the general policy guidelines for the development and implementation of the Plan and, once approved by the Council of Ministers, will carry out the strategic monitoring of the Plan.
- A Technical Committee has been set up, composed of 20 members of the public administration and chaired by the Secretary-General for European Funds, which will provide technical and legal support to the Ministerial Commission and will also act as a support body for the responsible authority in the development of its coordination functions.
- The General Secretariat for European Funds has been created within the Ministry of Finance as the authority responsible for the Plan, which will act as coordinator with the latter. This Secretariat will have two Directorates-General: the Directorate General for European Funds and the new Directorate-General for the Recovery and Resilience Plan and Mechanism. This unit will promote the development of the Plan and coordination with the Ministries, public bodies, Autonomous Communities, local entities and other national and EU bodies involved in the Recovery Plan.

Impact on GDP of the plan⁵⁸: The RRP includes the estimated impact of the transfers received from the Recovery and Resilience Mechanism with a bottom-up approach, taking into account the plans that make up the different levers. On the one hand, the Plan includes a large number of structural reforms that will transform the productive and social fabric in the long term, which could lead to potential growth of the Spanish economy in the medium to long term of four-tenths of a percentage point. On the other hand, the Plan implies a short and medium-term impact of boosting demand through the injection of public funds, which would push GDP by 2%. In terms of employment, it is estimated that the Plan could generate 800,000 jobs, as well as an improvement in exports of 0.2 percentage points in the long-term export growth rate.

ASSESSMENT OF MEASURES ADOPTED IN THE SPANISH RRP TO ADDRESS STRUCTURAL CHALLENGES

The following is a summary of the measures adopted to mitigate the vulnerabilities, either accentuated or emerging, as a result of the COVID-19 pandemic:

Measures adopted concerning the consolidation of public finances: These measures are included under Lever X. "Modernisation of the fiscal system for inclusive and sustainable economic growth" of the Spanish RRP, specifically within Components 27 to 29.

Component 27, "Measures and actions to prevent and combat tax fraud", aims to implement reforms to avoid new forms of tax fraud, increase the effectiveness of tax control, encourage voluntary compliance by taxpayers with their tax obligations, advance in cooperative compliance, and

⁵⁸ These results cannot be directly compared to the numbers reported in the European Commission Assessment of Spain plan given that there are differences in the assumptions and methodology.

incorporate reforms that are in line with the actions adopted at the international level. Among the necessary reforms for the modernisation of the tax system and the Tax Administration addressed by this component are the updating of the list of tax havens, the limitation of cash payments for certain economic operations, the modification of the regime of the list of debtors to the Public Treasury, the prohibition of tax amnesties, the creation of Integral Digital Assistance Administrations, and the exploitation of information derived from international instruments, among others. The planned investment is 191 million euros for 2020 to 2024, although not financed through Next Generation funds.

Component 28, "Adapting the tax system to the reality of the 21st century" aims to make the Spanish tax system more equitable, progressive and fair, while at the same time strengthening the design of a green tax system, incorporating the gender perspective and promoting public policies of general interest, such as health protection. All this, paying attention to the balance of public finances and significantly reducing the structural deficit to guarantee the Welfare State. No budget is included in this component.⁵⁹

Finally, Component 29, "Improving the efficiency of public spending" aims at strengthening the consolidation of public finances and the sustainability of public debt in the medium term, as well as redirecting spending towards more productive uses. The budget to achieve this objective amounts to EUR 6.8 million, which does not come from the funds granted to Spain under the Next Generation Plan.

According to the European Commission, these components respond to several of the recommendations made to Spain between 2019 and 2020, such as strengthening the budgetary and public procurement frameworks at all levels of government and implementing, where economic conditions allow, budgetary policies aimed at achieving prudent budgetary positions in the medium term to ensure debt sustainability, while encouraging investment (European Commission, 2020f). In our opinion, there is a lack of specificity regarding the structural reforms to be adopted; the objectives are set but the measures to be adopted are not specified, especially with regard to the reduction of the Spanish deficit, the structural deficit in particular..

Measures adopted concerning the sustainability of the public pension system: Reforms relating to the public pension system are also included within Lever X, "Modernisation of the fiscal system for inclusive and sustainable economic growth" of the Spanish RRP, specifically under Component 30. "Sustainability of the public pension system in the framework of the Toledo Pact"⁶⁰. The overall objective is to ensure the financial sustainability of the public pension system in the short, medium and long term, maintaining the purchasing power of pensioners, reinforcing protection against poverty and guaranteeing intergenerational equity, all within the unanimous agreement reached by the plenary of Congress on 19 November 2020. As more specific objectives, it proposes, firstly, to eliminate the deficit of the social security system; secondly, to adjust the parametric adjustments to progressively increase the retirement age and encourage the voluntary delay of access to retirement; thirdly, to guarantee the purchasing power of pensioners by linking the revaluation of pensions to the inflation rate; and fourthly, to promote supplementary pension systems in the business and professional sphere.

⁵⁹ Within the framework of the Recovery, Transformation and Resilience Plan, the Spanish government commissioned a committee of experts to analyse, after the Covid-19 pandemic, the necessary adaptation of the tax system to the demands of the evolution of economic activity in a global world undergoing intense technological transformation and which must seriously address the problem of climate change. This commission led to the presentation, on 3 March 2022, of a white paper proposing reforms in areas such as international taxation, environmental taxation and the digital transformation of the economy, promoting sustainable economic growth.

⁶⁰ Las recomendaciones del Pacto de Toledo pueden consultarse en el siguiente enlace: https://www.congreso.es/public_oficiales/L14/CONG/BOCG/D/BOCG-14-D-175.PDF

The Commission considers that this component responds to the country-specific recommendations on preserving the pension system's sustainability and on implementing, where economic conditions allow, budgetary policies aimed at achieving prudent medium-term budgetary positions and ensuring debt sustainability while fostering investment (European Commission, 2020f). However, we believe that the measures do not go far enough to maintain the pension system and to avoid a further increase in the Spanish public deficit, and that public pressure is likely to push back some of these proposals.

Measures adopted concerning the labour market: Labour market reforms are included, on the one hand, under Lever VII, "Education and knowledge, lifelong learning and skills development", specifically under Component 19, "National Digital Skills Plan" and Component 20; "Strategic plan to boost vocational training" and, on the other hand, under Lever VIII, "New care economy and employment policies", specifically under Component 22, "Shock plan for the care economy and reinforcement of inclusion policies" and Component 23, "New public policies for a dynamic, resilient and inclusive labour market". This aims to develop the digital skills of citizens, with actions mainly aimed at training the active population in general and ICT specialists in particular, as well as the digital transformation in education so that Spanish companies can face the challenges and take advantage of the opportunities of the digital economy. To this end, 3,593 million euros have been allocated from the Recovery and Resilience Mechanism, to be implemented between 2021 and 2024 by the Ministry of Economic Affairs and Digital Transformation, the Ministry of Education and Vocational Training and the Ministry of Foreign Affairs, European Union and Cooperation, as well as the Autonomous Regions, Provincial Councils and Local Entities.

Component 20, "Strategic Plan to boost Vocational Training" aims to transform and modernise the vocational training system to become one of the backbones of a new economic model based on knowledge. It can compensate for the constant transformations in the labour supply and maintain productivity.

Component 22, "Shock plan for the citizens' economy and reinforcement of inclusion policies" aims to increase the employment rate of people benefiting from the Minimum Vital Income through the development of employment incentives and the coordination and governance between the relevant agents for the inclusion policy.

Finally, Component 23, "New public policies for a dynamic, resilient and inclusive labour market" focuses on implementing a package of reforms to reduce structural and youth unemployment, reduce temporary employment, correct labour market duality, increase investment in human capital, modernise collective bargaining instruments and increase the efficiency of public employment policies. However, the labour reform has already been approved to make the Spanish labour market more flexible, as well as reduce precariousness and temporality and duality.

According to the European Commission, all these components respond to many of the recommendations presented to Spain in the last two years; it encourages innovation and facilitates access to digital learning. In addition, it addresses measures to tackle early school leaving, intensifies cooperation between the education and business sectors intending to improve the skills and qualifications demanded in the labour market, especially in the field of ICTs, supports employment through measures aimed at preserving jobs with effective incentives for hiring and facilitates the transition to permanent contracts. And finally, it ensures that employment and social services are able to provide adequate support by improving support for families, reducing the fragmentation of the national unemployment assistance system and filling gaps in the coverage of regional minimum income schemes (European Commission, 2020f). However, we detect a lack of specificity in terms of public and private cooperation, and we have serious doubts about reducing Spain's temporary unemployment rate.

Green transition: Spain needs considerable investments in renewable energy, energy infrastructure, energy efficiency, and sustainable transport over a long period. There is still scope for action to reduce energy consumption in buildings, the development of smart grids and the supply of electricity from renewable energy sources. Spain should promote sustainable transport both in terms of promoting electric vehicles and the use of rail for freight transport. Another important factor is that some areas of Spain are among the most exposed to climate change in Europe. Water resources, water and waste management infrastructure are uneven between northern and southern regions (European Commission, 2020e). In the last decade, while Spain has reduced carbon dioxide emissions and the use of non-renewable energy, it continues to maintain a high level of water stress in a context where water tariffs do not cover the cost of the service. Moreover, Spain still has room to reduce emissions from agriculture, transport and buildings (OECD 2021, 2021b).

The Spanish RRP allocates 39.7% of the total allocation, i.e. EUR 27.6 billion, to achieving the environmental objectives in Regulation (EU) No 2020/852. Investments contributing to the climate objectives have been included in all components of the Plan. However, the most significant contribution is made around nine elements: The "Shock plan for sustainable, safe and connected mobility in urban and metropolitan environments" aims to create more breathable and sustainable urban environments and promote the decarbonisation of urban mobility to improve air quality. Component 2, "Urban rehabilitation and regeneration plan" includes the energy rehabilitation of existing buildings. Component 4, "Conservation and restoration of ecosystems and biodiversity" aims at preserving the conservation status of ecosystems through their ecological restoration, as well as reversing the loss of biodiversity, ensuring sustainable use of natural resources and the preservation and improvement of their ecosystem services. This component includes the following reforms.

