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**Commission's Recommendation  
for the Broad Guidelines of the Economic Policies  
of the Member States and the Community**

drawn up in conformity with Article 103 (2) of the  
Treaty establishing the European Community

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## I. GENERAL ECONOMIC POLICY GUIDELINES

### 1. Main priority: strong, sustainable growth and employment

#### *1.1 Launch of the euro*

The successful birth of the euro on 1 January 1999 constituted a milestone in the process of European integration. It is the culmination of an unprecedented degree of economic and political co-operation. This process has deeply transformed the structure and functioning of the EU economy and has made an essential contribution to prosperity and stability within the Union. The introduction of the euro is bound to act as a powerful lever for further economic and political integration and to strengthen the Union's economic and political position in the world economy.

At the same time, new challenges lie ahead. More than ever, economic and social conditions in each of the participating Member States will be profoundly influenced by economic developments and policies in partner Member States. The durable success of economic and monetary union will demand discipline from all policy actors, including the social partners, as well as deepened and strengthened policy co-ordination.

The new institutional framework and enhanced surveillance and co-ordination instruments ensure that economic policy making in the euro area rests on solid foundations that have the potential to achieve substantial benefits in terms of durably higher economic growth and

employment. However, the realisation of this potential is not assured. Exploiting to the full and in a resolute and co-ordinated manner the mutually-reinforcing effects of stability-oriented macroeconomic policies and sound structural policies will be the key. By pursuing this overall sound policy approach, the euro area will also make a positive contribution to solving global economic problems.

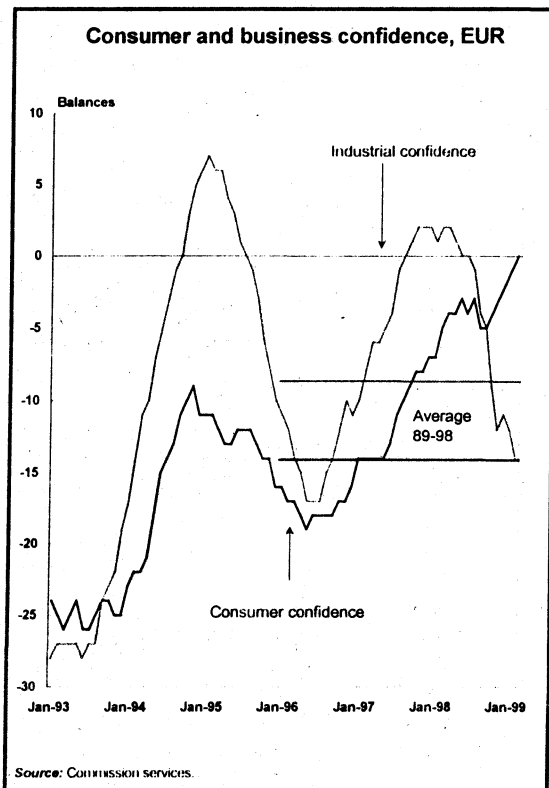
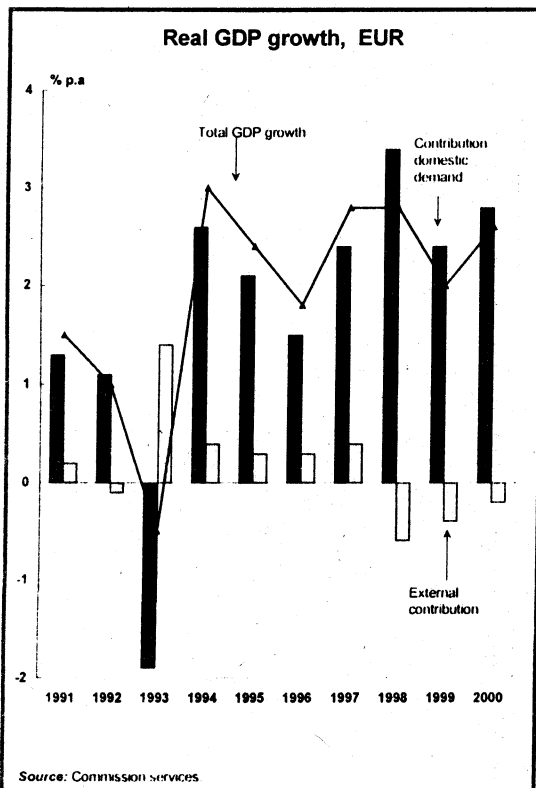
#### *1.2 Economic and employment situation*

Since the summer of 1998, when the previous Broad Economic Policy Guidelines were adopted, the recovery of the EU economy lost momentum. This essentially reflects the direct and indirect impact of the sharp deterioration in the world economic situation on exports and investment in the Union. On the back of sound economic fundamentals and confidence-building economic policies, economic activity should soon regain its momentum and accelerate further and above the potential rate in 2000, in the context of continued low inflation.

The pace of job creation in the EU quickened markedly during the last two years and in late 1998 the EU unemployment rate dropped below 10 % for the first time since 1992. Employment growth is expected to continue at a moderate pace, implying a further, albeit gradual, reduction in unemployment.

