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Europe's paradox: weak investment despite abundant savings

Note written by Jacques de Larosière

Europe has no shortage of savings nor liquidity. What it lacks is productive investment. This observation should alert anyone wondering about the persistent weakness of growth and productivity on the continent. Monetary policies are once more showing themselves to be highly accommodating, and financing conditions have returned to being particularly favourable. And yet investment remains sluggish. This paradox is neither cyclical nor accidental. It is the result of repeated economic choices that have favoured short-term ease at the expense of the future.

A comparison with international peers is particularly eye-opening. This phenomenon is significantly less pronounced in the United States, where the economic and institutional environment remains more conducive to productive investment: lower tax burden on businesses, coherent and integrated single market for goods, services, and capital, increased energy independence, longer working hours and higher labour force participation rates, a better-educated population, sustained efforts in research and innovation, and less burdensome regulations and bureaucracy. These factors explain why investment, particularly in intangible assets, has held up better there than in Europe, where structural rigidities and market fragmentation are a long-lasting obstacle to risk-taking.

Recent data¹ highlight that the United States is actually on the cusp of reindustrialisation. Indeed, in 2025, the US captured 44% of global and industrial investment, which represented 26% of all projects volume-wise. One cannot underestimate this change for industrial investment in the United States has nearly doubled over the last year from USD404 billion to USD793 billion.

This paradox raises an obvious question: why have financial systems saturated with liquidity and exceptionally expansionary monetary policies not been able to generate a more robust investment environment? What if the answer lies precisely in this prolonged monetary abundance?

John Maynard Keynes had warned of the risk of a "liquidity trap". When interest rates remain low for a long time, they cease to effectively channel

savings into productive investment. If the return on capital no longer compensates for industrial risk nor the long-term immobilization of funds, savings are funnelled into liquid, low-risk, and low-yield assets. When interest rates hover around zero or turn negative in real terms, the incentive to commit funds to long-term savings diminishes. This phenomenon is particularly pronounced in Europe, where households traditionally favour security over risk-taking.

For more than a decade, ultra-accommodative monetary policy has thus shortened the horizon for European savings. Savings are abundant, but increasingly liquid, volatile, and less oriented toward financing productive projects. This observation is now widely documented, notably by the work of the European Savings Observatory and the Bank for International Settlements.

However, this monetary policy cannot be analysed independently of fiscal policies. By allowing governments to finance themselves at real interest rates close to zero, easy money has encouraged chronic public deficits and delayed structural reforms. When borrowing costs nothing, budgetary constraints disappear and economic discipline fades away. Monetary easing has served as a substitute for reform, at the cost of a gradual weakening of the productive apparatus.

This shift towards consumption is not just a result of monetary excess. It is also a symptom of increasingly apparent "fiscal dominance". The excessive debt levels of certain European countries has gradually led central banks to favour supporting public financing over the efficient allocation of capital. In such a context, raising interest rates in a sustainable manner would increase the cost of sovereign debt. Monetary policy is thus subordinated to budgetary imperatives, to the detriment of productive investment, employment, and productivity. This logic penalizes the real economy and traps Europe in sluggish growth. It is time to cautiously break out of this cycle.

This combination of highly accommodative monetary and fiscal policies has led to an increasing misallocation of resources, particularly in Europe.

1. Trendeo and McKinsey, "Baromètre annuel des investissements industriels mondiaux", 22 February 2026.

A significant portion of savings are absorbed by public operating expenditures, bureaucracy, and redistribution mechanisms, the expansion of which ultimately discourages initiative and risk-taking. Liquidity in the banking and non-banking sectors has increased significantly, as has outstanding credit, without any real benefit to productive investment.

How can we explain why expansionary fiscal policies and abundant financing have not led to stronger investment momentum and sustainable productivity gains? Part of the answer lies in the liquidity trap. But the other, equally decisive factor is the growing rigidity of productive supply. When the productive apparatus lacks capacity, flexibility, and innovation, abundant liquidity does not translate into more investment or production, but rather into price pressures. Stimulus then fuels inflation rather than productivity.

This inelasticity of supply has been brutally exposed by recent shocks. Between 2021 and 2023, the recovery in demand has been hampered by a weakened productive apparatus that is unable to respond quickly. The return of inflation has thus highlighted long-standing weaknesses: underinvestment, deindustrialization and a loss of skills. It has also revealed the complete disregard for excessive monetary creation during this period. When the creation of money overtakes an economy's productive capacity, excess liquidity drives up prices rather than generating real growth.

Supply has become rigid because the savings horizon has been shortened, productive investment has been relegated to the background, structural reforms have been systematically postponed. Cyclical support policies have too often replaced policies aimed at sustainably strengthening productive capacity.

It is time to address this paradox at its root and put productivity back at the heart of the economic debate. This means rehabilitating structural reforms: making labour markets more flexible and reducing the burden on businesses – which implies cutting public spending – and developing pension funds capable of financing long-term investment. It is also essential to better reward long-term risks, rather than systematically penalizing them.

Europe should finally be more concerned about the flight of its capital to areas offering more attractive returns, rather than seeking a policy of systematically low interest rates. Low productivity gains are not primarily a question of new financial instruments or additional European debt. It is a fundamental question: why are there fewer projects and fewer companies capable of pursuing long-term productive ambitions?

The answer is clear. It lies in an economic policy that is too often focused on immediate relief and structurally unfavourable to productive supply, innovation, and investment in the future. A society that lives on the benefits of the present by sacrificing its future cannot prosper in the long term.

It is essential to react, but not by repeating the recipes that have led to the current impasse. Distributing more without restoring productive investment and economic discipline will only exacerbate imbalances. As Raymond Aron pointed out, "internal consolidation is a prerequisite for any successful international integration." It is this imperative of responsibility and lucidity that Europe must now face if it wants to return to growth, economic sovereignty, and sustainable prosperity.

European common debt: is this Europe's Hamiltonian moment?

Note written by Jacques de Larosière

First, let us recall the meaning of the term 'Hamiltonian moment'.

Alexander Hamilton was the United States' first Secretary of the Treasury, serving from September 1789 to January 1795. He incorporated the war debts incurred by the thirteen former American colonies into the unified federal public debt of the nascent United States. This was the price of freedom. However, he left non-military debts to be paid by the individual states.

For a long time, Europe was unable to establish a federal-style community debt as Hamilton had done.

However, since the Covid-19 crisis, some observers have suggested that Europe now has reached a significant amount of common debt and that the 'Hamiltonian moment' has arrived.

What is the current situation?

1. The debt issued by the European Economic Union has become substantial

1.1 Background

The EU's response to the pandemic has been significant, with €800 billion allocated for measures to boost productivity, climate action, digital transition, and most recently, the response to the energy crisis triggered by the war in Ukraine.

This debt is conditional in that it is applied flexibly to national plans rather than to specific projects.

Its main objective is to allow the economically lagging Member States to 'catch up' productivity-wise.

Of all the Community funding programmes, the NGEU (NextGenerationEU) debt programme was by far the largest. This program was financed through debt contracted by the European Commission on the market in the form EU bills and bonds, all with different maturities.

1.2 The amount of debt raised insignificant

EU debt rose from €50 billion before the pandemic to €695 billion by mid-2025.

By the end of the process, the total amount of shared debt is expected to reach between €800 billion and €950 billion.

This rapid development deserves to be highlighted.

2. Is it possible to compare EU debt with public debt denominated in dollars?

a) On the one hand, debt issued in dollars totals \$55 trillion, of which \$18 trillion is held by non-residents.

On the other hand, given that the EU debt is barely set to reach €1 trillion in a few years' time, the amounts are simply not comparable.

However, these two debts differ not only in their amount, but in their fundamental characteristics too.

b) The US government is responsible for public debt issued in dollars. It is the sole authority in charge of servicing interest and principle repayments. There is no need for the government to negotiate with individual states.

The situation with European common debt is different. There is no unified European state that is the natural guarantor of the debt issued by the Commission. The burden lies with the Commission itself.

However, as there is no sovereign state, the Commission is obliged to negotiate with the Member States in order to service and meet the maturities of the common debt.

In principle, it is the responsibility of the European Union's budget to ensure that payments are made. This, however, assumes that the European budget is sufficient, or can be made sufficient, in order to finance the operations in question.

Yet amending the European budget is no easy task. It is the result of a political consensus that is difficult to achieve.

Let's take a closer look.

- The part of NGEU that involves **loans** to Member States is less problematic. Beneficiary states receive loans from the Commission. When these loans mature, the beneficiary states repay them to the Commission. However, it should be noted

that the loans received benefited from lower spreads than those normally applied to the various states. Therefore, there is an element of community solidarity here, as the Commission has given member states with high spreads more favourable terms.

- Let us now analyse the part of the NGEU that is allocated in the form of **grants**.

Here, we see a significant redistribution.

Grants are preferably allocated to Member States with low productivity. The major beneficiaries of the grants (Portugal, Italy, Greece and Spain) received 78% of the total grants, which is well above their budgetary share. However, they only contribute 28% of GDP.

This is, in fact, a redistributive mechanism.

Subsidies go to the less wealthy states, while the debt financing that made them possible will most likely be financed by all states via the Community budget.

In this sense, the 'good payers' will bear most of the cost.

Ultimately, the NGEU will be funded by the Community budget. However, it is unclear whether this redistribution will be politically accepted.

The comparison with the United States can be formalised as follows:

- In the United States, public debt depends on American power. Debt is a matter for the government. It does not need to be negotiated with the states. The United States is a single state with a deep and unified financial market.
- In Europe, however, the Commission, which issues Common debt, has to negotiate its financing.

The attitude of the markets therefore differs depending on the area in question.

Dollar-denominated debt is 'self-sustaining', whereas European debt requires support in the form of budgetary agreements.

I would also like to point out that the idea that EU financing will somehow be 'self-financed' by the productivity gains generated by the NGEU is unrealistic. There is no evidence to suggest that the NGEU has increased productivity. The indications gathered so far are ambiguous and the future is very uncertain.

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Before we welcome the arrival of a 'Hamiltonian moment', we must remember that Hamilton incorporated the states' war debts into a single federal budget, which the federation then repaid. We are a long way from that.

The euro's future in the face of economic divergence across Member States

Note written by Didier Cahen with Kiann Conlon

The euro was conceived not merely as a currency, but as a means to pursue and promote stability, economic convergence, cross-border capital flows and political integration across the European union. Thanks to the euro, exchange rate risk disappeared, price transparency improved, and value chains integrated. The euro is the most recognisable component of the European Union.

However, for the past 25 years, Europe has fallen behind the United States particularly regarding productivity and economic growth. The cooperation between EU member states is still insufficient. The refusal of some founding Member States to respect the common fiscal rules laid out at the euro's inception – enabled by the Commission's weak enforcement of the Stability and Growth Pact – has stalled European economic and financial integration. Despite abundant savings, productive investment has weakened, and surplus savings are flowing out of Europe instead of circulating among EU member states. The euro finds itself in dire straits – if not in serious danger. Despite the upheaval of the current world order, the threat currently facing the euro does not stem from external factors, but rather from internal economic and financial divergences that have accumulated gradually and are now reaching a dangerous threshold.

This paper will first present the facts at hand before explaining the causes that have led to the current situation. It will then highlight what Europe must not do to extract itself from this situation – the traps one must not fall into in order to resolve the EU Member States' problems. Lastly, this paper will present a series of solutions, measures to be taken, in order to set EU Member States on the right path.

1. European Economic Decline and Structural Divergence

1. Europe's economic and financial decline

The most striking development of the past 25 years has been Europe's economic decline relative to its

peers. Since the global financial crisis, economic growth in the Euro area has significantly lagged behind that of the United States. Whilst GDP in the US has grown in real terms by 37% between 2008 and 2024, GDP has grown by only 15% over the same period in the Euro area. Between 1995 and 2024, labour productivity has grown by 45% in the US, compared to a meagre 10% in the Eurozone.

The facts are as clear as day: productivity growth has weakened, innovation capacity has eroded and Europe's share of global output has diminished. Europe largely missed the technological revolution. No European company is currently in the top 20 largest companies in the world by market capitalization¹. Europe's global influence has declined.