"Conservation of coastal space and water resources" focuses on planning in terms of water use, increasing the resilience of the Spanish coastline to the effects of climate change, as well as consolidating the implementation of Marine Strategies and the implementation of Maritime Space Management Plans.

"Sustainable, safe and connected mobility" aims to rebalance the modal distribution of transport towards more sustainable modes, reduce the high contribution of the transport sector in polluting emissions, and improve cross-border connections with France and Portugal as well as connections with ports.

"Electricity infrastructure, promotion of smart grids and deployment of flexibility and storage" promotes the development of a more flexible, decentralised and dynamic energy system that can efficiently absorb the new generation of renewable energies, the development of new innovative and sustainable business models and the participation of new actors in the electricity system.

"Roadmap for renewable hydrogen and its sector integration" aims to position Spain as a technological reference in large-scale renewable hydrogen production and use, and to structure it territorially.

"Just Transition Strategy" seeks to minimise the impact on the economy and employment of the cessation of activities such as coal mining, coal-fired thermal power plants or nuclear power plants.

Finally, Component 26, "Plan for promoting the sports sector" focuses on developing safe and sustainable sports infrastructures.

According to the European Commission's assessment, these measures are expected to contribute to the green transition and meet its challenges. Grade A is awarded according to the Resilience and Recovery Mechanism Regulation (European Commission, 2021b).

Digital transition: The COVID-19 crisis has highlighted the importance of digitalisation to maintain access to public services and education, preserve jobs, and sustain economic activity. Before the pandemic, only around 50% of schools had good online learning platforms, and there were substantial regional and urban-rural differences in this respect. The pandemic has also highlighted the difficulty of access to devices or connections from home for the most vulnerable students and the need for more students and future experts in science and digital technologies. For their part, Spanish companies, mainly SMEs, would also need greater digitalisation, which would foster their competitiveness in global value chains and exports (European Commission, 2020e).

In 2021, Spain ranked 9th out of 27 EU Member States in the 2021 edition of the DESI (Digital Economy and Society Index). This index, in turn, is made up of four sub-indices: human capital, connectivity, digital technology integration and digital public services. According to the report published in 2021, Spain performed very well in terms of connectivity - ranking 3rd only behind Denmark and the Netherlands - due to the high performance of very high capacity networks, as well as the efforts made in recent years to bridge the gap between rural and urban areas. Thus, in 2020, 92% of households had very high capacity fixed network coverage thanks to the deployment of fibre optic networks - compared to 59% of the EU average. Spain also performed very well in terms of digital public services, ranking 7th, showing a high level of online interaction between public authorities, citizens and businesses. In terms of human capital, Spain ranked 12th. Although its position has moved up in recent years, there is still room for improvement, mainly in terms of ICT specialists who in 2020 represented only 3.8% of the active population (understood as the population between 15 and 74 years of age). However, the worst result was obtained for integrating digital technologies, where Spain ranked 16th. Even though the number of SMEs selling online has increased considerably, Spanish companies are still not taking advantage of the full potential of new technologies such as artificial intelligence (AI), big data, and the cloud, which could increase productivity and more significant productivity development of e-commerce.

Against this backdrop, Spain has earmarked a total of 19.6 billion euros within the RRP for the digital transition - which represents 28.2% of the total budget - focusing mainly on promoting the digitalisation of companies, especially SMEs (25% of the budget is earmarked for the digital area), strengthening the digital skills of the Spanish population (22%), improving connectivity throughout the national territory (15%), continuing with the digitalisation of public administrations (28%) and promoting digital R&D and the implementation of digital technologies (10%) (European Commission, 2021c).

Given its cross-cutting nature, the digital transformation is deployed across the ten policy levers. However, the most significant contribution is made through seven components. Component 8, "Electricity infrastructure, smart grids and flexibility and deployment of flexibility and storage" encourages the development of new innovative business models. Component 11, "Modernisation of Public Administrations" focuses on the digitisation and modernisation of the administration and its processes. Component 13, "Boosting SMEs" aims to boost their digitalisation to improve their resilience and competitiveness. Component 15, "Digital connectivity, boosting cybersecurity and 5G deployment" aims at better and more secure access for networks to access public services. Component 16, "National Artificial Intelligence Strategy" seeks to position Spain as a leading country in Artificial Intelligence, to lead the world using the Spanish language in AI, to promote the creation of qualified employees, and to attract global talent in AI. Component 19, "National Digital Skills Plan" aims to train the population in digital skills, with particular emphasis on at-risk groups and the gender gap, to develop digital skills for learning in education, to promote digital skills among employees and SMEs and to foster the training of ICT specialists. Finally, Component 25, "Spain audiovisual hub of Europe

(Spain AVS Hub)" brings together a series of investments and reforms to strengthen the business fabric, improve the investment climate, and consolidate Spain as a global audiovisual investment platform and exporting country of audiovisual products.

According to the European Commission's assessment, these measures are expected to significantly contribute to the digital transition and address the challenges arising from it. Grade A is awarded according to the Resilience and Recovery Mechanism Regulation (European Commission, 2021b).

Summary assessment

According to the Commission's Report to the European Parliament and the Council on the implementation of the Recovery and Resilience Mechanism (European Commission, 2022), Spain was the first country to submit an operational agreement, key to request the first payment claim. Spain's first payment claim relates to the successful fulfilment of 52 milestones, mainly related to reforms that have already been implemented in the second quarter of 2021. Given the retrospective nature of most of the milestones and given that Spain had shared with the Commission most of the information necessary to carry out its assessment prior to the formal submission of the payment claim, the Commission was able to process the evaluation of the payment claim swiftly. It disbursed €10 billion of the financial contribution (net of pre-financing) to Spain on 27 December 2021. By recognising the achievement of the milestones and targets underpinning the respective RRP measures, the first payment to Spain already illustrates the progress made in the implementation of the RRF. The milestones included in the payment demonstrate significant steps in the performance of Spain's recovery and resilience plan and its comprehensive reform programme. They include important measures such as the Climate Change and Energy Transition Law (enshrining climate neutrality by 2050), the reform of minimum income support, measures supporting the digitisation of SMEs and boosting digital skills, and reforms strengthening the capacity to conduct and monitor spending reviews. This example shows how the Facility already has tangible effects on the ground, supporting the implementation of important reforms.

After a detailed analysis of the country's vulnerabilities and the reforms and investments presented and their monitoring mechanism, we believe that the final effect will be very positive for the Spanish economy, and that the impact of the plan will undoubtedly go a long way towards correcting the aforementioned imbalances, which would not have been possible without the implementation of the NGEU. But at the same time it seems that some vulnerabilities are only partially addressed. From a critical point of view, and even more so nowadays where the uncertainty of the invasion of Ukraine establishes a very different political and economic geostrategic framework than just a few months ago, we consider that some aspects such as high deficit (especially the structural deficit) and public debt will not be fully corrected, a fact to which strong inflationary pressures are being added, as well as the duality and co-responsibility between labour supply and demand and the efficiency in terms of the actions of the different levels of government. Moreover, some approved reforms, such as labour market or pension reforms, while correcting, do not fully address the national problems.

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ASSESSING THE NATIONAL RECOVERY AND RESILIENCE PLAN: PORTUGAL

	2017	2018	2019	2020	2021*	2022*
GDP growth	3.5	2.8	2.5	-7.6	3.9	5.1
Consumer price index (harmonised)	1.6	1.2	0.3	-0.1	0.9	1.1
Unemployment rate	9.0	7.1	6.5	6.9	6.8	6.5
General government gross debt (% of GDP)	126.1	121.5	116.8	133.6	127.2	122.3
General government fiscal balance (% of GDP)	-3.0	-0.3	0.1	-5.7	-4.7	-3.4

Source: AMECO.

Vulnerabilities

- High deficit and public debt to GDP ratios.
- A labour market suffering from severe structural weaknesses.
- Reduced investment, both public and private.
- Inefficient public administration.
- Deficient regional and cross-border communication infrastructures.
- Energy inefficiency and lagging ecological transition.

Portugal was the last country in Western Europe to be affected by the COVID-19 virus, and it was only on 2 March 2020 that the first case was detected.⁶¹ However, the country's government took action very quickly. Just two weeks after the first case and before the first coronavirus-related death, it took extraordinary measures to contain and mitigate the pandemic⁶²: non-essential movement and all public gatherings were banned, schools and non-essential businesses were closed, and border movements and international flights were severely restricted, among others.

The state of emergency was decreed only a few days later on 19 March and ended, after being renewed twice, on 2 May 2020. By the end of May 2020, Portugal was one of the least affected countries in terms of both infections and deaths from COVID-19 (Paes Mamede, Pereira, & Simoes, 2020)