However, at about 61 % in 1998, the employment rate in the EU as a whole is low, both in historical and international comparative terms. Achieving a significantly higher employment rate and lower unemployment rate over the medium term would be beneficial for improving living standards significantly, facilitating the sustainability of public finances and ensuring a cohesive society. The overall EU employment situation masks, however, important differences between countries. The countries that have made most progress in structural reforms while pursuing sound macro-economic policies, have achieved the greatest improvement in their employment and growth performance in recent years.

A rapid rise of production capacity is required to achieve a high employment rate. It is essential, therefore, that the currently favourable investment conditions, in terms of high profitability and low interest rates, are fully exploited. In addition, the realisation of the transeuropean transport, energy and communication networks should be actively pursued. Investment in infrastructure, knowledge and skills should also be enhanced to accelerate the development of the high-technology, high-skilled and service-based sectors of the economy. The Community's financial instruments and the EIB are already playing a key role. These efforts should be stepped up and partnerships between the public and private sectors should be encouraged.



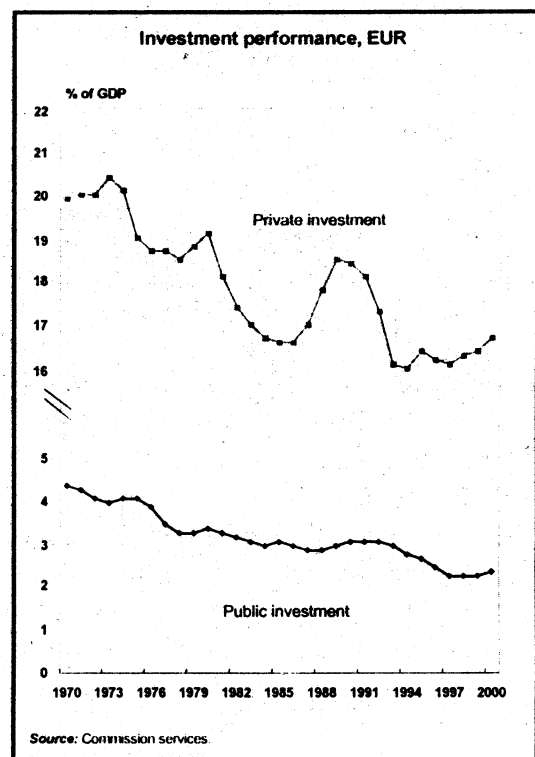
### 1.3 Policy strategy for growth and employment

Europe's employment challenge has become the key priority for economic policy. The successful launch of the euro and a well-functioning EMU set a favourable framework. However, the achievement over the medium term of high and sustainable growth and employment will require a comprehensive and coherent strategy that consists of three mutually-reinforcing key components:

- (i) sound macroeconomic policies that are conducive to growth, employment and price stability, involving full respect of the Stability and Growth Pact and continued appropriate wage developments;
- (ii) policies that improve the overall functioning of labour markets and in particular improve employability, entrepreneurship, adaptability and equal opportunities via a steadfast, prompt and transparent implementation of the Employment Guidelines tailored to Member States' conditions; and
- (iii) economic reforms that enhance the efficiency and flexibility of goods, services and capital markets and favours an environmentally sustainable growth path, involving a close monitoring of the Single Market, a vigorous competition policy, regulatory reforms and more efficient taxation systems.

### 1.4 Towards a European Employment Pact

The pursuit of this strategy by all actors will be essential to contain the depth and duration of the slowdown on the one hand and to achieve self-sustaining, non-inflationary, investment-supported growth over the medium and longer term on the other. To this end, on the national and the European level, all economic policy actors have to deliver their respective contributions with regard to appropriate wage developments, sound public finances, economic reforms and a stability-oriented monetary policy. To place the responsibility for an appropriate policy mix unilaterally on one of the actors would entail social tensions and result in economically non-optimal outcomes.



All actors and groups of actors are urged to co-ordinate closer and better their policy actions with a view to realising positive synergies, including the greater synergy requested by the Vienna European Council between the Broad Economic Policy Guidelines and the Employment Guidelines. In this context, it will be essential to enhance the policy dialogue on the basis of mutual trust on both the national and European level, with particular emphasis to be given to improve the effectiveness of the policy co-ordination in the Council and reinforce the dialogue between the Commission, Council, the ECB and the social partners.

