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STUDY

Economic policy coordination in the euro area under the European Semester

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Provided at the request of the
Economic and Monetary Affairs Committee

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Abstract

The European Semester is a yearly process of the European Union to improve economic policy coordination and ensure the implementation of the EU's economic rules. Each Semester concludes 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 beginning of the Semester in 2011, and has deteriorated since. The European Semester is not particularly effective at 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 continue to have major limitations.

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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, we make a positive (and not normative) assessment by taking Council recommendations made in the context of the European Semester as given and evaluating their implementation and consistency, without assessing the desirability of these recommendations. Section 4, which assesses options to improve compliance with the recommendations, is by definition more subjective.

The key conclusion of Section 2, which analyses the implementation of European Semester recommendations in comparison with OECD Going for Growth recommendations, is 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. In spite of the efforts made to improve the European Semester recent years the implementation index has even steadily fallen to 29 percent by 2014.
- Euro-area countries, for which policy coordination should be stronger in principle, implemented their recommendations only somewhat more than non-euro area countries (31 percent versus 23 percent for the 2014 recommendations), while the implementation rate fell steadily in both country groups from 2011-14.
- Despite huge efforts by European institutions to coordinate economic policies within the European Semester, the rate of implementation of these recommendations is not higher than the rate of implementation of the OECD's purely unilateral recommendations. Overlaps between the European Semester and OECD recommendations only partly explain this similarity.
- The rate of implementation of recommendations related to the Stability and Growth Pact (SGP) is 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 rate is even lower, suggesting that the European Semester is not particularly effective in enforcing the EU's fiscal and macroeconomic imbalance rules.
- 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 those countries, reform momentum fades once the situation normalises.

Section 3 takes the 2015 recommendations for the euro area as given and assesses their consistency with the country-specific recommendations (CSRs) to 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):

- On 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 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 even state what this aggregate stance is. There is no top-down approach to determine national fiscal stances that correspond with the optimal aggregate, and it is therefore accidental if the sum of country-specific fiscal stances corresponds with 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 euro-area 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 Italy, the Netherlands and Spain.
- The euro-area 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 well reflected in the CSRs of the five largest euro-area countries. Each country, except for the Netherlands, received a recommendation to reform its services sector.
- While a recommendation on the need for symmetric intra-euro adjustment was made for the euro area in 2012, 2013 and 2014, it was not included in the 2015 recommendations.

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

- The proposal to split the European Semester into two stages, with only euro-area issues discussed in the first stage and country-specific issues reflecting the euro-area conclusions in the second stage, is a welcome reform. Yet in the absence of a euro-area instrument for stabilising economic cycles or a mechanism to force countries to run 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 (ie 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, and the available fiscal space.
- Decentralisation efforts, such as the establishment of national competitiveness authorities and a greater involvement of national governments, parliaments and social partners in discussions and decisions on the reform process, are welcome. These measures would likely increase domestic ownership of the reform process, which would be a great improvement, though we are sceptical about whether cross-country spillover effects will be better internalised.
- Formalising the convergence process might help the reform process, but we see major difficulties in the definition of benchmarks, in making them binding and in 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 that have sound fiscal positions.
- *Ex post* monitoring of reform implementation by an independent EU-level “structural council” would be worthwhile to consider, not least because it could improve transparency and could highlight the steps the European Commission may take to improve the cross-country consistency of CSRs.

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. For 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 recommendations can lead to warnings, further recommendations and enhanced monitoring, and in the case of EDP and EIP requirements, non-compliance can even lead to financial sanctions (see Box 1).

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, which aims to achieve greater focus, and allows more discussion time and more opportunities to engage on substance with various stakeholders. Also, in June 2015 the so-called “Five Presidents’ Report” (Juncker, 2015) set out a plan for strengthening the Economic and Monetary Union, and on 22 October 2015, the European Commission published a first set of concrete proposals (European Commission, 2015b). 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. The proposed package of measures also includes the introduction of national Competitiveness Boards and an advisory European Fiscal Board, a more unified representation of the euro area in international organisations, and steps towards a Financial Union, notably via a European Deposit Insurance Scheme.

In this Briefing Paper, we first analyse the track record of implementation of CSRs made in 2011-14 in comparison to the implementation of the OECD's Going for Growth recommendations. We then evaluate the consistency between the 2015 euro-area recommendations and CSRs. Finally, we discuss various proposals for improving the effectiveness of the European Semester.

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.