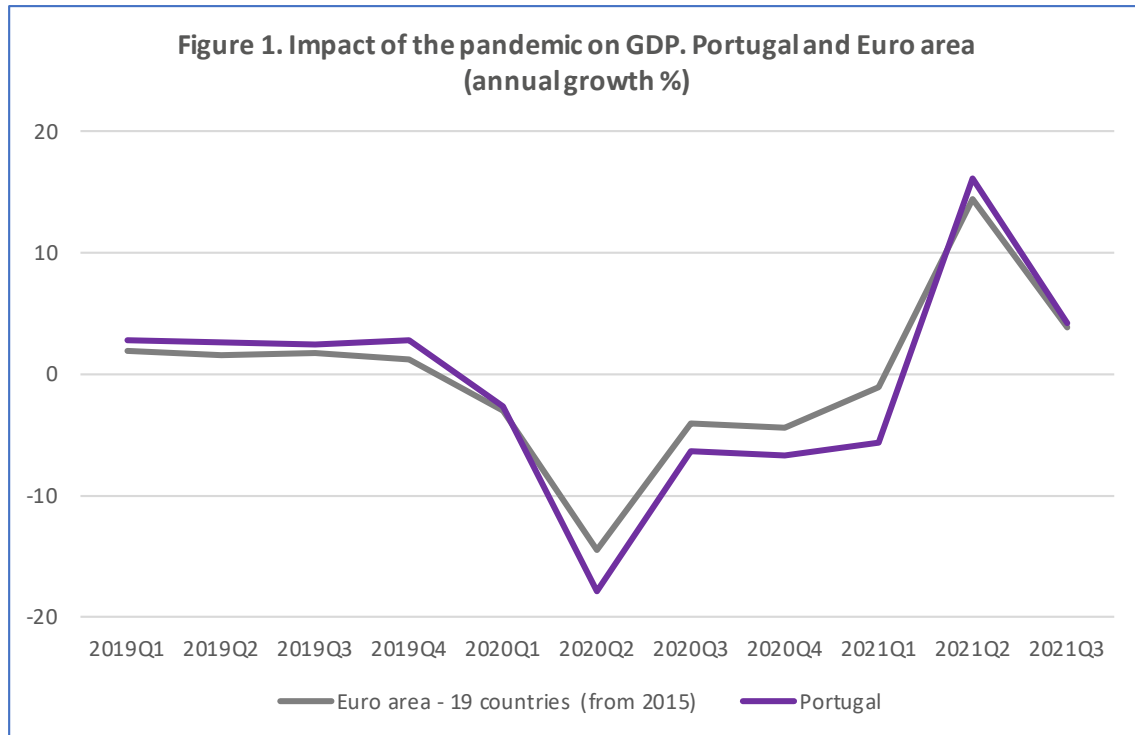
Although Portugal dodged the first pandemic wave thanks to its swift action, this was not the case in subsequent months. On 9 November the state of emergency was decreed again and renewed uninterruptedly until 1 May 2021. However, the most challenging days were after Christmas, when there was a significant spike in infections and deaths. The Portuguese health system almost collapsed,

⁶¹ The first case of coronavirus infection in Western Europe was detected on 20 February 2020 in Italy, while the first case in Portugal occurred only on 2 March, according to a communiqué from the Direção-Geral da Saúde de Portugal: <https://covid19.min-saude.pt/wp-content/uploads/2020/03/Atualizaçã-o-de-02032020-1728.pdf>

⁶² Press release of the government of 12 March 2020: <https://www.portugal.gov.pt/pt/gc22/governo/comunicado-de-conselho-de-ministros?i=330>

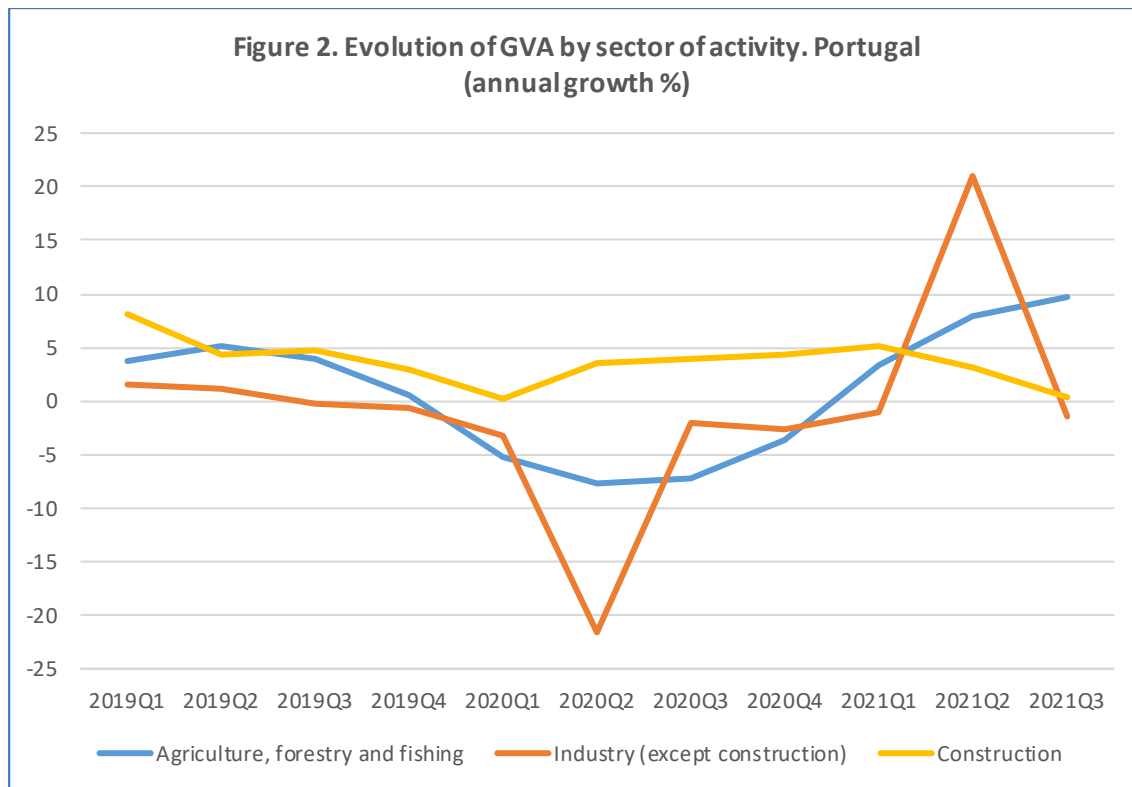
forcing the government to toughen the measures and establish general confinement of the population from 15 January until 1 May 2021.

The impact of the measures taken to contain the pandemic was severe, especially from January onwards, triggering an abrupt reduction in economic activity and tensions in the financial markets. The Portuguese economy was simultaneously affected by both supply and demand shocks. On the supply side, the suspension of non-core activities, the temporary or permanent closure of companies and the closing of borders led to disruptions in production and supply chains. On the demand side, in addition to the impact of the pandemic on domestic demand, there was also a sharp contraction in external demand, especially in the tourism sector, which is of great importance to the Portuguese economy (Banco de Portugal, 2021).

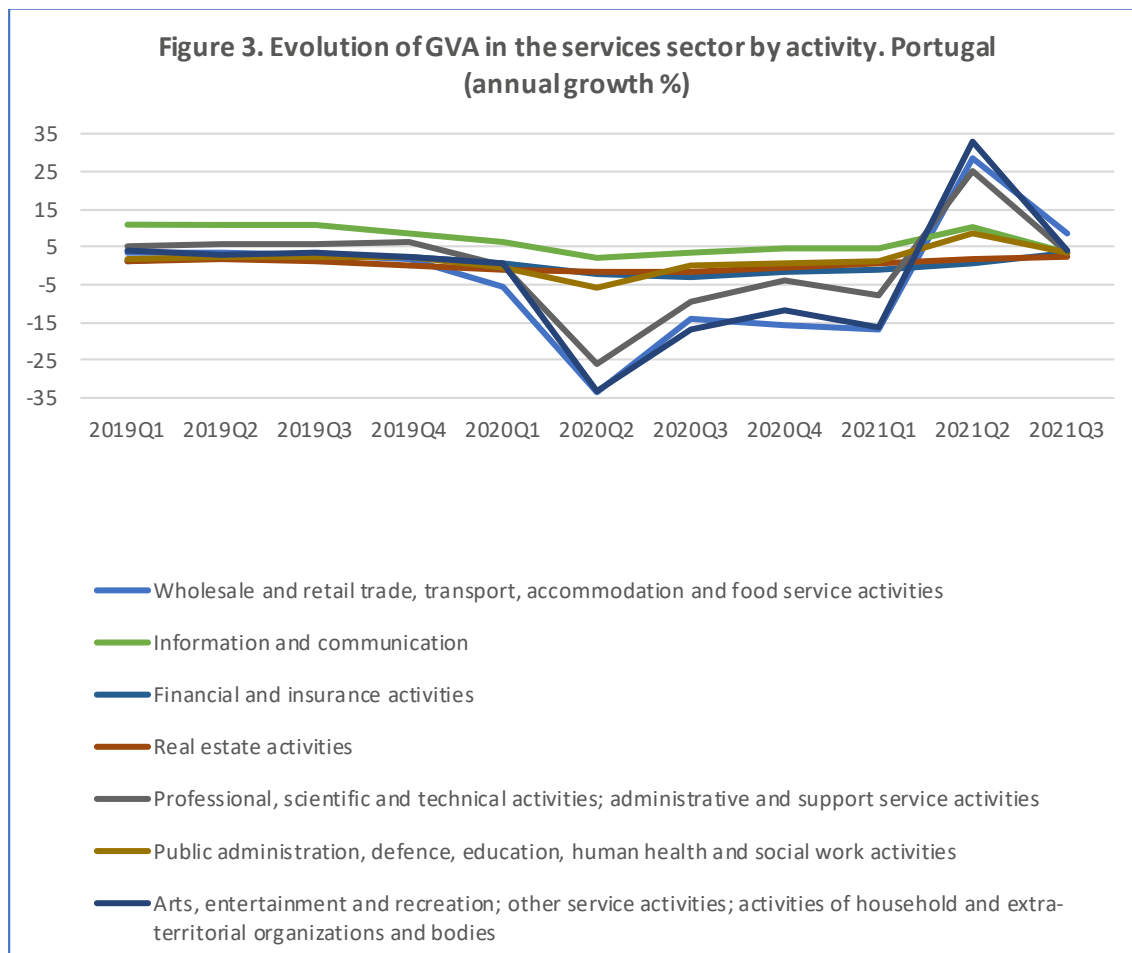


Note: Seasonally and calendar adjusted data. Percentage change compared with the same period a year earlier.

Source: Eurostat.