On this basis, the European Employment Pact should define the process whereby

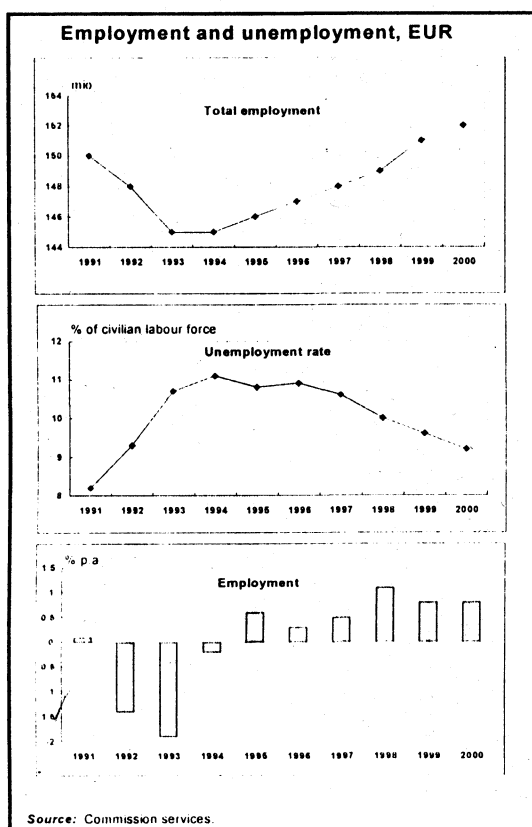
all the policy actors enter into a dialogue with a view to achieving the Union's central economic and social objective of high employment within the framework of a strong and sustained medium-term growth process.

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The 1999 Broad Economic Policy Guidelines consist of general guidelines and country-specific guidelines that are equally valid. The general guidelines, which are applicable to all Member States, indicate the required direction of economic policies. Within this broader frame, the country-specific guidelines seek to identify economic policy priorities for each Member State, taking account of their particular circumstances. It must be noted in this context that Member States are currently revising their National Action Plans for Employment to take account of the 1999 Employment Guidelines. The country-specific guidelines, in so far as labour market issues are concerned, are therefore intended to complement the 1999 Employment Guidelines and to underpin implementation of the revised National Action Plans. Finally, the basis for the 1999 Broad Economic Policy Guidelines is the economic situation and outlook in the Member States and the Union as outlined in the Commission services' Spring 1999 Economic Forecasts. Although a substantially different unfolding of economic developments would not profoundly alter the strategy articulated in the guidelines, it might nevertheless require an adjustment of the policy setting.



## 2. Growth and stability-oriented macroeconomic policies

### 2.1 Macroeconomic policy mix in the euro area

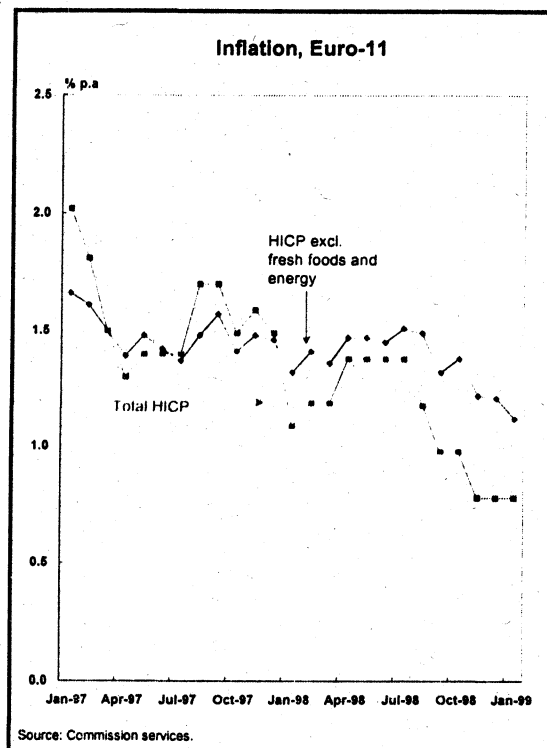
A policy mix conducive to growth, employment and stability in the euro area should contain the following elements:

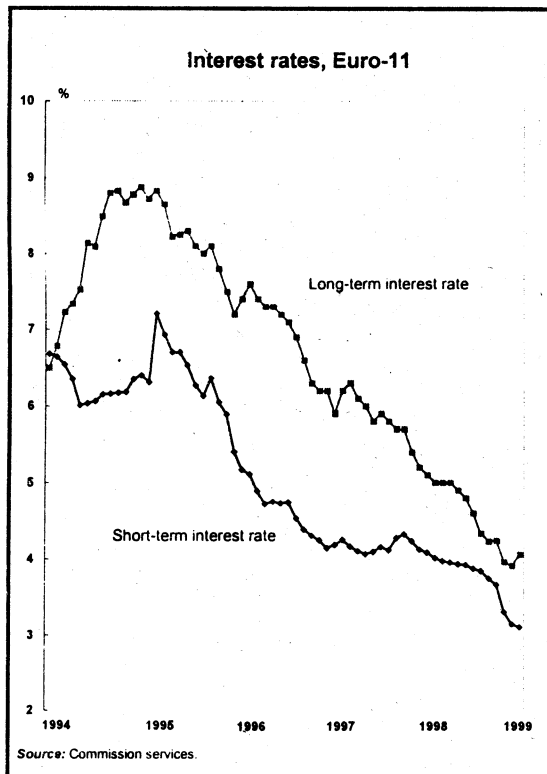
- (i) sustained efforts to bring budgets securely to close to balance or to a surplus over the medium term through a full and determined implementation by Member States of their stability programmes (see section 2.3);
- (ii) a continued responsible behaviour on the part of the social partners that ensures wage developments that are consistent with price stability and job creation (see section 2.4); and
- (iii) a commitment from the Member States to press ahead with front-loaded, coherent and comprehensive economic reforms with a view to enhancing the adaptability and efficiency of product, capital and labour markets (see section 3).

