

THE IMPACT OF THE COVID-19 CRISIS ON THE EUROPEAN GREEN DEAL.

A Focus on Romania and Southeast Europe

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Abstract

The COVID-19 outbreak prompted governments worldwide to impose unprecedented restrictions on travel and economic activity. Coupled with a drop in global oil prices, which it largely caused, this crisis is producing imbalances in the energy sector, affecting both investments and the transition to decarbonisation. The dip in carbon prices, also a result of lower energy demand, shows the adversarial impact that the coronavirus crisis can have on the recently launched European Green Deal.

Efforts are being made to ensure that the economic recovery measures adopted at EU and national levels are in line with the long-term climate efforts. In this regard, particular attention should be given to the Southeast European member states that are both more vulnerable to such economic shocks and face distinct challenges in the energy transition.

In Romania, a drop in energy prices threatens further investments in the sector, while potentially ill-conceived governmental interventions risk creating lasting and unforeseen imbalances. In transportation, the renewal rate of vehicles is discouraged by low oil prices, while an influx of second-hand vehicles from Western Europe will further disincentivise the replacement of internal combustion engine cars. In the buildings sector, facing stricter and more costly energy performance standards, and largely dependent on shrinking public funds, the renovation rate of buildings could also be negatively affected.

In order to address this multifaceted crisis, an economic recovery plan should be designed to take into account both the more limited resources for countries in the Southeast Europe and the need to safeguard long-term climate objectives. Emergency short-term solutions for combatting the immediate social and economic risks of the coronavirus crisis should be combined with a set of policy and regulatory revisions that can ensure a smooth and sustainable post-crisis recovery.

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1. The COVID-19 crisis: an unprecedented global economic breakdown

The coronavirus pandemic of COVID-19, a respiratory illness caused by the SARS-CoV-2 virus, is the greatest public health crisis in recent memory, having already infected more than a million people and having caused more than 100,000 deaths worldwide. In their efforts to stunt the spread of this highly contagious virus, governments have imposed unprecedented restrictions on travel and economic activity.

Indicators showing the magnitude of the drop in economic activity worldwide resulted from the COVID-19 are already forbidding. According to UNCTAD's *Investment Trends Monitor* of March 2020, globally, the energy sector saw a downward revision for the 2020 earnings estimation of -208%, followed by airlines with -116%, and the automotive industry with - 47%.¹ The visible demand shock that is currently reverberating throughout the global economy will likely hinder investments. Moreover, the coronavirus outbreak will add tension to the older trends of decoupling – i.e. the loosening and reconfiguring of global supply chains, (GSCs) – driven partly by geopolitics and partly by the effort of companies to become more resilient.

Compared to the Global Financial Crisis of 2008-2009 (GFC), the ultimate impact on the economy could be greater, because the COVID-19 downturn could prove to be *more widespread*, affecting foreign direct investments (FDIs) and capex all over the world; *more immediate*, with interruptions and postponements of investment projects;² and it could also evolve into a *financial crisis*, once the affected businesses become unable to pay their debt, which then entails cascading consequences on the investment flows that can result in a credit crunch. Real capital expenditures and greenfield investments are hampered by slowdowns and shutdowns.

In an optimistic scenario, assuming the drastic, but necessary, medical and sanitary measures are properly implemented, a resumption of economic growth may happen in Q4 of this year, provided that decision-makers throw at this unparalleled crisis the full gamut of monetary and fiscal measures: zero or negative interest rates, quantitative easing, credit facilitation, as well as state aid and cash transfers to companies and households – all of them at unprecedented scale and speed.

The prospects of such potent economic interventions are more limited for the emerging countries, which also face a series of additional risks and obstacles. As stated by the IMF chief, Kristalina Georgieva, „advanced economies are generally in better shape to deal with the crisis, but many emerging markets and low-income countries face significant challenges, including

¹ [UNCTAD \(2020\)](#), Impact of the COVID-19 pandemic on global FDI and GVCs, *Investment Trends Monitor*, Special Issue, March 2020

² As noted by Nouriel [Roubini \(2020\)](#), „[in the Great Depression and the Global Financial Crisis] stock markets collapsed by 50% or more, credit markets froze up, massive bankruptcies followed, unemployment rates soared above 10%, and GDP contracted at an annualized rate of 10% or more. But all of this took around three years to play out. In the current crisis, similarly dire macroeconomic and financial outcomes have materialized in three weeks.” (A Greater Depression?, *Project Syndicate*, March 24, 2020).

outward capital flows".³ Indeed, investors have already withdrawn more than \$83bn from emerging markets since the start of the outbreak, the largest capital outflow on record.

Against this backdrop, the Southeast European (SEE) countries need to ensure that the economic stimuli and social protection measures they adopt do not cause uncontrolled inflation. Where the measures and mechanisms are exclusively financed through additional government indebtedness, the interest rates would quickly rise, raising the costs of further intervention. Therefore, the support of the international financial institutions,⁴ and even more so, of the European Commission and the European Investment Bank are paramount, as shown in section 2.3.

The COVID-19 recession may also represent unfavourable news for the shift to clean energy, because of increasingly difficult access to capital, and the major disruption of GSCs through which Europe is securing its supply of green technology: photovoltaic panels, wind turbines, batteries, and the like. Accordingly, BloombergNEF (BNEF) has downgraded expectations for global demand for solar investments in 2020 by 16% – from 121-152GW to 108-143 GW – noting that the sector is heavily reliant on demand in China, where strict limits on movement, industrial, and commercial activity were enforced.