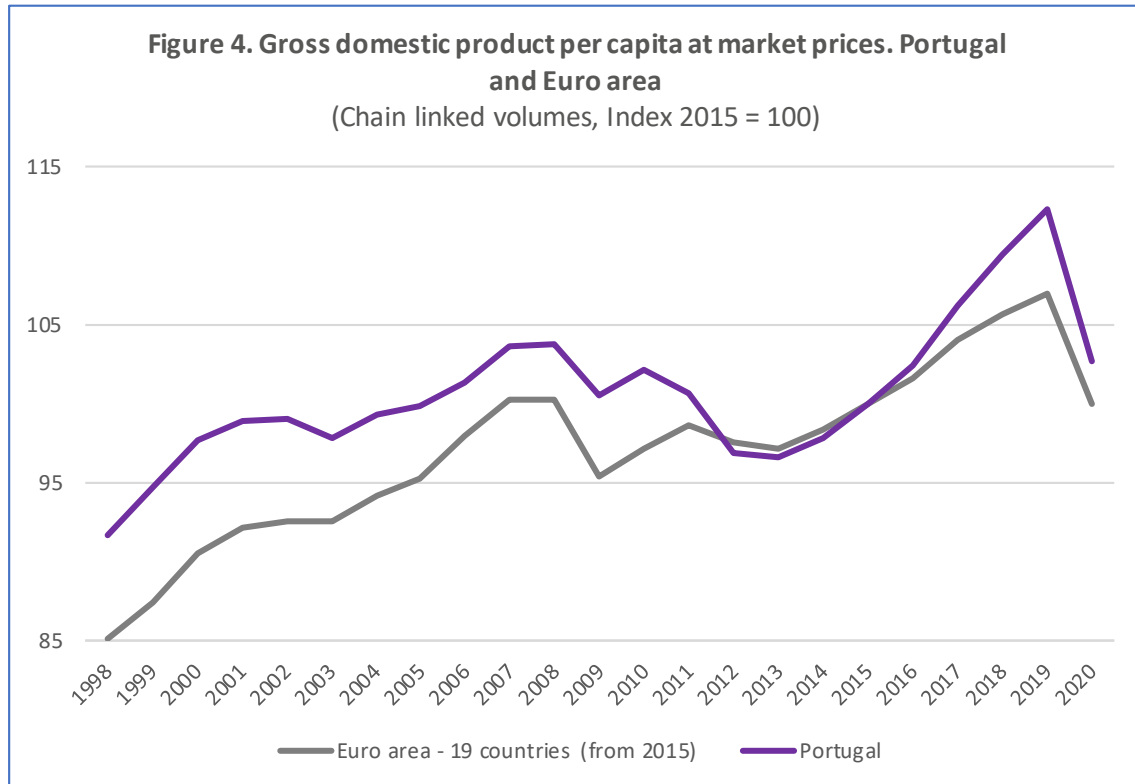


Source: Eurostat.



Source: Eurostat.

The pandemic triggered a deep recession in the Portuguese economy, making it one of the hardest-hit economies among developed countries. GDP contracted by 4.3% year-on-year in the first quarter of 2020, with the most significant decline in the second quarter, when it plummeted by 21.5%, while in the third and fourth quarters of 2020 it fell by 8.7% and 8.8%, respectively, and in the first quarter of 2021 by 4.3%. This was mainly due to the considerable weight in the Portuguese economy of sectors most affected by contact and mobility restrictions, such as hotels, restaurants and tourism, as well as manufacturing industry (OECD, 2021).



Source: Eurostat.

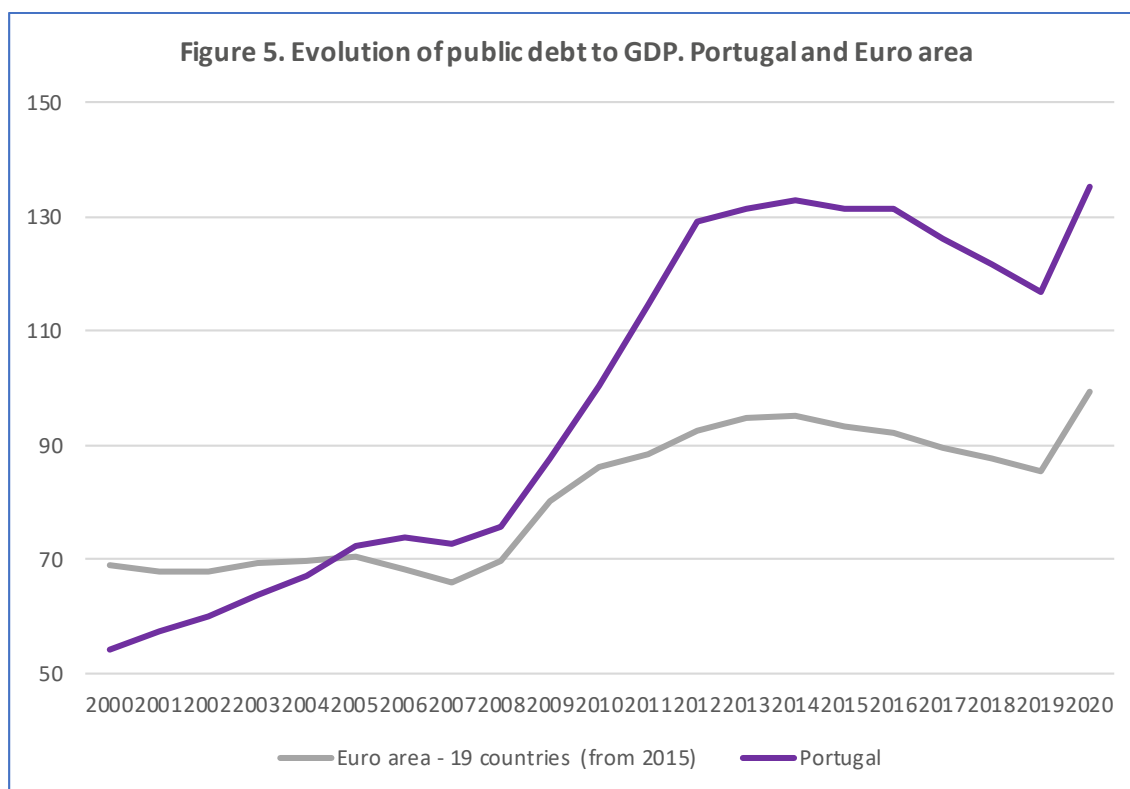
Since 2013, the Portuguese economy had been growing at a sustained pace, supported by strong growth in the tourism sector as well as exports in various manufacturing sectors, reflecting the improvement in the quality of products and the reduction in their relative prices. Thus, in 2019, the real per capita income of the Portuguese economy had grown by 10.1% since 2013, compared to 5.3% in the euro area. However, although the Portuguese economy substantially corrected some of its imbalances during this period, such as the ratio of public debt and deficit to GDP, the latter remained high, the poverty rate of the working-age population remained high, and the perception of subjective well-being was at lower levels than during the 2008 crisis (OECD, 2020).

The Portuguese government's fiscal response to the pandemic has been significant, with the overall direct budgetary cost estimated to be close to 3% of GDP. The adopted measures aimed to strengthen the health system's resilience, preserve jobs, reinforce social services, and safeguard business continuity and the resumption of economic activity (European Commission, 2020b).

PORTUGUESE VULNERABILITIES

High deficit and public debt to GDP ratios: Before the outbreak of the COVID-19 crisis, the Portuguese economy had large net external liabilities and private and public debt, as well as a high

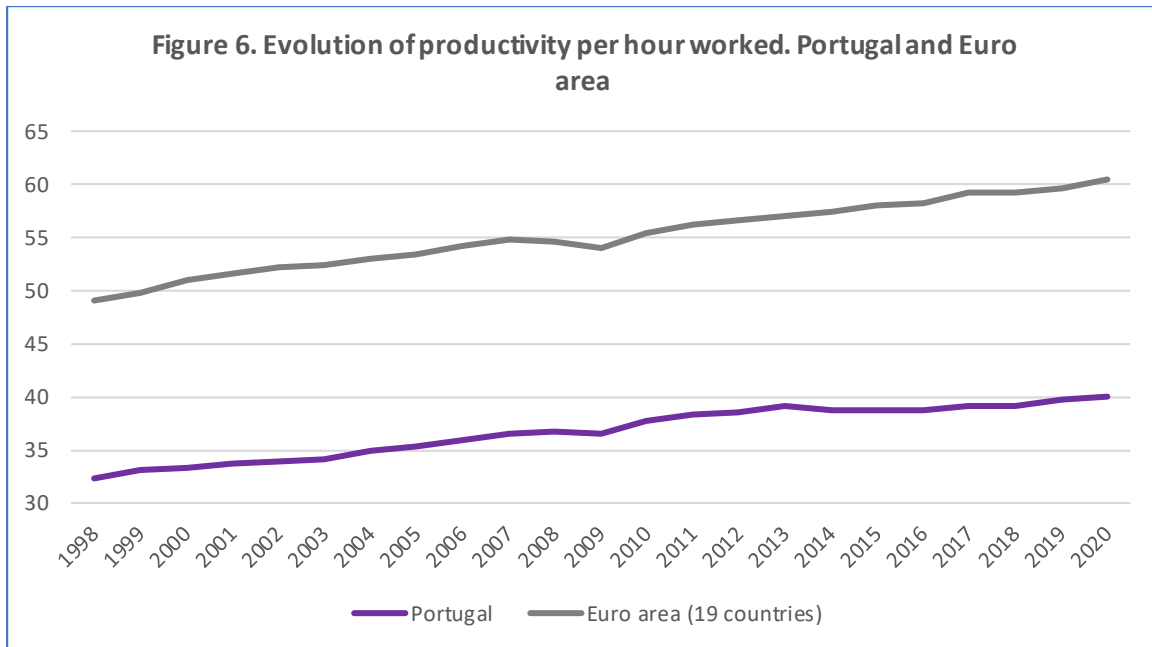
share of non-performing loans, in a context of low productivity growth. Moreover, public finances were under severe pressure due to an ageing population, putting the sustainability of the pension and health care systems at risk. Moreover, state-owned enterprises were making losses, which did not help the sustainability of public finances (European Council, 2019) and (European Commission, 2020c). Thus, the Portuguese public deficit has grown steadily since the 2008 crisis. Since then, the public debt has risen from 75.6% of GDP to 116.6% in 2019.



