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STUDY

Economic policy coordination in the euro area under the European Semester

External authors: Zsolt Darvas
Álvaro Leandro
Bruegel

Provided at the request of the
Economic and Monetary Affairs Committee

ECON

November 2015
EN

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Provided in advance of the Economic Dialogue with the President of the Eurogroup in ECON on 10 November 2015

Abstract

This paper assesses economic policy coordination in the euro area under the European Semester, which is a yearly process of the European Union aimed at improving economic policy coordination and ensuring the implementation of the EU's economic rules. Each Semester is concluded with recommendations for the euro area as a whole and for each EU Member State. We show that implementation of recommendations was poor at the inception of the Semester in 2011 and has deteriorated even further since. The European Semester is not particularly effectve in enforcing even the EU's fiscal and macroeconomic imbalance rules. We assess that euro-area recommendations with tangible economic goals are not well reflected in the recommendations issued to Member States. Finally, we review various proposals to improve the efficiency of the European Semester and conclude that while certain steps could be helpful, policy coordination will likely have major limitations in the future too.

November 2015
ECON EN

PE 542.680

This paper was requested by the European Parliament's Economic and Monetary Affairs Committee.

AUTHORS

Zsolt Darvas, Bruegel
Álvaro Leandro, Bruegel

RESPONSIBLE ADMINISTRATOR

Martin Hradiský
Economic Governance Support Unit
Directorate for Economic and Scientific Policies
Directorate-General for the Internal Policies of the Union
European Parliament
B-1047 Brussels

LANGUAGE VERSION

Original: EN

ABOUT THE EDITOR

Economic Governance Support Unit provides in-house and external expertise to support EP committees and other parliamentary bodies in playing an effective role within the European Union framework for coordination and surveillance of economic and fiscal policies.
E-mail: egov@ep.europa.eu

This document is also available on Economic and Monetary Affairs Committee homepage at:
http://www.europarl.europa.eu/committees/en/ECON/home.html

Manuscript completed in November 2015

CONTENTS

LIST OF ABBREVIATIONS

CSRs	Country-Specific Recommendations
ECB	European Central Bank
EDP	Excessive Deficit Procedure
EIP	Excessive Imbalance Procedure
EU	European Union
GDP	Gross Domestic Product
IMF	International Monetary Fund
MIP	Macroeconomic Imbalance Procedure
OECD	Organisation for Economic Co-ordination and Development
R&D	Research and Development
SGP	Stability and Growth Pact

DE	Germany
EA	Euro Area
ES	Spain
FR	France
GR	Greece
IE	Ireland
IT	Italy
NL	Netherlands
PT	Portugal

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EXECUTIVE SUMMARY

This paper assesses economic policy coordination in the euro area under the European Semester. In Sections 2 and 3 of the paper we make a positive (and not normative) assessment by taking recommendations as given and evaluating their implementation and consistency without assessing the desirability of the recommendations. Section 4, which assesses possible ways to improve compliance, is by definition more subjective.

The key conclusions of Section 2, which analyses the implementation of European Semester recommendations in comparison with OECD Going for Growth recommendations, show that the European Semester is not effective:

- Implementation of recommendations given under the European Semester was modest (40 percent according to our indicator) at its inception in 2011, yet instead of improved implementation in later years as the European Semester matured, the implementation index has steadily fallen to 29 percent by 2014.

- Euro-area countries, for which policy coordination should be stronger in principle, implemented their recommendations only somewhat better than non-euro area countries (31 percent versus 23 percent concerning the 2014 recommendations), while the implementation rate has fallen steadily in both country groups over the period 2011-14.

- Despite the huge efforts by European institutions to coordinate economic policies within the European Semester, implementation of these recommendations is not higher than implementation of the purely unilateral recommendations by the OECD. Overlaps between the European Semester and OECD recommendations only partly explain this similarity.

- The OECD reform responsiveness rates were practically the same in 2013-14 and in 2007-08, suggesting that reform efforts have not increased compared to the pre-crisis period.

- Countries tend to undertake more reforms when they are under a financial assistance programme, experience market pressure or face high unemployment. Yet even in these countries, reform momentum fades once the situation normalises.

- Implementation of recommendations related to the Stability and Growth Pact (SGP) are typically higher (44 percent on average in 2012-14) than the implementation of recommendations related to the Macroeconomic Imbalance Procedure (32 percent in 2012-14) and other recommendations (29 percent in 2012-14). Even though SGP recommendations have the strongest legal basis, the average 44 percent implementation rate cannot be regarded as large, while the EIP implementation is even lower, suggesting that the European Semester is not particularly effective in enforcing the EU’s fiscal and macroeconomic imbalance rules.

Section 3 takes the 2015 recommendations for the euro area as given and assesses their consistency with the country-specific recommendations of the five largest Member States. Our general conclusion is that the 2015 euro-area recommendations with tangible economic goals are not well reflected in the recommendations issued to Member States (with the exception of reforming services markets):

- Concerning the 2015 euro-area recommendations with tangible economic goals, we conclude that:
    - The reference to the euro area aggregate fiscal stance is not much more than empty

rhetoric. It does not define how the optimal aggregate fiscal stance should be determined. The Council recommends that the aggregate fiscal stance should be in line with sustainability risks and cyclical conditions, but it does not state what this aggregate stance is. There is no top-down approach to determine national fiscal stances which correspond to the optimal aggregate, and it is therefore accidental if the sum of country-specific fiscal stances corresponds to the optimal aggregate fiscal stance.

  - Fostering investment is a key goal mentioned in two euro-area recommendations, but CSRs to the five largest euro area countries are not consistent with this goal.

  - The recommendation to correct excessive internal and external debt is not well reflected in the CSRs to the five largest euro area countries despite the fact that the Alert Mechanism Report of 2015, which was published before the CSRs, identifies this as an excessive imbalance in the cases of Italy, the Netherlands and Spain.

  - The recommendation to reduce the high tax wedges on labour is not well reflected in the CSRs to the five largest euro area countries despite the highlighted importance of this issue in the preamble of the Council recommendation for the euro area.

  - Reform of services markets: this euro area recommendation is indeed well reflected in the CSRs of the five largest euro area countries. Each country, except the Netherlands, was recommended to reform the services sector in some way or another.

- While a recommendation on the need for symmetric intra-euro adjustment has been made for the euro area in 2012, 2013 and 2014, it has not been included in the 2015 recommendations.

The key conclusions of Section 4, which reviews various proposals to improve the efficiency of the European Semester, indicate that while certain steps could be helpful, policy coordination will likely still have major limitations in the future:

- In the absence of a euro-area budget or a mechanism to force counties to have larger budget deficits, the optimal aggregate fiscal stance will not be achieved by anything other than pure chance.

- The establishment of an independent advisory European Fiscal Board is welcome. It could increase transparency and foster the debate about fiscal policies in the euro area. It should be entrusted with the definition of an unconstrained optimal aggregate fiscal stance (i.e. the fiscal stance disregarding SGP rules) and its constrained version, which considers the SGP rules for the euro area as a whole and for each Member State, as well as the available fiscal space.

- The proposal to split the European Semester into two stages, whereby only euro-area issues will be discussed in the first stage and country-specific issues reflecting the euro-area conclusions in the second stage, is welcome.

- Decentralisation efforts, such as the establishment of national competitiveness authorities and a higher involvement of national governments, parliaments and social partners in the discussion and decision on the reform process, are welcome. It would likely increase domestic ownership of the reform process, though we are sceptical about whether cross-country slipover effects will be better internalised.

- Formalising the convergence process may help the reform process, but we see major difficulties in the definition of benchmarks, making them binding and political enforcement should a country not comply.

- Financial incentives for the reform process, such as grants in exchange for reforms or a reallocation of EU investments to countries complying with European Semester recommendations, risk limiting the domestic ownership of reforms, would be unfair to countries that have already implemented reforms and are unlikely to influence those countries which have sound fiscal positions.

1. INTRODUCTION

The European Semester is a yearly cycle of economic policy coordination within the European Union. It is supposed to improve economic policy coordination within the union and ensure the implementation of the EU's economic rules (such as those in the Stability and Growth Pact –SGP- and the Macroeconomic Imbalance Procedure –MIP–). In autumn each year, the European Commission sets out the EU priorities for the coming year in the Annual Growth Survey and publishes its opinions on each country's draft budgetary plan. After each country presents its Stability (euro-area countries) or Convergence (non-euro area countries) Programme and its National Reform Programme (later, in the spring), which set out their budgetary and economic policies, respectively, the European Commission proposes Country-Specific Recommendations (CSRs) for budgetary and economic policies. The Council discusses these recommendations, amends them if deemed appropriate and adopts them. Recommendations made in the context of an Excessive Deficit Procedure (EDP) and an Excessive Imbalance Procedure (EIP) are binding, while as regards other recommendations, Member states "*shall take due account of the guidance addressed to them in the development of their economic, employment and budgetary policies before taking key decisions on their national budgets for the succeeding years*" [1]. Non-compliance with EDP and EIP requirements can lead to warnings and even financial sanctions (Box 1), while non-compliance with other recommendations may lead to warnings, further recommendations and enhanced monitoring.

The track record of implementation has been rather weak. Therefore, various changes have already been implemented to improve compliance with recommendations, including the "Streamlined European Semester" from 2015[2], which aims to achieve greater focus, more time to discuss and more opportunities to engage on substance with various stakeholders. In July 2015 the so-called "Five Presidents' Report[3]" set out a plan for strengthening the Economic and Monetary Union, and on 22 October the European Commission unveiled a first set of concrete proposals. One of the proposals is a revised approach to the European Semester, with more focus on the situation of the euro area as a whole in the first part of the Semester and a better reflection of this situation in the discussion of each country's situation and the resulting CSRs[4]. In particular, there will be a more concrete discussion of the euro area's aggregate fiscal stance: the Report says that "*It is important to ensure also that the sum of national budget balances leads to an appropriate fiscal stance at the level of the euro area as a whole*".

This briefing paper has three goals. First, we analyse the track record of implementation of CSRs made in 2011-2014 in comparison to the implementation of the OECD's Going for Growth recommendations, which allows us to draw a number of unpleasant conclusions about the effectiveness of the European Semester. Second, we evaluate the consistency between the 2015 euro-area and Country Specific Recommendations. Finally, we discuss various proposals for improving the effectiveness of the European Semester.

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[1] See Regulation (EU) No 1175/2011 of the European Parliament and of the Council of 16 November 2011 amending Council Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, which was part of the so-called Six Pack agreed by all European Union Member States in 2011. We note that the Excessive Imbalance Procedure has not yet been activated for any EU country.

[2] Which was announced in European Commission (2015) "Communication from the Commission to the European Parliament, the Council and the European Central Bank on steps towards Completing Economic and Monetary Union", Brussels, 21 October, COM (2015) 600 final.

[3] Juncker, Jean-Claude (2015) "Completing Europe's Economic and Monetary Union", Brussels, 22 June.

[4] Other proposals included the introduction of Competitiveness Boards, the introduction of an advisory European Fiscal Board, and specific steps for completing the banking union, notably via a European Deposit Insurance Guarantee Scheme.

Box 1: Sanctions in the EU economic governance framework

Non-compliance with the Stability and Growth Pact and the Macroeconomic Imbalance Procedure may lead to sanctions.

Stability and Growth Pact (SGP): The SGP has two phases: a “preventive arm” and a “corrective arm”. Countries which were identified as having excessive deficits are in the corrective arm, while the rest of the countries are in the preventive arm.