Taking that concern a step further, the Polish Climate Minister, Michał Kurtyka, recently warned in a letter to top EU policymakers that green projects in his country were threatened by possible delays in delivery, as a result a disproportionately high dependence that the EU has on goods imported from China. He further urged the EU to take „immediate action to shield investment as well as put in place measures to develop its own supply chain for renewable energy.”⁵

The wind sector may fare somewhat better, on account of tighter delivery and construction schedules, and specialized equipment being rented for a more limited time.⁶ Nonetheless, BNEF warns that despite expecting 2020 to be a record year for newly built wind power capacity, there are still significant potential risks faced by onshore and offshore wind projects.

The effect of plummeting energy demand has been compounded by the ongoing price war among the world's largest oil producers, resulting in a price drop for the Brent benchmark from over \$50 a barrel to just over \$20 in less than a month⁷. The downturn on the oil markets

³ [Aljazeera \(2020\)](#), IMF: COVID-19 may trigger global recession in 2020, March 24.

⁴ On March 30, the Romanian Finance Minister, Florin Cîțu said the government is seeking to close unconditional agreements with the IMF and EBRD to bolster „targeted economic aid” during the COVID-19 crisis. „Most importantly, I want to make sure that people are their salaries, pensions and unemployment benefits in time.” He estimates Romania’s budgetary deficit for 2020 to reach 6%.

⁵ Ewa [Krukowska \(2020\)](#), Green Energy's Reliance on China Spurs Poland to Seek EU Action, *Bloomberg Green*, March 26

⁶ Michael Holder and James Murray (2020), ‘Coronavirus dampens 2020 outlook for clean energy and electric vehicles’, *GreenBiz*, March 17

⁷ Since March 7, the price of the Brent barrel plummeted in the low of \$20s, the deepest fall since 2002. The American shale and Canadian tar sands producers are broadly unprofitable at these price levels. The new price war within the global oil industry was started by Saudi Arabia, on March 6, after a failed renewed agreement with Russia, just as OPEC was expected to cut its output as a response to the COVID-19 demand crisis. After weeks of record high oil output, which led to an oversupply of some 35 mb/day,

is also likely to slow the implementation of the European Green Deal, since cheaper energy generally leads to less efficient energy consumption. Lower prices at the gas pump are also depressing sales of electric vehicles and make owners less inclined to invest in improving the energy performance of homes and offices. Such concerns might be compensated by automakers' commitments to vehicle standards according to EU legislation, but the renewal rate of the vehicle fleet is still likely to slow down. As underscored by IEA's Director, Fatih Birol,⁸ the way to at least partly countervail such tendencies is for governments to roll out ambitious measures in support of clean energy projects.

Moving forward, there is a genuine danger that the attention of politicians and the public alike is diverted away from climate change toward more immediate health, financial economic concerns, which can have lasting consequences for the global efforts to tackle climate change. China has already indicated that it will relax environmental supervision of companies to help them overcome the coronavirus pandemic, allowing addition time for rectifying environmental problems.⁹ Meanwhile, the \$2 trillion stimulus bill passed by the US Congress on March 26 does not include any relief for renewable energy projects, such as the extension of tax credit for solar and wind power.¹⁰

The past few weeks revealed a distinct shift of the political rhetoric in the context of COVID-19 pandemic, echoing and amplifying pre-existent themes of populism and climate denialism, including calls to deprioritise or altogether scrap the EU climate action. In Czechia, Poland and Romania, high-ranking officials and party leaders have asked for the abandonment of the entire European Green Deal, or the suspension of one of its pillar, the EU ETS cap-and-trade system, which was depicted as an unnecessary diversion of funds from the urgent needs of the health systems and economic recovery.

However, while the public health emergency is undoubtedly the most pressing urgency for now and the upcoming weeks, short-term policy interventions should not come at the cost of the energy transition and climate action. An adequate response requires a well-designed package of targeted economic and policy measures, coupled with a set of revised regulatory frameworks that can smoothen the post-crisis recovery.

This is a potentially tall order for the Southeast European countries, which usually feature poorer access to capital, weaker administrative capacity and subpar regulatory frameworks. In order to devise a correct response to the current crisis, in a way that is congruous with the long-term objectives of the EU climate policy, it is important to understand the tenets of the

the leading oil-producing countries agreed on April 12 to a production cut of 10 mb/day – the largest ever, but still insufficient to push the oil price close to the pre-crisis levels. Prices are still volatile, with Brent trading at just above \$31 a barrel on April 13. This gives some respite to the oil companies, which must face for months the reality of the international oil benchmark trading under \$40 a barrel.

⁸ Fatih Birol (2020), 'Put clean energy at the heart of stimulus plans to counter the coronavirus crisis', IEA, March 14

⁹ Muyu Xu and Brenda Goh (2020), 'China to modify environmental supervision of firms to boost post-coronavirus recovery', *Reuters*, March 10

¹⁰ Meehan Crist (2020), What the Coronavirus Means for Climate Change, *New York Times*, March 27

European Green Deal, the roadmap to EU's long-term sustainability, as well as the specificities of the energy sector in Southeast Europe.

2. Is the European Green Deal under threat?

2.1 The launch of the European Green Deal

Only three months ago, the President of the new European Commission, Ursula von der Leyen, released the plans for the European Green Deal, a bold vision for a clean and decarbonised continent within the next three decades, coupled with ambitious intermediate steps. This implies that, instead of merely representing a footnote concern for various sectors, climate change mitigation will become the first organisational principle for the entire EU economy. Energy, transport, industrial and even agricultural policies will be shaped according to the necessity to reduce their carbon footprint. This fundamental shift would constitute the new development strategy for the EU economy for the next three decades.

