

ANALYSE HEBDOMADAIRE

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21 December 2020

How far can risk premiums go down in Europe?

EU finally to release 750 bn in recovery spending. GDP likely to contract in Q4. ECB to increase its support programmes. Fall in risk premiums reaches its limits. Risks return to the markets.

Key points

- End of 1st element of suspense: EU will finally be able to distribute 750 billion in Covid relief
- End of 2nd element of suspense: Brexit will be effective with or without an agreement as of 31 December 2020
- GDP rebound will likely be followed by a contraction in Q4
- Expected GDP growth of +4.5% in 2021
- ECB remains expansionary and reassuring
- How far can risk premiums go down in the Eurozone?
- Strength of the euro puts it back in the 1.20-1.30 fluctuation band
- Return of short-term risks for European equities

End of 1st element of suspense: EU will finally be able to distribute 750 billion in Covid relief funds

In July 2020 the 27 members of the European Union adopted a massive EUR 750 bn recovery plan aimed at countering the effects of the health crisis on the economies of EU countries, but the vetoes of Poland and Hungary quickly blocked the implementation of this much-needed recovery plan. The Brussels summit on 10 December finally helped lift these two vetoes thanks to the efforts of the German Chancellor, who holds the EU presidency for just a few more days. Unfortunately, it took almost six months to unblock the situation and start supporting the countries and economies most affected by the health crisis.

The recovery plan called “Next Generation EU” was supposed to finally enable the European Commission to borrow EUR 750 billion in the financial markets on behalf of its member states. This plan was intended to finance the reconstruction of European economies affected by the Covid-19 crisis by preparing the European economy overall for the challenges of the 21st century.

The plan comprised a grant component (EUR 312 billion) and a traditional borrowing component (EUR 360 billion). A further 78 billion was earmarked for the European budget (2021-2027) and for the React-EU, Just Transition Fund and Horizon Europe programmes. The bulk of the funds was to be distributed in 2021 and 2022. Italy (65.5 billion) and Spain (59.2 billion) were to be the main beneficiaries of the plan, ahead of France (37.4 billion) and Poland (23.1 billion).

Both Poland and Hungary had initially refused the agreed-upon conditions for granting support funds, which concerned in particular compliance with the rule of law as well as guarantees in terms of corruption and judicial independence. The 27 therefore seem to have reached an agreement, but we will still have to wait for ratification by the European Parliament and the parliaments of each member state. It is thus not clear that uncertainty has completely abated.

Furthermore, in the best-case scenario, the funds will be released only from the middle of next year. In the meantime, Poland and Hungary may still decide to challenge the agreement before the European Court of Justice. Thus, the EU may well have to find another way to deal with the appeals that these two countries are likely to file in January, which could delay the implementation of the scheme until 2022 or even 2023.