Possible sanctions in the preventive arm: If the Commission finds evidence of significant deviation from the medium-term objective (MTO) or the adjustment path towards it the Commission shall address a warning to the Member State concerned, which is followed by a Council recommendation within one month. If not respected, this can be followed, in the case of **euro area Member States**, by a sanction equal to an interest-bearing deposit of 0.2% of GDP as a rule.

Possible sanction in the corrective arm: a non-interest-bearing deposit of 0.2% of GDP can be requested from a **euro area** Member State that is newly placed in the EDP. When a **euro area** Member State is already subject to the EDP and the Council decides that it has not taken effective action to correct its excessive deficit in response to the recommendation by the Council, a fine of 0.2% of GDP is imposed as a rule. Member States that **are not part of the euro area** do not face sanctions in the form of a financial deposit or a fine. But failure to comply with the recommendations under the Excessive Deficit Procedure may lead to the suspension of Cohesion Funds commitments.

Macroeconomic Imbalance Procedure (MIP): The MIP has six phases: “No imbalances”, “Imbalances, which require policy action and monitoring”, “Imbalances, which require decisive policy action and specific monitoring”, “Excessive imbalances, which require decisive policy action and specific monitoring”, “Excessive imbalances, which require decisive policy action and the activation of the Excessive Imbalance Procedure”. Once the Excessive Imbalance Procedure is activated, an interest-bearing deposit can be imposed after one failure to comply with the recommended corrective action. After a second compliance failure, this interest-bearing deposit can be converted into a fine (of 0.1% of GDP). Sanctions can also be imposed for failing twice to submit a sufficient corrective action plan.

2. REFORM IMPLEMENTATION

2.1 Our new European Semester reform implementation index

In order to assess the implementation of recommendations under the European Semester we extend the work by Deroose and Griesse (2014), and calculate a *reform implementation index*, which ranges between zero (no or very limited progress with all recommendations) and one (full implementation or substantial progress with all recommendations). The index is based on the qualitative assessment included in various reports of the European Parliament[5], which in turn primarily depend on the own assessment of the European Commission[6], augmented (at least for 2011-12) with assessments from the IMF and OECD when available. The assessment of the 2011 recommendations classified implementation into three categories: “no implementation”, “partial implementation” and “full implementation”, while the assessments of recommendations made in later years were classified into five categories:: “fully implemented”, ”substantial progress”, “some progress” and “limited progress” and “no progress”. Deroose and Griesse (2014) create a synthetic indicator using the 5-scale assessment for 2012-13, by giving scores 1, 0.75, 0.5, 0.25 and 0 to the five categories, respectively. In order to include the assessments of the 2011 recommendations, we use a 3-scale assessment and give a score of 1 to “fully implemented” and “substantial progress”, a score of 0.5 to “some progress” and a score of zero to “limited and no progress”: our indicator is the ratio of the sum of the scores to the total number of recommendations.

Certainly, there are some issues limiting the comparability of this index across time and across countries, as highlighted by Deroose and Griesse (2014). Not all recommendations have the same ‘importance’ or ‘difficulty’. Countries may implement the ‘easier’ reforms first and postpone the more difficult ones to later years. Implemented recommendations are not repeated in later years, but several non-fully implemented reforms are recommended again. Therefore, the difficulty of recommendations may increase over time. Yet very few recommendations have been fully implemented and partial implementation of a recommendation in one year may be followed by the same recommendation the next year, which would be easier to implement given the partial implementation in the previous years. Also, most recommendations included several sub-recommendations and the qualitative assessment assessed each of these sub-recommendations one by one, so even ‘easy’ recommendations generally included a number of sub-components. The assessments of these sub-recommendations form the basis of making an overall assessment for the main recommendations[7]. Therefore, while the issue of comparability across countries and time can be important and therefore results should be assessed carefully, we believe that using a single summary index of reform implementation can provide a useful summary indicator.

Figure 1 shows that the track record of implementation of CSRs is modest and deteriorating. The average value of our reform implementation index for the 21 EU countries for which recommendations were made in every year since 2011 was 40 percent. This score is modest at best. Yet instead of improved implementation in later years as the European Semester matured, the implementation index has steadily fallen to 29 percent by 2014. In 2014, out of the 157 main recommendations issued to European countries, only 10 were fully implemented or have shown substantial progress[8], 70 main

[5] European Parliament (2014a) “A traffic - light approach to the implementation of the 2011 and 2012 Country Specific Recommendations (CSRs)”,,European Parliament (2014b) “Implementation of the 2013 Country Specific Recommendations”, and European Parliament (2015) “Implementation of the 2014 Country Specific Recommendations”. These reports were published by the Economic Governance Support Unit of the European Parliament.

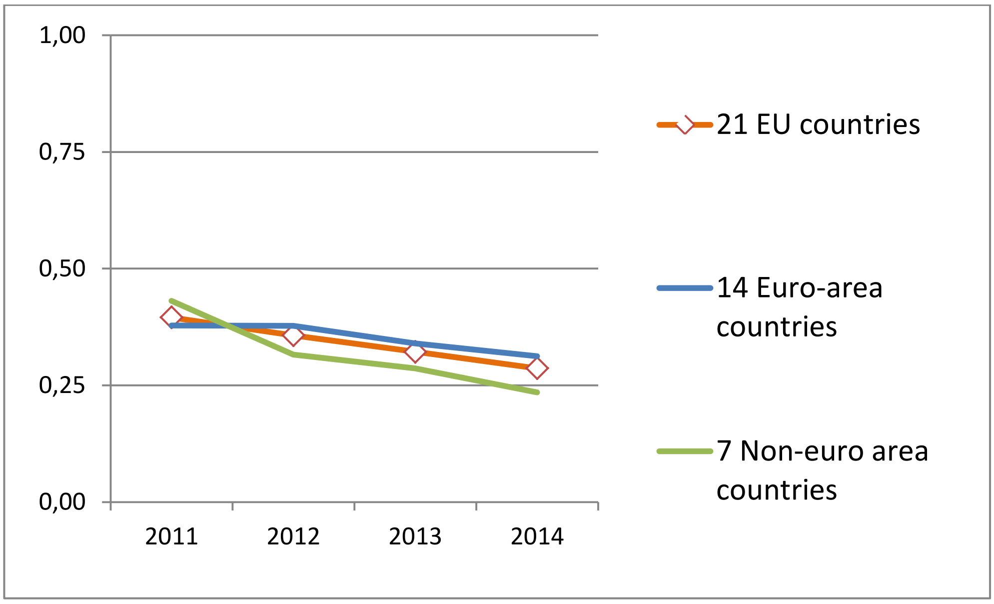
[6] Each year, the European Commission publishes a Staff Working Document which accompanies each Country Specific Recommendation. These Working Documents include, among other things, a qualitative assessment of each country’s implementation of the previous year’s recommendations.

[7] We note that the most recent 2015 recommendations are different: they are fewer and much shorter compared to recommendations made in earlier years.

[8] On average, six recommendations were made to each country in 2014. The following ten countries implemented one recommendation in full or achieved substantial progress: Austria, Belgium, Denmark, Croatia, Lithuania, Malta, Netherlands,

recommendations were followed by some progress, while there was no or limited progress for 77 main recommendations. Implementation was slightly higher in euro-area countries than in non-euro countries in the past three years, but the difference is small and the downward trend is visible in both country groups.

Figure 1: European Semester reform implementation index



Source: Authors' calculations.

Note: we gave a score of 1 to "full/substantial progress", a score of 0.5 to "some progress" and a score of zero to "no/limited progress": our indicator is the ratio of the sum of the scores to the total number of recommendations. Progress assessments are based on European Parliament studies. We report an unweighted average of those 21 EU countries for which data is available for all years: Austria, Belgium, Bulgaria, Czech Republic, Denmark, Estonia, Finland, France, Germany, Hungary, Italy, Lithuania, Luxembourg, Malta, Netherlands, Poland, Slovakia, Slovenia, Spain, Sweden and the United Kingdom. The horizontal axis indicates the date of the European Semester recommendations.

2.2 European Semester vs OECD recommendations

We would like to assess whether reform implementation has increased compared to the pre-crisis period (i.e. whether the European Semester had a positive impact on reform implementation), including reform implementation in countries under a financial assistance programme, which are not included in the regular European Semester recommendations and are also exempt from the obligation to submit medium-term budgetary plans as well as reform programmes. Therefore, we include in our analysis the implementation of the OECD's Going for Growth recommendations, which are available for a longer time period for OECD member states, including countries which are under a financial assistance programme. These recommendations by the OECD are not part of any cross-country surveillance process and therefore there is no mechanism to coordinate these reforms across countries and to enforce them. The OECD calculates an indicator called "*Overall reform responsiveness rates*", which is based on OECD staff assessment. This responsiveness indicator is calculated over two-year periods: for comparability, we also calculate our European Semester reform implementation index over the same periods. The results are reported in Figure 2. The top-left panel of the figure shows a striking result: the two indicators are practically the same for those 16 countries for which both European Semester and

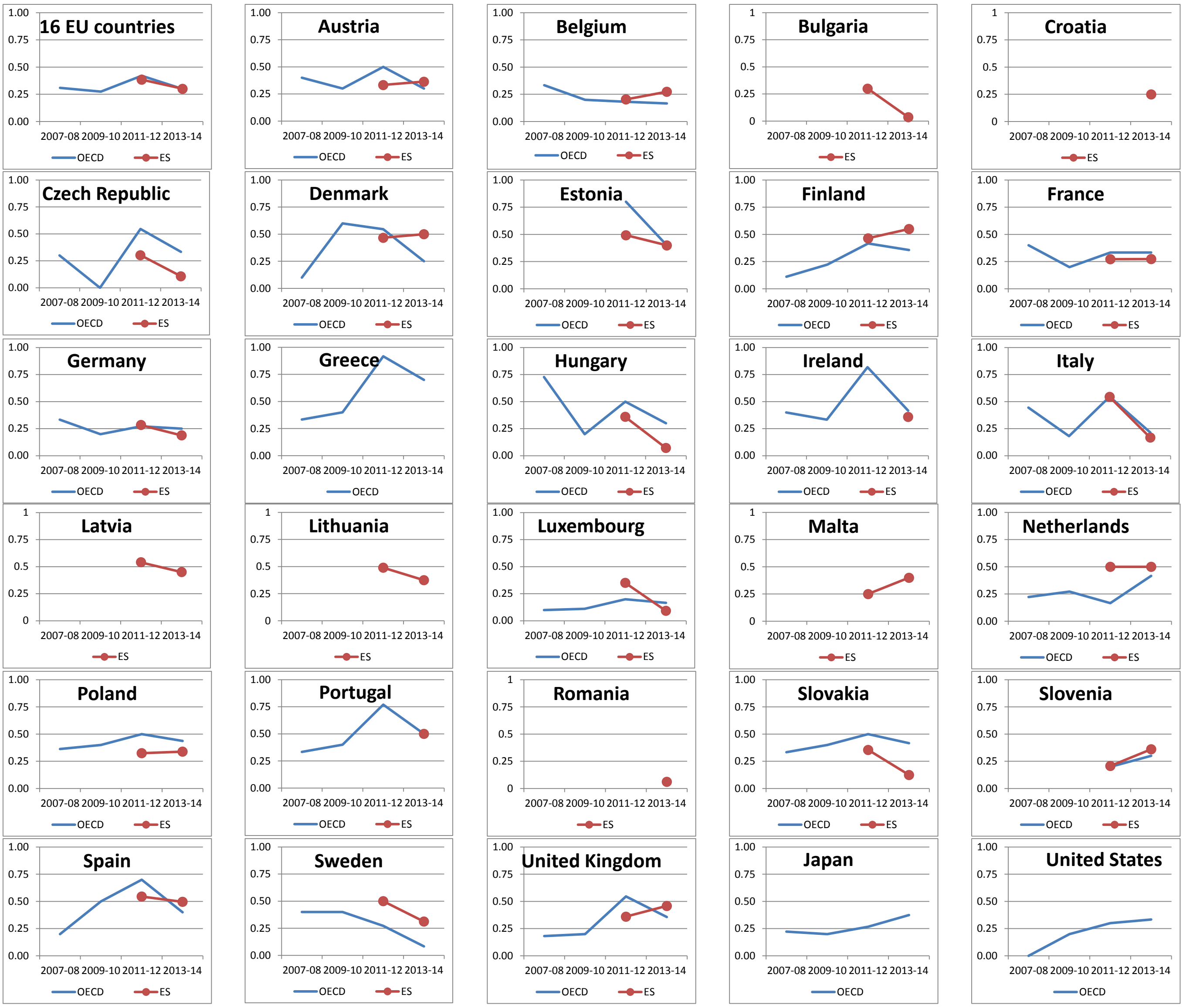
Portugal, Slovenia and the United Kingdom.