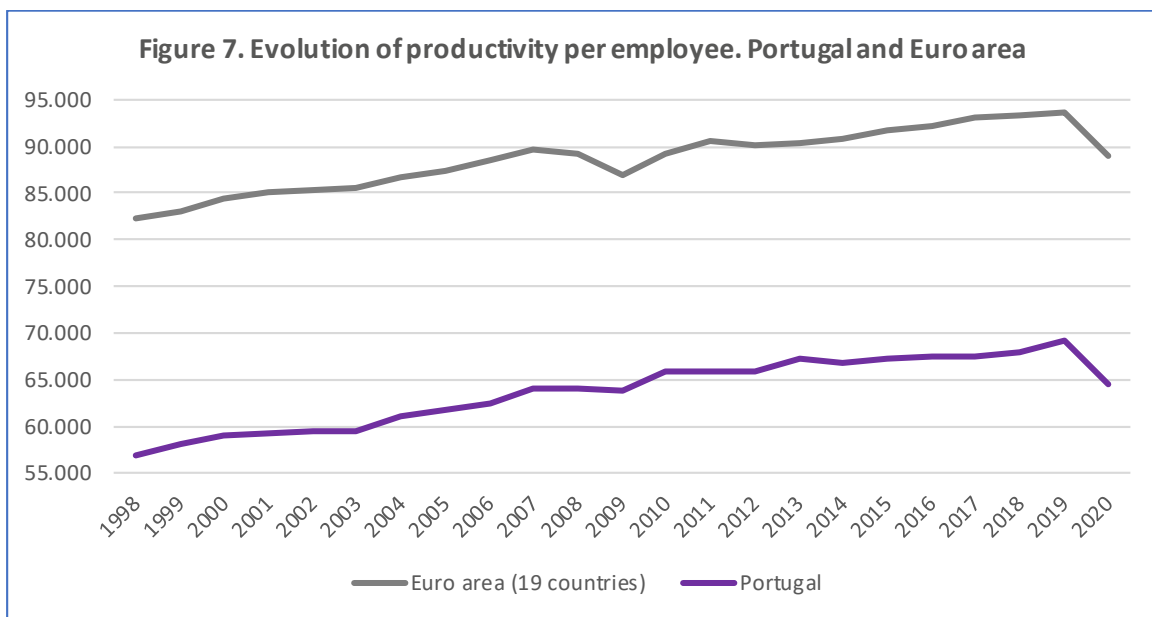
Source: Eurostat.

In 2020, the government deficit amounted to -5.7%, compared with a surplus of 0.1% in 2019. Meanwhile, the public debt-to-GDP ratio soared to 133.6%, 16.8 percentage points higher than in 2019. In addition, there has been a notable increase in non-performing loans.

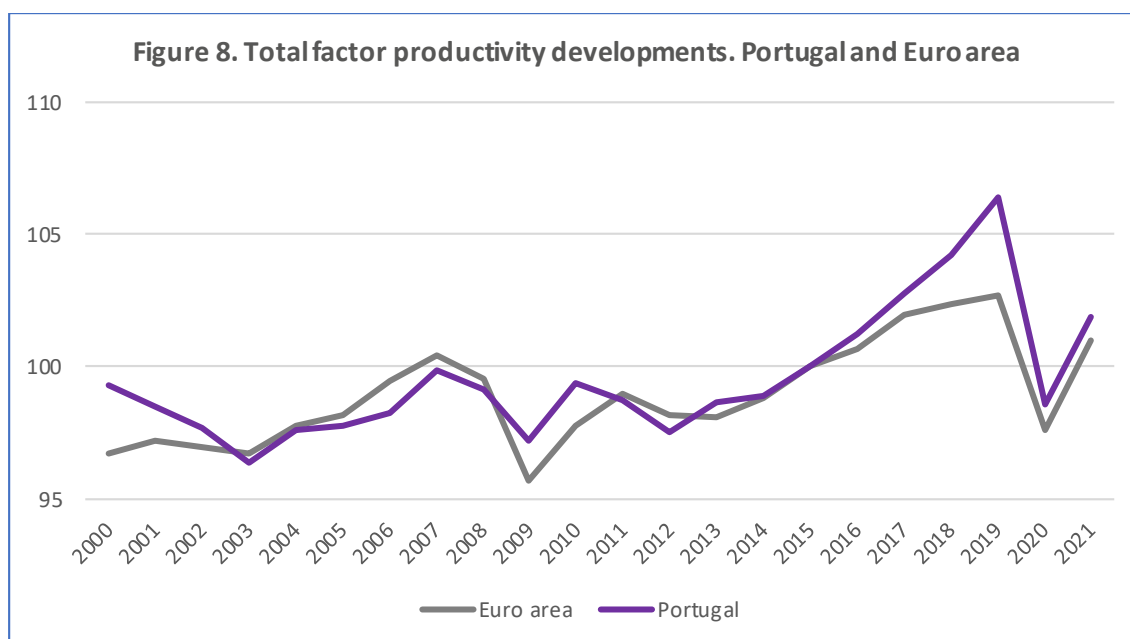
Low productivity growth since the mid-1990s is limiting the economy's potential growth and the process of convergence with the euro area: Productivity progressively converged with developed economies from the transition to democracy until the mid-1990s, thanks to improvements in human capital and resource allocation, as well as to increased investment following entry into the European Economic Community, and finally because Portugal started from a much more backward position than the more advanced countries. However, since then, productivity growth has slowed down, largely due to insufficient investment in ICT and R&D, the rigidity of its labour market and the survival of state-owned enterprises that are less exposed to competition and therefore less efficient, as well as the structure of its productive fabric, in which small companies predominate, and the predominance of more labour-intensive productive sectors such as trade and services -especially tourism- (Pineiro Alves, 2017).



Source: AMECO.



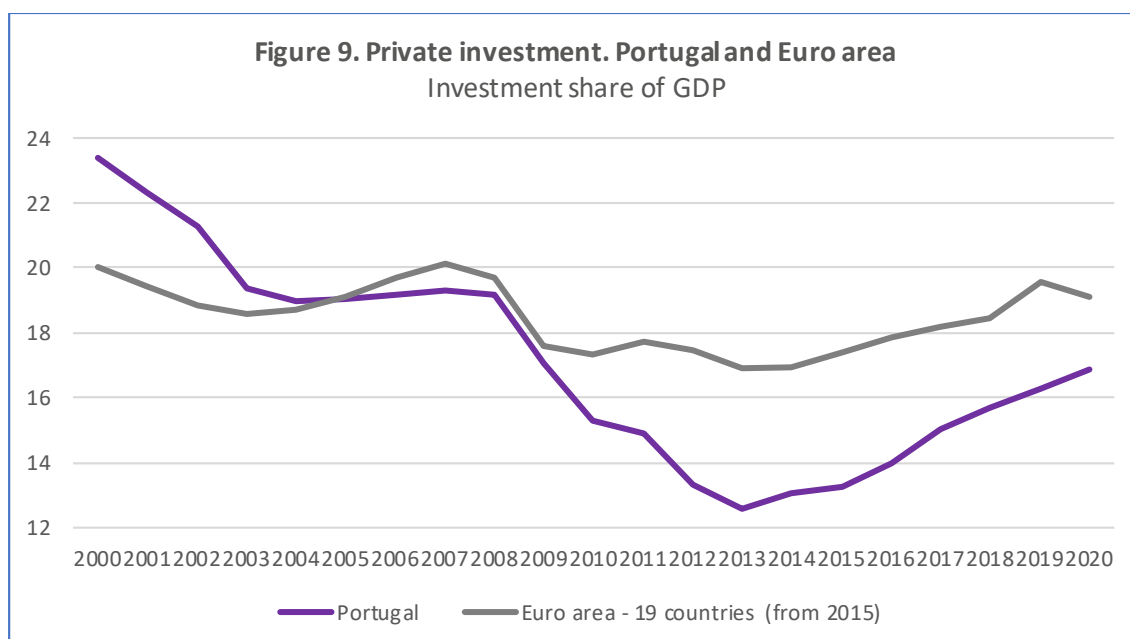
Source: AMECO.



Source: AMECO.

Reduced public and private investment: Portugal maintained investment levels above the euro area average during the period 2001 to 2010. However, since then and up to the present, it has recorded much lower investment rates. Thus, during this period, the average investment as a percentage of GDP stood at 16.7% in Portugal, while in the euro area it was 20.8%. As a result, total investment observed in Portugal was lower than fixed capital consumption during the period 2012-2018, and total net investment only became slightly positive in 2019.

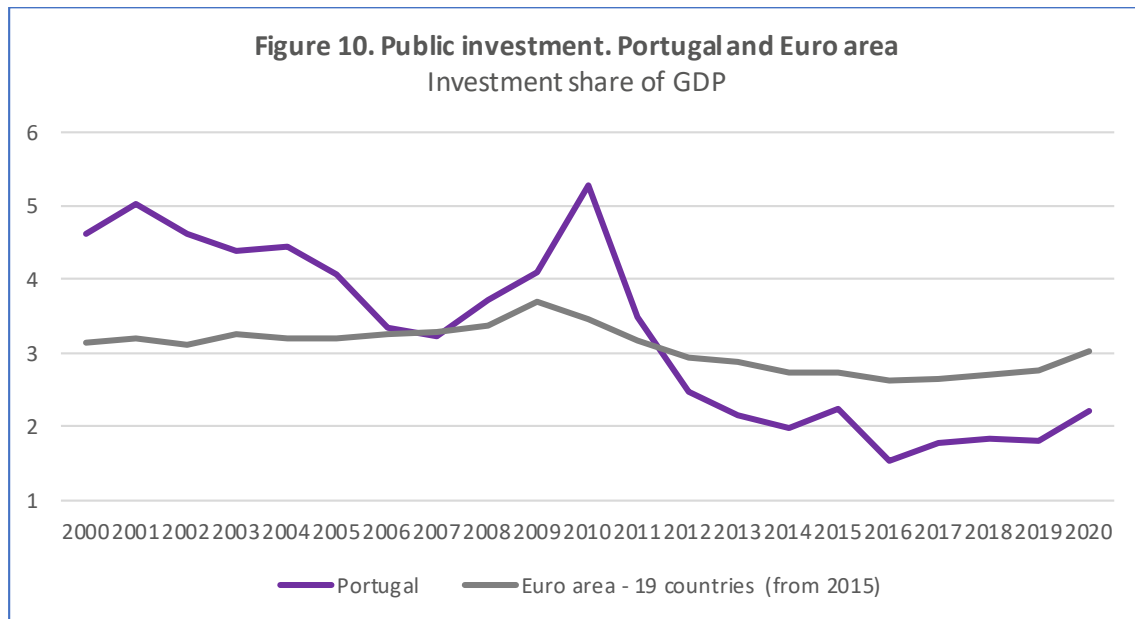
As for private investment as a percentage of GDP, since 2013, when it reached its trough (12.6%), it maintained a growth path until 2020 (16.9%). However, net business investment did not start to turn positive until 2019.



