The recovery as a springboard for change

EIB Investment Report 2021/22

Debora Revoltella
Chief Economist EIB

Luxembourg, 12-13 January 2022
Key messages

- Policy support has been successful in avoiding the worst
  - Real GDP and Investment* are back to pre-pandemic levels in just 2 years, but it is not over

- Today – the challenge is to adapt to the new normal and to reap the benefits of the green and digital transformation

- Policy focus on investment:
  - Protect public investment
  - Maximize the impact of the Recovery and Resilience Facility
  - Create the conditions for private investment

* EU excl Ireland
Recovery, in less than 2 years

**Real GDP**
cumulative, 2019 Q4 = 100

**Real investment by sector**
Q4 2019 = 100

Policy support was widespread, preserving jobs.

Pandemic response fiscal measures
2020-June 2021, % of 2019 GDP

<table>
<thead>
<tr>
<th>Year</th>
<th>US</th>
<th>EU</th>
</tr>
</thead>
<tbody>
<tr>
<td>2020q1</td>
<td>20</td>
<td>15</td>
</tr>
<tr>
<td>2020q2</td>
<td>25</td>
<td>20</td>
</tr>
<tr>
<td>2020q3</td>
<td>30</td>
<td>25</td>
</tr>
<tr>
<td>2020q4</td>
<td>35</td>
<td>30</td>
</tr>
<tr>
<td>2021q1</td>
<td>40</td>
<td>35</td>
</tr>
<tr>
<td>2021q2</td>
<td>45</td>
<td>40</td>
</tr>
<tr>
<td>2021q3</td>
<td>50</td>
<td>45</td>
</tr>
</tbody>
</table>

Labor market adjustment
Vacancy rates and unemployment rates, EU vs US

<table>
<thead>
<tr>
<th>Year</th>
<th>US</th>
<th>EU</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019q4</td>
<td>2%</td>
<td>1%</td>
</tr>
<tr>
<td>2020q1</td>
<td>3%</td>
<td>2%</td>
</tr>
<tr>
<td>2020q2</td>
<td>4%</td>
<td>3%</td>
</tr>
<tr>
<td>2020q3</td>
<td>5%</td>
<td>4%</td>
</tr>
<tr>
<td>2020q4</td>
<td>6%</td>
<td>5%</td>
</tr>
<tr>
<td>2021q1</td>
<td>7%</td>
<td>6%</td>
</tr>
<tr>
<td>2021q2</td>
<td>8%</td>
<td>7%</td>
</tr>
</tbody>
</table>

Sources: (1) IMF Fiscal Monitor Database of country fiscal measures in response to the COVID-19 pandemic; (2) Eurostat, BLS, EIBIS 2021
Note: Private sector vacancies for the United States, non-farm business vacancies for the European Union.
...it was widespread at firm level....

Share of firms receiving policy support

% of firms

- Any support
- Guaranteed credit
- Deferral of payment
- Subsidies
- Other financial support

Source: EIBIS 2021
Firms with large declines in sales were more likely to receive financial support… ... allowing them to keep investment plans, independent of the sale loss

Source: EIBIS 2021
Many firms reacted to the pandemic, starting their “digitalisation journey”, but to a lesser extent than in the US.

Source: EIBIS 2021.
The pandemic put on hold climate investment, but EU climate policy leadership is likely to pay off for the future.

EU investment in climate change mitigation was stable at 1.5% of GDP.

- Strong policy direction: an asset for Europe
- Awareness increasing
- EU leading in climate innovation

**Firms’ investment to deal with climate change**

% of firms planning to invest over next 3 years

% of firms that already invested

Source: EIBIS 2021
The risk of an asymmetric recovery remains

**Impact across sectors**
(share of firms with more than 25% sales losses)

- Hotels, Restaurants
- Textiles
- Transportation
- Machinery and transport
- Trade
- Petroleum and raw materials
- Construction
- IT and Telecommunication
- Computer and electronics
- Food
- Chemicals and... 
- Electricity, Gas and Water

**Vulnerabilities across countries**
(Economic shock and share of firms at risk, by country)

Source: (1) EIBIS 2021 share of firms reporting losses (indicative data). (2) Vulnerable firms estimates based on ORBIS_EIBIS match database, with simulations up to mid 2021. Red dots are countries in Southern Europe.
Policy support was widespread... Resilience to withdrawal of firms support likely to vary across countries.
The divide across territories, firms and people might have increased

- The crisis has been tougher with the least educated and poses challenges for the young
  - Covid-19 induced school closure could reduce students’ lifetime income by about 3.5% on average
- In cohesion regions, many structural gaps (infrastructure, digitalization, skills) made it hard to adapt
- SMEs and firms that were non-digital before the pandemic, were much less likely to transform – increasing the digital divide
- The share of firms investing in training dropped by 10 pp to 52% and more strongly for SMEs.
  - The share of firms investing in training remains lowest in non-transforming firms and less developed regions adding to transformation challenges

Source: EIB Investment Report 2021-2022
The new normal requires fast adaptation, with investment to reap the benefit of the green and digital transition.

A policy focus on investment is crucial.
Fully exploit the potential embedded in the Recovery and Resilience Facility and protect public investment from fiscal consolidation.

Estimated impact of the RRF by 2030 (% GDP)

As it stands, the Growth and Stability Pact would require a primary surplus of 3% of GDP vs. 1% on average during 2015-2019, in the most indebted countries.

Source: EIB Investment Report, based on Rohmolo, JRC-EIB. The bars indicate the estimate impact of the RRF in terms of wider GDP.
Unlock private investment by addressing barriers: lack of skills, risk sharing, policy clarity and infrastructure

Barriers to investment
% of firms

- Availability of staff
- Uncertainty
- Business Regulation
- Energy Costs
- Labour Regulation
- Demand
- Transport Infrastructure
- Availability Finance
- Digital Infrastructure

Sources: EIBIS
Conclusions

- So far so good but vulnerabilities and asymmetries remain

- Accelerating investment is crucial, to adapt to the new normal and reap the benefits of the green and digital transformation

- Going forward, policy focus should target investment:
  - Protect public investment
  - Maximize impact of the Recovery and Resilience Facility
  - Prioritize policies with the potential to unleash more private investment: skills, risk sharing, policy clarity and infrastructure

- Deal with asymmetries and inequality by incentivizing transformation