PLATAFORMA PYMES
Por un Capitalismo Inclusivo

Executive Summary

Proposal of the Plataforma Pymes to sign a State Pact before the concurrence to the financial assistance (bail-out/rescue) with conditionality in the framework of a new Inclusive Capitalism

Madrid, 15 May 2020.

The **Plataforma Pymes** has been supporting the convenience of forming a great State Pact, similar to those agreed in 1977 (Moncloa Pacts), in 1959 (Stability Plan) or in the period 2010-2012. In all cases, these agreements occurred at critical moments for the Spanish economy that required a "bailout" through the advice of international economic organizations, including the International Monetary Fund (IMF).

Similarly, the Covid-19 crisis will require an imminent rescue, based on the mechanisms articulated by the European Commission, the European Central Bank (ECB) - including the OMT program created in 2012 and not yet used by any Euro Zone country the IMF and the Eurogroup. The aim is to address the extraordinary public spending caused by economic paralysis.

The New State Pact must configure once the **conditional terms of the planned rescue** have been established. Presumably the rescue mechanism will require, for its concession, the acceptance of a qualified majority by the Kingdom of Spain.

In this sense, it would have been desirable that Spain, as a Member State of the EU, had reached at least a principle of political, social and economic agreement, before its participation in the last European Council on 23 April, in which the instruments of economic and financial support agreed in the last Eurogroup were approved, whose access it will be possible next 1 June.

The new Congress Commission for Social and Economic Reconstruction (CRSE in its spanish acronim) after the Covid-19, could be the appropriate instrument for the birth of the State Pact, at least in its most immediate aspects. The urgency of the deadlines requires urgent action.

The agreement reached in this Commission should constitute the framework for the Stability Programme and National Reform Plan 2020, already submitted by the government to European institutions, incorporating any new agreements that may have been reached. Also, it should be framed within the principles to be analysed at the next Conference on the Future of Europe.

Time pressure and health, social and economic emergencies may prevent this State Pact - which could lead to a transfer of national economic sovereignty - from being submitted ad referendum to the citizens of Spain.

It would be desirable for the Congress Commission for Social and Economic Reconstruction include in its deliberations, in addition to the traditional social agents, **new actors with a plurality of ideas and socio-economic principles**. The Plataforma Pymes offers to appear in this Commission to propose the structural economic reforms proposed in its Framework Document, with the aim of achieving a transition from the current neoclassical, extractive and rentier capitalism to an Inclusive Capitalism, which from an ex-ante distribution of wealth, and not ex-post, will allow an increase in the standard of living of the citizens of Spain and the EU.

European instruments for reconstruction

- Short term (before 1 June)

  - **Pandemic Crisis Support through the ESM (Regional Financing Arrangement for the Euro Zone),** with a budget of up to €240 billion. Each country in the Euro Zone can apply for 2% of its GDP (about €20 billion for Spain).

    Its function is to finance healthcare, cure and prevention costs of the Covid-19. Each applicant country must submit a Pandemic Response Plan according to a common template developed by the ESM. This is a low-cost, 10-year funding scheme.

    The ESM and the European Commission will only monitor the use of the funds according to the programme of each applicant Member State. Applicant countries will be subject to the usual control and monitoring instruments of EU economic and fiscal coordination.

    Opinion of the Plataforma Pymes: the State Pact must include the immediate application for this line of financing from 1 June for its maximum amount, about €20 billion.

  - **SURE Program**: endowed with up to €100 billion to support the expenditure derived from the figure of Short-Time Works Allowance. In order to mobilize these funds, Member States must first provide guarantees of up to €25 billion to support the raising of funds on the market.

    The funds will be used to support the short-time work allowance schemes and the benefits that the self-employed may receive. For each request from a Member State, the Commission will require information on the increase in public expenditure that the fund would entail, which will make it possible to assess the specific terms of the loan: amount, maturity, financial conditions

    Additionally and in parallel, the European Commission would accelerate a proposal for a European Unemployment Reinsurance Scheme.

    Opinion of the Plataforma Pymes: the State Pact should include the presentation by Spain of its guarantee to constitute this fund before 1 June for the amount that would correspond to it, some €2 billion. The idea is to speed up the constitution of the fund in order to be eligible for some €13 billion in financing.

    At present, Spain has some 4.5 million workers in Short-Time Works Allowance and 1 million self-employed workers who have stopped working. The approximate monthly cost is about €4 billion. The SURE loan could cover about 3.5 months, which would justify the recent extension of the Short-Time Works Allowance, until 30 June.

    Once the conditions of the benefit per worker and the percentage of the workforce on which SURE financing can be applied are known, the terms of the Short-Time Works Allowance could be adjusted to make the two amounts coincide.

- **Financing from the European Investment Bank (IEB) through the EU's Promotional Banks**

  Pan-European guaranteed fund (€25 billion) to provide €200 billion in financing to companies, mainly SMEs.

  Opinion of the Plataforma Pymes: the constitution of the EIB guarantee should be accelerated so that financing can be provided to SMEs through the ICO and commercial banks. It is necessary to ensure a procedure that avoids errors made in the granting of credits from the ICO-Covid-19 guarantee lines, in particular:

  1. Allocate all funds to companies - SMEs or not - without access to the corporate bond purchase programmes by the ECB.

  2. Granting of the funds to SMEs by EU financial institutions not resident in Spain. The aim would be to achieve greater capillarity in the concession, in line with what has been done by the Community Banks in the USA.

  3. Express prohibition of the use of these funds to cancel previous debtor positions of SMEs before the financial system. The aim is to achieve a positive net balance of bank financing for SMEs.

- **€1.5 trillion EU Recovery Fund**

  The Spanish Government's proposal establishes that, if this fund is set up, it should be financed with perpetual debt, linked to the EU MFF and guaranteed with EU funds, being non-refundable transfers.