OECD recommendations are available in 2011-14. One reason for the similar values of the two indices is that there is some overlap between the European Semester and OECD recommendations (see Annex 1). Yet the overlap is far from being perfect and therefore the similar implementation rates highlight the ineffectiveness of the European Semester: its implementation is not better than the purely unilateral recommendations by the OECD, despite the huge efforts by European institutions to coordinate economic policies within the European Semester. Moreover, the OECD's reform responsiveness rate was practically the same in 2013-14 (30 percent) as in 2007-08 (31 percent), while it was somewhat higher in 2011-12 (42 percent). The somewhat higher rate in 2011-12 could be explained by increased efforts during the crisis (see below), but from 2007-08 to 2013-14 there was no increase in reform implementation, despite the new European economic governance framework. The other panels of Figure 2 show the two indicators (when available) for all EU countries but one, as well as for the United States and Japan[9]. The similarity we highlighted holds for almost every EU country.

Figure 2 highlights that the countries under a financial assistance programme or undergoing severe macroeconomic adjustments are those which implement the most. The highest reform responsiveness rate, 92 percent, is observed in Greece in 2011-12 according to the OECD. In the same period, the reform responsiveness rate was 82 percent for Ireland and 77 percent for Portugal. Estonia had a high score too (80 percent), a country undergoing severe macroeconomic adjustment. These countries are followed by Spain with a reform responsiveness rate of 70 percent. The only other occasion with a similarly high reform responsiveness rate was for Hungary in 2007-2008 (73 percent), when this country had already started a major fiscal and macroeconomic adjustment process. Yet in all of these countries, the reform responsiveness rate fell the in next time period (though typically remained above the EU average), when either the financial assistance programme ended (Ireland and Portugal), or market pressure eased (Hungary and Spain), or when reform fatigue set in while continuing the financial assistance programme (Greece). For those countries not under a financial assistance programme or not undergoing severe macroeconomic adjustment, the reform implementation index remained very low, a result which also holds for the United States and Japan[10].

[9] Cyprus entered a financial assistance programme in 2012 and therefore European Semester recommendations were made only in the first 2011 round, for which the reform implementation rate was 27 percent. Moreover, Cyprus is not included in the OECD Going for Growth studies.
[10] By studying the OECD reform responsiveness rate, the regression analysis by Terzi (2015a) suggests that an IMF programme, a high unemployment rate and financial market stress all tend to increase reform efforts.

Figure 2: Reform implementation: comparison of European Semester and OECD Going for Growth recommendations



Source: Authors' calculation using European Commission, European Parliament and OECD data.

Note: The European Semester reform implementation index is our calculation: see the notes to Figure 1. For the OECD Going for Growth recommendations we report the "Overall reform responsiveness rate", which is calculated by the OECD. The first panel shows the unweighted average for those 16 EU countries for which data is available in the full period: Austria, Belgium, Czech Republic, Denmark, Finland, France, Germany, Hungary, Italy, Luxembourg, Netherlands, Poland, Slovakia, Spain, Sweden and the United Kingdom. For Croatia, Ireland and Portugal the 2013-14 2014 ES reform implementation index considers only the 2014 recommendations, while the 2011-12 value for Latvia considers only the 2012 recommendations.

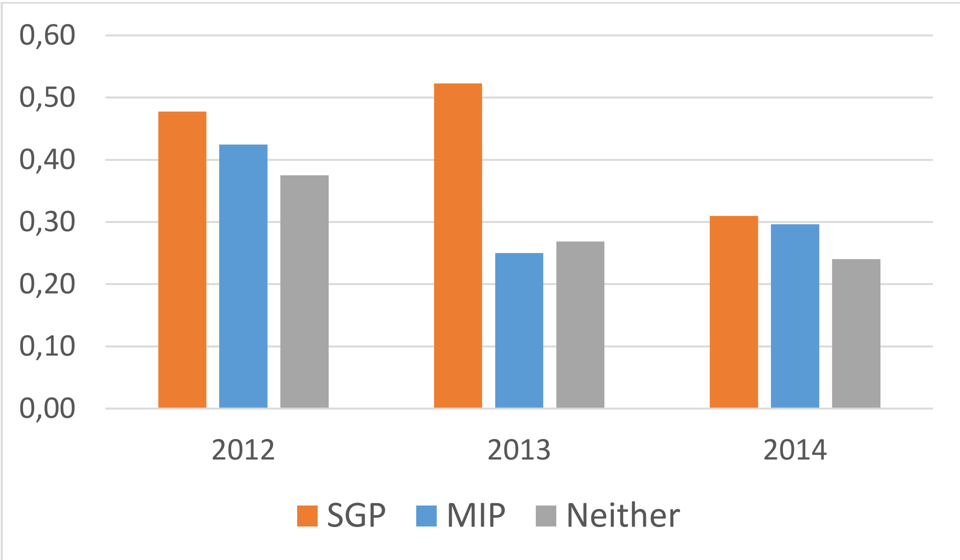
2.4 Stability and Growth Pact and Macroeconomic Imbalance Procedure implementation

We also check the implementation rates for the two main procedures incuded in the European Semester: the Stability and Growth Pact (SGP) and the Macroeconomic Imbalance Procedure (MIP), in comparison with recommendations which are not related to either of these procedures. Again, our indicators are based on the assessment of the European Commission.

Given that the SGP has strong legal enforement tools, one would expect a high implementation rate for recommendations related to the SGP. There are some enforcement tools for the MIP under the Excessive Imbalance Procedure, yet this procedure has not been activated for any country (see Box 1 for the six stages of the MIP: no country has yet reached the sixth stage).

Figure 3 shows that the implementation rate of recommendations related to the SGP tend to be higher than MIP and other recommendations. The difference was particulaly large concerning the 2013 recommendations, which narrowed by 2014. The average SGP implementation rate in 2012-14 was 44 percent, which is not particularly high and suggests that the European Semester is not particularly effectve in enforcing the EU's fiscal rules.

Figure 3: European Semester implementation rates according to the type of recommendations



Source: Authors' calculation using European Commission and European Parliament data.

Note: see the notes to Figure 1 for the method of calculating our index. Averages for the recommendations made for 21 countries are reported (programme countries and Croatia, which joined the EU in 2014, are not included). Some recommendations are related for both the SGP and MIP, which are taken into account for both procedures.

2.5 Summary

The findings in this section allow us to draw a number of unpleasant conclusions about the European Semester:

- Implementation of recommendations given under the European Semester was modest (40 percent according to our indicator) at its inception in 2011, yet instead of improved implementation in later years as the European Semester matured, the implementation index has steadily fallen to 29 percent by 2014.

- Euro-area countries, for which policy coordination should be stronger in principle, implemented their recommendations only somewhat better than non-euro area countries (31 percent versus 23 percent concerning the 2014 recommendations), while the implementation rate has fallen steadily in both country groups over the period 2011-14.
- Despite the huge efforts by European institutions to coordinate economic policies within the

European Semester, implementation of these recommendations is not higher than implementation of the purely unilateral recommendations by the OECD. Overlaps between the European Semester and OECD recommendations only partly explain this similarity.

- The OECD reform responsiveness rates were practically the same in 2013-14 and in 2007-08, suggesting that reform efforts have not increased compared to the pre-crisis period.

- Countries tend to undertake more reforms when they are under a financial assistance programme, experience market pressure or face high unemployment. Yet even in these countries, reform momentum fades once the situation normalises.

- Implementation of recommendations related to the Stability and Growth Pact (SGP) are typically higher (44 percent on average in 2012-14) than the implementation of recommendations related to the Macroeconomic Imbalance Procedure (32 percent in 2012-14) and other recommendations (29 percent in 2012-14). Even though SGP recommendations have the strongest legal basis, the average 44 percent implementation rate cannot be regarded as large, while the EIP implementation is even lower, suggesting that the European Semester is not particularly effective in enforcing the EU’s fiscal and macroeconomic imbalance rules.

3. THE 2015 EURO-AREA RECOMMENDATIONS

On 14 July 2015 the European Council adopted four recommendations for the euro area[11]:

1. "*Use peer pressure to promote structural reforms that facilitate the correction of large external and internal debts and support investment.*" The specific elements mentioned are monitoring and assessing reforms by Member States only in those countries that are under the Macroeconomic Imbalances Procedure; regular thematic assessment of structural reforms; a coordination exercise to reduce tax wedge on labour and to reform services markets.

2. "*Coordinate fiscal policies to ensure that the aggregate euro area fiscal stance is in line with sustainability risks and cyclical conditions.*" The specific elements emphasise the supremacy of Stability and Growth Pact rules; the need for thematic discussions on improvements in the quality and sustainability of public finances; and monitoring the functioning of national fiscal frameworks.

3. Completing the EU's financial unions: banking union (follow up of the ECB's Comprehensive Assessment; implementation of the Bank Recovery and Resolution Directive; ratification of the Single Resolution Fund agreement) and capital markets union ("*Promote measures to deepen market-based finance, to improve access to finance for SMEs and develop alternative sources of finance.*"). Further reforms of national insolvency frameworks are also encouraged.

4. "*Take forward work on deepening Economic and Monetary Union…*", a recommendation which includes a reference to the Five Presidents' report.

Since our goal in this paper is to assess policy coordination under the European Semester, we take these recommendations as given and do not assess their desirability, though we note that in general, we agree with the aims of these headline recommendations. We highlight that in 2015 no recommendation has been made on the need for a symmetric adjustments within the euro area, even though such a recommendation had been made in 2012, 2013 and 2014, and the preamble of the 2015 Council recommendation for the euro area also recognises that "*External rebalancing is ongoing, but progress has been asymmetric and elevated current account surpluses in a few Member States persist*".

We assess the four recommendations (and the lack of a recommendation for a more symmetric adjustment) along three dimensions:

- First, we briefly comment whether the specifics listed in the euro-area recommendations seem sufficient to achieve the stated goals.
- Second, we assess the consistency between the euro-area and Country Specific Recommendations, by focusing on the five largest countries of the euro area.
- And third, we discuss the missing aspect of the symmetric adjustment in the euro area.

3.1 The specifics of the 2015 euro-area recommendations

Taking these headline recommendations as given, we find that the specifics listed for the first two recommendations are unlikely to be sufficient for achieving the stated goals. The third and fourth recommendations are more general and therefore such assessment cannot be made.