On March 4, the European Commission proposed the new Climate 'Law', aiming to enshrine the target of net-zero GHG emissions by 2050 into legislation. In effect, as of 2050 any remaining GHG emissions in EU's economy would need to be balanced by carbon sinks. Crucially, the proposed regulation also extends the usage of National Energy and Climate Plans (NECPs) until 2050, to become a fundamental governing tool of the EU energy and climate transition. The Commission is currently reviewing the final draft NECPs 2021-2030 submitted by member states – even if several member states have still not submitted their plans, which may complicate the Commission's impact assessment for raising the 2030 GHG emissions target to 50% or 55%.

In terms of policy, the target of net-zero by 2050 and the European Green Deal also require the renegotiation the Renewable Energy Directive, the Energy Efficiency Directive, the Emissions Trading Directive, the Effort Sharing Regulation, and the LULUCF Directive, which the Commission has committed to do by March 2021. This increased level of ambition will likely translate into higher targets, steeper implementation calendars and improved coherence between these policies. Ascertaining the importance of national governments as promoters of this clean transition, the State Aid rules will also be revised accordingly.

Besides revised policies, the implementation of the European Green Deal also depends on large-scale mobilisation of public and private funding. As an acknowledgement of the enormity of the financial needs compared to the size of the available EU budget, the Commission's proposal for bankrolling the transition uses public funds as a leverage for private money.

Thus, the Sustainable Europe Investment Plan¹¹, which the Commission proposes to be the investment pillar of the European Green Deal, was conceived to mobilise €1 trillion of private and public sustainable investment projects over the next decade. This will be accomplished through leveraging €279 billion using the InvestEU Fund, a new Just Transition Mechanism for ensuring a socially fair transition in carbon-dependent regions, the Innovation and Modernisation Funds¹², which are part of the EU Emissions Trading Scheme, and more than half trillion euros in climate and environmental spending under the EU multiannual budget.

At the same time, the European Investment Bank (EIB) will turn in the EU's "climate bank", gradually increasing its share of financing dedicated to climate action and environmental sustainability to 50% by 2025, in addition to eliminating any investments in energy projects that use fossil fuels, including natural gas, as of 2021. The European Central Bank, likewise, will play a more active role in financing climate investments in the Eurozone, for example by increasing the share of green bonds in its portfolio. In order to mainstream the procedure for the selection of such projects and for producing transparent, uniform and enforceable standards, a new EU taxonomy for sustainable activities¹³ is also in the process of being implemented.

2.2 The impact of the coronavirus outbreak

Upon the release of the European Green Deal, the Commission President referred to this project as "Europe's man on the moon moment". Much attention in Brussels and across Europe converged on the subsequent implementation proposals. A few months later, in the midst of a global pandemic and public health crisis, the European Green Deal, which seemed to have mustered unstoppable momentum, has all but evaporated from the forefront of public agenda. Its outlook changed rapidly in the face of this new crisis.¹⁴

With the introduction of severe restrictions on mobility and industrial production across the EU, energy demand and GHG emissions have dropped considerably. This, however, will be a short-lived effect, similarly to the situation after the 2008-2009 crisis, after which both energy demand and emissions bounced back.

Consequentially, the EUA price under the EU ETS has dropped to around €16 per tonne of emissions. While this may appear as a temporary relief for a coal industry that was suffocated by a higher carbon price, it is no motive to rejoice for the Central and Eastern Europeans countries, which depend to significant extents on solid fossil fuels. Part of the energy

¹¹ European Commission (2020) 'Sustainable Europe Investment Plan. European Green Deal Investment Plan.', COM (2020) 21 final, Brussels, 14 January 2020.

¹² The Modernisation Fund (MF) only applies to the 10 lower-income EU member states of Central and Eastern Europe.

¹³ See EU (2020), *Taxonomy: Final Report of the Technical Expert Group on Sustainable Finance – Financing a Sustainable European Economy*, March 2020.

¹⁴ For a more detailed account of the implications of the coronavirus for the European Green Deal, see [CEPS \(2020\)](#).

transitions in these countries is to be financed through the Modernisation Fund (MF)¹⁵, a new tool developed through the revision of the ETS Directive.

The Fund, which concerns investments in the modernisation of energy systems in 10 beneficiary EU member states, is financed through the auction of specifically allocated EUAs. Therefore, the lower the carbon price, the lower the available funding for sustainable investments in member states where financing opportunities are already rather scarce. With governmental spending focused on emergency health services and economic relief, green investments are under threat. The appetite among private investors will also decrease in economically uncertain times.

The pursuit of the Commission's policy agenda is further complicated by the current circumstances. A proposal that is particularly vulnerable to disruption is the upwards revision of the GHG emissions reduction target for 2030 from 40% to 50 or 55%. Concerned about the ability of health services to cope with the pandemic and the magnitude and indefinite duration of the economic downturn, officials in some East European member states have, as previously mentioned, called for the abandonment of the high ambitions of the European Green Deal and/or the burdensome ETS system.

Nonetheless, such a response is unmistakably wrong. The European Green Deal should not be seen as a mere set of restrictions on the carbon content of economic production, but really as a growth and development strategy for Europe. Acknowledging this by no means contradicts the significance of the current emergency and the need for the temporary deflection of attention and funding to resolve it.