These commitments regarding budgetary policies, wage developments and structural policies are essential to ensure that monetary policy has adequate room for manoeuvre in the light of prevailing economic conditions characterised by a considerable slack in product and labour markets. Concrete actions by governments and the social partners to follow through on their commitments will permit monetary policy, in accordance with Article 105(1), to support the general economic policies in the Community with a view to contributing to the achievement

of the objectives of the Community as laid down in Article 2, without prejudice to the objective of price stability.

The implementation of economic policies that are adequate in the present context is a key test for the EMU system. The institutional framework for an effective co-ordination between all policy actors has been established but experience with the rules needs to be gained. To overcome the current difficult environment, it will be essential to establish an open dialogue involving all policy actors, including, where appropriate, the European social partners, with a view to exchanging information and standpoints, achieving common policy views and creating a climate of mutual trust in the ability of policy actors to deliver on their commitments.





The introduction of the euro and the completion of the single market have led to the creation of one of the largest economic entities in the world. This implies global responsibilities for the euro area and the necessity to speak with one voice and to be represented effectively. In the face of the current global financial crisis, the Union is confronted with a twofold need:

- (i) to engage in an effective dialogue with its main trading partners with a view to promoting sound economic policies in all of the major currency areas, thereby securing a high level of exchange rate stability in the international monetary system; and
- (ii) to help ensure that the architecture of the international financial and monetary system is adapted to the

globalisation of financial markets, by promoting inter alia: enhanced institutional arrangements for the international monetary system; improved transparency and better policy making procedures; strengthened financial sector surveillance; a well-sequenced and orderly approach to liberalising financial markets and mechanisms for co-operative crisis management involving the private sector.

## 2.2 *Macroeconomic policy mix in the Member States outside the euro area*

The Member States not participating in the euro area are subject to different macroeconomic policy constraints than the euro-area Member States insofar as they retain national responsibility for monetary policy and their exchange rate and are not subject to all provisions of the Stability and Growth Pact. Nevertheless, the non-euro-area Member States will also need to maintain stability-oriented macroeconomic policies as the basis for sustained growth and employment creation. In addition, monetary and budgetary policies will need to be conducted so as to maintain, and where appropriate foster, convergence of inflation and budgetary performances in preparation for the eventual adoption of the euro.

In the two Member States whose currencies participate in the ERM2, the main focus must be on respecting exchange rate commitments within the mechanism through the conduct of supportive monetary and budgetary



policies. In the two Member States that pursue a direct inflation target, it is important that the conduct of monetary and fiscal policy be consistent with the achievement of that target, while avoiding any excessive exchange rate volatility. To these ends, all of the pre-ins Member States should be committed to the rigorous implementation of their convergence programmes.

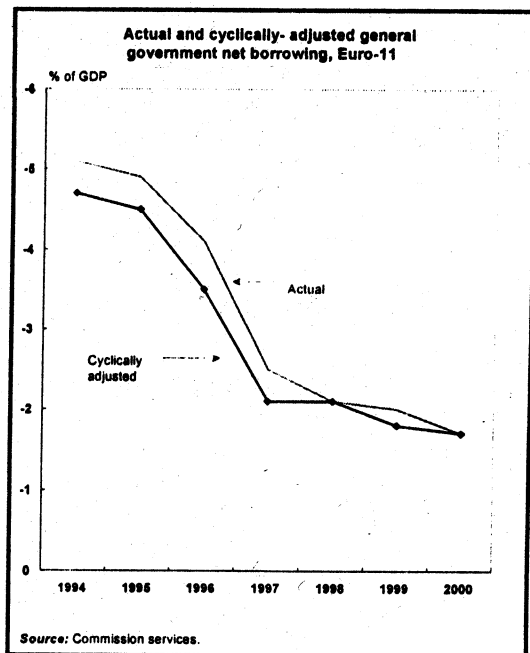
### 2.3 *Sound and efficient public finances*

Visible progress in reducing general government budget deficits was made in 1996 and 1997. Disappointingly, budgetary consolidation was only modest in 1998 even though economic activity generally expanded at a strong pace and the budgetary positions of most Member States are not yet in line with the requirements of the Stability and Growth Pact.

Further budgetary consolidation is therefore needed. This will create the necessary scope to face adverse cyclical developments, reduce the vulnerability of budgets to rising interest rates, make government spending and taxation more conducive to growth and employment creation and will help prepare for the longer term budgetary challenges associated with an ageing population.

In conducting budgetary policies during 1999 and beyond, Member States are urged:

- (i) given the expectation of a mild, temporary slowdown, to meet fully



their 1999 budgetary targets except where budgetary positions are already close to balance or in surplus; in those countries where economic growth remains strong, governments are encouraged to achieve better budgetary results;

- (ii) to achieve budgetary positions of close to balance or in surplus no later than by the end of 2002 in conformity with the stability and convergence programmes; and
- (iii) provided the economic outlook unfolds as expected, to front-load the adjustment efforts envisaged in their stability and convergence programmes as of the year 2000 and, where programmes target minimum adjustment, to aspire to more ambitious objectives and update stability/convergence programmes accordingly.

