

State aid and Covid-19: a European dilemma

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In response to the economic impact of the Covid-19 crisis, the European Commission has authorised a temporary easing of the framework governing the use of State aid. While this measure was necessary in an emergency situation, it is likely to distort competition in the internal market if it is used on a wide, prolonged and heterogeneous basis.

State aid is prohibited by EU law ([Article 107 TFEU](#)), with some exceptions, as it is deemed contrary to the free competition principles of the internal market. For example, in 2018, the European Court of Justice ruled that state aid granted by the Belgian government to [Ryanair](#) was illegal.

However, according to Article 107 TFEU, this framework may be eased in the event of "exceptional occurrences" or "serious disturbances" to the economy. As early as 19 March in the context of the Covid-19 crisis, the Commission defined a Temporary Framework for State aid measures to enable EU countries to support their companies in difficulty as a result of this crisis, by granting, by end-2020 and for a limited period of time, subsidies, State-guaranteed loans (SGL) and soft loans. It then extended this framework on [3 April](#), [8 May](#) and [29 June](#) to cover aid for disease control, recapitalisation (possible until mid-2021) and start-ups.

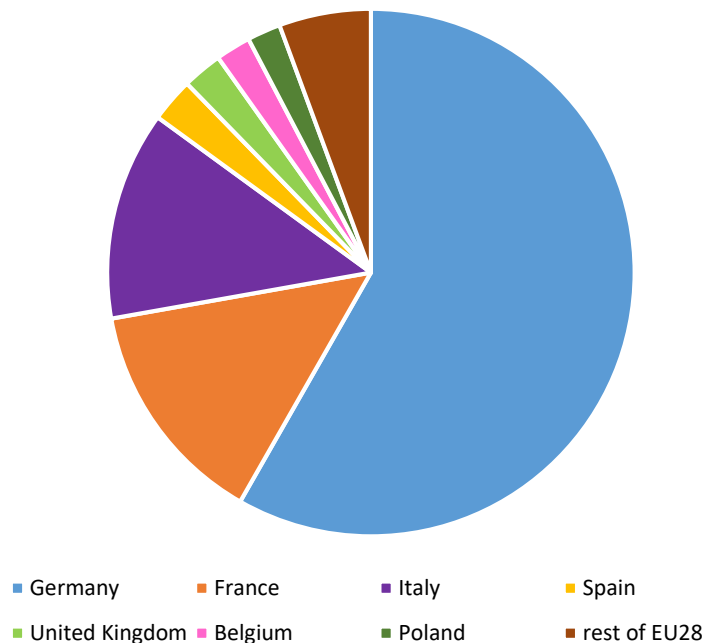
This aid has helped to support sectors that would not have been supported in the absence of a crisis, such as aviation. This framework has been widely used: according to the Commission the amount of authorised State aid, mostly in the form of SGLs and soft loans, amounted to over [EUR 2,190 billion](#) at the beginning of June 2020.

The scale of the crisis called for a rapid response. However, the idea that the most affected economies were also those that had received the most State aid was not entirely borne out in reality.

Heterogeneous distribution of State aid

In terms of amount, authorised State aid until July 2020 concerns first and foremost the major economies: Germany (58% of the total), France (14%) and Italy (13%) (Chart 1).

Chart 1: Breakdown by country of State aid ceilings authorised by the Commission from 19 March to 8 July 2020



Sources: European Commission data (estimated ceiling amounts) and author's calculations. The amount of State aid paid out can be de facto much lower than the ceiling amount, in particular in the case of loan guarantees (e.g. Germany).

It should be noted that for Germany, and to a lesser extent Italy, these are Commission estimates because several State aid measures granted by these countries do not specify an amount, particularly those in the form of SGLs. The budgeted measures correspond to ceilings, and are not de facto necessarily used to their full amount.

In addition, only roughly EUR 338 billion are allocated to specific sectors, in particular disease control (medical equipment, R&D) and sectors where most of the activities cannot be carried out by teleworking (e.g. transport). The other measures are less targeted, sometimes concerning companies in difficulty of a specific size (e.g. SMEs) or companies in difficulty of various sizes and sectors.

Why are there such differences between Member States? According to what rules is State aid granted?