This is not primarily a failure of the currency itself. The euro continues to provide undeniable benefits. Rather, the problem lies in the growing heterogeneity of national economic policies within the monetary union. Instead of improving competitiveness, some Member States let public finances deteriorate by supporting consumption and redistribution rather than investment and private initiatives. A single currency cannot be expected to succeed when fiscal trajectories, competitiveness levels and reform efforts diverge too widely. Convergence was seen as an inexorable result of the monetary union. Instead, disparities have amplified in its wake. Debt levels have diverged across Member States. Productivity gaps have widened. Living standards have evolved unevenly. In several countries, especially in those with already fragile public finances, expenditure kept on increasing whilst vital reforms have been postponed time and time again due to political complacency. The final product is a monetary area where stability is maintained in appearance only, but where underlying imbalances gnaw at its foundations.

The divergence between France and Germany is the clearest illustration possible of this problem. At the launch of the euro, both countries displayed similar debt levels and comparable competitiveness. Both countries stood at around 61% of GDP. Today, their trajectories differ markedly. Germany has preserved fiscal discipline and accumulated current-account

1. LVMH (France) and Novo Nordisk (Denmark), both of which were among the world's top 20 companies at the beginning of 2024, are no longer in this ranking today.

surpluses, while France faces persistent deficits and rising public debt. In 2024, Germany stood at 62.5% of GDP, whereas France had reached 113% of GDP. As of December 2025, France had a 7.7% unemployment rate, whereas Germany stood at only 3.7%. Since 2000, the French balance of payment has oscillated around -1% to -2% of GDP, whereas Germany has stood at a constant +6-7%. Despite having a population of nearly 10 million more people, Germany has one million civil servants fewer than France.

Such divergence weakens not only economic cohesion but also the political trust that was so necessary to European integration. If France and Germany – the two biggest Member States and the driving couple behind EU integration since the Schumann declaration – can't even align their economic trajectories, then how can the EU expect to be taken seriously on the world stage as a coherent entity?

1.2 The numerous causes behind Europe's economic decline

1.2.1 The Disappearance of Adjustment Mechanisms

The main weakness of the current framework lies in the disappearance of automatic correction mechanisms. Under the previous European Monetary System, unsustainable policies quickly triggered market reactions. Fiscal indiscipline and uncompetitive policies were met with rising interest rates and currency depreciation that eroded purchasing power. This inevitably led to political backlash, which forced national leaders to correct course.

The single currency eliminated these mechanisms without fully replacing them with credible and enforceable alternatives. As a result, solutions to current problems no longer arise from impersonal market forces but instead depend entirely on political decision-makers and have therefore become inherently political in nature.

1.2.2 The blatant disregard for the Stability and Growth Pact

The Stability and Growth Pact was intended to provide the discipline needed for the success of the single currency. Indeed, the Stability and Growth Pact dictates that Member States' deficit should be no larger than 3% of GDP and their debt levels should remain under 60% of GDP. Yet the Stability and Growth Pact's repeated suspension and flexible interpretation have undermined its authority.

The facts are damning:

From 2000 to 2025, six countries recorded a deficit exceeding 3% of GDP for at least ten years. These

countries are Belgium (12 years), Italy (14 years), Spain (16 years), Portugal (17 years), Greece (18 years) and the most damning of all: France (20 years).

By contrast, Germany (9 years), Austria (8 years), the Netherlands (6 years) and Finland (4 years) did not exceed the 10 years of non-compliance threshold.

It is thus no coincidence that the countries which have most frequently breached the 3% rule are also those whose public debt has deviated the most from the 60% ceiling. For example, according to European Commission, France's public debt stood at 57.4 percentage points above the ceiling by the end of 2025, whereas it stood at 0.3 points below the threshold in 2000. Spain and Italy are in a similar situation, with their respective debts growing from -2.2 points to 40.9 points and from 48.7 to 76.7 points over the same period.

Beyond its economic implications, this dynamic also raises a deeper moral and political issue, the blatant disregard of the Growth Pact has dire moral implications for all parties involved. Indeed, the current situation in the European Union strongly resembles that of the prisoner's dilemma. Member States unwilling to take the necessary measures to control their spending and reduce their deficit are currently shielded from the consequences of their own actions. If the fiscal, inflationary, and economic drift in the Eurozone were to continue, the 'virtuous' countries would end up paying for it. That would be the definition of an uncooperative game, in which most players try to evade their obligations by passing on the costs to those who respect them. We must therefore take the Union's destiny into our own hands and not let it drift. If this were the case, the logical outcome would be a new and inevitable crisis in the Eurozone.

In addition, when rules are not consistently enforced, it encourages an "everyone for themselves" mentality. A generalised climate of distrust sets in. This creates an obstacle to the development of collective projects, particularly when it comes to exposure to public or private risk. Ultimately, persistent fiscal laxity in large countries has blocked deeper Economic and Monetary Union.

1.2.3 The Commission and Council's role in Member States' erosion of discipline

The erosion of discipline cannot be attributed solely to national governments. The European institutions entrusted with safeguarding the Treaties, namely the Commission and the Council, have also failed to exercise fully the prerogatives conferred upon them. Whether through political complacency, fear of confrontation, connivance or structural

limitations inherent in their mandate, enforcement of the common fiscal framework has repeatedly been softened, delayed or suspended.

The Commission, formally the guardian of the Treaties, has too often acted as a mediator of political compromise rather than as an impartial enforcer of agreed rules. The Council, representing the Member States, has likewise preferred consensus over discipline, even when collective credibility was at stake. The result is a paradox at the heart of the Union: institutions designed to ensure compliance have found themselves constrained by the very governments they are meant to supervise. This inability – or unwillingness – to uphold the rules not only weakens fiscal credibility; it raises deeper concerns about institutional independence and the effective functioning of the Union's governance framework. A monetary union cannot rely solely on goodwill. If enforcement becomes negotiable, the architecture itself becomes fragile.

1.2.4 The euro has not only shielded weaker EU economies but has more fundamentally masked underlying structural imbalances

The euro has acted as a shield for weaker EU economies. By suppressing exchange-rate adjustments and compressing sovereign spreads, it has **protected** Member States from the immediate consequences of deteriorating competitiveness or fiscal slippage. This protection has had an unintended side effect: it has **masked** the gradual erosion of structural fundamentals across member states. Diverging productivity paths, rigid labour markets, persistent primary deficits and declining industrial capacity could accumulate beneath the surface without triggering the abrupt corrective signals that once forced reform. The currency thus provided financial stability, but at the cost of delaying adjustment. Imbalances that would previously have surfaced rapidly through currency crises instead deepened quietly within the monetary union.

1.2.5 The compounding effect of asymmetrical differences

The consequences of the Euro don't stop there. For highly competitive northern economies, the euro may be undervalued relative to their productivity levels, supporting exports and industrial strength. For structurally weaker southern economies, the same currency may function as an overvalued exchange rate, limiting their competitiveness. The single currency thus imposes uniform monetary conditions on structurally diverse economies,

making domestic reforms and productive investment not optional, but indispensable.

1.2.6 Monetary Expansion, rather than alleviating the pressures faced by Member States has only deepened their vulnerabilities

The prolonged period of ultra-accommodative monetary policy between 2008 and 2022 has fundamentally altered the economic landscape. Massive liquidity injections and historically low interest rates prevented financial collapse and stabilised sovereign debt markets.

Yet maintaining a persistently expansionary monetary policy has had negative consequences for both financial stability and the real economy in the Euro area, contributing to its relative decline compared to other advanced economies in recent years.

This policy has had at least five major adverse effects²:

1. It has led to a sharp rise in debt levels, driven by persistently low interest rates, thereby increasing the risks to financial stability.
2. It has dampened productive investment by encouraging a preference for liquidity and short-term returns over long term capital formation.
3. It has facilitated the proliferation of zombie companies made viable only by overly accommodative financial conditions, which has weighed on overall productivity.
4. Fourthly, it has contributed to the formation of speculative bubbles, disconnecting asset prices from their fundamentals due to artificially low rates.
5. Lastly, it has weakened the incentives for Member States, particularly those benefiting from the ECB's public debt purchase programmes, to implement the structural reforms necessary to boost their long-term growth potential. When borrowing appears costless, the urgency of reform diminishes. Monetary policy, initially designed to stabilise the system, gradually became a substitute for structural adjustment.

The link between monetary expansion and the fall of productive investment deserves to be further analysed: why did unprecedented monetary expansion not translate into stronger productive investment?

Indeed, Europe has not suffered from a shortage of savings or liquidity. On the contrary, the Euro area

2. See Chapter 3 of Part 1 of Dider Cahen's book *The Euro is in Danger* for further information.

has accumulated vast pools of savings, and yet investment remained persistently weak, particularly in intangible assets, innovation and industrial modernisation. This paradox is in fact not cyclical. It reflects a structural malfunction in the transmission of savings into productive capital.

Prolonged periods of near-zero interest rates alter behaviour. With persistently low – and sometimes negative – interest rates, the investment horizon for financial actors is considerably shortened, with private investors favouring safe, short-term investments. This is particularly pronounced in Europe, where households are significantly more risk-averse than their American counterparts. When the return on long-term productive investment no longer sufficiently compensates for industrial risk, savings naturally gravitate toward liquid, low-risk financial assets. This corresponds to the *Liquidity trap* concept laid out by Keynes, where abundant liquidity does not automatically generate productive capacity; but instead encourages asset price inflation, short-termism and defensive balance-sheet strategies. This has now been demonstrated by a number of studies³.

In addition, the liquidity abundance has fuelled an unprecedented financial bubble, driving up the value of stocks, bonds and real estate well beyond levels justified by economic fundamentals. In recent years, stock market performance has been largely driven by central bank monetary expansion; property prices also soared under the overwhelming influence of central bank liquidity.

While rising asset prices may strengthen balance sheets and generate wealth effects, they do not necessarily translate into higher productive capacity. Indeed, capital gains are not synonymous with capital formation when savings are invested in non-productive or speculative assets (residential properties acquired solely for resale). This type of investment does not benefit the real economy, unlike innovation, industrial expansion or technological upgrading.

The Bank of International Settlement (BIS) in its 2024 annual report notes that: “No healthy economy should operate with negative interest rates for too long because capital is misallocated and growth is hampered. Persistent strong and monetary easing contribute to the build up of financial vulnerabilities.”

Another consequence of an expansionary monetary policy is capital outflow. Currently, a substantially amount of European capital is invested in American public debt and equity markets. Said outflow

currently represents EUR300 billion a year. There are two main causes for this outflow. On the one hand, the expansionist monetary policy in Europe keeps interest rates artificially low. Investors are thus attracted to the naturally higher rates in the US. On the other hand, the return on equity offered by American companies is substantially higher than European ones. Structurally lower fiscal pressure and a more accommodating business environment allow for higher returns. Ultimately, European savings end up financing foreign expansion rather than domestic productive renewal.

1.3 The Euro area is again at a critical juncture

1.3.1 Fiscal Fragility and the French Question threaten the Euro itself

Public finances now constitute the central vulnerability. Several founding members of the Euro area carry debt levels exceeding 110 % of GDP, with limited fiscal buffers to absorb future shocks. Rising interest rates, even if moderate by historical standards, significantly increase debt servicing costs in highly indebted countries. When growth remains weak, the arithmetic of sustainability becomes increasingly unfavourable. Markets may tolerate gradual deterioration for a time, but confidence can shift abruptly. History shows that sovereign spreads often widen slowly before accelerating sharply once doubts emerge about a government's capacity or willingness to restore balance.

In this context, France occupies a pivotal position. As the Euro area's second-largest economy, its fiscal trajectory carries systemic implications. Public spending lies at 57% of public GDP, eight points above the Eurozone average. There has been no primary budget surplus since 2002. In a context of rising interest rates and low growth, if the current trajectory for public finances remains, interest payments will reach €100 billion in the next two years, representing 3% GDP in a country growing at 1%.

Should France's financing conditions continue to tighten, it risks an erosion of market confidence and, eventually, a financial crisis. Markets may not react to France's worsening public debt at the Euro area level, but contagion could still spread to the Eurozone's most indebted countries.

One would be gravely mistaken however to place blame solely on France. EU countries don't operate alone. They are a part of a larger institutional

3. For instance, see, G. Naacke, “What Is the Impact of Low Interest Rates on the Holding of Liquidity by Individual Investors and Companies?”, Les Cahiers du Centre, January 2022.

ecosystem which has a role to play in the health of all Member states' public finances. On the 26th of July 2024, the Council of the European Union approved the European Commission's recommendation to initiate excessive deficit procedures against Belgium, France, Italy, Hungary, Malta, Poland and Slovakia since these countries exceeded the 3% public deficit limit set by the Stability and Growth Pact in 2023.

However, on the 26th of November 2024, the European Commission approved France's draft budget for 2025 and its budget plans for the following year. Despite the resignation of the Barnier government and the French Parliament's rejection of the 2025 draft budget on the 11th of December 2024, the Council still endorsed the Commission's proposal. The height of absurdity indeed.