**General government  
net lending/borrowing  
(% of GDP)**

Stability and convergence programme projections

**Stability programmes**

	Date <sup>1)</sup>	1998	1999	2000	2001	2002
B	12/98	-1.6	-1.3	-1.0	-0.7	-0.3
D	1/99	-2.5	-2.0	-2.0	-1.5	-1.0
E	12/98	-1.9	-1.6	-1.0	-0.4	0.1
F	1/99	-2.9	-2.3	-2.0	-1.6	-1.2 <sup>2)</sup>
IRL	12/98	-2.6	-2.0	-1.5	-1.0	-
I	12/98	-2.6	-2.0	-1.5	-1.0	-
L	02/99	2.1	1.1	1.2	1.3	1.7
NL <sup>3)</sup>	10/98	-1.3	-1.3	-	-	-1.1
A	11/98	-2.2	-2.0	-1.7	-1.5	-1.4
P	12/98	-	-2.0	-1.5	-1.2	-0.8
FIN	9/98	-1.1	2.4	2.2	2.1	2.3

**Convergence programmes**

DK	10/98	1.1	2.5	2.8	2.6	2.9 <sup>5)</sup>
EL	6/98	-2.4	-2.1	-1.7	-0.8	-
S	12/98	1.5	0.3	1.6	2.5	-
UK <sup>6)</sup>	12/98	0.8	-0.3	-0.3	-0.1	0.2 <sup>7)</sup>

1) Date when programme was adopted.

2) Prudent scenario; favourable scenario projection: -1.7, -1.2 and -0.8 % of GDP, respectively, in the years 2000 to 2002.

3) No annual data provided for the years 2000/01.

4) Cautious scenario; middle and favourable scenario projections: -0.25 and 0.25% of GDP, respectively, in the year 2002.

5) Projection for the year 2005: 3.5% of GDP.

6) Data for the financial years beginning in each of the calendar years indicated.

7) Projection in the financial year 2003/04: 0.1 % of GDP.

Source: Commission Services.

For budgetary adjustment and restructuring to take place efficiently, it has to take into account the particularities of each Member State's economic, social and institutional conditions. In general, and without threatening the necessary ongoing consolidation process, Member States are urged to:

(i) improve their budgetary positions through expenditure restraint rather than through tax increases; in this context, to enhance the credibility of budgetary consolidation and to influence private sector expectations positively, Member States would be well advised to introduce or enhance the mechanisms and institutions that help control spending so that taxes, especially on labour, could be cut without jeopardising the achievement or maintenance of healthy budgetary positions; and

(ii) improve the sustainability and efficiency of their public finances through:

(a) reviewing pension and health care systems in order to be able to cope with the financial burden on welfare spending of the ageing of the population and the need to influence future labour supply, in line with the options already being examined by the Member States;

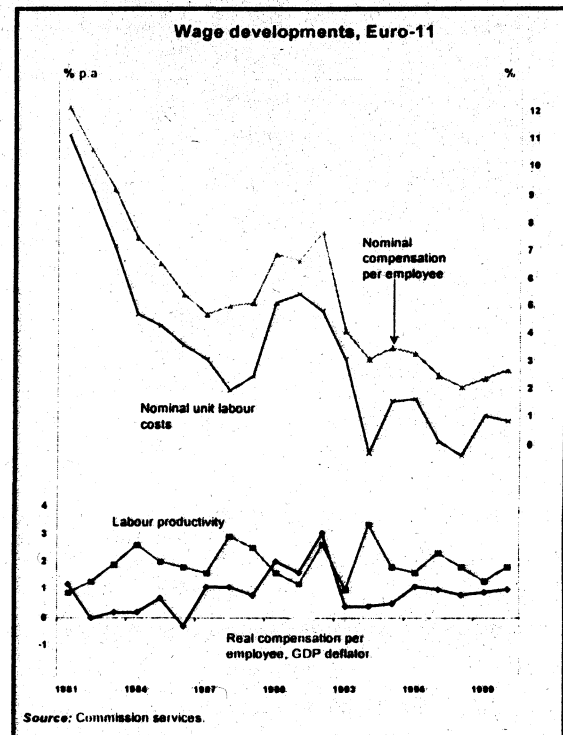
(b) reversing the decline in government investment; in this context the Union and the Member States should implement with resolve the Commission's four-point action

plan that was submitted to the Vienna European Council;

- (c) providing for the necessary financing of investment in human capital and other active labour market policies that are called for in the Employment Guidelines;
- (d) reducing the overall tax burden and especially the tax wedge on the lower paid via reduced spending or shifts to environmental, energy or consumption taxes; to increase the employment effects of reductions in the fiscal burden on labour and non-wage labour costs, the social partners are urged, at their various levels of responsibility and action, to commit themselves to actions aimed at improving the conditions for job creation and investment;
- (e) improving the efficiency of their taxation systems; and
- (f) pursuing tax-co-ordination further so as to ensure a smooth functioning of the Single Market and avoid harmful tax competition; the VAT-system, the taxation of corporate income and the taxation of the interest on savings form the core of these efforts towards strengthened co-ordination.