Note: Private investment is calculated as the total investment of all sectors, excluding public investment.

Source: Eurostat.

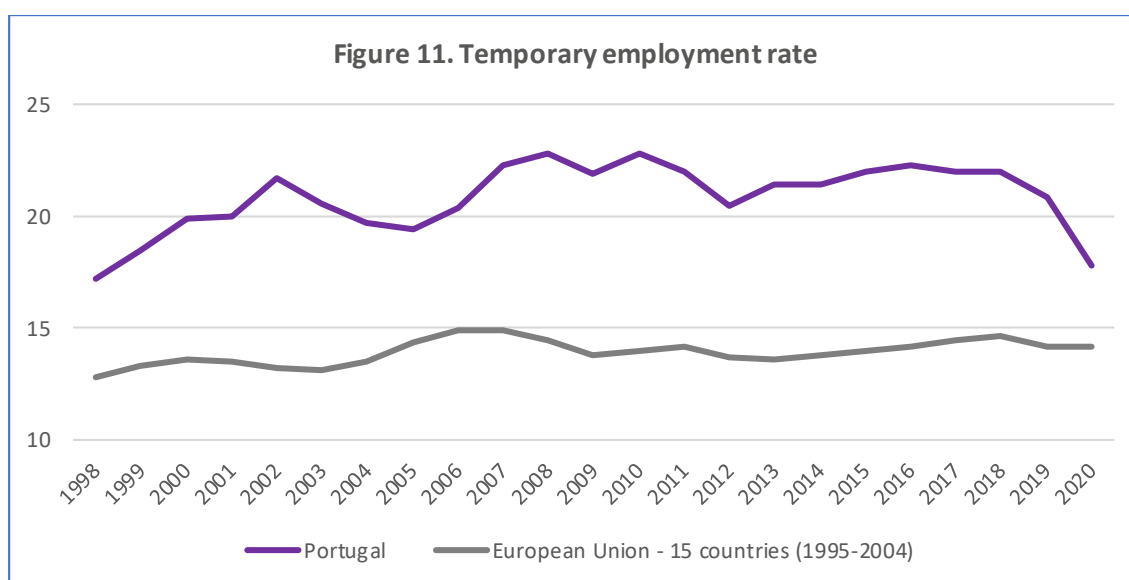
The ratio of public investment to GDP fell sharply from 2010 onwards, with a downward trend until 2016, when it reached its lowest point (1.5%). From then on, a slight recovery began, although on average, from 2017 to 2020, public investment in relation to GDP in Portugal stood at an average of 1.9%, far from the 2.8% of the euro area (European Commission, 2021).



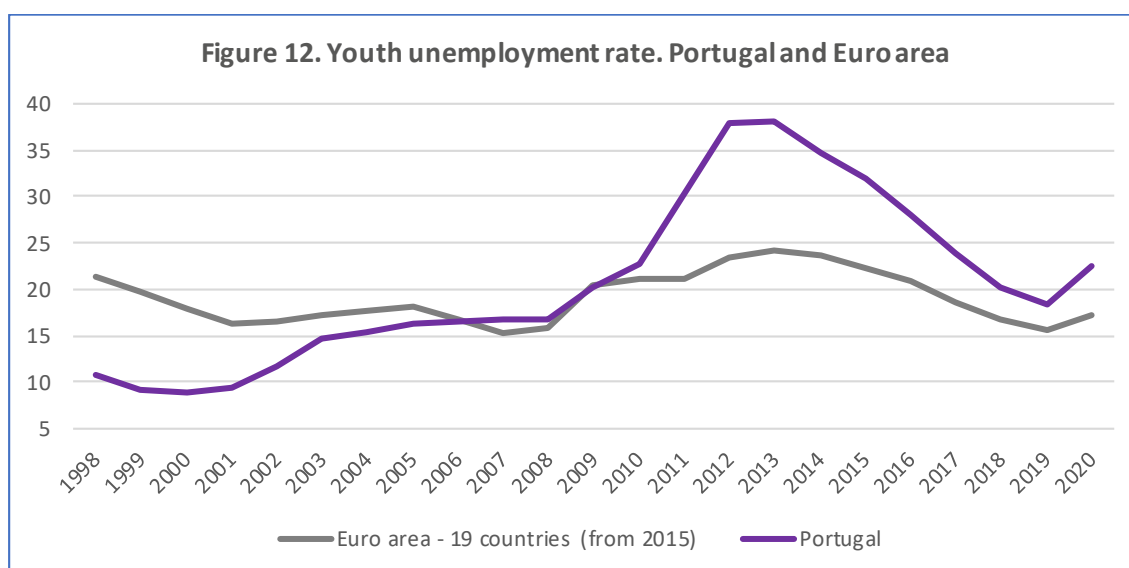
Source: Eurostat.

A labour market that suffers from severe structural weaknesses: High labour market segmentation and collective bargaining deficiencies result in a high percentage of temporary workers, higher than the EU average, job insecurity and a high level of inequality, the latter fostered by an inefficient system of social transfers. Moreover, the low skill level of the labour force, especially in digital skills, is an obstacle to productivity growth and investment. Finally, regulatory and administrative restrictions are still imposed on some professional services (European Council, 2019) and (European Commission, 2020c)

The COVID-19 pandemic hit the Portuguese labour market hard, mainly affecting young and temporary workers (OECD, 2021), accentuating social inequalities. However, some fiscal measures adopted by the Portuguese government - for enterprises and the self-employed - prevented more intense job destruction.



Source: Eurostat.



Note: Population aged 15-24.

Source: Eurostat.

Vulnerabilities in the health sector: By the end of 2020, during the third wave, public hospitals almost reached their maximum capacity, delays in medical care occurred, and shortages of health personnel became evident. In addition, the pandemic has accentuated mental health problems, which requires employing more mental health professionals.

The pandemic has exposed a public health system with a shortage of permanent staff and a structure that pays too little attention to mental health. In addition, the system must adapt to the new needs of an ageing population (OECD, 2021).

Inefficient public administration: The level of bureaucracy required for any procedure vis-à-vis the administration is still high, and authorisation regimes are still used instead of declarations of compliance, as in most EU countries. The judicial system suffers from long delays, resulting in a high backlog of cases pending before the courts (European Council, 2019) and (European Commission, 2020a).

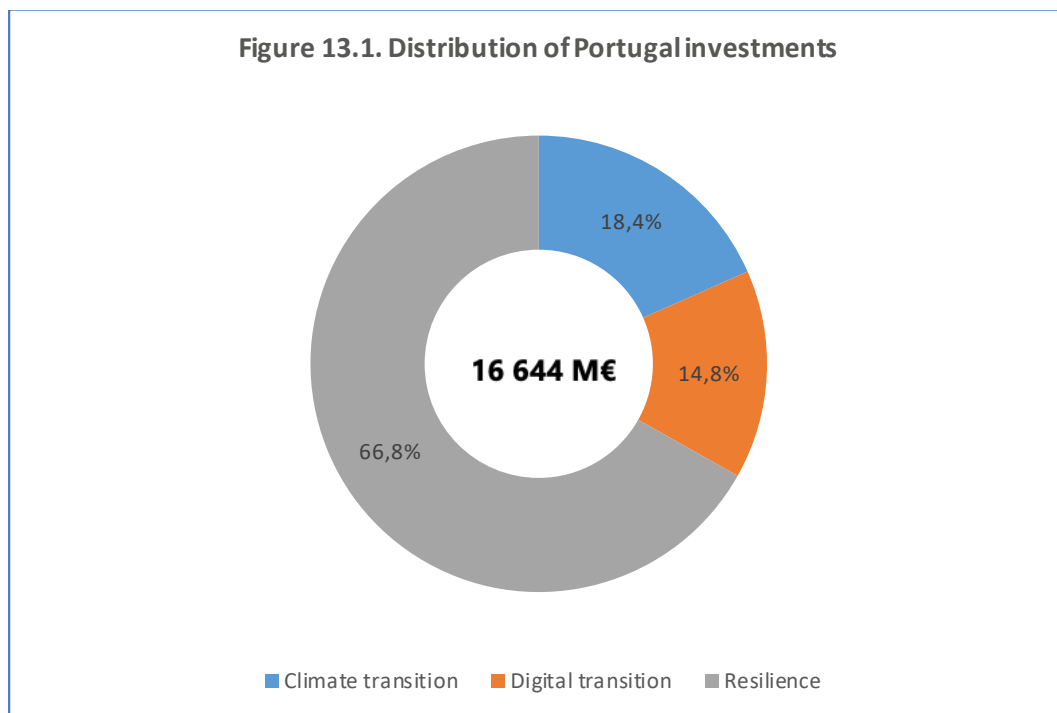
Deficient regional and cross-border communication infrastructures: There are insufficient maritime and rail links, and the rail network with connections to Spain, and thus to the rest of the Union, remains under-utilized, making it difficult for export-oriented companies to benefit fully from the potential of the Single Market (European Council, 2019).