A European framework for nationally funded aid

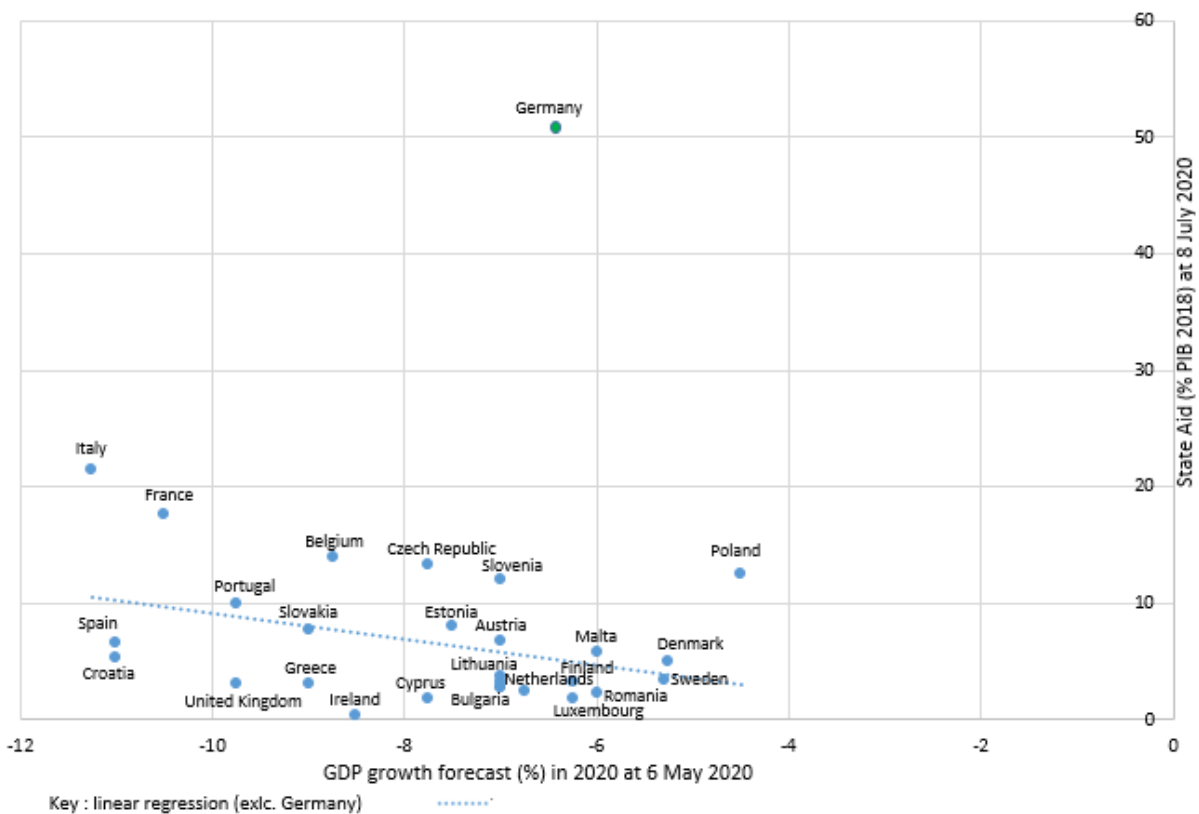
State aid is authorised by the Commission. It checks that the aid complies with the conditions laid down in the Temporary Framework and the TFEU, both in terms of the time

horizon and the financial viability of the beneficiary companies, which should not have been in difficulty on 31 December 2019.

State aid is financed at national level, which tends to favour countries with greater budgetary room for manoeuvre. This could explain the significance of German State aid (as a percentage of GDP), even though Germany is not the EU country most affected from a health and economic standpoint (Chart 2).

However, the introduction of State aid does not mean that it is consumed quickly or entirely. This makes comparisons more difficult and calls for qualifying the amount of German State aid, which is mainly composed of SGLs and soft loans. [Anderson et Al.](#) (Bruegel, 2020) have put forward an analysis of the actual use of SGLs: the amount of State guaranteed loans committed in Germany at end-June 2020 is estimated at around 1% of GDP in Germany, i.e. below the Italian (2.2%), French (4.4%) and Spanish (6.2%) levels. While the difference between the amounts announced and committed so far seems to strongly limit the distorting effect on the internal market, it is advisable to remain cautious at this stage, as this risk remains.

Chart 2: State aid (ceilings in % of GDP) vs. growth forecast for 2020



Sources: European Commission (European Economic Forecast, Summer 2020), and authors' calculations

Excessive easing?

In view of the total amount of State aid granted, it is necessary to consider what risks a massive and prolonged recourse to these measures would entail, especially as Margrethe Vestager, European Commissioner for Competition, pointed out [in a speech on 7 September 2020 in Berlin on Competition Day](#), there are differences in the ability of national budgets to respond to the crisis and support businesses, and as a result, differences in the aid amounts approved across the EU.

Indeed, this State aid is likely to distort competition in the internal market, which can lead to subsidy race ([Motta and Peitz, 2020](#)). Businesses in a government-supported sector in one country may jeopardise non-supported businesses operating in the same sector but in other countries. The latter are therefore encouraged to also support their businesses, provided they have sufficient budgetary capacity. **There is therefore also a risk of divergence between EU economies resulting from governments' capacity to finance such aid.**

Finally, if State aid is granted without any strict conditionality, there is a risk of losing sight of the EU's objective of greening the economy. Currently, ecological conditionality is left to Member States' discretion: while the Temporary Framework mentions the ecological objective, the Commission's [communication](#) dated 13 May 2020 states nevertheless that it is the responsibility of Member States "to design national support measures in a way that meets their policy objectives". This objective must however guide future policies, with at least 25% of the EU's long-term budget (cf. [Green Pact for the EU](#), European Commission, December 2019) and 30% of the expenditure of the [July 2020 recovery plan](#) to be allocated to climate action.

All in all, the Commission's State aid policy has led to a broad acceptance of State aid. The potentially large divergences observed across EU countries, if they were to materialise and become sustainable, could distort competition within the internal market. One solution would have been to grant some of this aid at European level via the recovery plan, but the Solvency Support Instrument, [proposed by the Commission](#) in the framework of Next Generation EU, was not approved by the European Council. In this context, the European Commission's action to ensure compliance with competition rules appears all the more necessary and valuable in this crisis, in order to limit the distortions that could arise from the allocations of aid to businesses generated by the Covid-19 crisis.