2.3 The European Union's response to the current emergency

The EU institutions and member states reacted to this outbreak. The ECB quickly deployed an additional €750 billion in emergency bond-buying¹⁶ to weather the effects of current restrictions on the eurozone. The Commission temporarily relaxed state aid rules to support the economy in the context of the COVID-19 outbreak.¹⁷

Moreover, the European Parliament and the Council of the EU also approved two Commission proposals for financial aid, the Coronavirus Response Investment worth €37 billion, and widening the scope of the EU Solidarity Fund to cover cases of public health emergency, equivalent to €800 million for 2020. The source of this funding is mostly from cohesion policy and from the unused pre-financing for structural funds. For Romania, this means an additional €3 billion that can be spent for coronavirus-related actions.

¹⁵ Directive (EU) 2018/410 of March 14 amending the Directive 2003/87/EC to enhance cost-effective emission reductions and low-carbon investments, and Decision (EU) 2015/1814.

¹⁶ Christine [Lagarde \(2020\)](#), 'Our response to the coronavirus emergency', European Central Bank Blog, 19 March 2020

¹⁷ European [Commission \(2020\)](#), 'State aid: Commission adopts Temporary Framework to enable Member States to further support the economy in the COVID-19 outbreak', *Press release*, 19 March 2020

After negotiations between European leaders, the European Council¹⁸ agreed to “prepare the measures necessary to get back to a normal functioning of our societies and economies and sustainable growth, integrating inter alia the green transition and digital transformation”. This is a clear acknowledgement that the necessity for climate action does not disappear with the emergency of the coronavirus pandemic. This view was further reinforced through a joint letter signed on April 9 by 13 European climate and environment ministers calling for the European Green Deal to become the pillar of the EU recovery plan, as it can create “a stable and forward-looking investment environment for Europe’s businesses, which is an essential precondition for green growth and job creation”.¹⁹

More recently, “in a spirit of solidarity”, the Eurogroup agreed on a €540 billion package designed to tackle the current ‘unprecedented challenge with severe socio-economic consequences’.²⁰ A €240 billion credit line will be created for Eurozone countries through the European Stability Mechanism, €200 billion will be further mobilised by the EIB for companies, and the novel SURE mechanism, a new initiative of the Commission, will mobilise €100 for an embryonic EU unemployment insurance scheme.

Reflecting these extraordinary circumstances, the Commission will also suggest changes to the multi-annual financial framework (MFF) proposal to address the fallout of the coronavirus crisis.²¹ Integrating the green transition in these modifications is important, as the EU budget represents the main leverage for climate investments under the European Green Deal.

3. A focus on Romania

As a case study, this section focuses on the effects that COVID-19 crisis has on Romania’s energy, transport and buildings sectors, and the way these are, in turn, likely to impact the early phases of the European Green Deal.

3.1 Energy prices

The energy prices in Romania plummeted to record lows in March and early April. The standard petrol price has fallen to about €0.9/litre on April 10, compared to €1.2/litre in early March – a fall of about 25%.²² On the electricity Day-Ahead Market, low demand and significant

¹⁸ European [Council \(2020\)](#) ‘Joint statement of the Members of the European Council’, Brussels, 26 March 2020

¹⁹ Signatory countries are Austria, Denmark, Finland, Italy, Latvia, Luxembourg, the Netherlands, Portugal, Spain, Sweden, France, Germany and Greece. The full letter can be accessed [here](#).

²⁰ [Eurogroup](#) (2020) ‘Report on the comprehensive economic policy response to the COVID-19 pandemic’, *Press Release*, 9 April 2020.

²¹ [European Commission \(2020\)](#) ‘Statement from Commission President von der Leyen on proposals to fight the economic effects of the coronavirus crisis’, *Statement*, 28 March 2020

²² <https://www.peco-online.ro/istoric.php>

contribution of wind power generation lowered the price from about €150/MWh at the beginning of March (before the current restrictions on the movement of people were imposed) to less than €100/MWh a month later.²³ Similarly, the price of natural gas on the spot platform of the Romanian Commodities Exchange (BRM) fell to an average €9/MWh in the first 10 days of April from €12.5 a month before.²⁴

On top of that, the Government Military Ordinance No. 4/March 29 introduced not only drastic restrictions to mobility, but also a cap on the prices of utilities and fuels, at the price level of the issuance day – a restriction difficult to enforce, given that the wholesale markets from which those commodities are purchased by the suppliers are still operating competitively and transnationally. So far, though, the market prices themselves have stayed under the level of the newly imposed price ceiling.

As mentioned before, one of the consequences of low energy prices is to disincentivise energy efficiency measures, as well as demand response measures and investments in storage - especially when coupled with the absence of strong policy incentives. Combined with diminished capital availability and market uncertainty, this will likely have a knock-on effect on new investment projects in the energy sector, in general. The more persistent the low energy prices and the depressed levels of energy demand, the more detrimental and long-lasting this effect.

A critical such example is the Neptun Deep project for the extraction of offshore natural gas from Romania's largest confirmed Black Sea deposit. ExxonMobil, one of the two operators of the project was reported to be seeking an exit even before it announced a plan to slash \$10 bn in capital investments in light of the combined burden of oil price and demand collapse.²⁵ Meanwhile, OMV, the majority share-holder in OMV Petrom, which is the equal joint venture partner in Neptun Deep, recently announced that it will implement a cost-cutting programme equivalent to \$4.35bn,²⁶ after having repeatedly postponed the final investment decision.²⁷ Along with the low prices for natural gas, an unfavourable regulatory environment for offshore explorations and, perhaps most importantly, the narrowing window of opportunity for the development of new gas projects in the EU amid ambitious climate objectives, these developments represent serious headwinds faced by the Neptun Deep project.

