The Visegrád Countries: Coronavirus Pandemic, EU Transfers, and their Impact on Austria

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The Visegrád economies have been hit hard by the COVID-19 pandemic, especially its second wave. In response, macroeconomic policies have been markedly relaxed, with fiscal stimulus packages reaching up to 14% of GDP in Poland and Czechia. The projected recovery of the Visegrád economies from 2021 onwards should be significantly helped by the massive inflow of EU transfers, particularly from the newly established Next Generation EU recovery fund. Such transfers will boost their economies by between 2.1% per year in Slovakia and 1% in Czechia, at a minimum; the effect should be stronger once EU transfers to other member states are taken into account. The cumulative boost to the Austrian economy in 2021-2022 from EU transfers to the Visegrád countries is estimated at least at 0.12%, thus partly offsetting the net contributions paid by Austria to the EU budget (which stood at 0.31% of Austria’s GNI in 2019). Given strong cross-border spillovers of fiscal policy measures and historically low interest rates, the governments of the Visegrád countries and Austria (and Germany) should be interested in a more expansionary fiscal policy at EU level for the benefit of the less-developed EU member states. In addition, greater co-ordination of national policies among the above-mentioned countries would be advisable in the planning and implementation of COVID-19 restrictions, as well as in the resolution of mass insolvencies that are likely to follow the withdrawal of large-scale fiscal stimulus measures. It might also be advisable to establish joint Central European working groups to analyse possible scenarios of the economic situation in the post-COVID world.

Keywords: fiscal policy, EU transfers, fiscal multiplier, input-output tables

JEL classification: F0, H30, H50, H77
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VISEGRÁD ECONOMIES HIT HARD BY THE PANDEMIC

The Visegrád countries – Czechia, Hungary, Poland and Slovakia – withstood the first wave of the coronavirus pandemic relatively well, and better than most countries in Western Europe. This was partly because of their swift policy response at the early stages of the pandemic: strict lockdowns were introduced early (in mid-March 2020), before the virus had time to spread. As a result, the incidence of new infections and deaths was generally low during the first wave of the pandemic, with Slovakia in particular ranking among the best-performing countries in the world.

However, the second wave of coronavirus infections, which started in September 2020, turned out to be much stronger, and the Visegrád countries have been among the worst-affected in Europe. Admittedly, the high number of new infections detected has been partly a consequence of increased testing, implying that many more asymptomatic cases have been uncovered than during the first wave. However, the number of hospitalisations and COVID-related deaths has gone up dramatically as well. On a cumulative basis, Czechia has suffered the most, with almost 50,000 COVID-19 cases and nearly 800 deaths per one million of population – which is approximately 50% and 100%, respectively, higher than in Austria (Figure 1).

Figure 1 / COVID-19 cases and COVID-related deaths, per 1 million population


In response to the second wave, the Visegrád countries reimposed relatively tight restrictions. Hungary closed its borders as early as 1 September and later introduced, along with Poland, a partial lockdown, while Czechia and Slovakia reimposed strict lockdowns. However, even in Czechia and Slovakia the lockdown restrictions have been less stringent than during the first wave.
As elsewhere, the stringency of imposed restrictions went hand in hand with the extent of the economic downturn. In the second quarter of 2020 the Visegrád economies shrank by between -7.9% in Poland and -13.6% in Hungary on an annual basis. However, the decline was smaller than in Austria (Figure 2) and in most other euro area countries, partly because of the lower dependence on the services sector, which has been hit hardest by the pandemic. Nevertheless, the small size of most Visegrád economies, their high degree of openness and their relatively high degree of specialisation in the automotive industry have aggravated the extent of economic decline. The automotive industry was initially hit hard by COVID-linked disruptions, as demand for cars collapsed and many factories suspended their production. With a much bigger and less open economy, with a lower dependence on car production, Poland performed much better than its peers in the Visegrád region during the first wave of the pandemic.

Figure 2 / Quarterly real GDP growth; %, y-o-y

Sources: wiw, Eurostat.