1. As we have highlighted in the previous section, implementation of European Semester

[11] The full text of the recommendations is presented in Appendix 2.

recommendations has been rather weak and even declining in 2011-14. While improving compliance would be important, recommendation No. 1 made in 2015 does not seem to have any power in improving compliance. Peer pressure did not work in the past four years and it is unclear why it would work better this year. Moreover, while "*supporting investment*" is included in the first sentence of this recommendation, no indication was provided as to how this goal should be achieved beyond peer pressure.

2. The reference to the aggregate fiscal stance is vague. We see two crucial problems: first, nothing is said about how the optimal fiscal stance should be determined and second, no indication is provided on what "coordination" specifically means to achieve it. Certainly, improving the quality and sustainability of public finances and monitoring the functioning of national fiscal frameworks are important issues, but they are not directly linked with the aggregate fiscal stance of the euro area.

3. The recommendation to complete Europe's financial unions is welcome. We only highlight that this recommendation does not foresee new initiatives, but primarily aims for the ratification and implementation of previous agreements. Unfortunately, there is no reference of a common deposit insurance facility, a topic intensively discussed nowadays.

4. Given that the Five Presidents' Report was published recently, a reference to this report was a must. We generally find the level of ambition of that report weak, but the assessment of that report is beyond the scope of this briefing paper.

3.2 Consistency of euro-area and country-specific recommendations

We classify euro-area recommendations in four categories:

1. Procedural recommendations, such as "*use peer pressure*" and "*continue/hold thematic assessment of structural reforms/thematic discussions on improvements in the quality and sustainability of public finances*";

2. Strategic thinking, such as "*Take forward work on deepening Economic and Monetary Union*";

3. Legal ratification and implementation of existing agreements, such as the completion of the ratification of the Intergovernmental Agreement on the Single Resolution Fund and the implementation of the Bank Recovery and Resolution Directive;

4. And recommendations which aim to achieve certain tangible economic goals, such as:
    - "*promote structural reforms that facilitate the correction of large internal and external debts*";
    - "*support investment*";
    - "*coordinate fiscal policies to ensure that the aggregate euro area fiscal stance is in line with sustainability risks and cyclical conditions*";
    - "*reducing the high tax wedge on labour*"
    - *"reforming services markets"*.

Euro-area recommendations belonging to the first two categories do indeed concern the Eurogroup and should not be repeated in country-specific recommendations. Recommendations concerning the implementation of existing laws should not be repeated in country-specific recommendations either, while ratification could be mentioned where it has not yet been done (category 3). Our focus therefore is on category 4 recommendations, which aim to achieve certain tangible economic goals. We assess whether they are sufficiently reflected in CSRs and whether the current institutional framework, along with the procedural recommendations in category 1, offer a good prospect for their implementation.

None of the category 4 recommendations include numerical targets, which complicates the assessment of their consistency with country-specific recommendations, while next year this feature will give a large degree of freedom for the Commission to assess compliance with these recommendations. In our assessment we presume that these economic goals are aimed to achieve ‘significant’ progress, given that in the 2015 “*streamlined*” European Semester only the most important recommendations are supposed to appear.

3.2.1 The aggregate fiscal stance

Over the past few years, the European institutions have started paying more attention to the aggregate fiscal stance of the euro area. While the first 2011 European Semester had not yet included a recommendation concerning the aggregate fiscal stance, such a recommendation has been made in all subsequent rounds of the Semester (**Error! Reference source not found.**). The wording was slightly different in different rounds, yet the main message was essentially the same as in 2015: “*to coordinate fiscal policies to ensure that the aggregate fiscal stance is in line with sustainability risks and cyclical conditions*”, which should be differentiated across countries and take into account the cyclical position and public debt sustainability of each country, while fiscal consolidation (where needed) should have a growth-friendly composition.

Table 1: Evolution of euro-area recommendations about the euro-area aggregate fiscal stance

Year	Recommendation
2011	The 2011 euro area recommendations did not include any mention of the aggregate fiscal stance.
2012	*“ensure a coherent aggregate fiscal stance in the euro area by pursuing fiscal consolidation as set out in Council recommendations and decisions, in line with the rules of the Stability and Growth Pact, which account for country-specific macro-financial situation”*
2013	*“ensure that the Eurogroup monitors and coordinates fiscal policies of the euro area Member States and the aggregate fiscal stance for the euro area as a whole to ensure a growth friendly and differentiated fiscal policy”*
2014	*“coordinate fiscal policies of the euro area Member States, in close cooperation with the Commission, in particular when assessing draft budgetary plans to ensure a coherent and growth -friendly fiscal stance across the euro a*
2015	“*euro area Member States take action within the Eurogroup to coordinate fiscal policies to ensure that the aggregate fiscal stance is in line with sustainability risks and cyclical conditions”*

Mario Draghi, the President of the European Central Bank, also emphasised the importance of the aggregate fiscal stance in his Jackson Hole speech in 2014[12]: “*it may be useful to have a discussion on the overall fiscal stance of the euro area. Unlike in other major advanced economies, our fiscal stance is not based on a single budget voted for by a single parliament, but on the aggregation of eighteen national budgets and the EU budget. Stronger coordination among the different national fiscal stances should in principle allow us to achieve a more growth-friendly overall fiscal stance for the euro area”*.

[12] Draghi, Mario (2014), “Unemployment in the euro area”, Speech at the Annual central bank symposium in Jackson Hole, 22 August 2014.

However, despite the recognition by the Council, the European Commission and President Draghi of the importance of the aggregate fiscal stance, we find that the reference for the aggregate euro area fiscal stance in euro-area and country-specific recommendations by the Council is little more than empty rhetoric. The first problem is that neither the Council, nor the Commission defines how the optimal fiscal stance should be determined. In addition, the Council does not even state what aggregate fiscal stance "*is in line with sustainability risks and cyclical conditions*". While the Commission Staff Working Document on the euro area states that the current neutral aggregate fiscal stance is broadly appropriate and strikes a good balance between fiscal sustainability and cyclical conditions[13], it is more a value judgement than the result of rigorous analysis and the Council has not adopted this judgement.

The second problem is that, irrespective of the way the optimal fiscal stance is defined, the approach to achieving a desired aggregate fiscal stance is not a top-down approach, whereby the optimal aggregate stance is taken as the starting point and national budgets are determined accordingly. Instead, the resulting aggregate stance is just the sum of national budgets and it is accidental if this sum is equal to what is considered as optimal. In fact, the preamble of the Council recommendation for the Euro area highlights that "*coordination of fiscal policies remains sub-optimal. A number of euro area Member States still need to continue with fiscal adjustment to bring down very high levels of debt. Other countries have more room for manoeuvre and could use it to encourage domestic demand, with a particular emphasis on investment; this would support domestic growth and the euro area as a whole*". It seems therefore that the conclusion about sub-optimal coordination was drawn because countries with more fiscal space did not seize the opportunity to encourage domestic demand, with an emphasis on investment. Despite this conclusion, the specific euro-area recommendation on the aggregate fiscal stance did not refer to the use of available fiscal space, and similar recommendations were not reflected in the CSRs of those countries that have "*more room for manoeuvre*".

In particular, for Germany, the European Commission recommendation proposed on 13 May 2015 included a slight attempt at fostering a reduction of the fiscal surplus[14]:

"*Further increase public investment in infrastructure, education and research, including by using the available fiscal space*."

Yet the recommendations approved by the Council no longer included the reference to the use of available fiscal space:

"*Further increase public investment in infrastructure, education and research*."

Certainly, it is the legitimate right of the Council to decide on a tighter fiscal stance than what is proposed by the Commission, similarly to a government which may adopt a tighter fiscal policy than what is suggested by its fiscal council. Yet the removal of the reference for the use of the available underlines that even tough that the Council acknowledged that sub-optimal fiscal policy coordination in the euro area is a problem, no attempt is needed to remedy this problem[15].

Furthermore, we highlight that while the conclusion about the desirability of the aggregate neutral fiscal stance is included only in the Commission Staff Working Document, but not in the Council recommendations, the CSRs for the five largest countries are not consistent with this aggregate view. For

[13] The Commission Staff Working Document accompanying the 2015 euro area states: "*The aggregate fiscal picture in the euro area has improved considerably since the crisis began and the aggregate fiscal stance is broadly neutral, which could be considered as an acceptable balance between ensuring sustainability and stabilising the business cycle.*"
[14] We call it a "slight attempt", because the Commission's proposal to the use of the available fiscal space was not well specified, as it did not quantify by how much the budget surplus of Germany should be reduced.
[15] We note that Germany has already over-achieved its Medium-Term Objective by around 1 percentage point of GDP, and plans to do so for the next 3 years at least.

France and Spain the fiscal consolidation recommendation is in-line with the on-going Excessive Deficit Procedure, while for Italy it is in line with the preventive arm of the SGP. Therefore, to achieve a neutral aggregate fiscal stance, fiscal consolidation in three of the five largest countries (France, Italy and Spain) should have been compensated by fiscal expansion in other large countries, but this was not recommended for Germany or the Netherlands.

3.2.2 Support investment

There is a lot of emphasis in various Commission reports on the importance of increasing investment. The Commission Staff Working Document on the euro area (which does not necessarily reflect the view of the College of Commissioners) presented a simulation result demonstrating the importance of public investment[16]. The importance of investment is also highlighted in the preamble of the Council recommendations ("*a wide investment gap has opened*") and is reflected by its inclusion in two of the four euro-area recommendations by the Council. Yet we conclude that this euro-area goal is not well reflected in CSRs.

For France, the 5th CSR includes a reference of investment: "*To promote investment, take action to reduce the taxes on production and the corporate income statutory rate, while broadening the tax base on consumption.*"

For Germany, the 1st recommendation is: "*Further increase public investment in infrastructure, education and research. To foster private investment, take measures to improve the efficiency of the tax system, in particular by reviewing the local trade tax and corporate taxation and by modernising the tax administration. Use the ongoing review to improve the design of fiscal relations between the federation, Länder and municipalities, particularly with a view to ensuring adequate public investment at all levels of government.*"

For the Netherlands, the 1st recommendation is: "*Shift public expenditure towards supporting investment in R&D and work on framework conditions for improving private R&D expenditure in order to counter the declining trend in public R&D expenditure and increase the potential for economic growth.*"
For Italy and Spain investment is not even mentioned in their CSRs.

We conclude that these CSRs are insufficient to foster a reasonable increase in public and private investments.

- Public investment: As we noted above, the Commission's proposal to use "*the available fiscal space*" has been deleted by the Council from the German recommendation regarding public investment. This implies that a public investment stimulus should not be expected, only a change in the composition of public expenditures in favour of investment, similarly to the Netherlands. In our view, one should not expect much from changing the composition of public spending, certainly not the 1 percent of GDP extra investment stimulus, of which the effects were simulated in the Commission Staff Working Document on the Euro area, as we cited above. France, Italy and Spain are not recommended to increase public investment.
- Private investments: France and Germany are recommended to make their tax systems more efficient, which is certainly welcome, but we do not expect a major private investment boom as a result. Italy, the Netherlands and Spain were not recommended to boost private investment.

[16] The simulation results quoted in the Commission Staff Working Document on the Euro area indicate that a temporary two-year increase in government investment of 1 percent of GDP in countries with fiscal space would have a persistent positive effect on growth not just in these countries (where the multiplier would be between 0.8-1), but also in the rest of euro area countries, where GDP would also be boosted by between 0.2-0.3 percent.

Therefore, we conclude that while fostering investment is a top priority at the euro-area level, this recommendation is not well reflected in the CSRs of the five largest euro-area countries.