For the European Green Deal, the protracted use of the existent energy production and infrastructure assets, many of them old, polluting and inefficient, oftentimes operating beyond their technical lifetimes, translates in flattening trajectories towards the 2030 targets for GHG emissions reduction, renewable energy sources and energy efficiency. As a result, these targets would then require redoubled ambitions and increased catch-up efforts, bolstered by raised spending for decreasing emissions and green projects. But then again, this may be

²³ <https://www.opcom.ro/rapoarte/pzu/RaportMarketResults.php?lang=ro>

²⁴ <https://brm2.itcm.ro/piata-spot-gn/>

²⁵ [Financial Times \(2020\)](#) 'Exxon slashes capital investment by \$10bn', 7 April 2020.

²⁶ [Reuters \(2020\)](#) 'UPDATE 1-Energy group OMV considers job cuts, plans further cost savings', 08 April 2020.

²⁷ [Reuters \(2020\)](#) 'OMV again postpones decision on Black Sea offshore investment', 13 March 2020.

particularly difficult to do, coming out of a potentially devastating economic crisis that will overstrain both public and private finances.

In the midst of a crisis, in which the entire attention span goes to immediate or short-term measures of public health, social protection and economic stimuli, the salience of the European Green Deal can only be maintained if it is understood and embraced as a source of additional resilience, economic efficiency, as well as environmental and climate protection, as opposed to distant, perfunctory targets and bureaucratic burdens, on top of the current economic challenges – especially in the Southeast European countries. In the absence of domestic promoters of such a perspective, however, the likely effect will be attempts by member states in the region to postpone and dilute climate ambitions.

3.2 ETS and power generation

Besides the depressed energy prices, another key aspect is the evolution of the EU ETS price, the main pillar of EU's climate policies. As indicated above, the EUAs have dropped from €25 in February to just above €15 in mid-March, bouncing back to €21 on April 9.²⁸

Under the current circumstances, it is important to understand the anti-cyclical nature of the ETS, as highlighted in a recent CEPS study²⁹: "As economic activity and allowance demand go down, so does the ETS price, thereby preventing the ETS becoming an additional burden to carbon-intensive sector." However, the relief brought by the lower carbon price is unlikely to offer much respite to the old coal-fired power plants (PPs) in Romania and Southeast Europe, where even an EUA price of €15 could be unbearable. Moreover, given the merit-order of electricity markets, in the current context of decreased energy demand and high production of low-marginal cost electricity from wind turbines, solid fossil fuel PPs are struggling to sell significant amounts of electricity on the competitive wholesale market.

On February 24, the European Commission approved a state aid scheme of the Romanian Government that grants a €251 million temporary loan to Complexul Energetic Oltenia, the state-owned lignite company, to cover its 2019 bill for EUAs. After six months, the loan needs to either be repaid in full – which is improbable given current market circumstances – or the company needs to "undertake a comprehensive restructuring in order to return to viability in the long term or be liquidated".³⁰ However, the long-term viability of the Oltenia Energy Complex is a virtual impossibility amid EU energy and climate policies, without large-scale divestment from lignite assets to lower carbon energy sources. Thus, the Romanian authorities could be obliged to consider liquidation – as soon as security of electricity supply is ensured, given that the Oltenia Energy Complex accounts for circa 25% to the national yearly power generation.

²⁸ <https://sandbag.be/index.php/carbon-price-viewer/>

²⁹ Milan Elkerbout et al. (2020), The European Green Deal After Corona: Implications for EU Climate Policy, CEPS Policy Insights, No. 2020-6, March 2020

³⁰ https://ec.europa.eu/commission/presscorner/detail/en/mex_20_323

In this context, the danger is that the Romanian Government would use the increased discretionary powers for state aid allowed by the COVID-19 emergency to inject more public money in the polluting and uneconomic assets of the coal companies. This could result in a double subsidy, on top of the improved operational conditions, due to lower EUA prices and potential delays for compliance deadlines under the EU ETS, on account of practical difficulties to organise the required reporting and verification. This would not only lead to multiple unintended economic and social consequences, but it could also hinder the achievement of the energy and climate objectives under the European Green Deal, since alternative investments in lower carbon energy sources would be delayed.

As explained in the past,³¹ and as shown in the final NECP draft of 2020, the current implicit coal phaseout strategy of the Romanian Government is a switch from coal- to gas-fired PPs in the two lignite and hard coal national companies, using mainly resources from the Modernisation Fund. However, as the Fund will be financed through the auction of up to 2% of the total EU ETS allowances for 2021-2030, i.e. about 310 million, hence its monetary value will directly depend on the EUA price.

Romania's share of 11.98% of the allocated EUAs in the Modernisation Fund comes to 37.14 million EUAs, whose value at €25 per EUA would be €928.5 million, while at an ETS price of €16 the value would be merely €594.2 million. Therefore, if a protracted COVID-19 slump results in lower ETS prices for longer, the plan of the Romanian Government to quickly start monetising its allocated allowances for urgently needed investments in power generation projects may have to be delayed until the carbon price recovers. Moreover, a lower value of Romania's resources under the Modernisation Fund, combined with the high priority placed by the Government on coal-to-gas switches, would further exacerbate the risk of crowding-out investments in renewables and energy efficiency. This could be even more damaging for Romania's long-term ability to achieve ambitious climate objectives.