It is Member States, aided by the European institutions that are putting the euro at risk.

Some observers may nonetheless argue that high levels of debt can remain sustainable under certain conditions.

1.3.2 The Temptation of an Erroneous Comparison to the United States

European leaders severely underestimate how dire the situation truly is. One might argue that concerns over European public debt are exaggerated. Indeed, The United States is supposedly in a comparatively difficult budgetary position due to the fact that it carries a debt burden exceeding 120 % of GDP which set to rise to 143% of GDP by 2035⁴. Such comparisons, however, risk conflating fundamentally different economic realities.

The United States combines high public indebtedness with robust growth dynamics, sustained productivity gains and unparalleled innovative capacity. Since the pandemic, the American economy has experienced markedly stronger growth than the Euro area, driven in large part by its leadership in high value-added sectors such as digital technologies, artificial intelligence and advanced services. Its deep capital markets, fiscal unity and global reserve currency status further distinguish its structural position.

Another important distinction lies in the share of output collected in taxes and compulsory contributions. In the United States, total tax revenue amounts to around 25–27 % of GDP, significantly below the 40 %-plus levels typical in the European Union, where countries like France

individually exceed 45 % of GDP in such levies. This lower tax burden in the U.S. reflects both political choices and differing welfare-state models, and it affects not only fiscal space but also incentives for growth and investment. Also, unlike most European countries, the United States has managed to attract industrial investment once more. Over the course of 2025, industrial invest in the US surged by 32%, reaching USD1.800 billion, most of which comes from the US itself⁵. It currently appears that the US is at the cusp of a full-on reindustrialisation.

While US debt levels undeniably pose long-term challenges, they are underpinned by a dynamic and expanding productive base with comparatively lighter tax burdens. The US benefits from having a single market of goods and services much more deeply integrated than the EU, a unified political authority, a technological leadership, energy independence. In contrast, several European economies face high and rising debt in a context of weaker productivity growth, fragmented capital markets, higher compulsory levies and limited technological dynamism. To equate the two situations is therefore misleading: debt sustainability cannot be assessed in isolation from growth potential, institutional architecture, fiscal structure, innovation capacity and output growth.

European leaders often refer to aggregate Euro area indicators to reassure markets and citizens. Yet averages can obscure structural divergences between Member States. Unlike the United States, the Euro area does not rest upon a fully unified fiscal authority, a deeply integrated capital market or a single political executive accountable for macroeconomic stabilisation. The currency therefore relies heavily on mutual trust and credible adherence to common rules. When that trust weakens, the architecture itself becomes more fragile.

Furthermore, the US also hosts the largest army in the world as well as having sole control of the world currency: the dollar. But most important of all, the federal government is directly responsible for repaying the debt. It has at its disposition the means and tools to levy additional resources in order to repay its debt. The EU does not have such tools at its disposal. The EU depends on its Member States' contributions and would thus have to negotiate with them in order to increase its cash inflows. The EU does not have the power to unilaterally do so. Finding extra resources appears all the more difficult.

4. https://m.economictimes.com/news/international/us/us-debt-crisis-america-to-surpass-italy-and-greece-for-first-time-in-100-years-can-washington-fix-it-before-its-too-late/amp_articleshow/124851494.cms?utm_source=chatgpt.com

5. GUICHARD Guillaume, « Les Etats-Unis de Trump continuent d'attirer un déluge d'annonces d'investissements industriels », Les Echos, 23 February 2026.

2. What Europe Must Not Do

2.1 Further indebtedness cannot replace the necessary structural reforms

Europe must first resist the temptation of false solutions. Structural problems cannot be solved by increasing debt, nor by monetary creation and inflation. Public leaders must imperatively understand that public debt cannot replace structural reforms and that using debt to artificially support demand or maintain an obsolete production system amounts to postponing problems and weakening the competitiveness of businesses.

France has been guilty of this for more than 20 years, relying on stimulating consumption through public deficits and artificially low interest rates to create growth and jobs. These policies have had the opposite effect, leading to debt, a decline in productive investment, and encouraging speculation. In other words, spending is not synonymous with recovery. In other words the paradigm of easy money, lax fiscal policy and systematic indebtedness – widely embraced over the last two decades – will not succeed in the future.

2.2 No federal state means no genuine European sovereign debt

The denial of reality by over-indebted states must also be strongly condemned. Settling into the ease of excessive deficits without reducing unproductive spending weakens the state itself, which becomes powerless under the weight of debt. Politicians have perpetuated the illusion that it is easier to go into debt than to reform or work harder, but this strategy is unsustainable and will lead to future crises for the euro. Far from correcting the debt problem, this combination would only exacerbate the economic and social costs and precipitate a new crisis. And no, European common borrowing is not a viable solution.

Mutualising debt without correcting the underlying divergences that produced it would merely redistribute risk without eliminating it. Financial solidarity cannot replace structural responsibility. A currency union built on shared liabilities but diverging fundamentals would become more fragile, not more stable.

There is no such thing as European “magic money”. European borrowing cannot resolve national imbalances. If Member States were unable to borrow in order to make ends meet, why would borrowing with Europe’s backing make any difference? Even if the EU budget provides a guarantee, the EU itself is not sovereign over its

own budget. The EU does not possess the tools to unilaterally raise additional revenue through taxes or levies as a sovereign state would. Rather, it is entirely dependent on the contributions and goodwill of the Member States. Moreover, the creation of common instruments, whether labelled Eurobonds or new joint facilities, cannot in itself generate productivity, competitiveness or growth. The problem is not borrowing more or finding new projects. It is about projects that companies have made more competitive and are capable of carrying out.

Mutualising debt would require profound institutional change and the agreement of the most solvent countries and their taxpayers, who would then have to contribute to the tax burden of over-indebted states. This is politically impossible as it would effectively mean creating a sovereign European federal state. This seems inconceivable in today’s political climate given the economic and political differences between major countries, not to mention the hostility of many national public opinions and the legal obstacles to such a significant institutional change in certain countries.

This prospect, perceived as unfair by the citizens of solvent countries, would risk undermining confidence in the euro and further feed populism and euroscepticism. This is all the more so given that any jointly issued European debt would, given the fiscal divergences between the main member countries, be considered riskier than the sovereign debt of more disciplined countries, which would lead to a heavier tax burden on the citizens of these so-called solvent countries. As long as the fragile countries do not regain their budgetary credibility and the vitality of their companies, the use of European debt will remain a pipe dream. Indeed, mutualising debt without correcting the underlying divergences that produced it would merely redistribute risk without eliminating it. Financial solidarity cannot replace structural responsibility. A currency union built on shared liabilities but diverging fundamentals would become more fragile, not more stable.

But more fundamentally, the problem with European debt is that of responsibility. Common debt issued by the EU is supposed to be backed by the European budget. However, the EU doesn’t have the tools at its disposal to unilaterally increase its resources to repay its debt. It is required to negotiate – or rather plead – with Member States in order for them to increase their contributions. Considering the current political climate and growing euroscepticism, does it appear realistic for Member States to agree to an increase in their contributions?

So far, no one has raised the issue of debt servicing at the EU level, and the can has once-more been kicked down the road. The problem is not about being able to borrow more: it is about encouraging initiative, risk-taking, and finding new projects that companies made more competitive are capable of carrying out. In other terms, Europe doesn't lack the **financing**, it lacks the **projects**. Before even considering financing, one should first figure out what they should invest **in**. The problem is exacerbated by the fact that, as a result of globalisation, companies in countries such as France have tended to invest directly abroad (FDI) rather than simply exporting, as German companies did.

2.3 Inflation and excessive monetary creation cannot solve the problem of excessive debt

Yet "magic European money" doesn't only refer to common debt issuance, but also to liquidity injection by the European Central Bank. Contrary to what many European leaders seem to believe, the ECB will not always be there to save the day. Neither monetary creation nor inflation can serve as a sustainable exit from excessive debt. The past decade has shown that prolonged expansionary monetary policy, while necessary in moments of acute crisis, carries long-term distortions. Persistently low interest rates compress risk premia, inflate non-productive asset values and encourage the financialisation of the economy. When liquidity becomes abundant and capital inexpensive, savings flow disproportionately toward non-productive assets (real estate, ...) rather than toward industrial modernisation or technological innovation. Asset price appreciation may create the illusion of wealth, but it does not expand the productive frontier.

In reality debt monetisation is neither a credible nor a durable solution. It causes inflation and risks eroding institutional credibility and deepening the disconnect between financial valuations and real economic performance. Europe cannot rely indefinitely on central bank balance sheets to compensate for structural weaknesses. Monetary policy cannot substitute for productivity growth.

2.4 A leap towards federalisation is still an illusion

There is currently amongst some European leaders a discourse of further federalisation to solve the economic and budgetary issues face by Member States. They are sorely mistaken. Federalisation is not a solution. Europe's vitality lies in the success

of its individual components. Those who advocate for an all-mighty paternalistic European state to save overindebted countries from their own folly pay too little attention to the moral imperative for overindebted countries to commit to measures that they themselves agreed to.

In any case, one can't have one's cake and eat it as well. Often, those who advocate for further federalisation don't fully understand – whether by short sightedness or wilful ignorance – what it entails. Indeed, a federal Europe would require the transition to a single state of all matters economic, financial, military or diplomatic. In other terms, a relinquishment of even more sovereignty. Are Member States willing to accept for their own dissolution? Can one seriously argue that European citizens, in the current political climate, are supportive of further federalisation?

Because, neither the states nor the citizens want it. Europe was not built on federalism after the second world war, but rather on a logic of compromise and cooperation and a careful balancing of diverging interests.

Federalisation would require such a fundamental shift in paradigm amongst the citizens and political elites that any such suggestion can't be taken seriously.

The only solution is therefore for structurally weaker countries to take the necessary reforms in order to ensure the convergence that the Euro was set out to do. Europe is not a country, but a coalition of states that identify and act upon shared interests.

3. The Conditions for Renewal: work more and invest more

A strong Europe cannot emerge from weak Member States. A chain is only as strong as its weakest link. Something as simple as a return to fiscal discipline would on its own allow for significant advances in terms of cooperation and integrations (Single Market, Innovation cooperation, industrial policy).

3.1 Internal consolidation is a sine qua non condition for further European integration

The quotation by Raymond Aron perfectly summarises the situation at hand: "Internal consolidation is a prerequisite for international consolidation"⁶. Indeed, a chain is only as strong as

6. R. Aron, "L'Unité économique de l'Europe, La Revue Libre, October 1952.

its weakest link. National problems require national solutions.

The first course of action is for over indebted countries to restore fiscal credibility. Member States must aim to achieve durable primary budget surpluses, not through indiscriminate tax increases, but by rationalising current expenditure and improving the efficiency of public spending. It has been shown time and time again that the most indebted states are also the least productive ones. Sustainable public finances are not an ideological objective; they are a prerequisite for sovereignty within a monetary union. Without fiscal buffers, governments lose room for manoeuvre precisely when shocks occur.

Portugal is a perfect example. The case of Portugal shows that a healthy economy goes hand in hand with sound public finances. After receiving financial assistance following the sovereign debt crisis, Portugal undertook ambitious reforms. These measures have allowed the Portuguese economy to recover become one of the best performers in the Euro area in terms of growth, productivity, competitiveness and fiscal consolidation. Despite persistent structural weaknesses such as rigidities in the labour market, complexity and rigidity in the tax system, transparency in the tax system and a lack of human capital, the Portuguese case demonstrates to all indebted countries that a healthy economy depends on sound public finances.

3.2 A fundamental paradigm shift is required: Member States must move away from a demand-based model to an approach based in stimulating productive supply

Europe must return to a growth model driven by productive supply rather than financial stimulus. The objective is not to stimulate demand artificially through permanent fiscal expansion, but to strengthen the economy's capacity to produce. This requires a decisive reorientation toward productive investment: industrial modernisation, digital infrastructure, energy resilience, research, innovation, education and skilled labour. Public policy must create the conditions under which private capital once again finds long-term industrial risk attractive.

In practical terms, this reorientation requires reducing the tax and regulatory burdens on productive sectors and improving returns on savings in order to redirect capital toward long-term investment. This echoes our previous point as this objective cannot be achieved without sound public finances and credible fiscal frameworks, which are essential to restoring investor confidence. Beyond fiscal discipline, structural reforms are

equally necessary, as illustrated by the experience of the United States. Greater labour market flexibility, the facilitation of corporate restructuring, and policies that encourage continuous workforce training all contribute to enhancing productivity and strengthening the economy's adaptive capacity. Together, these measures create an environment in which private investment can thrive and productive supply can sustainably expand.