## 2.4 *Appropriate wage developments*

As underlined in the Amsterdam resolution on growth and employment, the social partners are responsible -- at the national, regional, sectoral or even at a more decentralised level following their respective traditions -- for reconciling high employment with appropriate wage settlements and for setting up a suitable institutional framework for the wage formation process. In EMU, with a single monetary regime, the link between wages and employment will become more apparent and strict.



For wage developments to contribute to an employment-friendly policy mix, the social partners should continue to pursue a responsible course and conclude wage agreements in Member States in line with the general principles set out in previous Broad Economic Policy Guidelines:

- (i) nominal wage increases must be consistent with price stability; in the euro area, aggregate wage increases must be consistent with keeping price increases securely within the price stability objective of the ECB;
- (ii) real wage increases in relation to labour productivity growth should take into account the need to strengthen, where necessary, and subsequently maintain the profitability of investment, whilst allowing a steady increase in purchasing power and private consumption; and
- (iii) wage agreements should take into account differentials in productivity levels according to qualifications, regions and sectors; especially within the euro area, it will be of crucial importance to avoid a convergence of nominal and real wages across countries and regions in advance of productivity.

To achieve the right results, effective social dialogue at all the appropriate levels will be essential. The outcomes should be closely monitored and jointly assessed from a growth and employment point of view.

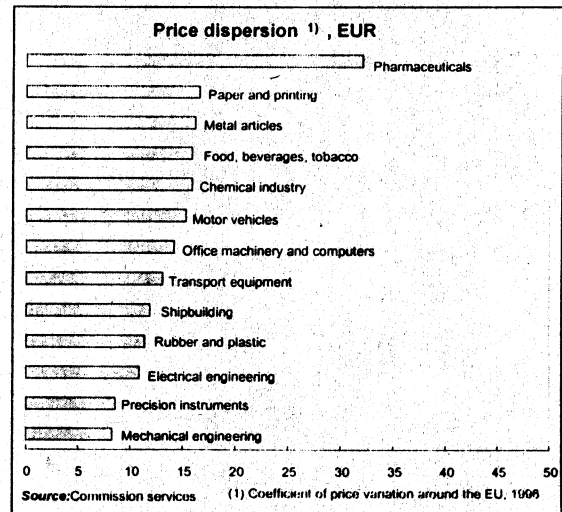
### 3. Comprehensive and co-ordinated economic reforms

Structural reforms have a key role to play in stimulating economic growth, restoring competitiveness and fostering employment in the European Union. Structural reform will enhance the ability to deal with globalisation and technological change. It is also essential to the success of Economic and Monetary Union: by removing supply-side bottlenecks, better functioning markets will make room for macroeconomic policies more conducive to growth and employment and will enhance private sector confidence. The fact that monetary policy is geared to macroeconomic requirements in the euro area as a whole underscores the need to ensure that product and labour markets are flexible enough to respond smoothly to country-specific economic developments.

Whilst reforms are being implemented throughout the EU, they often lack comprehensiveness and progress remains uneven across policy fields and Member States. In general, progress is relatively satisfactory in goods and capital markets, but much remains to be done in services, including financial services, and labour markets.

Member States should therefore carry out in a transparent manner the Employment Guidelines and use the Cardiff process on economic reforms to increase competition, speed up regulatory reforms and improve the working of the Single Market. It is particularly important to reform structures that favour "insiders" (those who already have a job or a business) at the expense of "outsiders"

(those without jobs and potential entrepreneurs).



#### 3.1 *More efficient product (goods and services) markets*

Thanks to the Single Market Programme, EU product markets are relatively integrated and function quite well. However, price differences between Member States and between the EU and the US suggest that there is scope for improvement. Regulatory reform is another cornerstone of efforts to improve the functioning of product markets. Regulatory reform consists of improving the quality of regulations, and may or may not involve deregulation. To attain these goals, Member States are urged to undertake the following measures:

- (i) the Single Market and competition policy should be strictly applied and closely monitored; more effective enforcement of the Single Market should be ensured especially in the areas of public procurement and

technical standards via renewed commitments from the public authorities;

- (ii) for state aids, the efforts of the Commission should be supported by continued action by the Member States to reduce the level of state aids and to switch away from sectoral, ad hoc and restructuring aid;
- (iii) regulatory reforms should be pursued and speeded up in telecommunications, transport and energy, with a view to increasing competition amongst service providers; benefits in terms of lower prices and/or higher quality resulting from the liberalisation process have to be transmitted without delay to consumers and industrial users;
- (iv) the quality of the legal and regulatory environment should be improved, especially for the start-up of new businesses; procedures and administrative delays for business start-ups should be reduced. In this sense, Member States should set themselves targets and deadlines for such reductions; and
- (v) VAT should be further revised towards an origin-based system in order to ensure that it is adapted to the Single Market.