3.2.3 Facilitate the correction of large internal and external debts

The first euro area recommendation invites euro area countries to use peer pressure to promote structural reforms that facilitate the correction of large internal and external debts.

The Commission itself, in the 2015 Alert Mechanism Report[17], identifies excessive imbalances concerning private debt (in the Netherlands and Spain) and public debt (in Italy and Spain). However there are almost no recommendations to address large private debt overhangs: only Italy is recommended to "*take measures to accelerate the broad-based reduction of non-performing loans".*

Regarding public debt, if we accept the premise that cutting deficits during a recession will successfully reduce public debt, then the euro area recommendation to correct large public debts is reflected in the cases of France and Spain, which are invited to correct their excessive deficits, and Italy, which is recommended to comply with the rules of the preventive arm of the SGP. Germany and the Netherlands do not have large public debts and therefore lack of a reference to it is normal.

3.2.4 Reduce the high tax wedge on labour

The first euro area recommendation includes a sub-recommendation to reduce high tax wedges on labour, and the importance of this issue is also mentioned in the preamble of the Council recommendations. Box 2 of the European Commission Staff Working Document accompanying the euro area recommendations presents numbers on the tax wedge and identifies very high tax burdens on labour in Germany, France, Spain and Italy. However, only Germany received a recommendation to "*take measures to reduce high labour taxes".*

Moreover, the same Staff Working Document admits that *"shifts away from labour taxes to more growth-friendly taxes such as consumption, recurrent property and environmental have been taking place but these reforms remain relatively modest compared to the challenge".* If reforms have been modest, it is surprising that this issue, which the Council agrees is important, has not appeared in the CSRs to the four other countries.

We conclude that the recommendation to reduce the high tax wedges on labour is not well reflected in the CSRs to the five largest euro area countries, despite the apparent consensus about the importance of the issue.

3.2.5 Reform services markets

This recommendation is indeed well reflected in the CSRs. France, for example, is recommended to *"Remove the restrictions on access to and the exercise of regulated professions, beyond the legal professions, in particular as regards the health professions as from 2015."* Germany is recommended to *"take more ambitious measures to stimulate competition in the services sector".*

In its sixth recommendation to Italy, the Council invites it to *"adopt competition-enhancing measures in all sectors covered by the competition law, and take decisive action to remove remaining barriers".* Finally, Spain is recommended to "*adopt the planned reform on professional services*". There is no

[17] European Commission (2014) "Alert Mechanism Report 2015", Brussels, 28 November, COM(2014) 904 final

related recommendation for the Netherlands.

We conclude that this euro area recommendation is indeed well reflected in the CSRs of the five largest euro area countries. Each country, except the Netherlands, was recommended to reform the services sector in some way or another.

3.3 Lack of symmetric adjustment within the euro area

In 2012, 2013 and 2014, the Council made a recommendation for more symmetric adjustment within the euro area, but such a recommendation has disappeared by 2015 (Table 2).

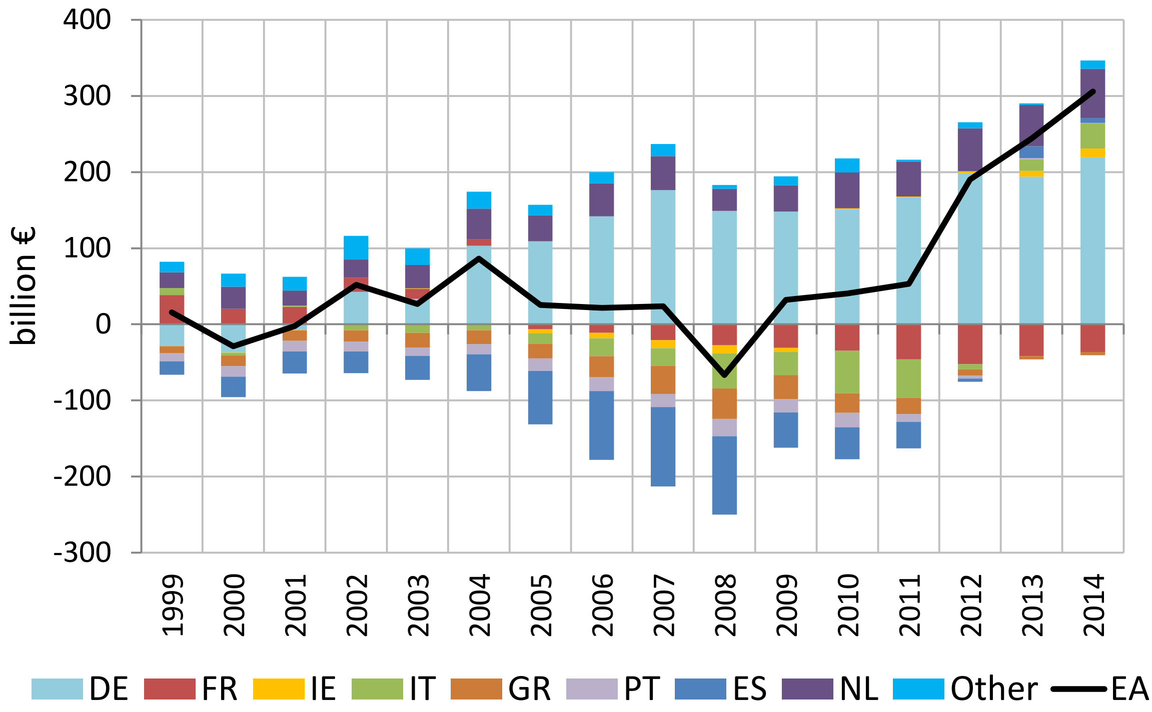
Table 2: Euro-area recommendations concerning symmetric intra-euro adjustment in 2011-2015

Year	Recommendation
2011	The 2011 euro area recommendations did not include any mention of symmetric adjustment and intra-euro area macroeconomic imbalances
2012	*"Implement structural reforms, which also promote flexible wage adjustments, and which – together with a differentiated fiscal stance – would promote an orderly unwinding of intra-euro area macroeconomic imbalances and thus growth and jobs. This would include action at national level which reflects the country-specific situation and takes account of the Council recommendations to individual euro area Member States."*
2013	*"Promote further adjustment in the euro area, ensuring a correction of external and internal imbalances, inter alia by following thoroughly the reforms that address distortions to saving and investment behaviour in Member States with both current account deficits and surpluses"*
2014	*"Promote and monitor, in close cooperation with the Commission, the implementation of structural reforms in those areas most relevant for the smooth functioning of the euro area in order to foster growth and convergence and adjustment of internal and external imbalances. Assess and stimulate progress in delivering on reform commitments in euro area Member States experiencing excessive imbalances and in reform implementation in the euro area Member States with imbalances requiring decisive action, to limit negative spillovers to the rest of the euro area. Foster appropriate policies in countries with large current account surpluses to contribute to positive spillovers."*
2015	The 2015 euro area recommendations did not include any mention of symmetric adjustment and intra-euro area macroeconomic imbalances

In 2012, the recommendation called for "*an orderly unwinding of intra-euro area macroeconomic imbalances*": by definition, intra-euro imbalances include both deficits and surpluses. In 2013, the recommendation was even clearer by explicitly mentioning current account surpluses: "*correction of external and internal imbalances*" was recommended, with a particular emphasis on addressing "*distortions to saving and investment behaviour in Member States with both current account deficits and surpluses*". In 2014 a similarly clear and strong recommendation has been made: "*Foster appropriate policies in countries with large current account surpluses to contribute to positive spillovers.*"
It is stunning that despite the importance of symmetric intra-euro adjustment, which was also recognised by the 2015 Commission Staff Working Document on the Euro area, this recommendation has disappeared from 2015 recommendations for the euro area. Relevant recommendations are not included in CSRs either.

Indeed, the adjustments of current account balances were asymmetric, whereby deficit countries adjusted, but surpluses continued growing (Figure 4).

Figure 4: Current account balance of the euro area



Source: AMECO

We highlight that the disappearance of the call for symmetric adjustment from the euro-area recommendations is in contrast to the main conclusions included in the Commission Staff Working Documents (which, as we already highlighted, may not necessarily reflect the views of the College of Commissioners). The Commission Staff Working Document agrees that "*the adjustment has been asymmetric and there has not been progress in adjustment of current account surpluses*"[18].

As the Commission argues in its Staff Working Document accompanying its 2015 CSRs to Germany, Germany's close links with the rest of the euro area, especially through trade and financial markets, mean that economic spillovers can be potentially large. Therefore both Germany and the rest of the euro area would benefit from higher levels of investment in Germany and a reduction in its current account surplus: the resulting higher domestic demand in surplus countries *"is the only other way of closing the output gap of the euro area as a whole"*[19], given the constraints on monetary and fiscal policy. The IMF (2015a, 2015c) drew the same conclusion. By estimating panel-econometric models for the medium-term determinants of current account balances, Darvas (2015) concluded that European current account surpluses became excessive during the past twelve years, while they were in line with model predictions in the preceding three decades.

Consequently, the disappearance of the call for symmetric adjustment from the euro-area recommendations suggests that the Council disagrees with the findings of Commission staff, IMF reports and some academic research.

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[18] Page 6 of the 2014 Commission Staff Working Document accompanying the Council Recommendations on the implementation of the broad guidelines for the economic policies of the Member States whose currency is the euro, SWD(2014) 401 final.
[19] Page 7 of the 2014 Commission Staff Working Document accompanying the Council Recommendations on the implementation of the broad guidelines for the economic policies of the Member States whose currency is the euro, SWD(2014) 401 final.

3.4 Summary

The key conclusions of Section 3 underline that that euro-area recommendations with tangible economic goals are generally not well reflected in the recommendations issued to Member States (with the exception of reforming services markets):

- Concerning 2015 euro-area recommendations with tangible economic goals, we conclude that:
    - The reference to the euro area aggregate fiscal stance is not much more than empty rhetoric. It is not defined how the optimal aggregate fiscal stance should be determined. The Council recommends that the aggregate fiscal stance should be in line with sustainability risks and cyclical conditions, but it does not state what this aggregate stance is. There is no top-down approach to determine national fiscal stances which correspond to the optimal aggregate and therefore it is accidental if the sum of country-specific fiscal stances corresponds to the optimal aggregate fiscal stance.
    - Fostering investment is a key goal mentioned in two euro-area recommendations, but CSRs to the five largest euro area countries are not consistent with this goal.
    - The recommendation to correct excessive internal and external debt is not well reflected in the CSRs to the five largest euro area countries, despite the fact that the Alert Mechanism Report of 2015, which was published before the CSRs, identifies this as an excessive imbalance in the cases of Italy, the Netherlands and Spain.
    - The recommendation to reduce the high tax wedges on labour is not well reflected in the CSRs to the five largest euro area countries, despite a box in the Staff Working Document accompanying the euro area recommendations which highlights the breadth and consequences of the issue.
    - Reform of services markets: this euro area recommendation is indeed well reflected in the CSRs of the five largest euro area countries. Each country, except the Netherlands, was recommended to reform the services sector in some way or another.
- While a recommendation on the need for symmetric intra-euro adjustment has been made for the euro area in 2012, 2013 and 2014, it has not been included in the 2015 recommendations.

