INVESTMENT REPORT
2022/2023

Resilience and renewal in Europe

European Investment Bank

Introduction

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Investment Report 2022/2023: Resilience and renewal in Europe.

About the report

The annual EIB report on investment and investment finance is a product of the EIB Economics Department. The report provides a comprehensive overview of the developments and drivers of investment and investment finance in the European Union. It combines an analysis and understanding of key market trends and developments, with a thematic focus explored in greater depth. This year, the focus is on how Europe is progressing towards a digital and green future amid an energy crisis. The report draws extensively on the results of the annual EIB Investment Survey (EIBIS) and the EIB Municipality Survey, combining internal EIB analysis with contributions from leading experts in the field.

About the Economics Department of the EIB

The mission of the EIB Economics Department is to provide economic analyses and studies to support the Bank in its operations and to help define its positioning, strategy and policy. The director of the Economics Department, Debora Revoltella, heads a team of 40 economists.

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Published by the European Investment Bank.

Printed on FSC® paper

Acknowledgements

Julie Callaert (Centre for Research and Development Monitoring, KU Leuven), Giacomo Casali and Serena Sorrentino provided research assistance.

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Download the complete report:
https://www.eib.org/en/publications/20220211-investment-report-2022
www.doi.org/10.2867/307689

Available as:

pdf: ISBN 978-92-861-5506-2 ISSN: 2599-8277

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Introduction

A string of economic shocks has increased pressure on European economies and businesses at a critical point in Europe's transition to a greener and more digital economy. Trends like digitalisation, the green transformation, ageing and growing inequality constitute major hurdles for the EU economy. At the same time, productivity growth in the European Union has been weak for the past 20 years, and productive investment has trailed the United States for the past ten. The challenges posed by the pandemic and the energy crisis further complicated the already difficult situation facing European businesses and policymakers. How Europe deals with these difficulties will determine how successfully its economy navigates the twin transition and exploits the opportunities it presents, while at the same time addressing inequality and ageing.

In the wake of the COVID-19 crisis, firms have been forced to make big choices with lasting consequences. The pandemic exposed vulnerabilities that had accumulated during a period of rapid globalisation, which benefited from low transportation costs. Businesses had built their supply chains to minimise costs, often at the expense of their resilience to major disruptions. To address these vulnerabilities, firms could choose to reduce globalisation and geographically diversify supply chains, which may also be shortened because of the rising cost of transportation. Finally, production networks will also be reshaped by a political push for strategic autonomy, especially in the European Union and the United States. These new developments will create winners and losers, and they may change global growth dynamics. For policymakers at the EU and global levels, the challenge is to tread the narrow path between increasing resilience and preserving the benefits of globalisation.

A severe energy crisis is supressing the post-pandemic economic recovery and threatens to undermine political and social support for the green transition. Soaring energy prices in Europe, especially for natural gas, reduced household incomes and affected the competitiveness of European firms. However, these effects differed across EU members, reflecting the fragmentation of the European energy market. The policy response at the national and European level was quick and commensurate with the size of the shock, but some measures threatened climate action, such as backsliding on fossil fuel subsidies and relying on higher-carbon fuels like coal to replace gas.

The energy crisis created significant uncertainty, yet it could ultimately accelerate the green transition. Elevated uncertainty shaped corporate investment plans in 2022, with consequences in the medium and long term. On one side, high energy prices squeezed corporate profits and households' disposable income. Financial conditions tightened and the economic outlook deteriorated, negatively affecting investment. At the same time, high fuel prices provided incentive to invest in renewable energy, technologies that reduce the use of fossil fuels and innovative solutions to save energy.

To remain competitive, European businesses need to digitalise. While EU firms are rapidly gaining on their US peers in the use of advanced digital technologies, Europe is trailing in digital innovation and remains dependent on critical technologies from third countries. To reap the full benefits of digitalisation, European policymakers should create better conditions for digital technologies and innovation at home.