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

We calculate a *European Semester reform implementation index*, which ranges between zero (no or limited progress on all recommendations) and one (full implementation of, or substantial progress on, all recommendations), as described in Box 2. The index is primarily based on the assessments of the European Commission. 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 every year since 2011 was 40 percent. This number does not mean that 40 percent of the reforms were implemented in 2011; rather, it is an indication of reform efforts. If “some progress” would have been achieved on all recommendations, our indicator would take the value of 50 percent. Since the aim of the recommendations is their implementation, one would expect some recommendations to be fully implemented, and at least some progress with others, so a score well above 50 percent would be appropriate. We therefore consider that the 40 percent score is modest at best. Yet instead of improved implementation in later years as the European Semester matured, the implementation index fell steadily to 29 percent in 2014. In 2014, out of the 157 main recommendations issued to European countries, only 10 were fully implemented or showed substantial progress². There was some progress on 70 main recommendations, while there was no or limited progress on 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.

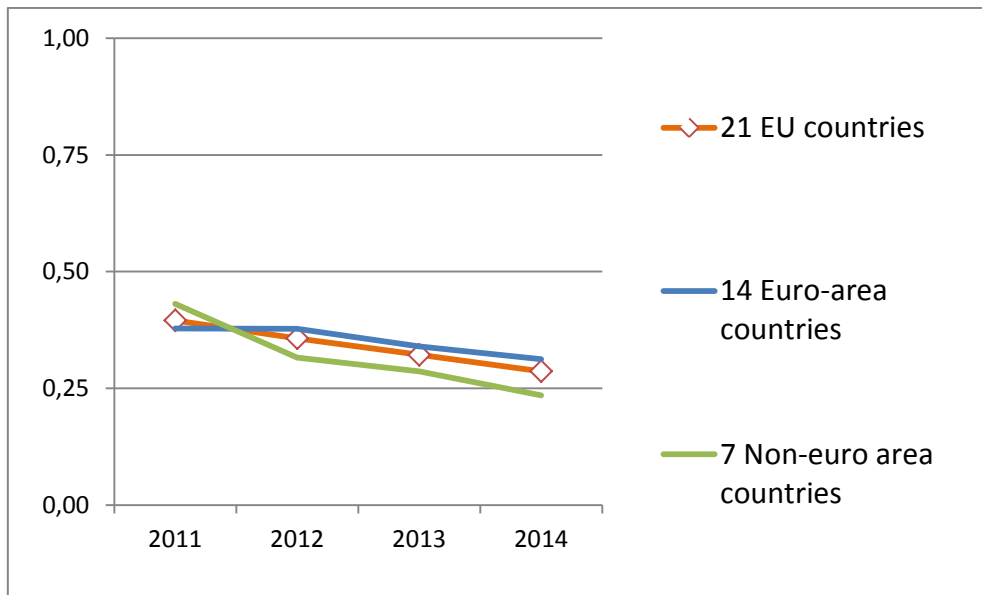
Box 2: Calculation of a European Semester reform implementation index

In order to assess the implementation of recommendations under the European Semester we build on the work by Deroose and Griesse (2014), and calculate a reform implementation index, which ranges between zero (no or limited progress on all recommendations) and one (full implementation of, or substantial progress on, all recommendations). The index is based on the qualitative assessment included in various European Parliament reports¹, which in turn primarily depend on the European Commission's own assessment¹, 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”, “limited progress” and “no progress”. Deroose and Griesse (2014) create a synthetic indicator using the 5-scale assessment for 2012-13, by giving scores of 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 might 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 might increase over time. But very few recommendations have been fully implemented and partial implementation of a recommendation in one year might be followed by the same recommendation the next year, which would be easier to implement given the partial implementation of the previous year's recommendation. Also, most recommendations included several sub-recommendations. 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 an overall assessment for the main recommendations¹. 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.

² On average, 6 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, Portugal, Slovenia and the United Kingdom.

Figure 1: European Semester reform implementation index, 2011-14



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 (ie 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 or 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. The OECD recommendations are not part of any cross-country surveillance process and therefore there is no mechanism to coordinate these reforms across countries or 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 for 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 (for 16 EU countries) shows a striking result: the two indicators are practically the same for those countries for which both European Semester and OECD recommendations were 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). However, 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 OECD's purely unilateral recommendations, 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