Therefore, we have to conclude that there was no improvement since 2013, when Darvas and Vihriälä (2013) concluded that: "*A major drawback is that the Council recommendations do not give sufficient importance to symmetric intra-euro area adjustments. Reference to the euro area's 'aggregate fiscal stance' is empty rhetoric. Insufficient attention is paid to demand management. The most comprehensive recommendations are made on structural reforms.*"

4. PROPOSALS FOR AN IMPROVED EUROPEAN SEMESTER

Our key conclusions showing that implementation of CSRs has been weak and has even declined, and that there are major consistency problems between the euro-area recommendations and CSRs are in sharp contrast to the self-congratulation included in the Commission Staff Working Document on the Euro Area[20]. Efforts to improve the European Semester are badly needed.

4.1 On-going reforms

The European Commission has already "*streamlined*" the 2015 European Semester by further prioritising and shortening the recommendations, by publishing CSRs and euro-area recommendations three months earlier than in previous years to enable more discussion with various stakeholders, and by aiming more intensive outreach. Thereby, some of the proposals of Hallerberg, Marzinotto and Wolff (2012a, 2012b) have been adopted. The length of recommendations generally increased from 2011-14, while there was a major fall in 2015.

Recent proposals to revamp the European Semester go in the right direction. According to the Five Presidents' report, and a more recent European Commission communication on the 21st of October 2015, the European Semester is to be split into two stages: first there will be discussions and recommendations about the euro area, and only then will Country Specific Recommendations be discussed and decided upon, which should reflect the common challenges identified in the first stage.

On 21 October 2015, the Commission also issued its decision on the establishment of an independent advisory European Fiscal Board[21]. It will provide to the Commission an evaluation of the implementation of the fiscal framework, but it will also *"advise the Commission on the prospective fiscal stance appropriate for the euro area as a whole"*, and *"may advise the Commission on the appropriate national fiscal stances that are consistent with its advice on the aggregate fiscal stance of the euro area within the rules of the Stability and Growth Pact"*. This is a very welcome development and at least partly in line with the proposal of Darvas and Vihriälä (2013), who suggested the establishment of an independent fiscal authority responsible for the definition and management of the euro area's aggregate fiscal stance. The Fiscal Board should promote a much-needed discussion of the aggregate fiscal stance in the first stage. It could also improve coordination by pointing out which countries have fiscal space and should implement more expansionary fiscal policy in order to bring the aggregate fiscal stance to desired levels: this was an element which was clearly missing in the CSRs, as we have pointed out.

However, according to the Commission's 21 October 2015 proposal, the Fiscal Board can give advice only within the SGP rules, so it will not be free to define the optimality of the aggregate fiscal stance. It will not have the power to manage the fiscal stance and the European Commission will not be obliged to incorporate the suggestions by the Fiscal Board when deciding about euro-area and CSRs. But even if the Fiscal Board one day concludes that some countries have to have more expansionary fiscal policy, and both the Commission and the Council endorse that conclusion, there will not be many instruments to enforce it: while countries can be required to reduce their debts and deficits according to the regulations of the Stability and Growth Pact, there exists no mechanism by which countries can be required to enact

[20] "*The recommendations addressed to the euro area in the context of the European Semester* ***have already proven their value*** *in fostering stronger policy coordination in the euro area. The* ***increased ownership of the euro area recommendations*** *by the Eurogroup has facilitated progress on a number of important policy areas over the last year. As a result, the review of the draft budgetary plans has led to firm commitments taken by Member States to adjust their fiscal policies. The Eurogroup has thoroughly discussed reform plans and fostered* ***common understanding on important issues*** *such as the potential benefits of structural reforms, including those to* ***address high taxes on labour****, and* ***the effects of asymmetric economic adjustment within EMU****. This has helped to find common understanding on current policy challenges, pinpoint best practices and helped to better coordinate policy responses into directions favourable to growth.*" [highlights selected by us]

[21] Commission Decision of 21.10.2015 establishing an independent advisory European Fiscal Board, C(2015) 8000 final.

fiscal expansion[22].

As regards the implementation of structural reforms, the most promising proposal in our view is the establishment of a euro-area system of competitiveness authorities, composed of independent national councils, a proposal which was made by Sapir and Wolff (2015) and was endorsed by the Five Presidents' report. The national councils are supposed to assess wage and productivity developments as well as economic reforms to foster competitiveness, while their European network should help to exploit their synergies.

We see the establishment of national competitiveness councils as a kind of decentralisation, whereby reform priorities would be defined nationally. It will likely increase the ownership of the reform process. The reason is that a conclusion by such a national council could be seen by the national parliament and the government as a recommendation coming from inside the country, but not as an intrusion coming from Brussels organisations. It needs to be seen to what extent national councils will be able to internalise the cross-border implications of the reform process, on which we are sceptical. Yet the establishment of such councils will be an improvement compared to the current governance framework even if the national councils will primarily focus on the domestic consequences of the reform process.

4.2 Further possible reforms

4.2.1 The aggregate fiscal stance

Federations have federal and local budgets. In a federation fiscal stabilisation is mostly the job of the federal government. In our own research we found that automatic stabilisers worked as well in seven non-EU advanced countries as in the euro area both in 2000-07 and in 2008-14. However, discretionary fiscal stabilisation was important in non-EU advanced countries both in 2000-07 and in 2008-14, but was practically zero in the euro area in 2008-14 (Claeys, Darvas and Leandro, *forthcoming*). We believe that a euro-area fiscal stabilisation instrument would be helpful in aligning the aggregate fiscal stance with the aggregate economic situation of the euro-area, while national fiscal policies could be left to follow national preferences when fiscal rules are not binding. While a number of proposals have been made about a euro-area fiscal capacity (see, for example, Darvas, 2012; Wolff, 2012; Pisani-Ferry, Vihriälä and Wolff, 2013), the report of the Five Presidents incorporated a related proposal only for the long term.

Similarly, the prospect for a euro-area mechanism which would force countries to have higher budget deficits, as suggested by for example by Sapir and Wolff (2015), is extremely unlikely as well. As we highlighted earlier, even the slight attempt by the European Commission to include in Germany's 2015 CSRs a clause to encourage the government to use its fiscal space was deleted by the Council. While parliaments and governments can change, we see no political possibility of countries agreeing to a binding process which may force them to have deficits larger than what their domestic preferences deem appropriate.

In the absence of a euro-area budget or a mechanism to force counties to have larger budget deficits, the remaining options are rather limited. In any case, the European Fiscal Board should be entrusted with the definition of an unconstrained optimal aggregate fiscal stance (i.e. the fiscal stance disregarding SGP rules) and its constrained version which considers the SGP rules. This exercise should be done for the euro-area as a whole as well as for each euro area Member State. Such an exercise will help foster

[22] A possible support to this process could be the use of the Excessive Imbalance Procedure for countries having too large current account surpluses, for example by requiring the increase of public investment. While non-compliance with such a recommendation could in principle lead to sanctions under the current rules, we believe financial sanctions will never be imposed in the EU. Even in the best case, influencing countries via the MIP to have higher public investment takes several years, while the optimal fiscal stance should be achieved promptly. Moreover, not all countries having fiscal space have excessive current account surpluses.

discussions, yet the problem will remain that there will be no enforcement mechanism to require expansionary fiscal policy.

Therefore, we see it extremely unlikely that any coordination mechanisms or the use of the MIP would enable to force countries to have larger deficits than what their national preferences would suggest. We are sceptical about whether the optimal aggregate fiscal stance could be achieved by anything other than pure chance. We expect that vague statements will continue to be made in the future about the aggregate fiscal stance and the benefits of coordination.

4.2.2 The implementation of structural reforms

As regards the implementation of structural reforms, a number of proposals have been made. The IMF (2015b) and Banerji *et al.* (2015) also suggested some ways to enhance the implementation of structural reforms. These include the definition of "outcome-based" benchmarks, which are sufficiently concrete, measurable and directly under the control of policymakers, and the use of EU legislation where possible instead of coordination. Such proposals were included in the Five Presidents' report for the medium term ("Stage 2", which should be completed by 2025). The proposal aims to formalise and make more binding the convergence process by "*agreeing on a set of common high-level standards that would be defined in EU legislation, as sovereignty over policies of common concern would be shared and strong decision-making at euro area level would be established*". While setting benchmarks may be useful, Terzi (2015b) highlights that structural reforms cannot be objectively measured. He demonstrates that some of the indicators proposed by Banerji *et al* (2015) show very large variations among the countries which are at the top of the World Economic Forum World Competitiveness Report rankings. We also see difficulties in enforcement and making the system binding if a country does not meet the standards by the agreed time.

Some further proposals were also made by IMF (2015b) and Banerji *et al.* (2015) to strengthen incentives, such as direct financial transfers form the EU to cover reform costs and support implementation, a proposal which echoes the 2013-14 discussion on "*contracts for competitiveness and growth*". One key problem with such a contract, as emphasised by Pisani-Ferry (2013), is that such a grant in exchange for a particular reform would be seen by domestic stakeholders as a bribe by which European partners want to enforce a reform on the country. The popularity of the government entering such a contract may fall quickly. Even if the reform proposal would originally come from the country in question, domestic stakeholders may perceive it as coming from European partners.

There are other problems too. Such contracts or any other financial incentives, such as a reallocation of EU-sponsored investments in countries which implement European Semester reform suggestions, would reward countries which have not implemented reforms. Those countries which followed the European Semester advice earlier would not benefit from such a contract, while providing retroactive contracts to reward those countries which have already implemented reforms would lead to a very messy system. Moreover, financial incentives would not really matter for larger countries having sound fiscal positions. For example, we see it unconceivable that Germany would speed up services market reforms if it would receive a few billion euros from other euro area countries.

As regards increasing the domestic ownership of the reform process, some proposals in the Five Presidents' report and the 21 October 2015 Commission Communication on steps towards Completing Economic and Monetary Union point to the right direction. For example, Hallerberg, Marzinotto and Wolff (2012a, 2012b) suggested to enhance the role of national parliaments at the EU level, to enhance the role of European institutions at Member State level and to increase the role of the European Parliament in the European Semester, suggestions which are endorsed by the Five Presidents' report. Similarly to the establishment of national competitiveness councils, we see the higher involvement of national parliaments, governments and social partners in the discussion of the reform process as a way of decentralisation, which can improve ownership of the process.

4.3 Summary

The key conclusions of Section 4 show that while certain steps could be helpful, policy coordination will likely have major limitations in the future too:

- In the absence of a euro-area budget or a mechanism to force counties to have larger budget deficits, the optimal aggregate fiscal stance will not be achieved by anything other than pure chance.

- The establishment of an independent advisory European Fiscal Board is welcome. It could increase transparency and foster the debate about fiscal policies in the euro area. It should be entrusted with the definition of an unconstrained optimal aggregate fiscal stance (i.e. the fiscal stance disregarding SGP rules) and its constrained version, which considers the SGP rules for the euro area as a whole and for each Member State, as well as the available fiscal space.

- The proposal to split the European Semester into two stages, whereby only euro-area issues will be discussed in the first stage and country-specific issues reflecting the euro-area conclusions in the second stage, is welcome.

- Decentralisation efforts, such as the establishment of national competitiveness authorities and a higher involvement of national governments, parliaments and social partners in the discussion and decision on the reform process, are welcome. It would likely increase domestic ownership of the reform process, though we are sceptical about whether cross-country slipover effects will be better internalised.

- Formalising the convergence process may help the reform process, but we see major difficulties in the definition of benchmarks, making it binding and political enforcement should a country not comply.

- Financial incentives for the reform process, such as grants in exchange for reforms or a reallocation of EU investments to countries complying with European Semester recommendations, risk limiting the domestic ownership of reforms, would be unfair to countries that have already implemented reforms and are unlikely to influence those countries which have sound fiscal positions.