Europe already possesses many of the structural advantages required to sustain renewed growth. It remains one of the world's largest economic areas, with a skilled workforce, and globally competitive research capacity. Above all, it holds a substantial stock of private savings. The central challenge is therefore not a lack of resources, but the insufficient capacity to mobilise and allocate them efficiently within the Union. With the right financial and regulatory conditions, Europe has the scale to foster globally competitive firms and to generate its own industrial champions.

3.3 A return to fiscal discipline all the parts of the Union will inevitably lead to trust and cooperation amongst Member States

If Member States pursue internal consolidation, shift towards a supply-driven growth model and implement structural reforms at both national and European levels, renewed trust and cooperation will follow as a natural consequence. Furthermore, savings would naturally be directed more towards the private sector and less towards financing public deficits.

Fiscal credibility strengthens confidence between partners. When commitments are honoured and public finances are sustainable, solidarity becomes politically viable rather than contentious. By reducing structural divergences and improving the mobilisation of Europe's savings and industrial capacity, reforms also ease the tensions that have fragmented the Union in recent years.

Trust cannot be proclaimed; it results from responsibility. In a monetary union of sovereign states, discipline and reform are the preconditions for durable cooperation. From economic consolidation can thus emerge a shared strategic vision grounded in competitiveness, resilience and collective autonomy.

3.4 Achieving the full potential of the Single Market, which includes a single market for banking and financial services

Europe must finalise the institutional framework that allows savings to be converted into long-term

investment. Deepening capital markets and strengthening the Banking Union would provide economic agents with better financing and investment opportunities. This would improve the productivity of capital and ensure a more efficient allocation of assets, thereby promoting a better match between savings and investment. Unlike the United States, the Eurozone lacks risk-sharing mechanisms capable of absorbing economic shocks.

Progress on the Banking Union has stalled. To address this impasse, the European Commission should propose a comprehensive legislative package to the Council of Finance Ministers (Ecofin). Based on a detailed analysis of the benefits of a completed Banking Union – and the costs of inaction – this package should include:

- An unconditional and legally binding internal support mechanism for cross-border banking groups. Parent companies would be required to support subsidiaries in distress using internal group funds, as specified in their recovery plans. These plans would include predefined triggers (e.g. if a subsidiary's liquidity ratio falls below X%, the parent company would inject Y billion in liquidity) and would be approved by the European supervisor, ensuring that the parent holds adequate capital.
- A European liquidity backstop for banks under resolution, to be developed in coordination with the ECB. Crucially, Italy must also ratify the revised treaty enabling the European Stability Mechanism (ESM) to act as a safety net for the Single Resolution Fund (SRF), which intervenes when a failing bank exhausts its own resources.
- A European Deposit Insurance Scheme (EDIS), to be implemented if and only if – it is accompanied by the full legal recognition of cross-border banking groups. This would ensure that prudential regulation and supervision are carried out on a consolidated basis, and that capital can circulate freely within banking groups.

In other words, banks will only support a shared European deposit guarantee scheme if they are assured that internal capital mobility within their group will be safeguarded.

EDIS should neither aim at weakening effective national mechanisms such as Institutional Protection Schemes (IPS), nor imposing premature mutualisation of losses. Rather, it would serve as a last-resort safety net, activated only when all prior lines of defence – including IPS – have been exhausted.

This approach ensures that all Member States – including those with robust systems like Germany – can be confident that European solidarity will not come at the expense of their institutional autonomy.

Considering that EU leaders have stated that the Banking Union is vital to financial stability and to the smooth functioning of the Economic and Monetary Union (EMU), adopting this proposal would send a strong political signal. It would mark renewed consensus in favour of deeper financial integration and greater European financial sovereignty.

A Vibrant capital markets requires:

- Capitalists.
- Investment plans and a healthy appetite for risk, one that is rewarded at least as generously in the United States.
- Pension funds capable of investing European savings into companies' equity capital.
- Regulations that are harmonised, simplified and uniformly applied across all Member States.
- European marketplaces that are competitive and therefore large and strong enough to operate in a global scale.

Member States and EU institutions must therefore focus on promoting equity financing and pension funds across all EU countries, supporting the development of securitisation and improving business profitability⁷.

Undertaken at Union level, these reforms would unlock scale effects and network benefits that far exceed the sum of national initiatives. Institutional reform, while necessary, is not sufficient. Europe's economic renewal also requires the recovery of a long-term strategic vision. A monetary union composed of sovereign states cannot function sustainably without a shared understanding of objectives and responsibilities. Strategic clarity – regarding competitiveness, fiscal sustainability, innovation and defence of the Single Market – must replace short-termism and reactive policymaking. Equally important is the restoration of mutual trust between Member States.

Fiscal responsibility, structural reforms and credible enforcement of common rules should not be perceived as externally imposed constraints, but as the foundations of collective resilience. Trust is built when commitments are honoured, when rules are applied consistently and when solidarity is matched by responsibility.

7. Although all these measures are necessary, they will not be enough to achieve a true Savings Investment Union. This would require a European Treasury bond to be created, but this cannot happen until there is a sovereign European state.

4. National Responsibility and Franco-German Convergence

A strategy of renewal must therefore begin at the national level, whether it consists in fixing one's public finances or adjusting one's industrial model.

France has long nurtured elevated ambitions for itself. Under Robert Schuman and Valéry Giscard d'Estaing it conceived of its role as that of a "major middle power" a state capable of shaping Europe and influencing the international order. Within the European project, France historically stood as *primus inter pares* among EU leaders. As one half of the Franco-German partnership, its political vision often helped determine the direction and tempo of integration.

Today, however, this ambition is weakened by structural fragilities. Persistent deficits, rising debt, high fiscal pressure and the erosion of a competitive industrial base have significantly weakened France's credibility and room for manoeuvre. This partly explains why France has struggled to garner momentum on issues such as European strategic autonomy and the choice of many Member States to continuously rely on US military protection.

A strategy of renewal must therefore begin at home. France must restore control over public finances, rationalise spending to ease the tax burden on productive activity, and reorient its economic model toward strengthening industrial supply rather than sustaining short-term demand.

As for Germany, the country is now faced with the necessity of readapting its economic model in response to intensifying Chinese industrial competition and the resurgence of American protectionism. These conjunctural issues are exacerbated by underlying structural weaknesses, namely an aging population and high energy costs. Unfortunately, its current trajectory reveals a predominantly national reflex. The large-scale rearmament effort launched since 2022 has been structured primarily around domestic industrial priorities, with significant spillovers toward American and Israeli defence suppliers, while cooperation with France has remained almost in-existent. Such an approach risks fragmenting rather than consolidating Europe's industrial and strategic base. By privileging national reconstruction over coordinated capability-building, Germany's path forward sidelines the objective of European strategic autonomy and weakens the collective leverage that only integrated action can provide.

5. Five Lessons for a Sustainable Monetary Union

At this juncture, several fundamental lessons emerge – lessons that may appear self-evident, yet are too often overlooked in practice.

First, a monetary union is not a cure-all. It cannot compensate for structural weaknesses, nor can it substitute for sound national governance. Its effectiveness depends entirely on its institutional design and on the commitment of its members to uphold common rules.

Second, sharing a single currency across twenty-one heterogeneous economic systems is, absent discipline and convergence, a recipe for future tensions. Divergent fiscal policies, productivity paths and competitiveness levels inevitably generate structural imbalances if not actively corrected.

Third, this inherent contradiction can only remain sustainable if European institutions – above all the Commission and the Council – enforce a minimum level of collective discipline, particularly in fiscal matters. Rules that are agreed but not applied erode trust and undermine the credibility of the entire architecture.

Fourth, the mere existence of a monetary union will not, in itself, secure Europe's prosperity. The strength of the Union ultimately depends on the strength of its Member States. The more competitive, responsible and reform-oriented the national economies, the more resilient the common currency becomes.

Finally, the sustainability of the euro requires long-term vision, strategic clarity and political will. Without a forward-looking commitment to productivity, innovation and structural reform, financial stability alone will not guarantee lasting prosperity.

Yet this diagnosis should not obscure an equally important reality: the European project retains considerable strengths. The creation of the world's largest single market remains one of the most ambitious economic achievements of the modern era, and the euro has established itself as the world's second reserve currency, reinforcing Europe's monetary sovereignty⁸.

Recent initiatives such as the Important Projects of Common European Interest (IPCEI) further demonstrate that the Union can coordinate strategic industrial action in critical sectors. The euro is not merely a constraint; properly governed, it can be a powerful catalyst for collective ambition.

8. If gold is included in the ranking of reserve assets, the euro ranks third, behind the US dollar and gold.

6. A Decisive Moment for Europe

The euro is not destined to fail. Europe retains immense assets: a highly educated population, deep pools of savings, and strong institutions. What is required is the political will to uphold shared commitments and to address divergences before they escalate into crises. A monetary union can endure only if its members accept the discipline that accompanies solidarity.

The present moment should therefore be understood not as inevitable decline, but as a decisive test. If Europe chooses responsibility, restores fiscal credibility and rebuilds its productive capacity, the euro can regain resilience and legitimacy. If divergences continue to widen and savings remain misallocated, the next shock could expose structural weaknesses that have long been masked by monetary accommodation.

A complete change in paradigm is required. Internal consolidation is required before Member States can even aspire to enhanced European cooperation and integration.

The fate of the euro ultimately depends not only on rules and institutions, but on Europe's capacity to transform its abundant savings into innovation, productivity and growth. Stability cannot rest indefinitely on central bank intervention alone. It must be grounded in disciplined governance, renewed competitiveness and a long-term strategic vision for productive investment.

In order to reach said goals, it is imperative that we demonstrate to national leaders and citizens that the benefits of collective action significantly outweigh the costs of compromise that European projects may require at the national level. Too often, ambitions are ascribed to the European Union that simply don't exist. Neither the euro nor the Union itself is the cause of Member States' economic difficulties. The EU cannot continue to serve as the scapegoat for domestic policy failures or poor national decisions.

NGEU: a game changer for the European Union?¹

Note written by Didier Cahen

Executive summary

On the 21st of July 2020, in response to the unprecedented Covid-19 crisis that took the world by surprise, the Council of the EU agreed upon a massive and unprecedented recovery plan: Next Generation EU. The plan aimed at kick-starting the European economy and supporting the energy and digital transitions in order to make the EU more resilient to future crises. The announcement of this program also aimed at reassuring markets about the EU's stability and strength, through a show of solidarity among Member States².

NGEU comprises a combination of loans (**€385 bn**) and grants (**€217 bn**) which Member States can call upon to finance national projects. The fund came into effect in February 2021 and is set to end in August 2026³. It cannot be understated how revolutionary NGEU was for its time due to being the first EU program financed by common debt issuance. Many political commentators have called it the EU's Hamiltonian moment.

Currently, despite being an initiative grounded in a qualitative and performance-based approach, NGEU remains significantly underutilized compared to its ambition. Its implementation has proven slower and more complex than expected, reflecting heavy administrative procedures and absorption constraints in several Member States.

At first glance, NGEU appeared to have a positive effect on several Southern European countries such as Spain, Italy and Portugal where investment levels increased compared to the pre-pandemic period. However, these additional capital flows have not yet generated measurable improvements in labour productivity. Productivity growth has slowed in Spain relative to the pre-Covid-19 phase and has even contracted in Italy as of the end of 2025. These issues raise the question of NGEU's efficacy. So far, NGEU has been slow to generate the

productivity gains that were hoped for at its inception. This both suggests critically inefficient resource allocation and a structurally slow disbursement issue.

Although NGEU has successfully secured market access for its financing, the sharp rise in interest rates since 2022 has fundamentally altered its long-term budgetary implications. **Annual interest and principal repayments are projected at around €24 billion from 2028**, or approximately **15% of the EU budget**, thereby transforming a temporary recovery tool into a **permanent** and politically salient expenditure item for the EU's next Multiannual Financial Framework (2027 onwards). This shift redirects the debate from **borrowing capacity to growth effectiveness** and fiscal sustainability: while investment has increased in several Member States, productivity gains remain **uneven**, raising uncertainty about whether NGEU will generate sufficient long-term growth dividends to ensure its repayment.