THE PORTUGUESE NATIONAL RECOVERY AND RESILIENCE PLAN

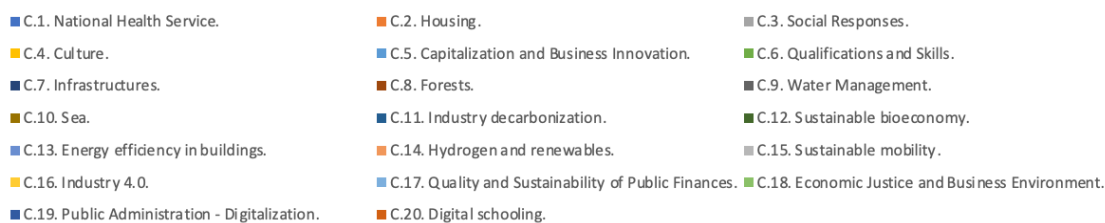
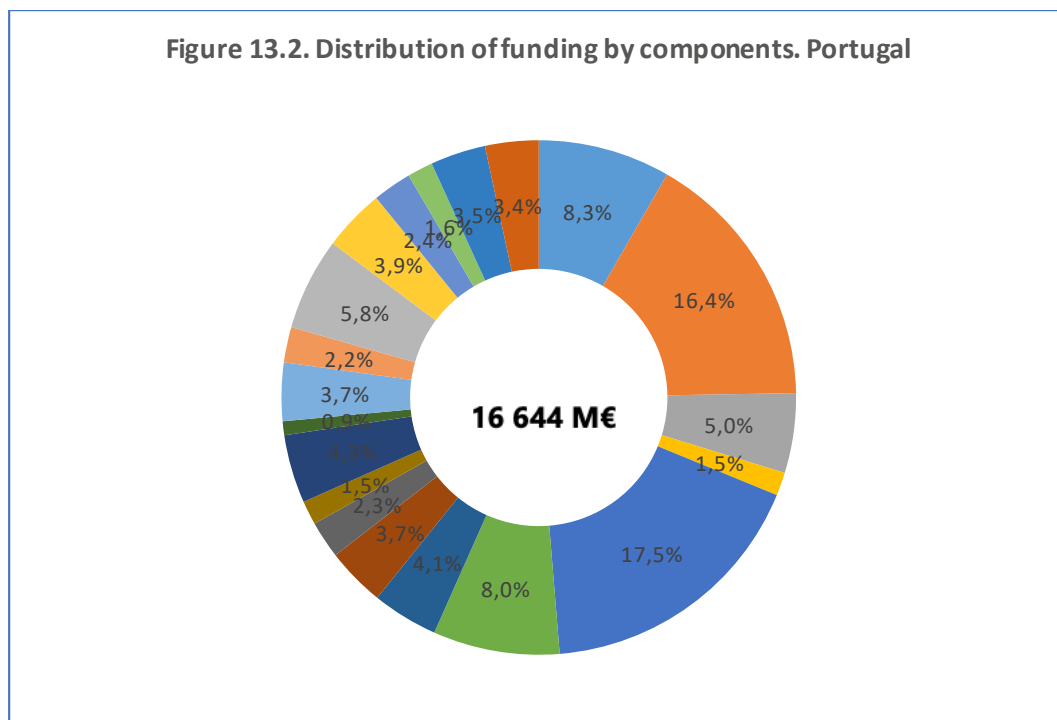
The Portuguese Recovery and Resilience Plan amounts to EUR 16.644 billion, distributed in approximately EUR 13.9 billion in grants and EUR 2.7 billion in loans. In addition, the national authorities will reassess, in the second half of 2022, the additional resource of up to EUR 2.3 billion in loans, depending on the level of demand generated by the RRP in business support measures, in particular in the area of capitalisation and business innovation, and depending on the dynamics of public finances.

The plan is organised around three structural dimensions: resilience, climate transition and digital transition. And it is structured in 20 components, including 37 reforms and 83 investments.

Figure 13. Destination of Portuguese Recovery and Resilience Plan funds



Distribution of funding by components



Source:

Own elaboration based on the Portuguese RRP.

Governance: To establish the governance model for the funds received from the Recovery and Resilience Mechanism for 2021-2026, the Portuguese government approved Decree-Law No. 29-B/2021 of 4 May. It establishes four levels of coordination intending to develop an agile, effective and transparent governance model:

- **Political coordination body:** this is an Interministerial Commission, which will be chaired by the Prime Minister and will be made up of the members of the government responsible for the areas of the economy, digital transition, foreign affairs, presidency, finance, planning, environment and climate action. Its functions will be to approve the plan as well as its amendments; to coordinate the overall policy and strategy of the program; to endorse proposals for revisions and reforms; to evaluate and approve, subject to the opinion of the National Monitoring Commission, the six-monthly follow-up reports; and to evaluate and approve the annual progress report, subject to the opinion of the National Monitoring Commission and the consideration of the Assembly of the Republic.
- **Monitoring body:** this is known as the National Monitoring Commission which will be chaired by an independent person of recognised merit appointed by the Prime Minister and will be made up of nine members approved by the Interministerial Commission;

non-governmental members of the Territorial Concertation Council; the president of the Economic and Social Council and the non-governmental members of the Permanent Commission for Social Concertation; a representative of the Council of Rectors of Portuguese Universities; a representative of the Coordinating Council of Higher Polytechnic Institutes; a representative of the National Council of Science, Technology and Innovation; a representative of the National Confederation of Solidarity Institutions; a representative of the Portuguese Union of Mercy; a representative of the Portuguese Union of Mutualities; a representative of the National Council for the Environment and Sustainable Development; and a representative of the Portuguese Confederation of Cooperatives. It shall meet at least twice a year and extraordinarily if its chairman so requests. Its functions will be to oversee the implementation of the plan; monitor information and communication and advocacy measures for greater transparency; monitor progress in the performance of the program and propose recommendations to improve implementation mechanisms; give an opinion on the six-monthly and annual monitoring reports submitted by the "Reclaim Portugal" mission structure and make recommendations, and review the results of the plan and the impact assessment reports.

- Technical coordination and monitoring body: This is entrusted to the structure of the 'Reclaim Portugal' mission, set up by a resolution of the Council of Ministers. Its role will be to ensure compliance with the obligations and requirements set out in Regulation (EU) 2021/241.
- Audit and control body: The Audit and Control Commission will be chaired by a representative of the General Inspectorate of Finance and will be composed of a representative of the Development and Cohesion Agency and a person with a track record of recognised merit in the area of audit and control, elected by the other members. Its functions will be to supervise the internal management and control system of the structure of the "Recover Portugal" mission, ensuring that it efficiently and effectively verifies the physical and financial performance of the interventions, preventing and detecting irregularities for the adoption of timely and appropriate corrective measures, and ensuring measures to avoid the duplication of aid and the risk of corruption and fraud; issuing a preliminary opinion on requests for disbursement of plan funding every six months; and conducting audits of the functioning of the plan's management and control system, presenting recommendations aimed at mitigating and correcting deviations identified in the internal control procedures of the 'Recover Portugal' mission structure.

Impact on GDP of the plan⁶³: According to estimates by the Office of Planning, Strategy and International Relations of the Ministry of Finance, using the European Commission's QUEST macro-econometric model, GDP would grow thanks to the investments and reforms implemented by the PRR at an average annual rate of 0.7 percentage points, so that in 2025 GDP would be 3.5% higher than it would be in a scenario without the PRR. That is, in 5 years, every euro invested in the RRP would translate into 1.4 euros. Regarding the labour market, in 2025, the unemployment rate is estimated to

⁶³ These results cannot be directly compared to the numbers reported in the European Commission Assessment of Portugal plan given that there are differences in the assumptions and methodology.

be 1.6 percentage points lower than in a scenario without RRP, employment 1.4 percentage points higher, and the budget balance 1.5 percentage points higher.

Figure 14. Quantification of the macroeconomic impact of the RRP (additional effects in % and percentage points)

	T-2	T-5
GDP (%)	1.4	3.5
Employment (p.p.)	0.7	1.4
Unemployment (p.p.)	-0.4	-1.6
General Government Fiscal Balance (p.p.)	0.5	1.5

Source: Portuguese RRP.

ASSESSMENT OF MEASURES ADOPTED IN THE PORTUGUESE RRP TO ADDRESS STRUCTURAL CHALLENGES

The following is a summary of the measures taken to mitigate the vulnerabilities, either accentuated or emerging, as a result of the COVID-19 pandemic:

Measures taken concerning the quality and sustainability of public finances: Reforms aim at improving the quality and sustainability of Portuguese public finances are included in Component 17, "Quality and Sustainability of Public Finances" of the Portuguese RRP, which aim to promote a wide range of structural reforms to improve the planning and management of public resources, including mechanisms for reviewing public expenditure, monitoring the state's public corporate sector expenditure and reducing arrears, as well as broadening the tax base through the effective management of public assets and rural properties. The investments to be implemented are: Information systems for the management of public finances; Modernization of the infrastructure of the Tax Agency's asset information system; and Digital conversion of the Social Security and amount to EUR 406 million. The RRP also includes a reform for the modernisation and simplification of public financial management.

The European Commission considers that this component contributes to addressing some of the country-specific recommendations by improving the quality of public finances, strengthening overall expenditure control, cost-effectiveness and proper budgeting. It allows improving the financial sustainability of state-owned enterprises, while ensuring more timely, transparent and comprehensive monitoring, and ensures, where economic conditions allow, budgetary policies aimed at achieving a prudent budgetary position over the medium term and thus ensuring debt sustainability. (European Commission, 2020d).

We found that the reforms could include a greater degree of specificity, especially with regard to reducing public debt and improving the quality of and reducing the level of bureaucracy in the Portuguese public administration. Moreover, in some cases, specific dates are not specified, nor is the body responsible for monitoring their proper implementation once they have been approved.

Measures taken concerning the National Health System: Reforms in the public health system are included in Component 1, "National Health Service" of the Portuguese RRP to strengthen the capacity

of the health system to respond to demographic and epidemiological changes, therapeutic and technological innovation, the trend towards increasing costs of services and the expectations of an increasingly informed and demanding society. To achieve these objectives, the plan includes three reforms - primary care reform, mental health reform and reform of the public hospital governance model - and nine investments - six on the mainland, two in the Autonomous Region of Madeira and one in the Autonomous Region of the Azores - totalling 466 million euros. The reforms are well specified, as are the investments and the dates for their implementation. However, some aspects do not identify the competent body responsible for implementing them, such as the investment in primary care, the investment in equipment for some hospitals, the investment in strengthening the Regional Mental Health Service, the investment in digital health transition and the investment in a universal active life support system.

According to the European Commission's assessment, all these measures support the CSRs on strengthening the overall control of expenditure, cost-effectiveness and adequate financing of the National Health System, focusing on a lasting reduction of hospital backlogs, as well as on strengthening the resilience of the health system and ensuring equal access to quality healthcare and long-term care. In addition, it also contributes to the green and digital transition within the health system (European Commission, 2020d).