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ANNEX 1: COMPARISON OF 2014 EUROPEAN SEMESTER AND 2013 OECD RECOMMENDATIONS

Table 3 compares the 2014 European Semester CSRs and the 2013 OECD recommendations for the six largest EU countries, France, Germany, Italy, Poland, Spain and the United Kingdom. OECD recommendations are set every two years, so these two sets of recommendations are broadly comparable (especially given the persistence through time of both CSRs and OECD recommendations). The table shows that while there are a few similar recommendations by the OECD, there are still many differences with the Country-Specific Recommendations made in the context of the European Semester. Also, European Semester recommendations are usually much more detailed, and may contain many "sub-recommendations". OECD recommendations typically do not. Thus, a single OECD recommendation might echo part of a European Semester recommendation, but not its entirety. Therefore, while there exist common recommendations given to each country in the context of the OECD Going for Growth and the European Semester, these do not explain the finding that implementation rates are very similar for both types of recommendations.

Table 3: 2014 European Semester vs 2013 OECD Going for Growth recommendations

France	
European Semester Country-Specific Recommendations	**OECD Going for Growth Recommendations**
Reinforce the budgetary strategy: • Comply with the rules of the SGP • Implement ambitious structural reforms to increase the adjustment capacity and boost growth and employment • Step up efforts to achieve efficiency gains across all sub-sectors of general government • Reinforce incentives to streamline local government expenditure • Take steps to tackle the increase in public expenditure on health • Take additional measures when and where needed to bring the pension system into balance by 2020	No similar recommendation
• Ensure that the labour cost reduction resulting from the "crédit d'impôt compétitivité emploi" is sustained • Take action to further lower employer social security contributions • Further evaluate the economic impact of social security contribution exemptions and take appropriate measures if necessary • Further reduce the cost of labour in a budget neutral way	No similar recommendation
• Simplify companies' administrative, fiscal and accounting rules and take concrete measures to implement the Government's ongoing "simplification plan" by December 2014 • Eliminate regulatory impediments to companies' growth • Simplify and improve the efficiency of innovation policy • Ensure that resources are focused on the most effective competitiveness poles and further promote the economic impact of innovation developed in the poles.	No similar recommendation

• Remove unjustified restrictions on the access to and exercise of regulated professions and reduce entry costs and promote competition in services • Take further action to reduce the regulatory burden affecting the functioning of the retail sector • Ensure that regulated gas and electricity tariffs for household customers are set at an appropriate level which does not represent an obstacle to competition • Strengthen electricity and gas interconnection capacity with Spain • In the railway sector, ensure the independence of the new unified infrastructure manager from the incumbent operator and take steps to open domestic passenger transport to competition	Reduce regulatory barriers to competition
Reduce the tax burden on labour and step up efforts to simplify and increase the efficiency of the tax system	Shift the tax burden away from labour, and continue to reduce the minimum cost of labour
• Take further action to combat labour-market rigidity • Take additional measures to reform the unemployment benefit system • Ensure that older workers benefit from adequate counselling and training and re-assess the relevant specific unemployment benefit arrangements with respect to their situation on the labour market.	Reform job protection and strengthen active labour market policies
• Pursue the modernisation of vocational education and training, implement the reform of compulsory education, and take further actions to reduce educational inequalities in particular by strengthening measures on early school leaving • Ensure that active labour market policies effectively support the most vulnerable groups • Improve the transition from school to work	Improve equity and outcomes in primary and secondary education Improve the quality and efficiency of tertiary education
Germany	
European Semester Country-Specific Recommendations	**OECD Going for Growth Recommendations**
Pursue growth-friendly fiscal policy and preserve a sound fiscal position: • Use available scope for increased public investment in infrastructure, education and research • Improve efficiency of tax system • Increase cost-effectiveness of public spending on health-care and long-term care • Ensure sustainability of public pension system • Complete implementation of the debt brake consistently across all Länder	No similar recommendation
Improve conditions that further support domestic demand: • By reducing high taxes and social security contributions • When implementing the general minimum wage, monitor its impact on employment • Improve employability of workers (through ALMPs and better education) • Reduce fiscal disincentives to work • Facilitate transition from mini-jobs to forms of employment subject to full mandatory social security contributions • Address regional shortages in the availability of fulltime childcare facilities and all-day schools while improving their overall educational quality	Reduce tax wedges on labour income and shift taxation towards less distortive sources.

Minimise costs of transforming the energy system	No similar recommendation
• Stimulate competition in the services sector • Identify reasons behind the low value of public contracts open to procurement under EU legislation • Remove unjustified planning regulations • Remove remaining barriers to competition in railway markets • Pursue consolidation efforts in the Landesbanken sector	Reduce regulatory barriers to competition, especially in the services sector
No similar recommendation	Improve tertiary education outcomes
No similar recommendation	Ease job protection for regular workers
No similar recommendation	Remove obstacles to full-time female labour participation
Italy	
European Semester Country-Specific Recommendations	**OECD Going for Growth Recommendations**
Reinforce the budgetary measures for 2014: • Comply with the rules of the SGP • Carry out the ambitious privatisation plan • implement a growth-friendly fiscal adjustment while preserving growth-enhancing spending like R&D, innovation, education and essential infrastructure projects • Guarantee the independence and full operationalisation of the fiscal council	No similar recommendation
• Further shift the tax burden from productive factors to consumption, property and the environment • Ensure more effective environmental taxation, including in the area of excise duties, and remove environmentally harmful subsidies • Implement the enabling law for tax reform by March 2015 • Further improve tax compliance by enhancing the predictability of the tax system, simplifying procedures, improving tax debt recovery and modernising tax administration • Pursue the fight against tax evasion and take additional steps against the shadow economy and undeclared work.	Improve the efficiency of the tax structure
• As part of a wider effort to improve the efficiency of public administration, clarify competences at all levels of Government • Ensure better management of EU funds by taking decisive action to improve administrative capacity, transparency, evaluation and quality control • Further enhance the effectiveness of anti-corruption measures • Monitor in a timely manner the impact of the reforms adopted to increase the efficiency of civil justice	No similar recommendation
• Reinforce the resilience of the banking sector and ensure its capacity to manage and dispose of impaired assets • Foster non-bank access to finance for firms • Continue to promote and monitor efficient corporate governance practices in the whole banking sector	No similar recommendation

• Evaluate, by the end of 2014, the impact of the labour market and wage-setting reforms on job creation, dismissals' procedures, labour market duality and cost competitiveness • Work towards a more comprehensive social protection for the unemployed • Strengthen the link between active and passive labour market policies • Adopt effective action to promote female employment • Provide adequate services across the country to non-registered young people and ensure stronger private sector commitment to offering quality apprenticeships and traineeships by the end of 2014 • Scale-up the new pilot social assistance scheme, in compliance with budgetary targets • Improve the effectiveness of family support schemes and quality services favouring low-income households with children.	Enhance active labour market policies
• Implement the National System for Evaluation of Schools to improve school outcomes in turn and reduce rates of early school leaving • Increase the use of work-based learning in upper secondary vocational education and training and strengthen vocationally-oriented tertiary education • Create a national register of qualifications to ensure wide recognition of skills. • Ensure that public funding better rewards the quality of higher education and research.	Improve equity and efficiency in education
• Approve the pending legislation or other equivalent measures aimed at simplifying the regulatory environment for businesses and citizens • Foster market opening and remove remaining barriers to, and restrictions on, competition in the professional and local public services, insurance, fuel distribution, retail and postal services sectors • Enhance the efficiency of public procurement • In local public services, rigorously implement the legislation providing for the rectification of contracts that do not comply with the requirements on in-house awards by 31 December 2014.	Reduce barriers to competition
• Ensure swift and full operationalisation of the Transport Authority by September 2014. • Approve the list of strategic infrastructure in the energy sector and enhance port management and connections with the hinterland.	No similar recommendation
No similar recommendation	Pursue rebalancing of protection from jobs to workers' income
Poland	
European Semester Country-Specific Recommendations	**OECD Going for Growth Recommendations**
Reinforce the budgetary strategy: • Comply with the rules of the SGP • Implement ambitious structural reforms to increase the adjustment capacity and boost growth and employment • Minimise cuts in growth-enhancing investment, improve the targeting of social policies and the cost effectiveness of spending and the overall efficiency of the healthcare sector, broaden the tax base for example by addressing the issue of an extensive system of reduced VAT rates, and improve tax compliance, in particular by increasing the efficiency of the tax administration • Establish an independent fiscal council.	No similar recommendation

• Strengthen efforts to reduce youth unemployment in line with the objectives of a youth guarantee • Increase adult participation in lifelong learning • Combat labour market segmentation	No similar recommendation
• Continue efforts to increase female labour market participation • Include farmers in the general pension system • Phase out the special pension system for miners • Underpin the general pension reform by stepping up efforts to promote the employability of older workers to raise exit ages from the labour market	No similar recommendation
Improve the effectiveness of tax incentives in promoting R&D in the private sector as part of the efforts to strengthen the links between research, innovation and industrial policy, and better target existing instruments at the different stages of the innovation cycle.	No similar recommendation
• Renew and extend energy generation capacity and improve efficiency in the whole energy chain • Speed up and extend the development of the electricity grid • Ensure effective implementation of railway investment projects • Accelerate efforts to increase fixed broadband coverage • Improve waste management	Upgrade transport, communication and energy infrastructure
• Take further steps to improve the business environment by simplifying contract enforcement and requirements for construction permits. • Step up efforts to reduce costs and time spent on tax compliance by businesses. • Complete the ongoing reform aimed at facilitating access to regulated professions.	
No similar recommendation	Reduce public ownership and lower barriers to product market competition
No similar recommendation	Reduce labour taxes and reform the welfare system
No similar recommendation	Improve equity and efficiency of the education system
No similar recommendation	Reform housing policies
Spain	
European Semester Country-Specific Recommendations	**OECD Going for Growth Recommendations**
Reinforce the budgetary strategy: • Comply with the rules of the SGP • Implement ambitious structural reforms to increase the adjustment capacity and boost growth and employment • Ensure that the new independent fiscal authority becomes fully operational • Ensure a full implementation of the preventive, corrective and enforcement measures in the Budgetary Stability Organic Law at all levels of government • Carry out by February 2015 a systematic review of expenditure at all levels of government • Continue to increase the cost-effectiveness of the healthcare sector • Adopt by the end of 2014 a comprehensive tax reform • Step up the fight against tax evasion	No similar recommendation

• Complete reform of the saving banks sector • Promote banks' efforts to sustain strong capital ratios • Monitor the asset management company Sareb's activity in order to ensure timely asset disposal while minimising the cost to the taxpayer • Complete the ongoing measures to widen SMEs access to finance • Remove remaining bottlenecks in the corporate insolvency framework • Develop a permanent framework for personal insolvency	No similar recommendation
• Reduce labour market segmentation • Continue regular monitoring of the labour market reforms • Strengthen the job-search requirement in unemployment benefits • Enhance the effectiveness and targeting of active labour market policies • Accelerate the modernisation of public employment services • Ensure the effective application of public-private cooperation in placement services before the end of 2014 • Ensure the effective functioning of the Single Job Portal and combine it with further measures to support labour mobility	Improve active labour market policies Reduce the gap in job protection between temporary and permanent contracts
• Implement the 2013-2016 Youth Entrepreneurship and Employment Strategy and evaluate its effectiveness • Provide good quality offers of employment, apprenticeships and traineeships for young people • Increase the quality of primary and secondary education • Enhance guidance and support for groups at risk of early school leaving • Increase the labour-market relevance of vocational education and training and of higher education	Improve educational attainment in secondary education and access to tertiary education
• Implement the 2013-2016 National Action Plan on Social Inclusion • Strengthen administrative capacity and coordination between employment and social services • Improve the targeting of family support schemes and quality services favouring low-income households with children	No similar recommendation
• Ensure an ambitious and swift implementation of Law No 20/2013 on Market Unity at all levels of administration • Adopt an ambitious reform of professional services and of professional associations by the end of 2014 • Further reduce the time, cost and number of procedures required for setting up an operating business • Identify sources of financing for the new national strategy for science, technology and innovation and make operational the new State Research Agency.	Lower entry barriers in services industries
• Following the reform of 2013, ensure the effective elimination of deficit in the electricity system as of 2014 • Address the problem of insolvent toll motorways • Set up an independent body to contribute to the assessment of future major infrastructure projects by the end of 2014 • Take measures to ensure effective competition in freight and passenger rail services	No similar recommendation