The grant component of NGEU also entails a specific repayment mechanism with important distributive implications. Unlike loans, which are repaid by beneficiary Member States, grants are financed through common EU borrowing and repaid collectively via the EU budget. Repayments are therefore allocated according to each Member State's contribution to the EU budget which is largely based on Gross National Income (GNI), rather than according to the amounts received. This implies that some countries will ultimately be net contributors to the repayment of NGEU grants, while others will remain net beneficiaries, reinforcing the redistributive dimension of the programme and potentially intensifying political sensitivities during the repayment phase. As of 2025, Portugal, Italy, Greece and Spain were the recipients of 78% of available funds whilst contributing to only 28% of GDP⁴.

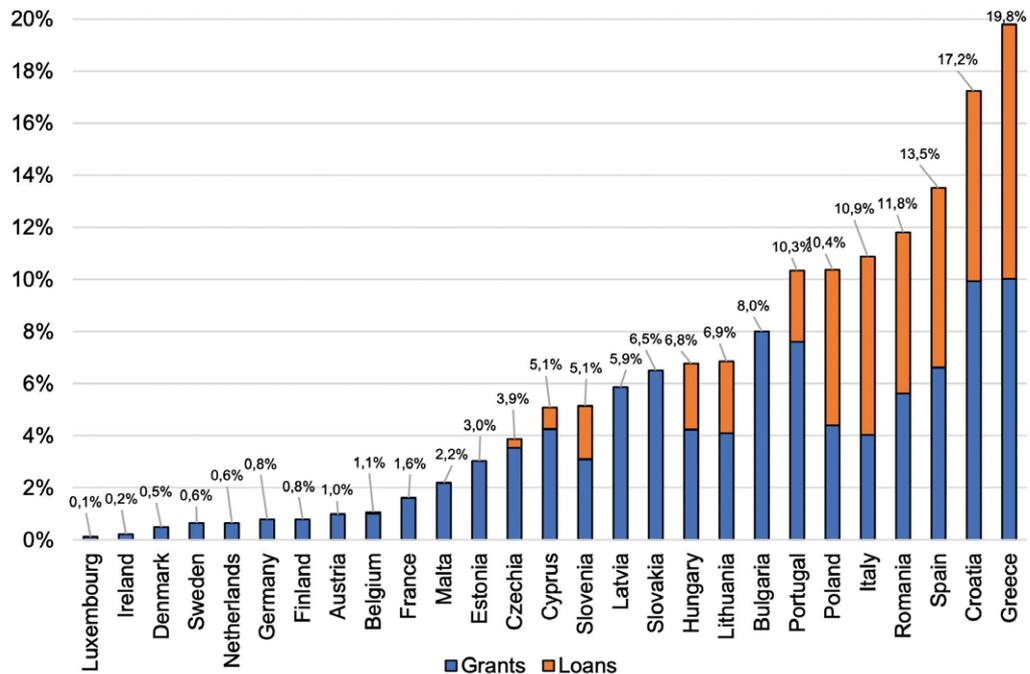
1. The author would like to thank Azra Ersevik (Master's student, Sciences Po Paris and Université Paris Nanterre) and Kiann Conlon (Master's student, HEC & Sciences Po) for their valuable contribution to this chapter.

2. European Commission, Europe's moment: Repair and Prepare for the Next Generation, Press Release IP/20/940, 27 May 2020, available at: https://ec.europa.eu/commission/presscorner/api/files/document/print/en/ip_20_940/IP_20_940_EN.pdf?utm_source=chatgpt.com

3. European Commission, "the EU as an issuer – the NextGenerationEU transformation", EU budget policy brief, July 2022.

4. Storbeck et al., Financial Times, Reversal of fortunes: Europe's thriving south and stagnant north, 14/01/2025.

CHART 1.
RRF funding (loans and grants) to be received by EU Member States, % of GDP



Source: EU Commission, NGEU tracker

The collective repayment of the programs' grant component will only further intensify distributive tensions, particularly in the absence of robust new own resources. Essentially, NGEU exposes the **limits of debt mutualisation without deeper fiscal federalisation**. Designed as an exceptional crisis response rather than a permanent fiscal instrument, NGEU now faces a decisive post-2028 stress test in which its sustainability will depend less on continued market confidence than on Member States' willingness to sustain durable fiscal commitments and on the Union's capacity to deliver visible economic convergence that can anchor the political economy of common debt over time.

5.1 NGEU: An Unprecedented €800 bn joint EU Response to Covid-19 supporting Green and Digital transitions

NGEU builds on earlier EU crisis-response instruments and embeds the post-pandemic recovery within the Union's longer-term objectives of climate neutrality and strategic autonomy, notably through its alignment with the European Green Deal and the Fit for 55 package.

Whilst NGEU is comprised of multiple investment vehicles totalling over €800bn, **the centrepiece of NGEU is the Recovery and Resilience Facility (RRF)**. The RRF represents €577 bn (5.2% of EU-27 GDP) (2019) and aims to finance the green and digital transitions: at least 37% of the RRF is dedicated to climate-related expenditure, with another 20% to support digitalisation.

Beyond the RRF, NGEU also includes REPowerEU. This fund was introduced in October 2022 in response to the energy shock induced by Russia's invasion of Ukraine. REPowerEU focuses on energy savings, renewable deployment and supply diversification.

Considering the extraordinary nature of NGEU and the politically sensitive ramifications of common debt issuance, a strong emphasis was placed on transparency and efficacy of funds. That is why NGEU funds such as the RRF operate as performance-based instruments: disbursements were conditional on the satisfactory fulfilment of predefined milestones and targets embedded in national recovery and resilience plans rather than on individual projects' eligibility. Grant allocations also reflect factors such as population size, GDP per capita and average unemployment rates. To safeguard the integrity of the framework, the Commission had the power to suspend or interrupt payments in case of deficiencies and apply ex post financial corrections when failures are identified.

5.2 NGEU financed by common debt: the largest EU bond-funded programme to date

NGEU is financed primarily through common debt, marking an unprecedented step in EU budgetary history. For the first time, large-scale common borrowing and a degree of risk-sharing have become central features of an EU spending programme. To fund NGEU, the European Commission issued debt through a diversified strategy combining short and

long-term instruments. These include EU-Bills and EU-Bonds across a wide range of maturities, as well as a significant share of green bonds.

Since the launch of SURE and NGEU, EU bond issuance has expanded rapidly. Outstanding EU debt rose from less than €50 billion before the pandemic to around €580 billion by the end of 2024 and approximately €695 billion by mid-2025⁵. By the end of NGEU, total issuance is expected to reach between €800 billion and €950 billion, placing the EU among the largest issuers in euro-denominated bond markets⁶. Despite the sharp rise in interest rates since 2022, EU bond issuance has proceeded smoothly, with continued strong investor demand across maturities. Green bonds play a central role in the NGEU funding strategy.

The EU plans to finance up to 30% of NGEU, around €240 billion, through green bonds dedicated to eligible climate-related expenditure, including clean energy, energy efficiency and sustainable transport. By early 2025, around €70 billion of NGEU green bonds had been issued. This strategy has positioned the EU as the world's largest green bond issuer and a major player in the euro-denominated debt market.

The debt raised by the EU Commission to fund NGEU is backed by the European Union's general budget⁷. This means that the European Commission is responsible for repaying the bonds using EU budget resources. In practice, if the Commission were unable to repay its debts from its usual budget revenue, it could request that Member States cover the shortfall up to the budget ceiling.

To reinforce this guarantee provided by the EU budget, the ceiling on the EU's own resources (the maximum amount that the Commission can request from Member States) has been temporarily increased by 0.6% of the EU's GNI, in addition to the permanent ceiling of 1.4%. This additional margin ensures that the EU can always meet its repayment obligations, whatever the circumstances.

Therefore, the Member States indirectly guarantee the debt through their commitment to contributing to the EU budget within the framework of the own resources ceiling.

In other words, net contributors to the EU budget are surreptitiously financing structurally weak countries most affected by the Covid-19 crisis (Italy, Spain) *i.e.* in a manner hidden from public scrutiny.

5.3 NGEU Current disbursement and key data of NGEU: an overview in numbers

By the end of January 2026, all 27 National Recovery and Resilience Plans (NRRPs) had been approved by the European Commission and formally adopted by the EU Council. All Member States also submitted amendments to their plans, primarily to integrate REPowerEU chapters aimed at strengthening energy security and addressing implementation bottlenecks in the final phase of the programme.

The total envelope of the Recovery and Resilience Facility (RRF) currently stands at €577 billion, reflecting both initial allocations and subsequent revisions. The envelope comprises €360 billion in grants and €217 billion in loans. The grant is funded by €338 billion coming from the original RRF allocation, complemented by €20 billion stemming from the auctioning of allowances under the Emissions Trading System (ETS) and €2 billion from the Brexit Adjustment Reserve (BAR)⁸.

As of today, cumulative disbursements amount to approximately €394 billion, including €238 billion in grants and €156 billion in loans. This amounts to around two-thirds of the overall RRF envelope.

TABLE 1.
RRF financial envelope and cumulative disbursements (January 2026)

	Total RRF	RRF Grants	RRF Loans
Available (EUR bn)	577	360	317
Disbursed (EUR bn)	394	237.53	155.88
Percentage disbursed	68%	66%	54%

Source: EU Commission

Notes: amounts are expressed in 2026 prices. The €360 billion in ent Reserve grants is split in €338 billion of original RRF grants, €20 billion in ETS grants and €2 billion in BAR (Brexit Adjustmts). The loan envelope reflects revisions recorded by end-January 2026, following the decommitment of approximately €74 billion in loans by several Member States

These data describe the situation as of January 2026, while the legal deadline for the completion of RRF-funded reforms and investments is set for August 2026. The programme is therefore in its final implementation phase, with a significant share of approved investments still to be executed over a compressed timeframe. This points to substantial progress in the mobilisation of NGEU resources, but they provide only a partial picture of the programme's effective economic transmission.

5. S&P Global Ratings. RatingsDirect: European Union and European Atomic Energy Community. Rapport, 30 juin 2025. PDF. Commission européenne (Luxembourg/Strasbourg). https://commission.europa.eu/system/files/2025-07/RatingsDirect_EuropeanUnionandEuropeanAtomicEnergyCommunity_3398360_Jun-30-2025.pdf

6. European American Chamber of Commerce (EACC), "European Commission to issue €90 billion in long-term EU-Bonds in the first half of 2025", 11 décembre 2024, communiqué, <https://eaccn.eu/european-commission-to-issue-e90-billion-in-long-term-eu-bonds-in-the-first-half-of-2025/>

7. Germany is the largest contributor to the EU budget (~22.5%), followed by France (~18.3%) and Italy (~12.9%).

8. European Commission, The Recovery and Resilience Facility : https://commission.europa.eu/business-economy-euro/economic-recovery/recovery-and-resilience-facility_en

Disbursement ratios reflect the formal fulfilment of milestones and targets, but do not necessarily capture the pace, balance or quality of on-the-ground execution. In several Member States, payments have advanced faster than project implementation, with effective expenditure remaining backloaded as the deadline approaches.

Execution and absorption constraints: the binding limitation of NGEU.

Despite its innovative, performance-based design, the implementation of NextGenerationEU has proven slower and more complex than initially anticipated. Administrative bottlenecks, heavy documentation requirements and delays in the assessment of payment requests have constrained execution across Member States. The coexistence of the RRF with other EU instruments, notably REPowerEU and traditional cohesion funds, has further increased the procedural complexity and strained administrative capacities, particularly at regional and municipal level. In other terms, the fragmentation of NGEU into different funds appears to seriously inhibit its efficacy and flexibility due to the additional administrative burdens.

As the August 2026 deadline approaches, implementation risks have intensified. Inflationary pressures and changing economic conditions have forced some projects to be rescaled or revised, while political transitions have led to renegotiations of national plans. Unlike previous EU programmes, NGEU requires near-complete absorption within a compressed timeframe of five and a half years, amplifying long-standing weaknesses in project preparation, coordination and administrative execution.

In practice, disbursements primarily reflect formal progress against milestones and targets, rather than effective expenditure or economic impact. Information on actual costs, implementation speed and efficiency remains limited, making it difficult to assess the real macroeconomic transmission of NGEU-funded investment. This gap between financial flows and on-the-ground execution indicates that the binding constraint of NGEU has shifted from financing capacity to execution capacity.

Beyond execution constraints, recent developments also highlight limits to EU common borrowing on the demand side. As EU borrowing conditions degraded over 2023–2025, several Member States chose not to draw on the loan component of NGEU. By early 2026, around €74 billion in recovery loans had been forgone⁹. As sovereign spreads narrowed

relative to the Commission's funding costs, the marginal financial advantage of EU loans diminished, while administrative complexity and tight spending deadlines remained unchanged.