  It would require previous technical work by the Eurogroup and the European Commission and would require the approval of the MFF for the next seven years, the negotiation of which within the EU is currently blocked.

  Opinion of the Plataforma Pymes: the creation of this fund would be linked to the acceptance by its applicants of a bailout with strict economic conditions. It should also be remembered that the European Parliament's declaration on April 17 advocates the creation of Recovery Bonds guaranteed by the EU budget, without this implying mutualisation of the current debt.

➢ Medium and long term (before 30 July 2020)

- **Study of Spain's request for a bailout with strict conditionality through the ECB's OMT programme or the Covid-19 lines opened by the IMF.**

In view of possibility that the instruments arbitrated so far by the ECB are insufficient to deal with the economic depression, the future State Pact should consider other alternatives:

1. Launching an emergency programme of temporary private and public asset purchases to deal with the pandemic, amounting to € 1 trillion.

2. Temporary deregulation of the requirements for collateral to be provided by Eurosystem financial banks to obtain financing.

3. Compensation for possible downgrading of government debt ratings of Euro Zone Member States below the minimum required by the ECB, through the admission of such government debt, if it had the minimum rating required by the ECB before 7 April.
4. Introduction of new long-term operations for refinancing financial institutions (PELTROs) without establishing an end to the financing of the resources obtained.

The scope of these measures must be considered in the light of the new macroeconomic context, of which we highlight the following:

1. Requests for massive financial aid by more than 100 countries to the IMF - an amount never seen before - as a consequence of the recession made explicit by Covid-19. This will lead to processes of restructuring public debts with reductions of debt and debt moratoriums, which will degrade the credit rating of the States by the rating agencies. It is very likely that soon, Argentina and Lebanon will open this process, which could also happen in the case of Italy and Spain before the end of the year. In this line, the ECB has decided to downgrade the rating of public debt required to be admitted as collateral.

2. Massive process of private restructuring of corporate debt of companies listed on the EU and USA equity markets. The European Commission is considering the possibility of allowing EU Member States to become shareholders in these entities

3. Consideration, as a new risk factor, of public health emergencies caused by virus outbreaks, among others.

4. Increase in the Euribor rate from -0.35% in August 2019 to -0.108%. The trend has become more acute since March 2020, which could lead to a positive Euribor at the end of the year. This is an indirect sign of the tension in loans between financial institutions and proves that the ECB's expansive monetary policy does not reassure the institutions. Last week the ECB launched a new TRLO line with the aim of reducing these tensions.

5. Possible process of hyperinflation in a context of stagflation, as a result of the ECB and the Federal Reserve's expansionary monetary policy, reinforced by the explicitly of the Covid-19 crisis. It seems that the purpose is to raise asset prices in the equity and real estate markets to avoid debt deflation. However, the risk of hyperinflation increases, which together with a massive fall of companies and over-indebted states, would require the need to raise interest rates.

6. In the second half of 2019, both the ECB and the Federal Reserve began a process of reviewing their monetary policy, Fed's Listens and Strategy Review respectively, which the ECB has decided to extend until June 2021. The ECB's Strategy Review considers that the HICP does not reflect actual inflation. The monetary policy implemented since 2014 has led to increases in the value of stock prices - as shown by the share price/earnings ratio - and in real estate assets, which are not included in the CPI. Therefore, the ECB is considering the possibility of introducing owner occupied-housing costs into the calculation of HIPCs, which would undoubtedly increase inflation data and consequently lead to an increase in interest rates.

7. Judgment of the German Constitutional Court last May on the ECB's asset purchase programme. The judgment asks the German government and parliament to justify the proportionality of the purchase of public and private assets, establishing that the Bundesbank cannot participate in these purchases until they are made by the ECB. The Bundesbank interprets the German Constitutional Court as wishing to establish that the ECB is not engaging in monetary financing, i.e. the purchase

of public debt on the secondary market without conditionality. A possible solution to the problem would be to admit the possibility of purchasing public debt on the primary market with strict conditionality. The consequence for Spain would be the unavoidable request for a rescue of the ECB through its OMT program, which would mean the loss of Spain's economic sovereignty and the need to undertake a profound program of structural economic reforms.

8. Excessive indebtedness of non-banking financial entities, such as investment funds, insurance companies and pension funds, about which the IMF and the ECB have been showing growing concern. Possible debt restructuring would result in large losses for such institutions, turning a liquidity problem into a solvency problem.

Opinion of the Plataforma Pymes:

The State Pact requires that consideration be given to the possible downgrading of Spain's public debt rating before the end of 2020. In order to avoid a break-up of the Euro Zone as a result of the interpretation of the German Constitutional Court ruling, the Plataforma Pymes proposes to request the ECB to include Spain in its OMT program.

This would involve the acquisition of government debt by the ECB in the primary market (rather than secondary) subject to strict macroeconomic conditionality. **This conditionality would have to be agreed in advance in the proposed State Pact**, which would give the legitimacy to start conditionality negotiations with the EU institutions and the ECB.

To be eligible for the OMT programme, Spain would first have to be covered by one of the ESM's financing lines.

Given the above, this section of the State Pact should, according to the Platform, reflect profound **structural economic reforms** in the product market that will **allow the Spanish economy to move**, within a period of 10 years, **from the current exhausted neoclassical, extractive and rentier capitalism to an Inclusive Capitalism that, from an exante distribution of wealth and not expost, through the elimination of excessive income oligopolies and superstars firms with a dominant position, will allow, through the promotion of competition, an improvement in productivity and thus contribute to the general interest by increasing the level of the standard of living of Spanish citizens and, by extension, those of the EU**.