In any event, the Romanian Government should focus on building administrative capacity in order to be capable to deal with the foreseeable flurry of project applications for the Modernisation Fund in early 2021. Increased administrative capacity is also needed more generally, for enabling an efficient and effective collaboration in the coming years with the institutional landscape of the European Green Deal on its manifold dimensions. In this light, the existing Romanian ministerial structure also needs more efficiency and clearer accountability for the responsibility of implementing the medium and long-term climate ambitious across all sectors of the economy.

3.3 Transportation

Activity in the transport sector has been greatly reduced in Romania during the COVID-19 crisis, on account of the economic lockdown and curtailment of individual mobility, imposed through a succession of restrictive military ordinances. Transportation is one of the largest

³¹ Radu Dudău and Mihnea Cătuți (2019), The Decarbonisation Challenge of Southeast Europe: A Case Study of Romania, *Intereconomics* 54, pp. 341-346

GHG emitting sectors of the country, especially road transport. As such, plummeting activity in the transport sector was shortly followed by cleaner air, most obviously in the larger cities, and a drop in GHG emissions. For air transport, activity in Europe has come almost to a standstill from early March to early April. The current health emergency may also have negative effects on the demand for public transport, at least on the short term. Given increased public awareness about the contagious nature of viruses such as SARS-CoV-2, there might be an increase in the preference for personal vehicle mobility, which can increase traffic and consequently both pollution and emissions.

Now, if the recovering curve of road transport will grow faster in the months ahead than the recovering curve for oil price – which is likely to be the case, considering the situation of the international oil market – the current gains in reductions of GHG and air pollutants emissions will be swiftly wiped off, since petrol-based transport will be incentivised by cheaper fuel, and the purchase of new, cleaner vehicles will likely be postponed.

The problem is compounded in Southeast Europe and Romania, in particular, by the fact that the private vehicle fleet is old, hence less fuel efficient and more polluting. Romania has about 6 million licensed cars, with only a marginal proportion of electric and hybrid ones. The average age of licensed cars is more than 12 years, one of the highest in Europe. More than three quarters of the new car registrations in Romania over the past five years were second-hand cars with internal combustion engines (ICE).

The tendency has actually seen a surge since February 2017, when the Government lifted the green tax on cars' registration. This overlapped with the adoption of increasingly restrictive regulations over Diesel cars and more ambitious support for e-mobility and plug-in hybrids in Western Europe, so that a wave of displaced second-hand ICE cars found its way to Eastern Europe, overwhelming these countries' national support programmes for the adoption of clean road transportation.

The existing governmental subsidy in Romania for the purchase of full electric and hybrid vehicles, although very generous per purchase (no less than €10,000 for an electric car) has a yearly budget of about €40 million, which is no match for the aforementioned trend. This particular issue ought to be treated as an EU-level market failure, requiring coordinated action of all member states.

3.4 Buildings

A large majority of Romania's 5.1 million residential buildings were built before 1990, at low energy efficiency standards, with energy performance of 180-400 kWh/m² year. The public buildings have an average of 200-250 kWh/m² year. 2.4 million flats built before 1985 need technical refurbishment and modernisation. One in seven residences has deteriorated floors, walls and windows, often with consequences on the inhabitants' health and well-being.³² Moreover, the quality of living differs greatly between the urban and rural areas, with the

³² [National Institute of Statistics \(2019\)](#), *The Living Conditions of the Romanian Population – 2018* (in Romanian)

latter having less than half of households with indoor plumbing. About 40% of heating energy in the residential sector comes from firewood,³³ an easily accessible fuel in the countryside, where 47.5% of Romanian residences are.

These data show the tremendous potential for improving energy efficiency in buildings, responsible for half of Romania's energy consumption. This is acknowledged in the new project of the National Strategy of Long-Term Renovation.³⁴ According to its recommended scenario – a moderate one at that – the renovation rate for 2021-2030 should be 1.88%, followed by 3.74% in 2031-2040 and 4.33% in 2041-2050, in order to achieve the objective of a decarbonised buildings stock by 2050. Nevertheless, even achieving the slowest recommended rate of these three periods – the one for the 2021-2030 timeframe³⁵ – would require a significant leap in increasing the renovation rate six-fold compared to 2011-2020.

The EU regulatory environment promotes large-scale renovations of buildings. As it was the case for the Energy Union, the *energy efficiency first* principle remains one of the bedrocks of the European Green Deal, enabling multiple programmes and channels for financing building renovations, with a significant latitude for member states to introduce additional support mechanisms for energy efficiency. Besides, the EU Taxonomy for Sustainable Finance, which includes standards on EU Green Bonds, was designed to further encourage the involvement of private capital in the buildings' renovation market.

Nonetheless, to the already pervasive problems of energy efficiency in Southeast Europe's building stock³⁶ – such as the "split incentives" between landlords and tenants, the financial risk that hinders private lending, the higher cost of capital, the lack of regulatory coherence surrounding ESCOs and insufficient availability of qualified workforce, among others – the COVID-19 crisis further restrains availability of private capital. This is increasingly problematic, because the current EU strategy for funding investments rests to a significant degree on leveraging private capital, including for energy efficiency projects.

Besides, the new nZEB (near-zero energy building) standards imposed by the Directive of Energy Performance in Buildings³⁷ are significantly raising the costs of renovation works, thus rendering them more dependent on EU or other public funding. The nZEB standards will cover an increasingly larger share of the buildings sector, since it has been compulsory for new public buildings since 2019 and will be so for new residential buildings and deep renovation projects from 2021.