The third quarter of 2020 saw a strong bounce-back in the Visegrád economies: retail trade turnover, industry and exports all rebounded markedly from the slumps recorded in spring. The supply shock in the crucial automotive industry, although very severe initially, was rectified rapidly and their supply chains resumed operation. Nevertheless, economic activity failed to reach pre-crisis levels: in the third quarter real GDP growth was still in negative territory on an annual basis, ranging from -1.8% in Poland to -5.2% in Czechia (Figure 2). The recovery of private consumption was primarily hampered by depressed demand for services, such as transport, accommodation, food services, entertainment and recreation. Although their rebound in the third quarter was often as strong as, or even stronger than, that of retail trade, it started from a much lower base and did not reach the levels of the previous year.

The reimposition of lockdowns in response to the second wave has weighed heavily on the Visegrád economies, almost certainly pushing them into renewed recessions (on a quarterly basis). However, the downturn does not appear as deep as during the first wave, not least because the important manufacturing sector has held up well this time. For 2020 as a whole, wiw estimates that the recessions reached -4.4% in Poland, -6.5% in Hungary, -6.6% in Czechia and -7.3% in Slovakia, the region’s smallest economy with the highest dependence on car production (wiw, 2020).

In the coming two years, the economies of the Visegrád region are projected to return to growth. Under wiw’s baseline scenario, which assumes that the pandemic will be successfully contained without resort
to new lengthy lockdowns, economic growth in 2021 is expected to range between 3% in Hungary and 4.1% in Slovakia (wiiw, 2020). However, this will not be enough fully to offset the losses incurred in 2020. It is not until 2022 that the level of economic activity will reach pre-crisis levels. The risks to the baseline forecast are primarily on the downside, given uncertainties associated with the effectiveness of the COVID-19 vaccines and the further spread of the pandemic.

**GOVERNMENT SUPPORT MEASURES**

In response to the coronavirus crisis, the Visegrád countries have adopted a wide range of measures. On the monetary side, policy interest rates were lowered substantially, while Slovakia – being a member of the euro area – benefited from the upgraded quantitative easing policies of the European Central Bank (ECB), and other Visegrád countries benefited from it indirectly. However, monetary policy relaxation has not translated into increased credit expansion, given the high perceived risks and uncertain earnings prospects.

On the fiscal side, the governments have taken advantage of the ample policy space: relatively low levels of public debt (except in Hungary) and low borrowing costs stemming from good credit ratings. Table 1 summarises the details of the adopted packages and demonstrates the differences in policy priorities across the Visegrád region. In Poland and Czechia, the fiscal stimulus packages are particularly large, at around 14% of GDP, and with heavy emphasis on state spending. In Slovakia and Hungary, they are smaller and, in the case of Hungary, primarily take the form of tax cuts, tax benefits and tax deferrals. Common to all Visegrád countries are labour market support measures, especially short-time work (STW) schemes, targeted support to the economic sectors hit hardest by the pandemic (household services), loan guarantees, and subsidised credit programmes, particularly for small and medium-sized enterprises (SMEs). In response to the second wave of the pandemic, the fiscal stimulus packages have been prolonged/upgraded, with many of the support measures extending into 2021 and beyond. However, the fiscal stimulus packages adopted in the Visegrád countries have been lower than in many West European countries. For instance, the fiscal stimulus package reached 32% of GDP in Italy and 31% in Germany (including measures at the regional and local levels), although in Austria (13% of GDP) it has been at a similar level to Poland and Czechia (IMF, 2020).

STW schemes, in particular, have played a very important role. Their design has been similar to that in Austria, albeit at a lower degree of subsidisation, with STW allowances as low as 50% of the original gross wage in the case of Poland. To this end, all Visegrád countries will receive support from the EU Commission in the form of loans granted on favourable terms, with the total amount ranging from 0.4% of GDP in Hungary to more than 2% of GDP in Poland. The funds can be used for the creation or extension of STW schemes, and for similar measures targeting the self-employed. Largely as a result of STW schemes, the slump in the number of hours worked in the second quarter of 2020 was much greater than the decline in jobs (Figure 3), mitigating the rise of unemployment. In most Visegrád countries, the unemployment rate in 2020 (according to labour force survey data) is estimated to be only about 1 percentage point (pp) higher than the year before, and in the case of Poland only 0.3 pp higher – a very good outcome under the current circumstances (wiiw, 2020).
### Table 1 / Adopted fiscal stimulus packages, by country