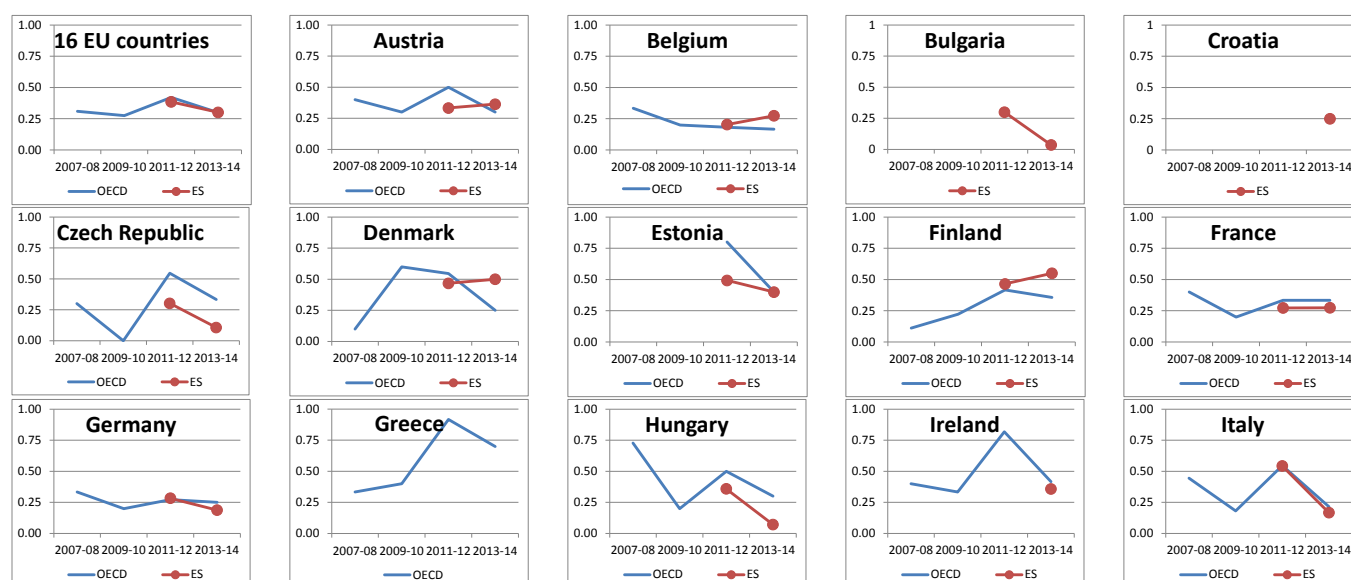
(42 percent). The somewhat higher rate in 2011-12 could be explained by increased efforts during the crisis, but from 2007-08 to 2013-14 there was no increase in reform implementation, notwithstanding the new European economic governance frameworks.

The other panels of Figure 2 show the two indicators (when available) for all EU countries except Cyprus, and for the United States and Japan³. 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, implement the most. The highest reform responsiveness rate, 92 percent, was 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, a country undergoing severe macroeconomic adjustment, had a high score too (80 percent). Next in the ranking is Spain with a reform responsiveness rate of 70 percent. The only other occasion with a similarly high reform responsiveness rate was for Hungary in 2007-08 (73 percent), when Hungary had already started a major fiscal and macroeconomic adjustment process. In all of these countries, the reform responsiveness rate fell in the next time period (though it 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).

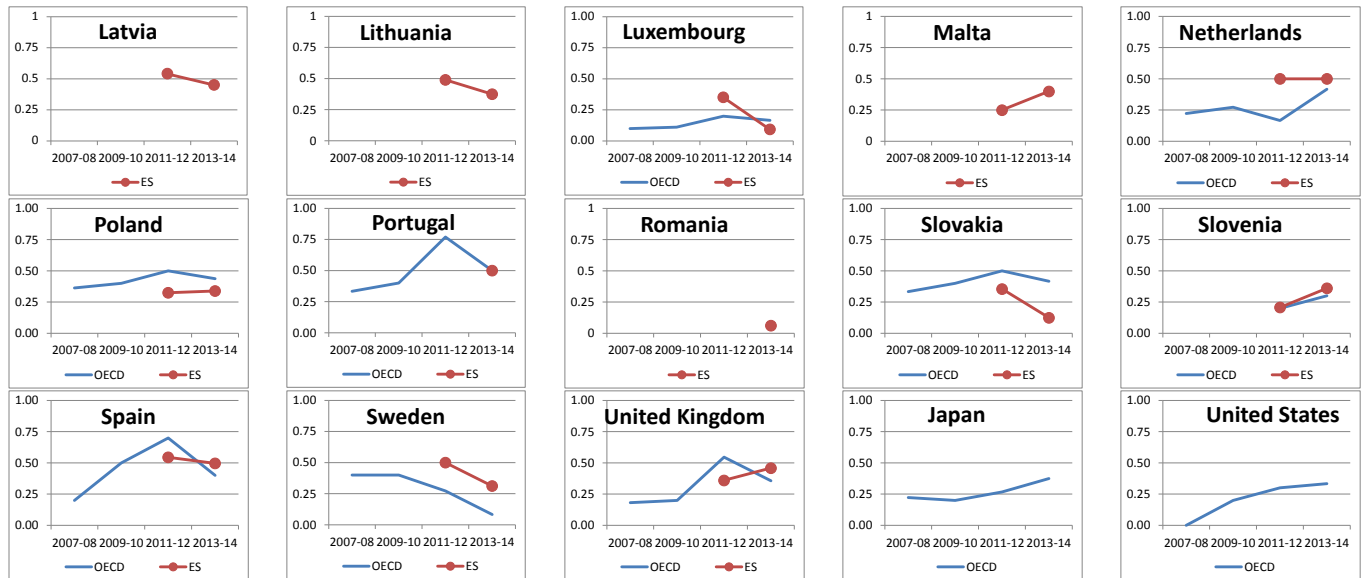
For those countries not under a financial assistance programme, or not undergoing severe macroeconomic adjustment, the reform implementation index remained very low, a result which also holds for the United States and Japan⁴. This suggests that implementation of reform suggestions coming from international organisations is generally low and that the European Semester was not able to improve this situation.