The twin green and digital transition may be threatened by growing social and geographical inequality. Higher energy and commodity prices hit poorer households particularly hard, as they have less financial resources and more of their income goes to energy and food. Certain regions have been more severely affected, particularly those that rely heavily on fossil fuels. The energy crisis will likely accelerate the green transition, but the transition will have serious negative consequences for social and territorial cohesion.

All these challenges are creating a perfect storm for macroeconomic policy in Europe. Following a surge in inflation, monetary policy entered a phase of dramatic tightening, which was accompanied by widening spreads between the rates of some countries' sovereign bonds. After a period of heavy spending during the pandemic, countries had planned to tighten their budgets as the pandemic wound down.

Large-scale programmes designed to dampen the blow of the energy crisis on people and businesses have undone some of that fiscal consolidation. At the same time, an extraordinary amount of public investment is needed to support the twin transition while ensuring social and territorial cohesion.

The €723.8 billion Recovery and Resilience Facility will likely be central to macroeconomic policy. Government investment is usually the first victim of cutting when countries face concerns about the sustainability of their debt. Historically, when governments consolidated their finances, they also reduced public investment. This is particularly true in times of crisis. This time around, investment was largely spared as the European Union suspended fiscal rules that constrain public spending and as the Recovery and Resilience Facility came into place. Substantial funds remain available under the facility (some 1% of gross domestic product per year until 2026). To benefit from them, governments must accelerate the implementation of negotiated reforms, remove barriers to investment and advance with planned projects.

Coordination at the EU level remains key to enhancing the impact of policies in different countries. EU members' immediate reaction to the energy crisis prioritised speed over intergovernmental coordination. However, over time, it has been possible to craft and deploy a more structured, cohesive and efficient policy response. The European Union played an important role in achieving this by imposing sanctions against Russia, facilitating the movement and labour market integration of Ukrainian refugees, and adopting the REPowerEU plan to reduce EU dependency on Russian energy imports. While the short-term responses to the energy crisis settle in, policies should begin addressing the medium and long-term challenges. The European Union needs a true common energy market — one that is more robust and less prone to fragmentation. A redesigned Stability and Growth Pact, the completion of the common market for services and a fully functioning capital markets union will enhance the European Union's economic resilience and help it adapt to global challenges.

An analysis reveals that Europe is building its resilience and renewing its economy after a long period of crisis. The EIB Investment Report 2022/2023 focuses on the effects of the COVID-19 and energy crises on the major structural challenges facing Europe — digitalisation and climate change — while stressing the importance of maintaining social and territorial cohesion. The first part of the report assesses the macroeconomic and financial environment in the European Union. It discusses trends and developments in overall investment, focusing on government and corporate investment as well as investment in intangible assets and climate action. The second part of the report delves into the challenges of climate change and digitalisation, analysing their effects on different social groups and regions.

The report's findings are underpinned by two proprietary surveys. The annual EIB Investment Survey (EIBIS), conducted for the seventh time in the summer of 2022, adds valuable information about European firms' investment activities and financing, as well as the obstacles they face. It also focuses on the effects of the COVID-19 crisis and the policies that addressed the pandemic. The survey's climate module, which was recently expanded, reveals the effect of climate change on firms' decisions in unique detail. The third wave of the EIB Municipality Survey in 2022 — after surveys in 2017 and 2020 — provides much-needed information about infrastructure investment by local EU governments, and looks closely at investment in climate action and digital infrastructure.

Throughout the report, EU members are generally grouped into three regions: Central and Eastern Europe, Western and Northern Europe, and Southern Europe. Central and Eastern Europe contains countries that have joined the European Union since 2004 and that rely substantially on EU cohesion and structural funds. Southern Europe encompasses Cyprus, Greece, Italy, Malta, Portugal and Spain. The remaining EU countries are grouped into the region Western and Northern Europe. While these regions are based on geographic location, the countries in each group share many economic characteristics, making the regions useful for economic analysis.