<table>
<thead>
<tr>
<th>Country</th>
<th>Description</th>
<th>Size (% of GDP)</th>
</tr>
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<tbody>
<tr>
<td>Czechia</td>
<td>Fiscal package of CZK 295bn (5.3% of GDP): CZK 100bn in direct support to firms; selective support for affected sectors (culture, sport, tourism, agriculture, restaurants, bus transportation); VAT lowered from 15% to 10%; 50% of rents covered by the state, mandated rent reductions during the first wave; direct payments to employees (wage compensations); deferred taxes and social security contributions; CZK 500 lump-sum payments to self-employed and very small businesses during the first and the second wave etc. On top of that, CZK 500bn (9% of GDP) in loan guarantees.</td>
<td>14.3%</td>
</tr>
<tr>
<td>Hungary</td>
<td>In response to the first wave: on the revenue side, emphasis on alleviating the fiscal burden on businesses: a reduction in certain taxes and social security contributions in exposed branches/sectors. On the spending side, HUF 245bn (0.6% of GDP) reallocated to the healthcare sector. The state has been paying a portion of the wage bill of firms affected. Job creation by supporting investments worth a total of HUF 450bn (1.1% of GDP). HUF 1.49tn (3.3% of GDP) package of financial support instruments for companies channelled through state-owned development bank MFB. Gradual reintroduction of the 13th-month pension. Since late summer the government's readiness for deficit spending has modestly increased. In response to the second wave: a tax relief package for the benefit of families and businesses.</td>
<td>Precise volume highly uncertain due to little transparency, but likely in the single digits</td>
</tr>
<tr>
<td>Poland</td>
<td>In response to the first wave: PLN 116bn (5.2% of GDP) fiscal package; PLN 70bn direct 'economic shield' mostly aimed at companies, including deferred tax and social security payments. Direct payments to the employees of businesses (SMEs in particular) etc. New credit guarantees and micro loans for entrepreneurs estimated at PLN 74bn (3.3% of GDP). PLN 100bn (4.5% of GDP) liquidity programme for businesses financed from the Polish Development Fund. Unemployment benefit for the first three months increased by 39%. A one-time PLN 500 voucher for each child entitled to Family 500+ benefits, to be spent at hotels or tourist events in Poland. In response to the second wave: ‘Anti-crisis Shield 6.0’ approved by the president on 15 December, estimated volume 1.5% of GDP. It targets the most affected sectors of the economy and includes exemption from social security contributions, as well as subsidised loans, wage subsidies and benefits for self-employed.</td>
<td>14.5%</td>
</tr>
<tr>
<td>Slovakia</td>
<td>Fiscal package of EUR 2.6bn (2.8% of GDP): wage compensation to affected businesses (extended until mid-2021); enhanced unemployment and social benefits; deferral of payroll and corporate tax payments for businesses whose revenues have declined by more than 40%. Several state guarantee schemes covering both SMEs and large firms to ease liquidity pressures (EUR 4bn; 4.3% of GDP). A second package announced on 14 October: aid to medical workers (higher sickness benefit), entrepreneurs, culture and tourism.</td>
<td>7.1%</td>
</tr>
</tbody>
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Sources: IMF (2020) and wiwi research, as of 17 December 2020.
EU TRANSFERS TO THE RESCUE

The projected recovery of the Visegrád economies in 2021-2022 will be helped by the expected large inflows of EU transfers. The cornerstone of these transfers will be the newly established Next Generation EU (NGEU) recovery fund, which was approved by the European Council on 10 December 2020 and is the core building block of the fiscal policy response to the coronavirus crisis at the EU level. The NGEU fund, totalling EUR 750bn to be distributed in 2021-2023 in the form of grants (EUR 390bn) and loans (EUR 360bn), is aimed at facilitating economic recovery and fostering structural reforms, especially in such areas as digitalisation and climate change. Within the NGEU, of central importance is the Recovery and Resilience Facility (RRF), through which EUR 312.5bn of the grants are set to flow throughout the EU, with fixed allocations by country in both 2021 and 2022 (in 2023 the size of RRF allocations will be dependent on economic performance in preceding years). Another important channel of NGEU support is the Recovery Assistance for Cohesion and the Territories of Europe (REACT-EU), which finances the STW schemes and labour market support measures more generally in 2020-2022.