Taken together, these elements confirm that NGEU's effectiveness now hinges less on the availability of resources than on Member States' ability to convert approved allocations into timely, high-quality investment and reforms. They also contribute to increasingly differentiated implementation trajectories and macroeconomic outcomes across countries.

5.4 Italy and Spain are the main recipients of the RRF

Italy and Spain together account for the largest share of RRF resources and therefore provide a relevant benchmark for assessing how differences in national execution conditions shape the macroeconomic transmission of NGEU.

By the end of NGEU's lifecycle, Spain is set to receive €163 billion (€79.8 billion in grants and €83.2 billion in loans) : 13.5% of its GDP and 28.9% of RRF. As of January 2026, Spain had already received €55.1 billion in RRF grants, representing approximately 69 % of its total grant allocation (€79.8 billion). These numbers highlight the sheer scale of RRF support to the Spanish economy.

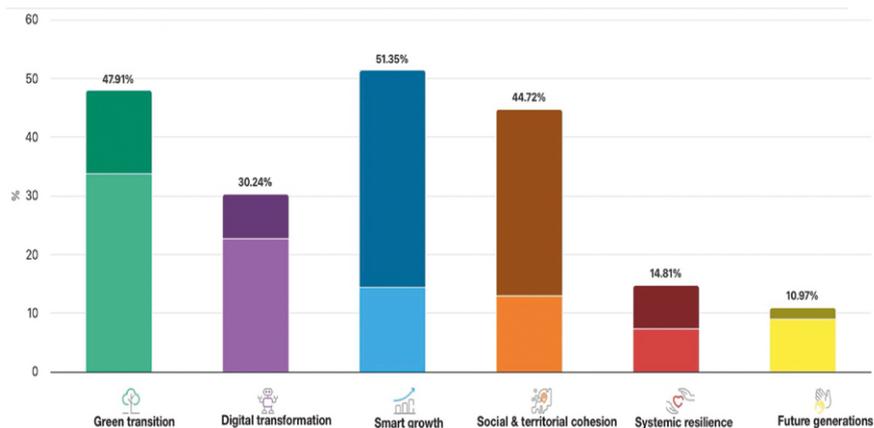
In terms of planned expenditure, Spain's RRF remains strongly aligned with the RRF's strategic priorities. Measures tagged under "smart, sustainable and inclusive growth" account for the largest share (74,48%), alongside substantial allocations to the green transition (48,25%) and digital transformation (22%). As reforms and investments are systematically tagged under both primary and secondary policy objectives, cumulative shares exceed 200%, reflecting the cross-cutting nature of the plan. Actual disbursements display a different timing. By the beginning of 2026, payments remained concentrated in growth and cohesion related pillars (€20.19 billion and €12.8 billion respectively), while green (€13.10 billion) and digital (€7.52 billion) disbursements lagged behind their programmed shares. This pattern reflects a sequencing effect rather than a misalignment with RRF objectives, as climate and digital intensive investments typically involve longer planning and implementation cycles.

Overall, Spain combines a strong formal compliance with RRF priorities and a relatively high absorption with a more gradual rollout of green and digital

9. Paola Tamma and Barney Jopson, "EU states spurn €74bn in unused Covid recovery loans", Financial Times, <https://www.ft.com/content/92168da8-f822-4b3b-adc5-3f0f6b45987a>

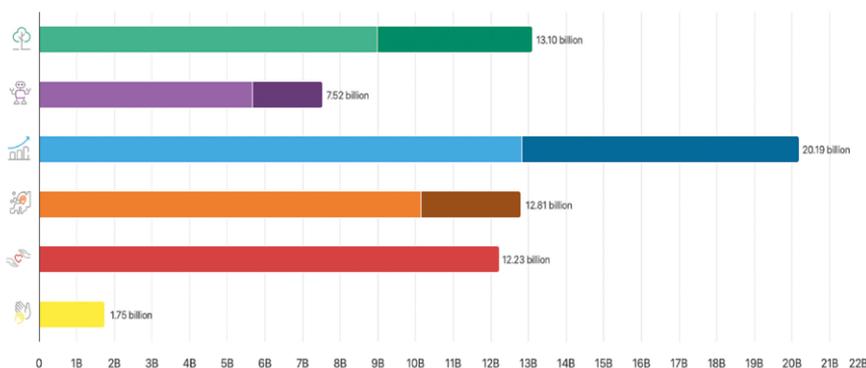
CHART 2.
Spain's RRP expenditures

Chart 2a : Share of the plan's estimated expenditure contributing to each policy pillar



This graph displays the share of the recovery and resilience plan's estimated contribution to each policy pillar. As each measure contributes towards two policy areas of the six pillars (primary and secondary assignments), the total contribution to all pillars displayed in the graph amounts to 200% of the RRF funds to the Member State.

Chart 2b : Disbursements per pillar



08 May 2024: The data in the 'Disbursements per pillar' graph was revised due to a technical issue. Each disbursement reflects progress in the implementation of the RRF, across the six policy pillars. This graph displays how disbursements under the RRF relate to the pillars. The amounts were calculated by linking the milestones and targets covered by a given disbursement to the pillar tagging (primary and secondary) of their respective measures. Over time, the pre-financing that Member States have received is offset with each payment that is disbursed. Therefore, the amounts per pillar in the above graph reflect the gross payments, i.e., the actual disbursements under each instalment together with the corresponding shares of pre-financing that has been cleared, i.e., set off with each paid amount. The amounts are updated after each payment.

Source: European Commission

spending. While this has had limited the immediate macroeconomic impact, available evidence suggests a credible and progressive transmission of NGEU-financed investment, conditional on timely completion of remaining projects ahead of the 2026 deadline.

Italy is the largest beneficiary of the RRF, with a total allocation of €194.4 billion, or 10.9% of its GDP and 26.1% of RRF. By the beginning of 2026, Italy had received €54.1 billion in grants and €99.1 billion in loans, bringing total disbursements to around €153 billion. This represents around

79% of its total allocation and roughly 7% of Italy's nominal GDP in 2025 (based on IMF estimates of \$2.39 trillion).¹⁰

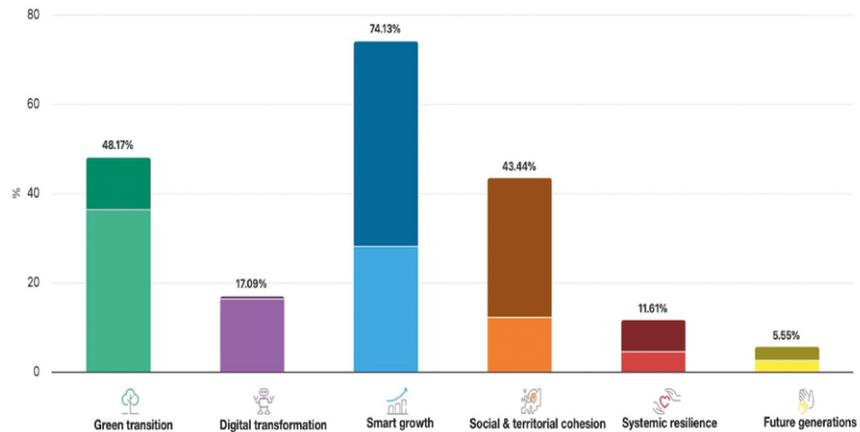
However, effective spending remained significantly lower, at around €86 billion. This amounts to approximately 44% of Italy's total RRF allocation (€86 bn / €194.4 bn ≈ 44.2%), or roughly 56% of the funds already disbursed (€86 bn / €153 bn ≈ 56%), highlighting a **persistent gap between formal disbursements and effective on-the-ground execution.**¹¹

10. IMF, World Economic Outlook Database, April 2024 edition, variable NGDPD (Nominal GDP, current prices), Italy, 2025 projection. url.me/gMQZ3V

11. European Parliamentary Research Service. China's Belt and Road Initiative – A Human Rights Assessment. EPRS Briefing 2021/698847, European Parliamentary Research Service, European Parliament, July 2025. [https://www.europarl.europa.eu/RegData/etudes/BRIE/2021/698847/EPRS_BRI\(2021\)698847_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/BRIE/2021/698847/EPRS_BRI(2021)698847_EN.pdf). https://ec.europa.eu/economy_finance/recovery-and-resilience-scoreboard/country_overview.html?country=Italy

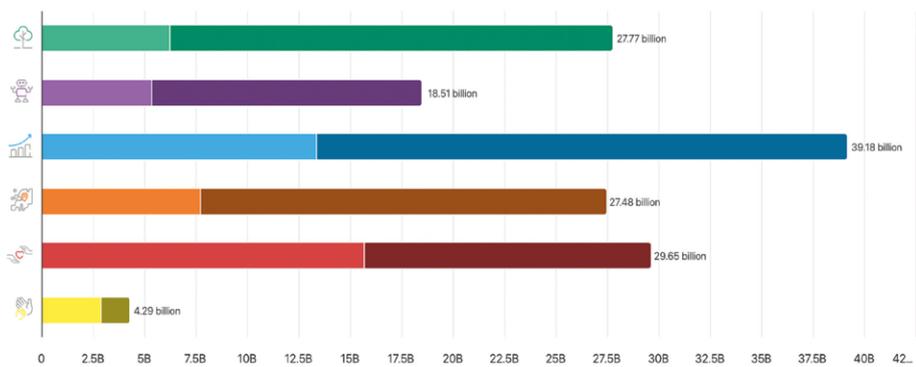
CHART 3.
Italy's RRP expenditures

Chart 3a : Share of the plan's estimated expenditure contributing to each policy pillar



This graph displays the share of the recovery and resilience plan's estimated contribution to each policy pillar. As each measure contributes towards two policy areas of the six pillars (primary and secondary assignments), the total contribution to all pillars displayed in the graph amounts to 200% of the RRF funds to the Member State.

Chart b : Disbursements per pillar



08 May 2024: The data in the 'Disbursements per pillar' graph was revised due to a technical issue. Each disbursement reflects progress in the implementation of the RRF, across the six policy pillars. This graph displays how disbursements under the RRF relate to the pillars. The amounts were calculated by linking the milestones and targets covered by a given disbursement to the pillar tagging (primary and secondary) of their respective measures. Over time, the pre-financing that Member States have received is offset with each payment that is disbursed. Therefore, the amounts per pillar in the above graph reflect the gross payments, i.e., the actual disbursements under each instalment together with the corresponding shares of pre-financing that has been cleared, i.e., set off with each paid amount. The amounts are updated after each payment.

Source: European Commission

While Italy's NRRP is formally aligned with RRF climate and digital objectives, 47.9% of planned expenditure tagged to climate objectives and 30.2% to digital transformation when accounting for primary and secondary policy tagging, actual disbursements remain skewed toward other pillars. As of early 2026, payments were concentrated in "smart, sustainable and inclusive growth" (€39.2 billion), health and resilience (€29.7 billion) and social and territorial cohesion (€27.5 billion), while the green transition (€27.8 billion) and digital transformation (€18.5 billion) lagged behind their programmed weight.

Although disbursements accelerated in 2025 and further progress is expected ahead of the August

2026 deadline, Italy's NGEU-related growth effects are therefore likely to remain backloaded and contingent on sustained improvements in administrative capacity and project execution.

There are numerous factors that have contributed to these delays. First and foremost, Italy suffers from structural administrative weaknesses. There is a significant lack of public engineering capacity. Moreover, the public procurement procedure has historically been cumbersome. Project monitoring and oversight is lacking. Many investments such as schools, hospitals and local infrastructure rely on a multitude of administrative strata (municipalities, provinces, regions and local public operators).

These issues have led the Italian Court of Auditors and the Bank of Italy to call for stronger administrative capacity and better financial planning. Centro Studi Confindustria has also expressed concern over the effectiveness of the Transition 5.0 measure and the risk of underspending by the deadline¹². There is a silver lining however. The implementation of NGEU had led Italy to undertake numerous reforms, especially in the speed and efficiency of the judicial branch.

5.5 Has NGEU succeeded in accomplishing its objectives?

Before examining country-specific implementation patterns, it is necessary to assess whether the increase in productive investment following the launch of NGEU has led to measurable productivity gains in the Euro area countries that benefited most from it.

The charts above highlight a central paradox in the post-pandemic Euro area recovery. While NGEU has mechanically supported investment in several

Southern European economies, notably Spain, Italy and Portugal, this investment surge has not resulted into measurable gains in labour productivity.

