IMPROVING ECONOMIC POLICY

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Euro area accession countries in the context of the pandemic

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Background and questions

- Seven of the eight non-euro EU member states are obliged to join the euro area (Denmark has an opt-out)
- Bulgaria and Croatia joined the exchange rate mechanism (ERM-II) and banking union in July 2020, while Romania expressed interest in joining
- Czech Republic, Hungary, Poland and Sweden do not seem to be interested in euro membership

- Questions:
  1. How will the pandemic affect the process of euro area accession?
  2. How will the instruments of the Recovery Package help the euro area accession countries?

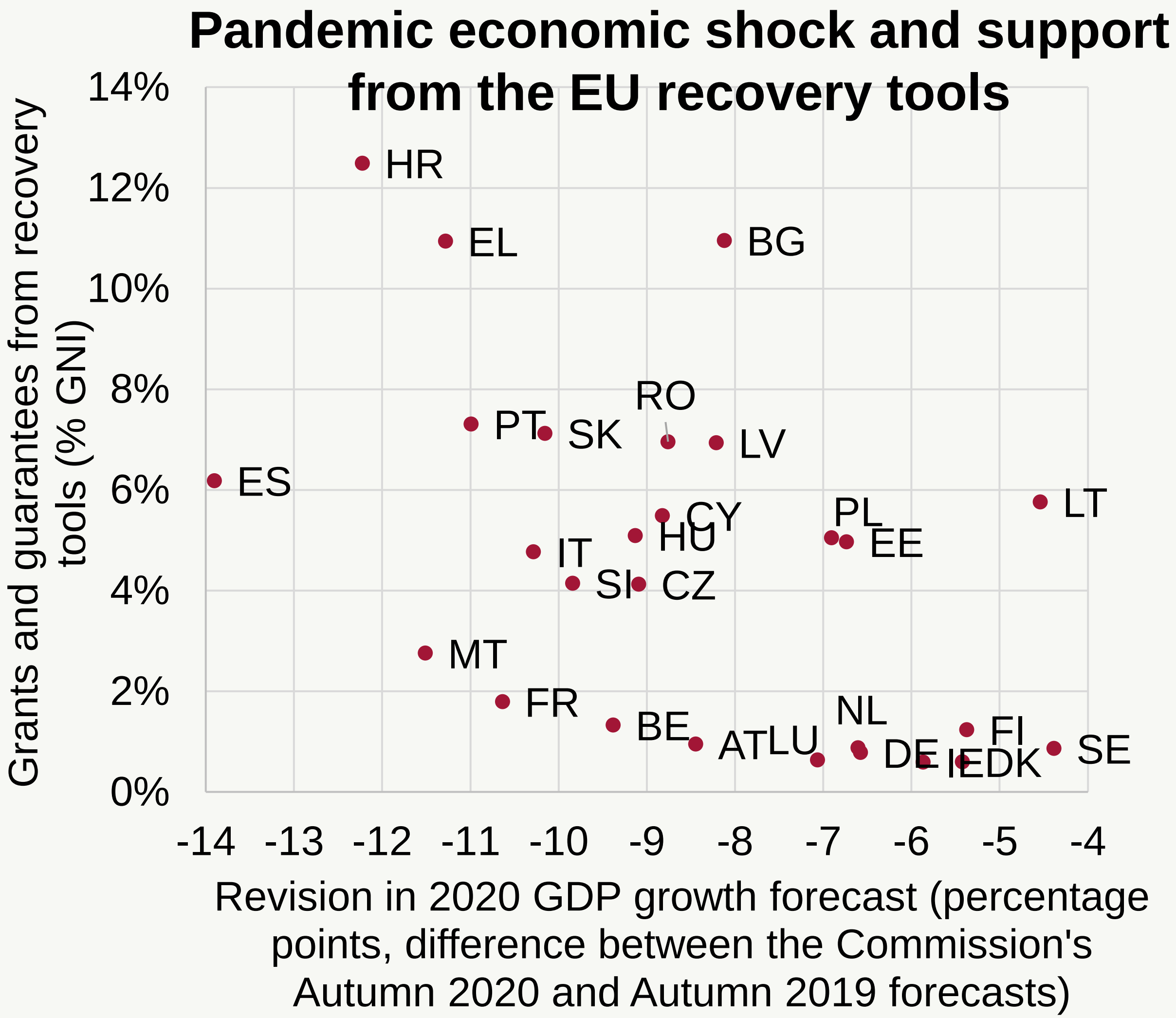
How will the pandemic affect the process of euro area accession?

- I do not foresee any direct implication of the pandemic on euro adoption
- ERM-II members Bulgaria and Croatia: no stress on currency markets
- No market stress in the other ‘outs’ either
- Euro-area specific policy responses:
  - *Various European Central Bank measures, yet national central banks in outs also introduced wide-ranging measures*
  - *European Stability Mechanism credit line: no demand for it*
- All other European pandemic responses were EU-wide
  - *E.g. 19 countries applied for loans from the employment-support facility SURE, including 6 of the 7 outs (except Sweden)*
- Thus, lack of euro membership did not hinder European crisis response measures in outs

Main aspects of euro adoption decision remain unchanged after the pandemic

- Maastricht criteria are inadequate for successful euro adoption
- In my research I found that euro membership was not a factor in explaining the success of recovery from the 2008-2012 global and euro area crises
- Euro introduction is more a political than an economic question
- Important aspects:
  - *Prevention of macro imbalances*
  - *Prevention of financial imbalances → prior banking union membership*
  - *Stability-oriented fiscal policy*
  - *Microeconomic flexibility*
- Less important aspect: euro area reform

How will the instruments of the Recovery Package help the euro area accession countries?



- Lower-income countries are the greatest beneficiaries of the package, because of the allocation method
- With the exception of Sweden, euro-outs are lower-income countries
- The insurance component (*harder-hit countries get more then less-hit countries*) is less important than the redistribution component (*lower-income countries get more than higher income countries*)

How will the instruments of the Recovery Package help the euro area accession countries?

- Most euro-outs have low public debts, lessened macroeconomic imbalances and benefitted from continued robust growth before the pandemic – EU recovery spending is less needed in these countries
- Except Sweden, extra EU recovery funds amount to 4-7% of GNI of most outs, even 11-13% for Croatia and Bulgaria – massive spending boost
- Additionally, countries can take 6.8% of GNI loans from the Recovery and Resilience Facility
- Will these countries be able to spend so much EU money, on top of the remaining sums from the 2014-2020 budget and the new amounts from the 2021-2027 budget?
- The EU budget veto of Hungary and Poland raises the possibility of an intergovernmental recovery fund without these two countries. If so, the two countries might face market pressure, with adverse economic impacts.