NGEU funds will be supplemented by allocations from the EU Multiannual Financial Framework (MFF) for 2021-2027, worth EUR 1.07trn, which was approved by the European Council on 17 December 2020. Historically, MFF transfers have played an important role for the Visegrád countries, especially when it comes to financing public infrastructure investments, with co-financing from national budgets. However, historical precedent suggests that the bulk of MFF funds (such as Cohesion Policy transfers) will not be appropriated before 2023, as it typically takes time to come up with projects eligible for Cohesion Policy funding. Only a few channels of MFF support with predefined fixed allocations per year, such as direct payments to agriculture within the European Agricultural Guarantee Fund (EAGF) and

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allocations from the European Agricultural Fund for Rural Development (EAFRD), will become operational during 2021.

Figure 4 shows only envisaged EU transfers to the Visegrád countries for which specific amounts have been assigned for 2021 and 2022. It includes the bulk of NGEU grants, but only a fraction of MFF funds. For this reason, the total amount of EU funds represented in Figure 4 should be seen as the lower boundary of the actual EU transfers to the Visegrád countries in 2021-2022. Eligibility for these funds will be subject to the newly built-in ‘rule of law’ clause, which may potentially prove binding for some Visegrád countries, such as Poland and Hungary (see Box 1).

**BOX 1 / EU TRANSFERS AND THE ‘RULE OF LAW’ CLAUSE**

Following the European Commission’s proposal from May 2018, the EU has introduced a new mechanism aimed at protecting the EU budget from financial risks linked to deficiencies regarding the rule of law in the member states. The goal of this mechanism is to ensure sound financial management of the EU budget and to protect taxpayers’ money. This ‘rule of law’ clause will apply not only to the recently adopted MFF for 2021-2027, but also to the Next Generation EU recovery fund.

The ‘rule of law’ clause could be of particular relevance to the Visegrád countries, especially Poland and Hungary, which repeatedly faced criticisms from the European Commission for undermining the independence of their judicial systems and the media over the past few years. The initial version of the legislation, which allowed the European Commission to sanction member states violating the rule of law by withdrawing transfers, was vetoed by both Poland and Hungary, which argued that such a mechanism would become a tool of political pressure rather than a mechanism of legal safeguarding.

After difficult negotiations, a substantially watered-down version of the legislation was adopted by the European Council on 10 December 2020. In line with the final version, linking the rule of law to funds will be governed by an objective process and limited only to the proper use of the EU’s money. The scope of the mechanism will effectively only apply to issues such as fraud, corruption and conflicts of interest – and not perceived rule of law deficiencies in general. Member states will be entitled to review the mechanism in court to ensure that it is in line with EU treaties. Any related sanctions will be subject to decision by the EU Court of Justice, which means that their implementation will be effectively delayed by years. According to the text of the agreement, ‘the European Council will strive to formulate a common position’ if a member state facing EU sanctions requests a discussion of its case. However, demands by Hungary and Poland that any decision by the European Council on sanctions should be made unanimously have been rejected.

As can be seen from Figure 4, the bulk of expected EU transfers to the Visegrád countries will be in the form of RRF funds. In Poland and Hungary, direct payments to agriculture will be quite important, owing to the large size of their agricultural sectors. Other channels of EU transfers, such as REACT-EU and

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EAFRD funds, will be less important in value terms. Overall, Poland will be by far the biggest recipient of EU transfers in the region (EUR 29.6bn over the two-year period), followed by Czechia (EUR 8.6bn), Hungary (EUR 6.4bn) and Slovakia (EUR 6.3bn). However, in relative terms, Slovakia will record the highest inflows of EU transfers (6.7% of 2019 GDP), followed by Hungary (6%), Poland (5.6%) and Czechia (2.9%).