As shown in Chart 4a, annual net corporate investment (excluding the consumption of fixed capital, thus reflecting the flow of new investment) increased markedly in Southern European countries between the pre- and post-Covid-19 periods. In Italy, it turned positive (from -0.2% to 1.2%); in Portugal, it almost doubled (from 2.67% to 4.36% of GDP); and in Spain, it remained high but did not increase further.

However, this increase in investment does not appear to have been accompanied by commensurate productivity gains (see Chart 4b). In Italy, for example, average annual labour productivity growth, which had been flat before the pandemic, turned negative between 2023 and 2025. In Spain, productivity growth slowed from 0.4% between 2014 and 2019 to 0.3% between 2023 and 2025. At the aggregate level of the Euro area, productivity growth weakened from 0.6% to -0.1%.

CHART 4.
Corporate investment and productivity across the EA Member States

Chart 4a : Net corporate investment, % of GDP, average annual during the period

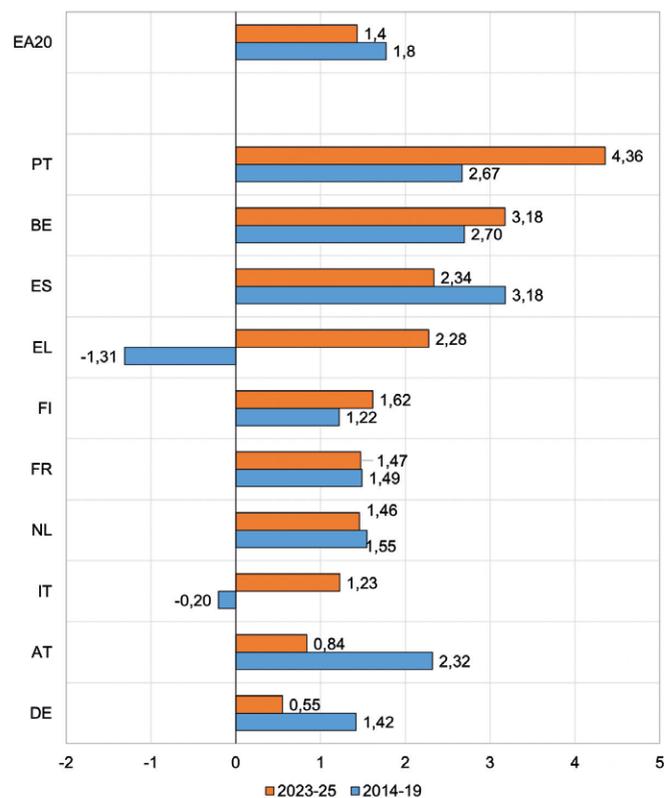
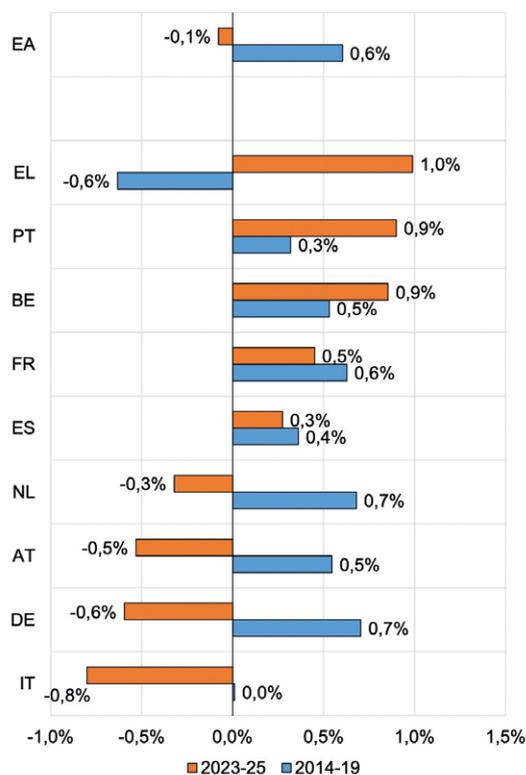


Chart 4b : Labour productivity, average annual change, %



Source: Ekomics, based on data from Eurostat

12. Banca d'Italia. 2025. Economic Bulletin No. 2/2025. Rome: Banca d'Italia. https://www.bancaditalia.it/media/notizia/economic-bulletin-no-2-2025/?com.dotmarketing.htmlpage.language=1&utm_source=c

However, this increase in investment does not appear to have been accompanied by commensurate productivity gains. In Italy, average annual labour productivity growth, which had been flat before Covid-19, turned negative between 2023 and 2025. In Spain, productivity growth slowed, from 0.4% between 2014-19 to 0.3% between 2023-25. At the Euro area aggregate level, productivity growth weakened from 0.6% to -0.1%.

This divergence between capital formation and productivity performance raises questions regarding the composition and efficiency of post-pandemic investment. According to the European Commission's assessment of the RRF, the growth impact of recovery funds depends critically on project selection, administrative capacity and the timely implementation of complementary reforms conditions that influence whether higher investment translates into durable productivity gains¹³.

5.6 Italy has faced implementation constraints with NGEU funds, whilst Spain has used them more efficiently

Spain: a gradual but observable macroeconomic transmission supported by investment additionality

As stated previously, Spain's Recovery and Resilience Plan is one of the largest under the RRF, reflecting both the severity of the pandemic shock and the allocation criteria applied at EU level. By 2026, Spain had absorbed a substantial share of its grant envelope following the fulfilment of milestones and targets, while loan take-up remained more limited and backloaded. Available macroeconomic estimates suggest that the programme is already having measurable effects: simulations by the Observatoire français des conjonctures économiques (OFCE)¹⁴ point to a GDP increase of around 1.2 percentage points over 2021–2031, with peak effects in the mid-2020s, while CaixaBank Research¹⁵ estimates a cumulative impact of 2–3% of GDP by 2026. Firm-level survey evidence analysed by the Banco de España and the Real Instituto Elcano indicates a high degree of additionality, with a large share of supported firms reporting that investments would have either not have occurred or been scaled down without RRF funding.

Spain relied on a relatively centralised governance structure and sequenced reforms and investments aimed at reducing early administrative bottlenecks, prioritising structural reforms before scaling up major investment projects. The European Commission has highlighted the strong climate and digital orientation of the plan, particularly in sustainable transport, renewables and digital public services. Implementation has nevertheless been uneven, with delays in capital-intensive projects and rising absorption risks as the August 2026 deadline approaches. Moreover, Spain's solid post-pandemic growth cannot be attributed to NGEU alone: cyclical factors such as tourism, immigration and favourable energy prices have also played an important role, while longstanding productivity weaknesses and investment gaps may limit the programme's long-term structural impact.

Italy: high nominal disbursements and weak macroeconomic transmission

Italy, in contrast to Spain, illustrates the limits of large scale financing in the absence of adequate execution capacity. Although it is the largest beneficiary of the Recovery and Resilience Facility, the translation of disbursements into effective expenditure has been uneven: by early 2026, roughly €153 billion had been received¹⁶, but only about €86 billion had been spent, leaving a persistent absorption gap. This timing mismatch has also produced temporary macro-fiscal effects, including a return to a small primary surplus in 2024–2025, partly because transfers preceded actual investment outlays.

Macroeconomic projections confirm the limited short-term growth impulse. The European Commission expects GDP growth to remain modest at below 1% in 2025–2026, while public debt is projected to edge up towards 137–138% of GDP¹⁷. Private forecasts by Prometeia¹⁸ similarly suggest that NRRP-related investment will peak only in 2026, implying backloaded macroeconomic effects. Structural bottlenecks such as administrative fragmentation, complex procurement rules and the heavy reliance on tax incentives have limited these productivity spillovers. Although implementation accelerated in 2025, the concentration of spending in the programme's final phase raises risks for both absorption capacity and expenditure quality ahead of the August 2026 deadline.

13. European Commission, Recovery and Resilience Facility Annual Report 2024, Brussels, 10 October 2024, https://reforms-investments.ec.europa.eu/technical-support-instrument-0/publications-0/recovery-and-resilience-facility-annual-report-2024_en

14. OFCE, Quel impact du plan de relance européen NGEU sur la croissance ?, Blog OFCE, 6 January 2025. https://www.ofce.sciences-po.fr/blog2024/fr/2025/20250106_CR/

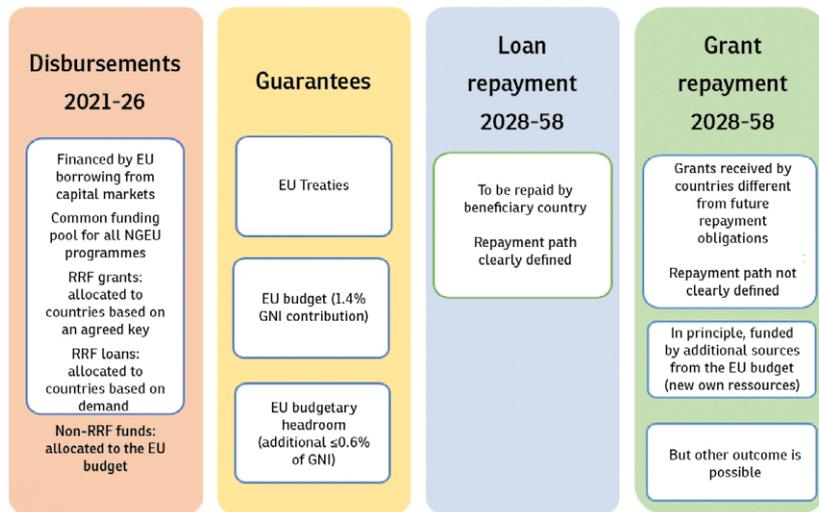
15. CaixaBank Research, How the NGEU funds are going in Spain: bread for today and hope for tomorrow, March 2025.

16. European Parliament Research Service, National Recovery and Resilience Plans: Latest State of Play, February 2025, <https://epthinktank.eu/2022/02/03/national-recovery-and-resilience-plans-latest-state-of-play/>

17. European Commission, Spring 2025 Economic Forecast, country chapter Italy. p.111. https://economy-finance.ec.europa.eu/publications/european-economic-forecast-autumn-2025_en

18. Prometeia, Italy in the Global Economy, February 2026. <https://prometeia.img.musvc3.net/static/7372/documenti/ConsoleDocuments/Prometeia-Brief-2026-2.pdf>

CHART 5.
Key features of EU debt within the NGEU/RRF program



Source: ECB

5.7 The transition of NGEU into its repayment phase

Before examining the implications of the repayment phase, it is important to distinguish between the two components of NGEU financing. Loans granted to Member States are to be repaid directly by the beneficiary countries themselves, in accordance with the terms set by the EU.

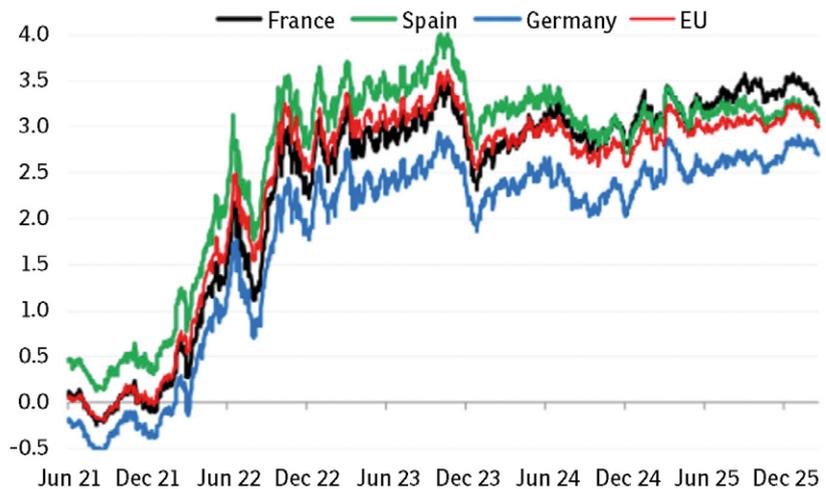
By contrast, the grant component is financed through common EU borrowing and will be repaid collectively via the EU budget, implying a mutualisation of repayment through EU budget revenues (see Section 6.2). All borrowing operations to finance NGEU must be completed by the end of 2026, while repayments of the associated debt are scheduled to extend over several decades, with final maturity no later than 2058.

Rising interest rates and the structural fragility of NGEU's repayment architecture

While market access has not constituted a binding constraint for NextGenerationEU, the financial environment in which EU common debt is being serviced has shifted markedly compared with the assumptions prevailing at the programme's launch in 2020. At that time, borrowing costs were expected to remain close to zero for a prolonged period, allowing the servicing of large-scale common debt to be absorbed gradually within the EU budget. This assumption has proven overly optimistic.