Measures taken in relation to the labour market: The reforms adopted to correct labour market dysfunctions are included in Component 6, "Skills and Competencies" of the Portuguese RRP to increase the responsiveness of the education and training system to combat social and gender inequalities and increase employment resilience, especially for young people and low-skilled adults. It includes five reforms - four of them to be implemented on the mainland and one in the Autonomous Region of the Azores - integrated within the "Portugal 2030 Strategy", with an investment amounting to €1.324 billion.

In line with European Commission, all these investments and reforms address the CSRs to effectively tackle the pandemic, sustain the economy and support the subsequent recovery; and include measures to address labour market segmentation; improve the level of skills of the population, in particular in terms of digital literacy; increase the number of higher education graduates, in particular in science and ICT; support the use of digital technologies to ensure equal access to quality education and training; boost the competitiveness of businesses; focus on economic research and innovation policy linked to investment; and reduce restrictions on highly regulated professions (European Commission, 2020d).

However, although the reforms are well specified, as are the investments, we have found that in some cases no specific dates for their entry into force are specified, nor the competent body responsible, and some of these measures we consider to be very ambitious and, in some cases, such as the reduction of restrictions in some regulated professions, may face social pressure.

Measures taken concerning business financing and investment: These measures are included in components 5 and 16 of the Portuguese RRP. "Business Capitalisation and Innovation" aims to increase the competitiveness and resilience of the economy based on R&D, innovation, diversification and specialisation of the productive structure, to capitalise companies which were economically viable before the outbreak of the economic recession caused by the pandemic, and to encourage productive investment in areas of strategic national and European interest. To this end, the objective is to approve five reforms with an investment of 2,914 million euros from the Recovery and Resilience Mechanism. Business 4.0 aims to reinforce the digitalisation of companies to update themselves in the digital transition process. To this end, reform will be implemented with a budget of 650 million euros.

The European Commission considered that both components address the CSRs submitted in recent years to the Portuguese government. Thus, component 5 promotes investment in the green, climate and digital transition, implements temporary measures to ensure access to liquidity for businesses, particularly small and medium-sized enterprises, and to promote private investment to stimulate economic recovery. Component 16 promotes the use of digital technologies to ensure equal access to quality education and training, boosts the competitiveness of enterprises, supports employment and prioritises job preservation measures, as well as contributes to improving the skills level of the population, in particular their digital literacy, in particular by making adult learning more relevant to labour market needs, and focuses investment on the digital transition (European Commission, 2020d).

The reform is well specified, although no concrete dates for its entry into force are established nor the competent body responsible for its implementation. In addition, we consider that it should further specify how it intends to boost job retention, with measures such as the reduction or adaptability of working hours in the face of production needs, among others.

Measures taken to improve the road infrastructure: These measures are included in the Component 7, "Infrastructure" of the Portuguese RRP, which aims to strengthen resilience and territorial cohesion by increasing the competitiveness of the productive fabric and reducing transport costs. To this end, six reforms are included with 690 million euros. However, only four of them are specifically aimed at this objective (the other two have the fundamental aim of green transition): the elimination of urban junctions and the increase in the capacity of the road network - 313 million euros-, the development of cross-border connections - 65 million euros-, the completion of road access to the Business Reception Areas - 142 million euros-, improving accessibility to population centres and centres of economic activity, (including main accessibility infrastructures of the Azores), the airfield/airport and seaports, work on bypasses and ring roads to the main urban centres, the installation of road and parking terminals outside urban centres and the requalification of signposting - 60 million euros.

According to the European Commission, this component supports the response to the country-specific recommendation to focus investment on the green transition, taking into account regional disparities and supporting the use of digital technologies to boost business competitiveness. (European Commission, 2020d).

The reforms are well specified, although no specific dates for their entry into force are put forward, nor the competent body responsible for their implementation. Moreover, the plan does not cover the issue of maritime and rail connections, nor does it specify how to coordinate with Spain and the rest of the Eurozone to improve communications and thus reduce transport costs and become more integrated into the European market.

Measures taken for the green transition: The Portuguese economy records very high energy consumption in buildings and businesses, which could be reduced by improving energy connectivity with the Iberian Peninsula, leading to greater competitiveness and facilitating renewable energies. Furthermore, Portugal is facing some adverse effects due to climate change, such as floods and forest fires, water and waste management and the circular economy (European Commission, 2020).

The Portuguese RRP allocates EUR 6.291 billion, or 37.9% of the total, to achieve the environmental objectives in Regulation (EU) No 2020/852. To this end, of the 20 components included in the plan, 16 include investments that contribute to climate objectives. Component 1, "National Health Service" and Component 3, "Social Responses" envisage the renewal of part of the health and social services fleet of vehicles with electric cars. Component 5, "Business Capitalisation and Innovation" includes measures to achieve more environmentally sustainable production processes. Component 7 "Infrastructure" promotes several measures aiming at more sustainable mobility. Component 8, "Forestry" includes

different criteria for the prevention and fight against forest fires. Component 9, "Water Management" provides for interventions to mitigate water scarcity, especially in vulnerable areas such as the South Tagus, Algarve, Alentejo, and the Madeira archipelago. Component 10, "The Sea" focuses on the blue economy and includes measures to protect marine resources and implement more efficient help and energy use solutions for fisheries. Component 11, "Decarbonisation of Industry" includes subsidies for industries to adopt low-carbon processes and technologies. Component 12, "Sustainable Bioeconomy" encourages the textile, clothing, footwear and natural resin sectors to use biological resources efficiently instead of fossil-based materials. Component 13, "The energy efficiency of buildings" includes the renovation of existing buildings and the construction of new, more energy-efficient buildings. Component 14, "Hydrogen and Renewables" promotes the energy transition by supporting renewable energies, with a strong focus on the production of hydrogen and other renewable gases. Finally, Component 15, "Sustainable Mobility" promotes the use of public transport and encourages the decarbonisation of the transport sector (Ministério do Planeamento, 2021).

According to the European Commission's assessment, these measures are expected to contribute to the green transition, to the protection of the environment in a way that promotes the fulfilment of the national energy and climate targets set in the NECP 2030 and RNC 2050, and thus to achieving carbon neutrality by 2050. However, the plan contains specific measures to enhance biodiversity - Component 8 "Forests" and Component 10 "The Sea". The Commission recommends that Portugal complement these challenges and investments with support from other EU funds. Grade A is awarded according to the Resilience and Recovery Mechanism Regulation (European Commission, 2021).

Measures taken for the digital transition: The COVID-19 pandemic has highlighted the severe weaknesses of the Portuguese economy in terms of digitisation: around 50,000 students do not have access to the internet, which has prevented them from following their teaching online, the coverage of the telecommunications network in rural areas is insufficient, and there is a deficit of basic digital skills in the population (European Commission, 2020). Thus, in 2021, Portugal ranked 16th out of 27 EU Member States in the DESI (Digital Economy and Society Index). The Portuguese economy ranks well in none of the four main sub-indices - human capital, connectivity, digital technology integration, and digital public services. In terms of human capital, it ranks 18th, with only 52% of the population having basic digital skills (compared to 56% in the EU). However, it should also be noted that it has a higher percentage of people with advanced digital skills than the EU. In terms of connectivity, it ranks 15th, with the priority being the replacement of the Atlantic submarine cable linking the mainland to the islands of Madeira and the Azores, which is at the end of its life cycle. In digital technology integration, Portugal ranks 17th, mainly because only 51% of enterprises report at least essential digital intensity (compared to 60% in the EU) and the lag in e-invoicing. Finally, in terms of digital public services, Portugal ranks 14th in the ranking, with only 57% of users carrying out their procedures online and only 48% of digital public services being open (compared to 64% and 78% in the EU, respectively).

The Portuguese RRP allocates EUR 3.67 billion to the digital transition, i.e. 22.1% of the total budget. The main measures are education and training in digital skills, the digital transformation of enterprises, and the digitisation of the public administration (European Commission). The plan directly addresses all these unprecedented challenges in 5 components and indirectly in four. The five are Component 16, "Enterprises", Component 17, "Quality and sustainability of public finances", Component 18, "Economic justice and business environment", Component 19, "Public administration - Capacity building, digitisation and interoperability and cybersecurity" and Component 20, "Digital School". The European Commission awarded the digital measures with a grade of A according to its Resilience and Recovery Mechanism Regulation (European Commission, 2021).

Summary assessment

According to the Report from the Commission to the European Parliament and the Council on the implementation of the Recovery and Resilience Mechanism (European Commission, 2022), Portugal has already submitted its operational agreement to request its first payment application on 25 January 2022. The report considers that the Portuguese government adequately addresses the six pillars to be considered for the Recovery and Resilience Mechanism, indicating among the most relevant measures the capitalisation of its national bank, the deregulation of regulated professions and insolvency problems -pillar 3, smart, sustainable and inclusive growth-; fiscal reforms to support the transition to a sustainable and circular bioeconomy -pillar 5, economic, social and institutional health and resilience-; investments to increase the number of digitally skilled workers -pillar 2, digital transformation-; programmes to ensure housing for the most vulnerable groups -pillar 4, social and territorial cohesion-, among others.

After an exhaustive analysis of the vulnerabilities of the Portuguese economy and the reforms and investments presented in its programme, we consider that all the exposures of its economy are covered. However, such vulnerabilities may not be fully corrected with the proposed measures and reforms. Thus, we believe that, although the Portuguese economy's public debt problem will be substantially alleviated thanks to the NGEU, it will find itself in serious difficulties when the general safeguard clause of the Stability and Growth Pact is deactivated. Moreover, it is difficult to predict an increase in private investment and, therefore, national productivity and production, especially within the current radical uncertainty in the international economy.

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This paper assesses the value added of the the RRP of France, Italy, Spain and Portugal in light of the vulnerabilities limiting their long-term growth, and of some main implementation risks, such as the need to avoid financing recurrent expenditures, the degree of additionality of the RRP, the preference for grants, the lack of EU value added, or insufficient administrative capacity. The paper calls for a political debate on such issues and, in particular, on the role of additionality.

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