Figure 2: Reform implementation: comparison of European Semester and OECD Going for Growth recommendations, 2008/9-2013/14



³ 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.

⁴ 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.



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 included in the European Semester: the Stability and Growth Pact (SGP) and the Macroeconomic Imbalance Procedure (MIP), in comparison to recommendations that are not related to either of these procedures. Again, our indicators are based on the European Commission's assessment.

Given that the SGP has strong legal enforcement 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, but this procedure has not been activated for any country so far. The MIP has six phases ranging from “No imbalances” to “Excessive imbalances, which require decisive policy action and the activation of the Excessive Imbalance Procedure”. Recommendations are more binding when the Excessive Imbalance Procedure is activated. Table 1 shows the 2015 status of the MIP.

Table 1: Situation of Member States with regard to the Macroeconomic Imbalances Procedure in 2015

MIP Category	Member States in 2015*
No imbalances	Austria, Czech Republic, Denmark, Estonia, Lithuania, Luxembourg, Latvia, Malta, Poland and Slovakia
Imbalances, which require policy action and monitoring	Belgium Netherlands, Romania**, Finland, Sweden, United Kingdom
Imbalances, which require decisive policy action and monitoring	Hungary, Germany

Imbalances, which require decisive policy action and specific monitoring	Ireland, Spain, Slovenia
Excessive imbalances, which require decisive policy action and specific monitoring	Bulgaria, France, Croatia, Italy, Portugal
Excessive imbalances, which require decisive policy action and the activation of the Excessive Imbalance Procedure	

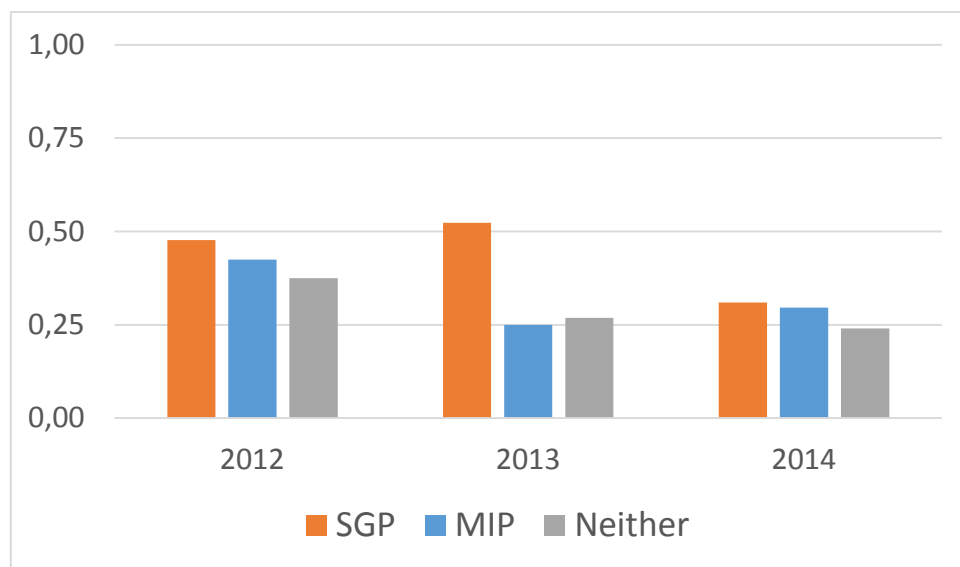
* Cyprus and Greece are in a macroeconomic adjustment programme.

** Romania is in a precautionary financial assistance programme.

Source: Box 1 of European Commission (2015b).

Figure 3 shows that the implementation rate of recommendations related to the SGP tends to be higher than that for the MIP and other recommendations. The difference was particularly large for the 2013 recommendations, but 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 effective in enforcing the EU's fiscal rules.

Figure 3: European Semester implementation rates according to the type of recommendations, 2012-14



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. In spite of the efforts made to improve the European Semester recent years the implementation index has even steadily fallen to 29 percent by 2014.

- Euro-area countries, for which policy coordination should be stronger in principle, implemented their recommendations only somewhat more than non-euro area countries (31 percent versus 23 percent for the 2014 recommendations), while the implementation rate fell steadily in both country groups from 2011-14.
- Despite huge efforts by European institutions to coordinate economic policies within the European Semester, the rate of implementation of these recommendations is not higher than the rate of implementation of the OECD's purely unilateral recommendations. Overlaps between the European Semester and OECD recommendations only partly explain this similarity.
- The rate of implementation of recommendations related to the Stability and Growth Pact (SGP) is typically higher (44 percent on average in 2012-1) 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 rate is even lower, suggesting that the European Semester is not particularly effective in enforcing the EU's fiscal and macroeconomic imbalance rules.
- 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 those countries, reform momentum fades once the situation normalises.