Figure 4 / Envisaged EU transfers for 2021-2022, by country
(a) in EUR m
(b) as % of 2019 GDP

Notes: RRF = Recovery and Resilience Facility (part of NGEU). REACT-EU = Recovery Assistance for Cohesion and the Territories of Europe (part of NGEU); allocations from REACT-EU are currently set for 2021 only. Direct payments = payments within the European Agricultural Guarantee Fund (EAGF, part of MFF). Rural development = allocations from the European Agricultural Fund for Rural Development (the figures presented here refer to MFF only). Current prices, except RRF. 2018 prices. Some EU transfers, such as Cohesion Policy and Just Transition Fund allocations, cannot be assigned to a particular year and are not presented. Therefore, the figures in the chart are to be interpreted as the lower boundary of the actual volume of EU transfers in 2021-2022.
Sources: European Commission; authors’ calculations.
The Impact of EU Transfers on Visegrad Countries and Austria

Figure 5 presents multi-country input-output data estimations of the likely growth impact of expected EU transfers to the Visegrad countries in 2021-2022 (which are depicted in Figure 4) on the recipient economies as well as their most important trading partners (including Austria and Germany). As can be seen, the inflow of EU transfers will stimulate local economies only in part. For instance, Slovakia will receive at least 6.7% of its GDP in EU transfers, but the boost to real GDP growth generated by them is estimated at only 4.2%. The rest will be ‘leaked’ to other countries in the form of higher demand for imported goods and services, including from Austria, which has extensive trade links with the Visegrad countries. The cumulative growth impact on the Austrian economy for 2021-2022 on account of planned EU transfers to the Visegrad countries is estimated at 0.12%. This is not a negligible amount, given that it reflects only direct demand spillovers from four economies, three of which are rather small, and disregards the effects of EU transfers to other member states such as Austria or Germany.

In contrast, Picek (2020) attempted to quantify the growth effects of NGEU grants to all EU member states, accounting for demand spillover effects across the EU. His estimates are reproduced in Figure 6 and are largely in line with wiw estimates in Figure 5. Picek (2020) found that NGEU funds may add 2 pp to annual average growth in Slovakia, 1.8 pp in Poland, 1.5 pp in Hungary and 1.2 pp in Czechia over the entire period 2021-2027. This is somewhat more than suggested by the wiw estimates, which can be explained by the fact that positive spillovers from EU transfers to other countries, such as Germany and Austria, on the Visegrad economies are accounted for by Picek (2020) as well. The impact on Austria, for example, is

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The authors are grateful to Robert Stehrer, wiw, for performing the calculations presented in Figure 5.
of course much higher also, as his estimates also include the direct impact of EU transfers to Austria on its economy. These results are mostly in line with Verwey et al. (2020), who use the EU Commission’s QUEST model. Their simulations show that, compared to a baseline scenario, the impact of the recovery instrument could be a 2% increase in GDP by 2024 for the EU average and about a 1% increase for the higher-income EU member states.

It should be noted that, for instance, Watzka and Watt (2020) find weaker average GDP effects of the RRF grants, in the order of about 0.6% in the Visegrád economies and below 0.2% in Austria and Germany, during the first years of the programme. However, owing to the peculiarities of their NiGEM simulation model, the authors believe that their estimates are at the lower bound for the longer-term RRF effects.

**Figure 6 / Next Generation EU grants: Average yearly increase in real GDP in 2021-2027**

Notes: the estimates are based on the assumptions that initial stimulus takes the form of a grant payment that takes place once between 2021 and 2027 and is not renewed or repeated. For simplicity, the cumulative growth impact of the one-time shock of NGEU transfers is divided by seven.

Source: Picek (2020).