• Implement at all government levels the recommendations of the committee for the reform of the public administration • Strengthen control mechanisms and increase the transparency of administrative decisions • Complete and monitor closely the ongoing measures to fight against the shadow economy and undeclared work • Adopt pending reforms on the structure of the judiciary and on the judicial map	No similar recommendation
No similar recommendation	Make wages more responsive to economic and firm-specific conditions
No similar recommendation	Reduce the disincentives for older workers to continue working
United Kingdom	
European Semester Country-Specific Recommendations	**OECD Going for Growth Recommendations**
Reinforce the budgetary strategy • Comply with the rules of the SGP • Consideration should be given to raising revenues through broadening the tax base • Address structural bottlenecks related to infrastructure, skills mismatches and access to finance for SMEs	No similar recommendation
• Increase the transparency of the use and impact of macro-prudential regulation in respect of the housing sector by the Bank of England's Financial Policy Committee • Deploy appropriate measures to respond to the rapid increases in property prices in areas that account for a substantial share of economic growth in the United Kingdom, particularly London, and mitigate risks related to high mortgage indebtedness • Monitor the Help to Buy 2 scheme and adjust it if deemed necessary • Consider reforms to the taxation of land and property • Continue efforts to increase the supply of housing.	No similar recommendation
• Maintain commitment to the Youth Contract • Ensure employer engagement by placing emphasis on addressing skills mismatches • Reduce the number of young people with low basic skills.	No similar recommendation
• Continue efforts to reduce child poverty in low-income households • Improve the availability of affordable quality childcare.	Strengthen work incentives by reforming welfare and childcare policies
• Continue efforts to improve the availability of bank and non-bank financing to SMEs. • Ensure the effective functioning of the Business Bank and support an increased presence of challenger banks.	No similar recommendation
• Follow up on the National Infrastructure Plan by increasing the predictability of the planning processes as well as providing clarity on funding commitments. • Ensure transparency and accountability by providing consistent and timely information on the implementation of the Plan.	No similar recommendation

No similar recommendation	Improve outcomes and equity in education
No similar recommendation	Improve public infrastructure, especially for transport
No similar recommendation	Strengthen public sector efficiency
No similar recommendation	Reform planning regulation

ANNEX 2: EUROPEAN SEMESTER 2015 RECOMMENDATIONS

Table 4: The 2015 recommendations for the euro-area and the five largest euro-area Member States

Euro area	1. Use peer pressure to promote structural reforms that facilitate the correction of large internal and external debts and support investment. Regularly assess the delivery of reforms in those Member States which require specific monitoring within the framework of the Macroeconomic Imbalances Procedure. Continue the regular thematic assessment of structural reforms. By spring 2016, take decisions on the follow-up to the coordination exercise on reducing the high tax wedge on labour and on reforming services markets. 2. Coordinate fiscal policies to ensure that the aggregate euro area fiscal stance is in line with sustainability risks and cyclical conditions. This is without prejudice to the fulfilment of the requirements of the Stability and Growth Pact. By spring 2016, hold thematic discussions on improvements in the quality and sustainability of public finances, focussing in particular on the prioritisation of tangible and intangible investment at national and EU levels, and on making tax systems more growth friendly. Monitor the effective functioning of the recently strengthened national fiscal frameworks. 3. Ensure the timely finalisation of the follow up of the Comprehensive Assessment carried out by the European Central Bank, implementation of Directive 2014/59/EU of the European Parliament and of the Council (1) (Bank Recovery and Resolution Directive), completion of the ratification of the Intergovernmental Agreement on the Single Resolution Fund and make the Fund fully operational as from January 2016. Promote measures to deepen market-based finance, to improve access to finance for SMEs and to develop alternative sources of finance. Encourage further reforms of national insolvency frameworks. 4. Take forward work on deepening Economic and Monetary Union, and contribute to the improvement of the economic surveillance framework in the context of the report on the next steps on better economic governance in the euro area, prepared by the President of the European Commission, Jean-Claude Juncker, in close cooperation with the President of the European Council, Donald Tusk, the President of the European Parliament, Martin Schulz, the President of the European Central Bank, Mario Draghi, and the President of the Eurogroup, Jeroen Dijsselbloem, and its follow-up.
France	1. Ensure effective action under the excessive deficit procedure and a durable correction of the excessive deficit by 2017 by reinforcing the budgetary strategy, taking the necessary measures for all years and using all windfall gains for deficit and debt reduction. Specify the expenditure cuts planned for these years and provide an independent evaluation of the impact of key measures. 2. Step up efforts to make the spending review effective, continue public policy evaluations and identify savings opportunities across all sub-sectors of general government, including on social security and local government. Take steps to limit the rise in local authorities' administrative expenditure. Take additional measures to bring the pension system into balance, in particular ensuring by March 2016 that the financial situation of complementary pension schemes is sustainable over the long term. 3. Ensure that the labour cost reductions stemming from the tax credit for competitiveness and employment and from the responsibility and solidarity pact are sustained, in particular by implementing them as planned in 2016. Evaluate the effectiveness of these schemes in the light of labour and product market rigidities. Reform in consultation with the social partners and in accordance with national practices, the wage-setting process to ensure that wages evolve in line with

	productivity. Ensure that minimum wage developments are consistent with the objectives of promoting employment and competitiveness. 4. By the end of 2015, reduce regulatory impediments to companies' growth, in particular by reviewing the size-related criteria in regulations to avoid threshold effects. Remove the restrictions on access to and the exercise of regulated professions, beyond the legal professions, in particular as regards the health professions as from 2015. 5. Simplify and improve the efficiency of the tax system, in particular by removing inefficient tax expenditure. To promote investment, take action to reduce the taxes on production and the corporate income statutory rate, while broadening the tax base on consumption. Take measures as from 2015 to abolish inefficient taxes that are yielding little or no revenue. 6. Reform the labour law to provide more incentives for employers to hire on open-ended contracts. Facilitate take up of derogations at company and branch level from general legal provisions, in particular as regards working time arrangements. Reform the law creating the *accords de maintien de l'emploi* by the end of 2015 in order to increase their take-up by companies. Take action in consultation with the social partners and in accordance with national practices to reform the unemployment benefit system in order to bring the system back to budgetary sustainability and provide more incentives to return to work.
Germany	1. Further increase public investment in infrastructure, education and research. To foster private investment, take measures to improve the efficiency of the tax system, in particular by reviewing the local trade tax and corporate taxation and by modernising the tax administration. Use the ongoing review to improve the design of fiscal relations between the federation, *Länder* and municipalities, particularly with a view to ensuring adequate public investment at all levels of government. 2. Increase incentives for later retirement. Take measures to reduce high labour taxes and social security contributions, especially for low-wage earners, and address the impact of fiscal drag. Revise the fiscal treatment of mini-jobs to facilitate the transition to other forms of employment. 3. Take more ambitious measures to stimulate competition in the services sector, in particular in professional services, by eliminating unjustified restrictions such as legal form and shareholding requirements and fixed tariffs. To this end, conclude the ongoing domestic review of these barriers and take follow-up measures. Remove the remaining barriers to competition in the railway markets, in particular in long-distance rail passenger transport.
Italy	1. Achieve a fiscal adjustment of at least 0,25 % of GDP towards the medium-term budgetary objective in 2015 and of 0,1 % of GDP in 2016 by taking the necessary structural measures in both 2015 and 2016, taking into account the allowed deviation for the implementation of major structural reforms. Ensure that the spending review is an integral part of the budgetary process. Swiftly and thoroughly implement the privatisation programme and use windfall gains to make further progress towards putting the general government debt ratio on an appropriate downward path. Implement the enabling law for tax reform by September 2015, in particular the revision of tax expenditures and cadastral values and the measures to enhance tax compliance. 2. Adopt the planned national strategic plan for ports and logistics, particularly to help promote intermodal transport through better connections. Ensure that the Agency for Territorial Cohesion is made fully operational so that the management of EU funds markedly improves. 3. Adopt and implement the pending laws aimed at improving the institutional framework and modernising the public administration. Revise the statute of limitations

	by mid-2015. Ensure that the reforms adopted to improve the efficiency of civil justice help reduce the length of proceedings. 4. By end-2015, introduce binding measures to tackle remaining weaknesses in the corporate governance of banks, implement the agreed reform of foundations, and take measures to accelerate the broad-based reduction of non-performing loans. 5. Adopt the legislative decrees on the design and use of wage supplementation schemes, the revision of contractual arrangements, work-life balance and the strengthening of active labour market policies. Promote, in consultation with the social partners and in accordance with national practices, an effective framework for second-level contractual bargaining. As part of efforts to tackle youth unemployment, adopt and implement the planned school reform and expand vocationally-oriented tertiary education. 6. Implement the simplification agenda for 2015-17 to ease the administrative and regulatory burden. Adopt competition-enhancing measures in all the sectors covered by the competition law, and take decisive action to remove remaining barriers. Ensure that local public services contracts not complying with the requirements on in-house awards are rectified by no later than end-2015.
Netherlands	1. Shift public expenditure towards supporting investment in R&D and work on framework conditions for improving private R&D expenditure in order to counter the declining trend in public R&D expenditure and increase the potential for economic growth. 2. With the strengthening of the recovery, accelerate the decrease in mortgage interest tax deductibility so that tax incentives to invest in unproductive assets are reduced. Provide for a more market-oriented pricing mechanism in the rental market and further relate rents to household income in the social housing sector. 3. Reduce the level of contributions to the second pillar of the pension system for those in the early years of working life.
Spain	1. Ensure a durable correction of the excessive deficit by 2016 by taking the necessary structural measures in 2015 and 2016 and using windfall gains to accelerate the deficit and debt reduction. Strengthen transparency and accountability of regional public finances. Improve the cost-effectiveness of the healthcare sector, and rationalise hospital pharmaceutical spending. 2. Complete the reform of the savings bank sector, including by means of legislative measures, and complete the restructuring and privatisation of state-owned savings banks. 3. Promote the alignment of wages and productivity, in consultation with the social partners and in accordance with national practices, taking into account differences in skills and local labour market conditions as well as divergences in economic performance across regions, sectors and companies. Take steps to increase the quality and effectiveness of job search assistance and counselling, including as part of tackling youth unemployment. Streamline minimum income and family support schemes and foster regional mobility. 4. Remove the barriers preventing businesses from growing, including barriers arising from size-contingent regulations; adopt the planned reform on professional services; accelerate the implementation of the law on market unity.

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QA-01-15-828-EN-C (paper)
QA-01-15-828-EN-N (pdf)

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PE 542.680

ISBN 978-92-823-8332-2 (paper)
ISBN 978-92-823-8331-5 (pdf)

doi:10.2861/244839 (paper)
doi:10.2861/14227 (pdf)