In this context, it is encouraging that the Ministry of Environment announced in February 2020 a new program for buildings renovation, allotting €90 million for individual houses and €80 million for public buildings, to be managed and disbursed by the National Environmental

³³ Eurostat (2020), Final energy consumption in the residential sector by fuel – Romania

³⁴ The project can be consulted [here](#), in Romanian.

³⁵ The investment requirement for this goal was estimated at €12.8 bn.

³⁶ For a useful synopsis with workable solutions, see [Jorge Nunez Ferrer \(2019\)](#) 'Leveraging funding for energy efficiency in buildings in South East Europe', CEPS Policy Insights, No. 2019-05/28 March

³⁷ [Directive 2010/31/EU](#) on the energy performance of buildings

Administration. Moreover, the Energy Ministry (MEEMA) is preparing to establish a National Fund for Energy Efficiency, in its own management, to support energy efficiency projects more generally.

Nonetheless, such public funds are ultimately insufficient for ensuring the needed renovation rate. It is therefore paramount that national governments create regulatory frameworks for energy efficiency that are coherent, transparent and attractive to private capital. This needs to be complemented by the simultaneous development of the institutional and administrative capacity necessary for a smooth collaboration with the EU and international financial institutions for creating financial mechanisms for large-scale buildings renovation projects.

Such mechanisms would include, among others, state guarantees, low-interest loans and grants based on measurable gains of energy efficiency, public financing for renovations of buildings in communities affected by energy poverty, a market for energy performance contracts, mandatory renovations, and the training of a qualified workforce for full variety of specialisations of the nZEB constructions and renovations industry.

4. How should the governments in Southeast Europe respond?

4.1 Outlining a roadmap for decision-makers

In their response to the economic contraction caused by the coronavirus crisis, countries have a wide array of tools at their disposal, from relaxing fiscal policy, to increasing liquidity through monetary policy, to targeted direct investments and bailouts of different sectors and companies, to providing support to citizens in the form of tax, rent and utility bills deferments, increased social spending and even direct cash transfers. Such measures ought to be used smartly, so as to minimise inflationary effects, and transparently, to avoid cronyism and oligopolistic concentration. But this is no mean feat, to be sure, under intense time pressure, when even most competent governments may want to prioritise distribution over efficiency.

At the same time, some of these measures could be coordinated at the EU level, where large-scale financial sources are mobilised, various regulatory and policy adaptations are enabled, and risks may be collectivised. In devising their recovery plans, EU countries, especially those in Southeast Europe should consider two important aspects.

The first is related to the sourcing of capital and the consequent increases in the fiscal deficit and debt-to-GDP ratio. The extraordinary circumstances of the COVID-19 pandemic require gargantuan, perhaps unprecedented governmental intervention, to be disbursed as quickly as possible. EU member states are presently better prepared to respond to economic shocks than they were during the 2008/09 financial crisis, and capital is more readily available at lower costs, without significant risk of spiralling inflation or credit crunch. Early signs from across the developed world have shown a resolute readiness to drastically increase public spending and a low appetite for repeating the austerity measures of the previous crisis.

While such developments should be emulated, Southeast European countries, such as Romania, have a more limited ability for sudden increases in spending, on account of generally poorer credit ratings, higher interest rates and greater risk of inflation. This will require both more proactive and creative approaches for raising credit, as well as efficient and coordinated use of more limited financial resources.

The second aspect that is paramount in devising recovery plans is the need to safeguard the long-term decarbonisation objectives. While the focus on public health, social protection and economic support for citizens and companies is the most immediate, the threat of climate change will not disappear with the coronavirus crisis, nor will the EU's commitment to climate mitigation and climate adaption.

The current expansion of state intervention to protect the people and support the economic recovery must keep countries like Romania on the path to decarbonisation. Any short-sighted measures lacking transparency run the risk of distorting the markets and, crucially, deferring low carbon investments and so potentially creating an irrecuperable handicap in achieving the long-term climate objectives. Therefore, the stimulus packages should be aligned with the principles of the European Green Deal.

This, however, does not imply an uncritical top-down policy transfer from the EU level. Both the EU institutions and the member states should acknowledge and work towards providing more regionally tailored solutions for the Southeast European member states. Equipped with less robust public institutions, limited availability of capital, underdeveloped market economies, and poor infrastructure and public services, the adoption and implementation of highly ambitious climate objectives can be prohibitively difficult in this region.

The neglect of this reality and the lack of compensatory measures could prove detrimental not just to the overall viability of the European Green Deal but also to the European project itself, risking to cause deep and pervasive divisions between groups of member states. At the same time, countries like Romania must engage more actively and constructively in the European debate about decarbonisation and the transition to net-zero emissions.

Moreover, in order to maximise the impact and long-term sustainability of its policies, Romania should also make smart adjustments in the regulatory frameworks that are needed to facilitate the energy transition, especially in a context of limited dedicated financing.

4.2 Policy recommendations for times of crisis: extraordinary action

In responding to the COVID-19 crisis, a set of immediate actions should be taken in the energy sector of Southeast Europe – smartly designed, as transparent as possible in times of urgency, and bolstered by adequate financing. They should be aimed in strictly defined timeframes at the social protection of household consumers – of which millions more are currently affected by technical unemployment, salary cuts, and even complete loss of income, for those lacking formal employment – and at the economic protection and stimulus for companies.