3. THE 2015 EURO-AREA RECOMMENDATIONS

On 14 July 2015, the European Council adopted four recommendations for the euro area⁵:

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 MIP; regular thematic assessment of structural reforms; a coordination exercise to reduce the 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 to 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 that includes a reference to the Five Presidents’ report.

Since our goal 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 adjustment within the euro area, even though such a recommendation was 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”*.

Our assessment of the four recommendations (and the lack of a recommendation for a more symmetric adjustment) takes three factors into account:

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

3.1 The specifics of the 2015 euro-area recommendations

The specific recommendations that underpin the first two euro-area recommendations are unlikely to be sufficient for achieving the stated goals. The third and fourth euro-area recommendations are more general and therefore such assessment cannot be made.

⁵ The full text of the recommendations is presented in Appendix 2.

1. As highlighted in the previous section, implementation of European Semester recommendations has been rather weak and even declining from 2011-14. While it is important to improve compliance, recommendation No. 1 made in 2015 does not seem to have had any power to improve compliance. Peer pressure did not work in the last 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 given of 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, but they are not directly linked to 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 to a common deposit insurance facility, which has become an intensively discussed topic⁶.
4. Given that the Five Presidents’ Report was published shortly ahead of the July 2015 European Council meeting, a reference to this report was a must. We generally find the level of ambition of the Five Presidents’ Report weak, but a detailed assessment of that report is beyond the scope of this Policy Contribution.

3.2 Consistency of euro-area and country-specific recommendations

We classify the 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. Recommendations that 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*”.

⁶ We note that the European Commission is in favour of developing a common deposit insurance scheme, as it is spelled out in its 21 October 2015 communication (see European Commission 2015b).

Euro-area recommendations belonging to the first two categories concern the Eurogroup and should not be repeated in country-specific recommendations. Recommendations on the implementation of existing laws should not be repeated in country-specific recommendations either, while ratification of agreements 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, offers a good prospect for their implementation.

None of the category 4 recommendations include numerical targets, which complicates the assessment of their consistency with CSRs, while next year this feature will give the Commission much freedom to assess compliance with these recommendations. In our assessment we assume that the aim is to achieve ‘significant’ progress towards these economic goals and therefore we assess whether CSRs, if implemented, would be able to achieve ‘significant’ (as opposed to ‘marginal’) progress.

3.2.1 The aggregate fiscal stance

Over the past few years, the EU institutions have started paying more attention to the aggregate fiscal stance of the euro area. While the first 2011 European Semester did not include a recommendation on the aggregate fiscal stance, such a recommendation has been made in all subsequent rounds of the Semester (Table 2). The wording has been slightly different in different rounds, but the main message has been 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 2: Evolution of euro-area recommendations about the euro-area aggregate fiscal stance, 2011-15

Year	Recommendation
2011	The 2011 euro area recommendations did not include any mention of the aggregate fiscal stance.
2012	<i>“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”</i>
2013	<i>“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”</i>
2014	<i>“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 area”</i>
2015	<i>“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”</i>

European Central Bank president Mario Draghi also emphasised the importance of the aggregate fiscal stance in his Jackson Hole speech in 2014 (Draghi, 2014): “*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*”.

However, notwithstanding the recognition by the Council, the European Commission and President Draghi of the importance of the aggregate fiscal stance, we find that the reference to the aggregate euro-

area fiscal stance by the Council in euro-area and country-specific recommendations is little more than empty rhetoric. First, 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 conditions⁷, it is more a value judgement than the result of rigorous analysis, and the Council has not adopted this judgement.

Second, irrespective of the way the optimal fiscal stance is defined, the approach to achieving a desired aggregate fiscal stance is not top-down, 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 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 reached because of two reasons: (1) countries with high debt may not have achieved sufficient fiscal consolidation to bring down public debt, and (2) countries with more fiscal space may not have seized 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 consider aspect (2) by referring 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 of 13 May 2015 included a slight attempt at fostering a reduction of the fiscal surplus⁸:

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

However, 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, similar to the right of a government to adopt a tighter fiscal policy than what is suggested by its fiscal council. But the removal of the reference to the use of the available fiscal space underlines that even though the Council acknowledged that one of the two aspects of sub-optimal fiscal policy coordination is that countries with fiscal space do not encourage domestic demand, no attempt is needed to remedy this problem⁹.

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 euro-area countries are not consistent with this aggregate view. For France and Spain the fiscal consolidation recommendation is in-line with the on-going

⁷ 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.*”

⁸ 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.