### ***3.2 More integrated and deeper capital markets***

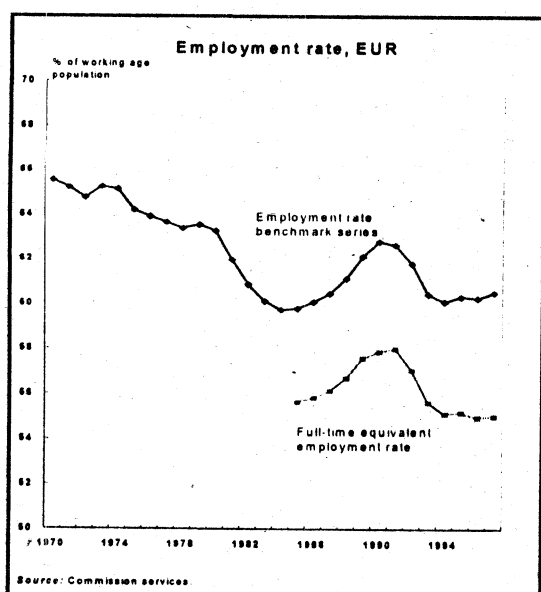
Despite substantial progress, differences in both national regulatory environments and fiscal regimes continue to fragment

the EU capital market. By offering the prospect of a large, single capital market, the introduction of the euro creates a strong incentive to increase transparency and to remove the remaining barriers. Also, deeper and better functioning risk capital markets would facilitate the expansion of small and medium-sized enterprises (SMEs), through easier access to fund-raising on the stock market and the development of venture capital, and promote Research and Development (R&D) and innovation. Therefore Member States are urged to:

- (i) reduce differences in national regulations and tax regimes, in particular concerning institutional investors;
- (ii) ensure that additional host country requirements only apply to financial services offered to individuals and not to professionals; this implies the pursuit of a policy distinguishing between consumers and operators acting in their professional capacity;
- (iii) ensure that existing national "general good" rules, which aim at ensuring consumer protection and promoting cross-border business, are applied in a transparent and proportionate manner as called for in the Commission Communication "Financial services: building a framework for action"; and
- (iv) implement the risk capital action plan, facilitating access to both risk capital for SMEs and capital for R&D for all enterprises.

### 3.3 Better functioning labour markets

Low employment rates and persistently high levels of unemployment suggest there is significant scope for improvement in the functioning of labour markets in the EU. However, the problem differs considerably between Member States, between regions within Member States and between categories of labour. These differences also suggest a number of lessons: (i) differences between Member States indicate that countries which have undertaken comprehensive structural reforms rather than scattered measures, have been able to improve their employment performance; (ii) differences in regional unemployment in several countries highlight the need to account for regional productivity differences in collective bargaining; and (iii) the particularly high incidence of unemployment among certain categories of labour (low skilled, females, youth) reflects the high costs of specific labour categories (in particular unskilled workers), the inadequacy of skills, recruitment patterns, and *de facto* discrimination.



To tackle these problems, the integrated four-pillar strategy set out in the Employment Guidelines should be fully implemented and in a prompt and transparent manner. Member States should give particular attention to the following:

- (i) policies should act on both the demand for and supply of labour by applying the preventive approach of the Employment Guidelines and by reducing the gender gap; this should include more efficient training and education, a lowering of taxes, especially on low-paid workers, and an assessment of duration and eligibility criteria in benefit systems; in accordance with the Vienna European Council conclusions the National Action Plans for Employment should include concrete national targets and deadlines where this is not already the case;
- (ii) reviewing and adapting the tax and benefit systems to ensure that they actively support employability and job creation; achieving the appropriate balance between economic efficiency and social inclusion; transfers of unemployed to expensive, passive systems should be avoided; and
- (iii) the social partners should be encouraged to modernise the organisation of work, including flexible and annualised working time arrangements; any overall reduction of working time would have to ensure both competitive wage developments and future needs in terms of increased labour supply; efforts to increase women's participation in working life are crucial in most Member States.

## II. COUNTRY-SPECIFIC ECONOMIC POLICY GUIDELINES

### 1. Belgium

Economic growth will decelerate in Belgium in 1999 to about its trend rate, but should be sufficient to bring about a further gradual decline in unemployment.

#### *Budgetary policy*

Budgetary policy should focus on the following:

- any risk of slippage from the 1999 budget target for the primary surplus of 6% of GDP should be offset by timely corrective measures, thus enabling the target of 1.3% of GDP for the total deficit to be met;
- real primary expenditure in the current and subsequent years should be monitored closely in order to ensure that its annual growth rate is contained within the 1½% limit set in the stability programme;
- in future years, the primary surplus should be maintained at 6% of GDP and the total government deficit reduced as planned in the Belgian stability programme so as to secure a continuing rapid reduction in the general government debt ratio; and
- within the Belgian institutional framework, it would be desirable to renew from 1999 the "co-operation" agreement signed in 1994 between the Federal government, the Regions and Communities, with a view to ensuring the co-ordination of

budgetary policy during the period covered by the stability programme.

#### *Product and capital markets*

Belgium's authorities have taken important steps to liberalise product and capital markets and to promote competition. However, further efforts are needed in specific areas:

- despite steady improvement since November 1997, Belgium's record on implementing Single Market directives could still be improved, especially in areas such as telecommunications and transport; and
- liberalisation of the network industries (telecommunications, post, energy, transport) is generally keeping pace with the requirements of Community legislation. Further opening-up of these markets should entail lower prices for business and consumers.