For the former, a good example is the recent bill adopted by the Romanian Parliament, meant to protect the household consumers by allowing for a three-months deferral of payment of

utility bills. EPG appraised this measure in a recent paper³⁸ as a good idea threatened by failure, on account of indiscriminate application to all the households, including those that do not need such protection. More consequently, the bill covers non-household consumers as well, including energy intensive companies, which have access to separate mechanisms of economic protection and stimulus, such as payment by the government of technical unemployment for their employees, diminished fiscal obligations upon anticipated payment, and prospective access to low-interest credit.

For small and medium enterprises (SMEs), the European Commission has approved on April 11 a State Aid scheme of €3.3 bn³⁹, to allow these companies the ability to cover their investment and operational costs during the COVID-19 crisis. The funds will be disbursed through direct grants, state guarantees, low-interest credits and *de minimis* financial support.

4.3 Short-term measures to relaunch the energy sector

Apart from the immediate economic measures required exceptionally in times of pandemic, a set of added actions, some of them long argued for, ought to be prioritised until the year's end, in order for activity in the energy sector to be relaunched smoothly, along the main lines of the European Green Deal. Regulatory and institutional revisions are needed both for increasing the efficiency of the post-crisis recovery and for ensuring the viability of achieving Romania's long-term objectives.

The Government ought to optimise its internal structure and build institutional and administrative capacity in key areas related to the upcoming dialogue the EU institutions for efficient access to the funds mobilised within the European Green Deal. As mentioned above, the capacity to access the funds of the Modernisation Fund and the Just Transition Fund, which will most definitely require dealing with a large number of project applications, requires swift institutional and procedural preparation.

The Government ought to also rethink the structure of some ministries, in order to better collaborate and with the EU institutions, given the vision of the European Green Deal. Thus, instead of the recent absorption of the former Energy Ministry in the newly minted Ministry of Economy, Energy and Business Environment (MEEMA), it would be more adequate to merge the Energy Ministry with the Ministry of Environment, Waters and Forests (MMAP).

Likewise, the issue area of energy efficiency is currently split among three ministries – MEEMA, for policy planning and implementation on energy efficiency, as well as the management of the upcoming National Fund for Energy Efficiency; the Ministry of Public Works, Development and Administration (MLPDA), for the buildings sector; and MMAP for the energy efficiency support scheme administered through the Environmental Fund

³⁸ [EPG \(2020\)](#), ‘Amânarea plății utilităților pentru trei luni, pe durata stării de urgență: o idee bună care riscă să dea greș’, April 5

³⁹ European [Commission \(2020\)](#), ‘State Aid: Commission approves €3.3 billion Romanian scheme to support SMEs in coronavirus outbreak’, April 11

Administration. Undoubtedly, the authority on this area should be centralised in one single institution to avoid duplication, diffused responsibility and unnecessary inefficiency.

Then, Romania has the obligation to develop in 2020 a national long-term emissions reduction strategy with the perspective of 2050. This should be consistent both with the National Energy-Climate Plan 2021-2030 and the EU's *Clean Planet for All* strategy: "A European strategic long-term vision for a prosperous, modern, competitive, and climate neutral economy."⁴⁰ The preparation of the long-term strategy and the implementation of the multi-sectoral National Energy and Climate Plan likewise require strong institutional capacity.

Furthermore, the Government should seek to quickly solve several outstanding legal and regulatory issues which are critical to investment in renewables and energy efficiency:

- lifting the legal barriers on ESCOs by adopting successful practice from other EU member states. ESCOs are central elements of the buildings renovation industry;
- explicitly introducing Power Purchase Agreements (PPAs) in the Romanian legislation.⁴¹ As of January 1, 2020, by virtue of Regulation 943/2019 on the internal market for electricity,⁴² PPAs should be permitted in all EU member states, yet the Romanian legislation has not been updated to de facto allow this right, to the effect of potential legal conflicts between the EU and national legislations;
- addressing the legal and regulatory barriers that keep the Black Sea investors from making a final investment decision on the development of Neptun Deep field, as mentioned above;
- adopting a framework for contracts for difference (CfDs) for clean energy sources. Although the Government has been working on this topic for couple of years now, there is no clear timeframe yet for the adoption of this mechanism. CfDs would finally provide a tool for organising auctions for renewable energy capacities;
- prioritising investment in grid reinforcement in order to increase reliability and, more generally, adequacy and flexibility (including through incentivising investment in utility-scale battery storage);
- incentivising regulations for investment in utility-scale battery storage, which could bring significant flexibility to the power grid;
- committing to bringing forward the deadline for a national roll-out of smart meters, which are the prerequisites for smart grids and increasing digitalisation, from 2028 at present to no later than 2022.

Another priority action that the current Government has already committed to resolving in 2020 is the introduction of a functional mechanism of social protection for vulnerable consumers, on which the very viability of liberalised energy markets depends. First and foremost, the 'vulnerable consumer' needs a proper operational definition, but more

⁴⁰ European [Commission \(2018\)](#)

⁴¹ Law No. 123/2012 of electricity and natural gas

⁴² Regulation [\(EU\) 943/2019](#) on the internal market for electricity

importantly, it needs the right set of protective measures, with dedicated financing streams. Protecting vulnerable consumers is not only about financial transfers and/or targeted prices ceilings for supplied energy, but also about dedicated buildings renovation programmes, publicly funded, by which the efficiency of energy consumption is greatly improved, along with the quality of living.