⁹ 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.

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 euro-area countries (France, Italy and Spain) should have been compensated for by fiscal expansion in other large countries, but this was not recommended to Germany or the Netherlands¹⁰.

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 investment¹¹. 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 Council's four euro-area recommendations. Yet we conclude that this euro-area goal is not well reflected in CSRs.

For France, the 5th CSR includes a reference to 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 investment.

- Public investment: As we noted above, the Commission's proposal to use “*the available fiscal space*” was deleted by the Council from the German recommendation on 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, the effects of which were simulated in the Commission Staff Working Document on the euro area, as we noted above. France, Italy and Spain did not receive recommendations to increase public investment.

¹⁰ We note that the actual aggregate fiscal stance of the euro area may even be expansionary in 2015, if countries which are required to consolidate do not to comply with their recommendations and if the large inflow of refugees and migrants into the EU necessitates extra public spending. However, the role of this Policy Contribution is not to speculate about expected outcomes, but to assess the consistency of recommendations.

¹¹ 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.

- Private investment: 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.

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 Report¹², 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 such a reference is to be expected.

3.2.4 Reduce the high tax wedge on labour

The first euro-area recommendation includes a sub-recommendation on reducing high tax wedges on labour. The importance of this issue is also mentioned in the preamble to 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 were 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 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*

¹² European Commission (2014) [“Alert Mechanism Report 2015”](#), Brussels, 28 November, COM(2014) 904 final

the planned reform on professional services”. There is no 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, received a recommendation to reform its services sector in some way.

3.3 Lack of symmetric adjustment within the euro area

In 2012, 2013 and 2014, the Council made recommendations for more symmetric adjustment within the euro area, but the recommendation has disappeared by 2015 (Table 3).

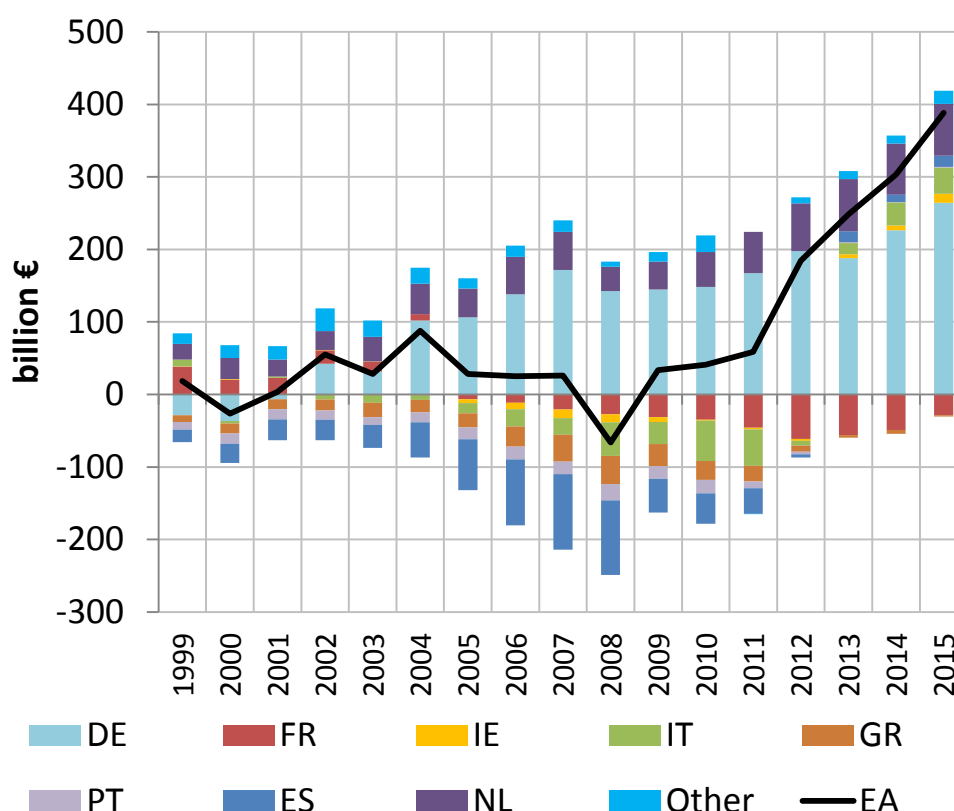
Table 3: Evolution of euro-area recommendations concerning symmetric intra-euro adjustment in 2011-15

Year	Recommendation
2011	The 2011 euro area recommendations did not include any mention of symmetric adjustment and intra-euro area macroeconomic imbalances
2012	<i>“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.”</i>
2013	<i>“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”</i>
2014	<i>“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.”</i>
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 was made: *“Foster appropriate policies in countries with large current account surpluses to contribute to positive spillovers.”* It is very surprising 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 the 2015 recommendations for the euro area. Relevant recommendations are not included in CSRs either.