Following the post-2022 tightening of global monetary conditions, yields on EU bonds rose sharply. Although financing conditions eased somewhat in 2025, interest rates remain structurally higher than initially anticipated in 2020-2021, particularly for long-dated issuances financing the grant component of NGEU. This shift materially alters the budgetary implications of common borrowing.

CHART 6.
10-year sovereign bond yields, %



Source: LSEG, Bloomberg, BNP Paribas

From 2028 onwards, the annual debt service linked to the non-repayable (grant) component of NGEU is estimated at around €24 billion per year, combining interest payments and the linear repayment of principal. As reported by *Le Monde* (11 February 2026)¹⁹, this would represent approximately 15% of the EU's annual budget. Far from being marginal, NGEU debt servicing would thus become one of the largest rigid expenditure items in the post-2027 Multiannual Financial Framework.

This projected servicing burden has already entered the political debate. In Berlin, officials have explicitly linked the magnitude of these repayments to concerns about fiscal room for manoeuvre and have argued that additional common borrowing would be difficult to justify in the absence of deeper structural reforms and measurable productivity gains.

The debate therefore shifts from the question of financial capacity to that of **growth effectiveness**. Beyond its immediate budgetary implications, the repayment phase reopens a broader structural issue: whether NGEU has generated sufficient productivity-enhancing transformation to sustain its long-term servicing. Unlike the United States' Inflation Reduction Act, which relies heavily on direct tax credits and incentive-based mechanisms rapidly deployed to firms and households, NGEU operates through nationally designed recovery plans, subject to administrative procedures, milestone verification and intergovernmental coordination. This model has reinforced an intra-state allocation logic and has limited the development of large-scale cross-border industrial projects at the Union level.

As debt servicing begins in 2028, the transition from fiscal expansion to repayment thus occurs in a context where productivity performance remains uneven and structural reforms incomplete. The distributive dimension of common borrowing consequently becomes more salient: the issue is no longer whether the EU can raise funds on capital markets, but whether it can generate sufficient long-term growth dividends to stabilise the political economy of its repayment.

These rising costs interact with a structurally asymmetric repayment architecture. While NGEU loans will be repaid directly by beneficiary Member States according to a clearly defined schedule

extending from 2028 to 2058²⁰, the servicing of the grant component and its associated interest costs will be borne collectively through the EU budget. In the absence of sufficient and predictable new own resources, this implies a sustained reliance on national GNI-based contributions over several decades, intensifying political sensitivities around burden-sharing and fiscal sovereignty²¹.

As Didier Cahen has emphasised, this asymmetry exposes a fundamental fragility of NGEU²². While debt issuance has been successfully mutualised ex ante, repayment remains politically unresolved ex post. Common borrowing postpones, rather than eliminates, the distributive question of who ultimately pays. This tension becomes more salient in a macroeconomic environment characterised by moderating growth dynamics and persistent structural weaknesses across several Member States. As previously shown, the expected productivity dividends of NGEU-funded investment remain uncertain and uneven, raising the question of whether the programme will generate sufficient long-term growth to ease its own servicing burden. Once debt servicing becomes a permanent and visible budgetary obligation, solidarity risks weakening, particularly in a context of competing spending priorities and tighter national fiscal constraints.

In this sense, NGEU illustrates the limits of debt mutualisation without fiscal federalisation: the EU has acquired the capacity to borrow at scale, but not the autonomous fiscal resources required to stabilise this borrowing over time in a context where member states are **unwilling – or unable – to increase their contribution to the EU budget**. This does not even take into account the fact that the national public opinion of Member States are generally not ready to relinquish national fiscal sovereignty.

This institutional fragility is compounded by adverse financial dynamics. As Didier Borowski²³ observes, post-pandemic debt servicing costs are significantly higher than initial projections due to the rise in interest rates since 2022, posing a structural challenge for the European Commission's budgetary planning. With principal repayments scheduled from 2028 onwards, servicing the grant component of NGEU debt will absorb a substantial share of the EU budget in the medium term,

19. *Le Monde*, "L'Allemagne et la France affichent désormais leurs désaccords sur les propositions défendues par Macron", 11 February 2026, https://www.lemonde.fr/international/article/2026/02/11/l-allemande-et-la-france-affichent-desormais-leurs-desaccords-sur-les-propositions-defendues-par-macron_6666298_3210.html

20. European Parliamentary Research Service (EPRS), *Future of EU long-term financing – post-2027 needs and how to finance them*, February 2025, https://www.europarl.europa.eu/RegData/etudes/BRIE/2025/767242/EPRS_BRI%282025%29767242_EN.pdf?utm_source=

21. Bob Lyddon, "EU Shadow Debts Start to Become All Too Real", Institute for Research in Economic and Fiscal Issues (IREF Europe), September 10, 2025, <https://en.irefeurope.org/publications/online-articles/article/eu-shadow-debts-start-to-become-all-too-real>

22. Didier Cahen, *The Euro Is in Danger*, Éditions Odile Jacob, 2025, pp. 206–207 and pp. 247 ff.

23. "Remboursement de la dette NGEU : un défi pour la nouvelle Commission européenne". *Option Finance*, <https://www.optionfinance.fr/analyses/remboursement-de-la-dette-ngeu-un-defi-pour-la-nouvelle-commission-europeenne.html>

underlining the importance of introducing and ratifying new own resources to cover these long-term liabilities.

The post-2028 phase therefore represents a decisive stress test. NGEU will cease to function as a recovery instrument and will instead become a conventional debt item embedded in the EU budget. Whether this transition can be managed without eroding political cohesion will depend less on market confidence, which has so far held, than on Member States' willingness to accept durable fiscal commitments at EU level. The sustainability of EU common debt thus hinges not on its issuance, but on the credibility of its long-term repayment framework.

NGEU: an exceptional instrument exposing the structural limits of EU fiscal governance

NextGenerationEU was conceived as an exceptional response to an exceptional crisis, rather than as a blueprint for a permanent transformation of EU fiscal policy. Its legal and budgetary architecture reflects this logic. NGEU was designed as a temporary top-up to the 2021–2027 Multiannual Financial Framework and integrated into the EU budget through external assigned revenues rather than ordinary budgetary channels²⁴. This construction preserved the formal constraints of the EU's fiscal framework while allowing for a one-off expansion of spending capacity.

While this exceptional design enabled a rapid and sizeable response to the pandemic, it also revealed important governance and integration limits. Implementation under the Recovery and Resilience Facility has largely followed a national logic, with EU objectives operationalised through country-specific plans. Monitoring mechanisms have focused primarily on compliance with milestones and targets, privileging inputs and outputs over longer-term outcomes. As a result, assessing the true structural impact of NGEU-funded spending remains difficult, and the visibility of its European added value has been diluted.

The institutional balance underpinning NGEU has further accentuated these tensions. Executive authority has been reinforced, particularly within the European Commission, while parliamentary involvement in defining priorities and exercising democratic oversight has remained limited. The growing complexity of fund management, combined with overlaps between NGEU and traditional EU instruments, has strained existing control and audit frameworks.

Beyond governance issues, the exceptional design of NGEU also carries long-term budgetary

implications. Although conceived as a temporary crisis instrument, the servicing of common debt from 2028 onwards will structurally constrain the EU budget, reinforcing the tension between emergency-driven solidarity and the absence of a permanent fiscal framework.

To conclude, it is worth highlighting several important points:

From 2028 onwards, the programme will cease to operate as a recovery instrument and will instead become a structural commitment embedded in the EU's budgetary framework. Debt servicing will become a visible and politically salient expenditure item, intensifying trade-offs between traditional EU policies, emerging strategic priorities and fiscal discipline within a constrained Multiannual Financial Framework.

This transition will test the political sustainability of common borrowing. As debt repayments become permanent, the focus shifts from mobilisation capacity to growth effectiveness and fiscal credibility. The sustainability of NGEU will depend not only on market conditions, but on the Union's ability to generate durable economic returns and secure stable resources capable of anchoring long-term repayment.

At the same time, NGEU's macroeconomic impact has proven uneven and more backloaded than initially anticipated. Administrative bottlenecks, limited sub-national capacity and long implementation cycles for capital-intensive green and digital projects have slowed delivery in several Member States. The comparison with the United States' Inflation Reduction Act highlights differences in implementation speed and incentive design. Whereas the IRA relies heavily on direct, tangible and rapidly deployable tax incentives, NGEU operates through nationally mediated plans, often subject to procedural complexity and fragmented execution.

The issue is therefore not primarily one of financial scale, but of transmission and coordination. If common borrowing is to remain politically viable, it must be associated with visible convergence effects across Member States. The sustainability of shared fiscal commitments ultimately depends on economic convergence: the more growth paths and productivity performances align, the more stable the political economy of common debt becomes. Absent such convergence, distributive tensions may resurface as solidarity shifts from expansion to repayment.

24. European Parliamentary Research Service (EPRS), Future of EU long-term financing – post-2027 needs and how to finance them, February 2025. https://www.europarl.europa.eu/RegData/etudes/BRIE/2025/767242/EPRS_BRI%282025%29767242_EN.pdf

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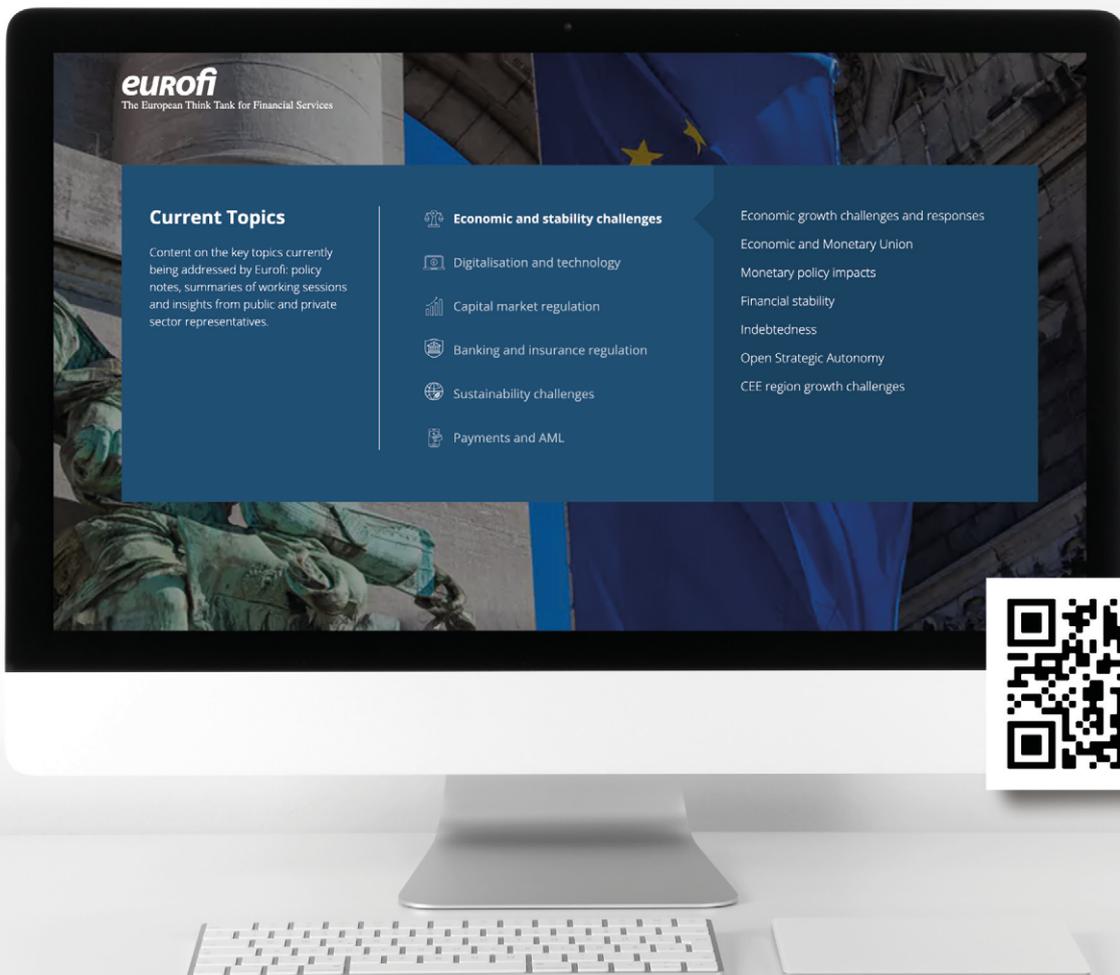
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