**CONCLUSIONS AND POLICY RECOMMENDATIONS**

The Visegrád countries have been hit hard by the second wave of the COVID-19 pandemic, with a much higher number of new infections and deaths than during the first wave. However, the economic impact of the second wave has been less strong, not least because the manufacturing sector (and especially the crucial automotive industry) has held up well this time. To cope with the economic fallout of the pandemic, the Visegrád governments have relaxed monetary and fiscal policies, with fiscal stimulus packages reaching up to 14% of GDP in Poland and Czechia. However, even there the size of the adopted packages has been lower than, for instance, in Germany and Italy (although in Austria it has been similar in magnitude).

Under the baseline scenario, which assumes that the pandemic is contained in 2021 without resorting to renewed lengthy lockdowns, the economies of the region are expected to return to growth, helped to a large degree by the inflows of EU transfers, particularly from the newly established Next Generation EU recovery fund. EU transfers to the Visegrád countries will boost their economies by between 2.1% per year in Slovakia and 1% in Czechia, and the effect should be stronger once transfers to other member states...
are taken into account. The cumulative boost to the Austrian economy over the 2021-2022 period from EU transfers to the Visegrád countries is estimated at 0.12%, which is not a negligible amount. By comparison, Austria’s operating budgetary balance with the EU (i.e. EU net transfers) stood at -0.31% of GNI in 2019. Thus, a large amount of EU funds transferred to the Visegrád economies can be expected to return to neighbouring net contributor countries, such as Austria. For a discussion of the overall gains of EU membership as well as EU net transfers, see European Parliament (2020) and the related policy recommendations in Bachtrögler-Unger et al. (2020). Moreover, intra-EU budget flows are only one part of a much more complex story. Trade and investment flows show strong benefits for Austria resulting from economic integration with the EU-CEE countries, especially the Visegrád group (Holzner and Schratzenstaller, 2020).

In this respect, it is interesting to note that the French economy and finance minister, Bruno Le Maire, mentioned in his keynote speech at the GLOBSEC 2020 Tatra Summit on 9 October 2020 that the Visegrád countries had helped to bridge the gap between the supporters and opponents of issuing common debt for the Next Generation EU Recovery Fund. Given the historically low long-run interest rates and the strong indirect profitability of EU transfers to the Visegrád region for neighbouring net contributing countries, such as Austria and Germany, these governments should be interested in a more expansionary fiscal policy at the EU level for the benefit of the less-developed EU member states. Certainly, this should not come at the cost of the rule-of-law regulations. Also, joint support for common EU debt and tax financing should be complemented by a clear vision of joint EU projects with a European value added on the expenditure side. This could include a number of genuinely European projects relevant for an ecological post-COVID-19 recovery, such as for instance a European Ultra-Rapid-Train network (Creel et al., 2020).

Moreover, apart from greater co-ordination of EU-level fiscal policy, the Visegrád economies and their net contributor neighbouring countries should also aim at co-ordinating national COVID-19 policies, both fiscal as well as other pandemic-related measures. This will be useful for the longer run, but even more so in the short and medium term, while European countries are still experiencing successive waves of coronavirus infections. At present, these policies are not synchronised and hence enable constant reinflections across borders. Joint planning and co-ordination of social-distancing measures, movement restrictions, public health measures, social and economic measures, and lockdowns could be key for a bigger strategy to control the pandemic at last.

Ultimately, Europe will have to face a wave of insolvencies once liquidity measures are cut back after the immediate COVID-19 health crisis recedes in spring. Given the interwoven character of the German, Austrian and Visegrád economies in terms of investment and related production capacities (Adarov and Hunya, 2020), and in particular the Austrian banks’ dominance in the Visegrád financial sectors (Bykova and Grübler, 2020), a joint handling of mass insolvencies would be in the interest of all the involved economies in Central Europe. Co-ordination of insolvency management could go all the way from defining common rules, particularly with regard to firms active across borders, to a joint trust that could provide convertible loans, which would either be repaid or, in the worst case, converted into equity at a future date. However, the current owners of these companies have an interest in averting the latter scenario, given the resulting stock dilution. In any case, it might be also advisable to establish joint Central European working groups in order to analyse possible scenarios of the economic situation in the post-COVID-19 world.
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