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

Figure 4: Current account balance of the euro area, 1999-2015



Source: AMECO database November 2015

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 have already highlighted, might 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*”¹³.

As the Commission argues in its Staff Working Document accompanying its 2015 CSRs to Germany, Germany’s close links to 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*”¹⁴, 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.

¹³ 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

¹⁴ 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

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.

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):

- On 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 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 even state what this aggregate stance is. There is no top-down approach to determine national fiscal stances that correspond with the optimal aggregate, and it is therefore accidental if the sum of country-specific fiscal stances corresponds with 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 euro-area 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 Italy, the Netherlands and Spain.
 - The euro-area 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 well reflected in the CSRs of the five largest euro-area countries. Each country, except for the Netherlands, received a recommendation to reform its services sector.
- While a recommendation on the need for symmetric intra-euro adjustment was made for the euro area in 2012, 2013 and 2014, it was not 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 2011-14 CSRs has been weak and has even declined, and that there are major consistency problems between the 2015 euro-area recommendations and CSRs, are in sharp contrast to the self-congratulation included in the Commission Staff Working Document on the Euro Area¹⁵. 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. Thus some of the proposals of Hallerberg, Marzinotto and Wolff (2012a, 2012b) have been adopted. The length of recommendations generally increased between 2011 and 2014, while there was a major cut-back in 2015.

Recent proposals to revamp the European Semester go in the right direction. According to the Five Presidents’ report, and a European Commission communication on 21 October 2015 (European Commission, 2015b), 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 CSRs be discussed and decided on, which should reflect the common challenges identified in the first stage. In our view, this is a welcome reform of the European Semester.

On 21 October 2015, the Commission also issued its decision on the establishment of an independent advisory European Fiscal Board (European Commission, 2015c). This board 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 in our view 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 that 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 of the Fiscal Board when deciding about euro-area recommendations and CSRs. But even if the Fiscal Board one day concludes that some countries should have more expansionary fiscal policies, 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

¹⁵ “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]

countries can be required to enact fiscal expansion. 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, 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.

In terms of 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 made by Sapir and Wolff (2015) and endorsed by the Five Presidents' report. On 21 October 2015 the European Commission proposed a recommendation for a Council Recommendation on the establishment of National Competitiveness Boards within the euro area (European Commission, 2015e). The national councils will assess wage and productivity developments and 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, through which reform priorities would be defined nationally. It will likely increase the ownership of the reform process because 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 from Brussels. In our view, this is a highly welcome proposal. However, it needs to be seen to what extent national councils would be able to internalise the cross-border implications of the reform process, and we are sceptical about this. The proposed recommendation includes a reference to euro-area considerations: *"The Commission should facilitate coordination between national competitiveness boards and exchange views with them, in particular to ensure the consideration of euro-area and EU objectives in the work of the boards."* While discussions and information exchanges can foster mutual understanding of cross-country spillover effects of domestic policies, ultimate decisions remain national. So far the MIP has been ineffective in internalising cross-country spillover effects, partly due to major disagreements in the importance of such affects, and therefore it remains to be seen if the coordination of national competitiveness boards would be able to achieve common understanding leading to policy actions. Nevertheless, the establishment of such competitiveness boards would be a major improvement compared to the current governance framework in our view, even if the national boards primarily focus on the domestic consequences of the reform process.

4.2 Further possible reforms

4.2.1 The aggregate fiscal stance

Political federations have central and sub-central budgets. In a federation, fiscal stabilisation (which has implications for the aggregate fiscal stance of the federation) is mostly the job of the federal government through automatic stabilisers and discretionary fiscal decisions. The euro area is not a political federation and it does not have a central budget. The EU has a budget, but its aim is not fiscal stabilisation. We believe that a euro-area fiscal stabilisation instrument would be more helpful for aligning the aggregate fiscal stance with the aggregate economic situation of the euro-area (see, for example, Darvas, 2012; Wolff, 2012; Pisani-Ferry, Vihriälä and Wolff, 2013) than the coordination of fiscal policies of member states. A federal stabilisation instrument could also leave national fiscal policies to follow national preferences when fiscal rules are not binding. However, there are also opposing views about the desirability of a (small) euro-area budget or any other centralised fiscal stabilisation instrument. Opponents argue that if European fiscal rules are met, member states will have sufficient room for manoeuvre for stabilizing their own economic cycles using their own fiscal policies. In any case, the Five Presidents' report incorporated a related proposal only for the long term, so we do not expect a euro-area fiscal instrument in the foreseeable future.

Similarly, the prospect of a euro-area mechanism that would force countries to have higher budget deficits, as suggested by, for example, Sapir and Wolff (2015), is extremely unlikely. As we highlighted earlier, even the modest attempt of the European Commission to include in Germany's 2015 CSR 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 that might force them to have deficits that are larger than their domestic preferences would deem appropriate.

In the absence of a euro-area fiscal stabilisation instrument or a mechanism to force countries to have larger budget deficits, the remaining options to influence the aggregate fiscal stance are rather limited. In any case, the European Fiscal Board should be entrusted with the definition of an unconstrained optimal aggregate fiscal stance (ie 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 and for each euro-area member state. Such an exercise would help foster discussions, but the problem will remain that there will be no enforcement mechanism to require expansionary fiscal policy.

To sum up, we see it as extremely unlikely that any coordination mechanisms or the use of the MIP would enable countries to be forced to have larger deficits than 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

A number of proposals have been made on the implementation of structural reforms. The IMF (2015b) and Banerji *et al* (2015) 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 significant variations between the countries that 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 from the EU to cover reform costs and support implementation, a proposal that 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 into such a contract might fall quickly. Even if the reform proposal originally comes from the country in question, domestic stakeholders might 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 to countries that implement European Semester reform suggestions, would reward countries that are slow to implement reforms. Those countries that followed the European Semester advice earlier would not benefit from such a contract, while providing retroactive contracts to reward those countries that have already implemented reforms would lead to a very messy system.

Moreover, financial incentives would not really matter for larger countries with sound fiscal positions. For example, we see it as inconceivable that Germany would speed up services market reforms on the basis that it would receive a few billion euros from other euro-area countries.

Banerji *et al* (2015) also suggest *ex post* monitoring of reform implementation by an independent EU-level “structural council”. We find this proposal worthwhile to consider, not least because an independent evaluation could improve transparency and could highlight the steps the European Commission could take to improve the cross-country consistency of CSRs.

In terms of 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 the economic and monetary union point in the right direction. For example, Hallerberg, Marzinotto and Wolff (2012a, 2012b) suggested enhancing the role of national parliaments at the EU level, enhancing the role of European institutions at member-state level and increasing the role of the European Parliament in the European Semester. These suggestions are endorsed by the Five Presidents’ report. Similarly to the establishment of national competitiveness councils, we see the greater involvement of national parliaments, governments and social partners in the discussion of the reform process as a means 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:

- The proposal to split the European Semester into two stages, with only euro-area issues discussed in the first stage and country-specific issues reflecting the euro-area conclusions in the second stage, is a welcome reform. Yet in the absence of a euro-area instrument for stabilising economic cycles or a mechanism to force countries to run 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 (ie 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, and the available fiscal space.
- Decentralisation efforts, such as the establishment of national competitiveness authorities and a greater involvement of national governments, parliaments and social partners in discussions and decisions on the reform process, are welcome. These measures would likely increase domestic ownership of the reform process, which would be a great improvement, though we are sceptical about whether cross-country spillover effects will be better internalised.
- Formalising the convergence process might help the reform process, but we see major difficulties in the definition of benchmarks, in making them binding and in 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 that have sound fiscal positions.
- *Ex post* monitoring of reform implementation by an independent EU-level “structural council” would be worthwhile to consider, not least because it could improve transparency and could highlight the steps the European Commission may take to improve the cross-country consistency of CSRs.

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

Table 4 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 4: The 2014 European Semester vs the 2013 OECD Going for Growth recommendations

France	
European Semester Country-Specific Recommendations	OECD Going for Growth Recommendations
Reinforce the budgetary strategy: <ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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

<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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: <ul style="list-style-type: none"> • 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: <ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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: <ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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

<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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: <ul style="list-style-type: none"> • 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

<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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: <ul style="list-style-type: none"> • 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

<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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

<ul style="list-style-type: none"> • 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 <ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • 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 5: The 2015 recommendations for the euro-area and the five largest euro-area Member States

Euro area	<p>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.</p> <p>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.</p> <p>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.</p> <p>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.</p>
France	<p>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.</p> <p>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.</p> <p>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</p>

	<p>productivity. Ensure that minimum wage developments are consistent with the objectives of promoting employment and competitiveness.</p> <p>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.</p> <p>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.</p> <p>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 <i>accords de maintien de l'emploi</i> 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.</p>
Germany	<p>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, <i>Länder</i> and municipalities, particularly with a view to ensuring adequate public investment at all levels of government.</p> <p>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.</p> <p>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.</p>
Italy	<p>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.</p> <p>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.</p> <p>3. Adopt and implement the pending laws aimed at improving the institutional framework and modernising the public administration. Revise the statute of limitations</p>

	<p>by mid-2015. Ensure that the reforms adopted to improve the efficiency of civil justice help reduce the length of proceedings.</p> <p>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.</p> <p>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.</p> <p>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.</p>
Netherlands	<p>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.</p> <p>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.</p> <p>3. Reduce the level of contributions to the second pillar of the pension system for those in the early years of working life.</p>
Spain	<p>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.</p> <p>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.</p> <p>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.</p> <p>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.</p>



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