#### *Labour markets*

The Belgian labour market is characterised by persistently high long-term unemployment and relatively low employment rates. Labour market policies are traditionally dominated by income maintenance measures. The trend towards an active policy has been reinforced with the 1998 National Action Plan for employment. As a consequence,



reforms should focus, in particular, on the following areas:

- while activation of the unemployed is being pursued with particular focus on low-skilled women and youngsters, more needs to be done, especially concerning unemployed adults;
- in order to create incentives to participate in the active measures and to take up new job offers, the active policy measures should be combined with a review of benefit duration and availability requirements;
- employment protection legislation in Belgium is considered to be relatively strict for white-collar workers.

Further consideration should be given to this matter since more flexible employment protection legislation is likely to improve Belgian labour market performance; and

- given substantial differences in regional unemployment, the rate of wage increases in some regions or sectors may need to reflect better productivity differences across regions and sectors. Whilst recent agreements by the social partners already allow for some differentiation of wage increases, this need should further be taken into account within the framework of the law setting upper limits for wage increases.

## 2. Denmark

A slowing in economic growth in Denmark to below its trend rate is likely in 1999 as economic activity is close to capacity limits and in response to counter-cyclical budgetary measures at central government level. Unemployment is likely to stabilise at its already low level.

### *Budgetary policy*

Budgetary policy should focus on the following:

- the implementation of budgetary policy should seek to maintain a strong government surplus in 1999 -- in line with the planned surplus of 2.5% of GDP -- through strict adherence to expenditure targets, in particular at the level of local governments; and
- in the medium term, the reduction of distortions in the tax system, especially in the field of tax deductions for interest payments (initiated in the 'Whitsun package'), should be pursued further.

### *Product and capital markets*

The Danish authorities have significantly advanced structural reforms in a number of markets. Nonetheless, further efforts are needed in specific areas:

- competition problems (high prices, high concentration ratios, high margins and low degrees of foreign penetration) are noticeable in certain sectors, calling for a strengthening

and a more vigorous application of existing regulations;

- the Danish public sector is comparatively large, so the authorities' efforts to increase its efficiency by introducing competitive tendering in the provision of public services are particularly appropriate;
- significant progress has been achieved in deregulating the network industries. Recently-agreed reforms in the electricity sector aimed at further liberalisation should be implemented without delay; and
- while liberalisation has started, regulations on land use and shop-opening hours should be reviewed further.

### *Labour market*

Denmark has a high employment rate and a low unemployment rate. The country is part of a group of Member States in which the implementation of comprehensive structural reforms, in particular in the labour markets, has produced clear positive results. Nevertheless, reforms should focus, in particular, on the following areas:

- given the relatively large part of the active population on benefits and the need to increase the labour supply, it is important that the recent reforms, including the reform of the early retirement scheme, are fully implemented and closely monitored, with a view to evaluating whether

incentives to take up or remain in jobs are sufficient;

- the latest tax reform aimed at, *inter alia*, reducing the tax burden on low incomes and increasing incentives should be evaluated with a view to a

possible reinforcement because the tax wedge on labour is still high; and

- the various leave schemes should be reconsidered in the light of the need to increase labour supply.

### 3. Germany

The slowdown in Germany in 1999 appears to be more pronounced than in most other Member States, because of a generally greater exposure to weaker world trade and some specific domestic influences, such as the depressed construction industry. This carries the risk of an interruption in the decline in unemployment.

#### *Budgetary policy*

Budgetary policy should focus on the following:

- implementation of budgetary policy in 1999 should respect the target for the government deficit of 2% of GDP. This should be possible through tight control of expenditure;
- the expected strengthening of the economy in 2000 and beyond should be used to make faster progress towards the medium-term objective for the deficit set in Germany's stability programme; and
- the guiding principle of the planned tax reform, i.e. a cut in tax rates and a simultaneous widening of the tax base, is appropriate. In order to maximise its positive impact, the reform should result in an effective simplification of the tax code.

#### *Product and capital markets*

There is evidence that the functioning of German product markets is improving. However, further efforts are needed in specific areas:

- since November 1997, Germany has made significant progress in completing the legislative work necessary for the implementation of the Single Market. In public procurement, however, further progress could be made;
- in the past, the level of state aids had increased due to reunification, but since then, it has decreased. This process should be continued, especially for sectoral aids;
- significant progress has been achieved in liberalising the network industries leading to lower prices. A similar effort should be considered for other services, including opening hours in retail distribution after the review of the 1996 liberalisation; and
- business registration procedures for creating SMEs were simplified and accelerated. Further accelerations seem to be possible.

#### *Labour markets*

The German labour market has been characterised by weak job creation over the past five years. The unemployment rate in the East is nearly twice as high as in the West. Active labour market policies have traditionally focussed on the promotion of vocational and prevocational training, job creation schemes, structural adjustment measures and rehabilitation measures, while the role of the Public Employment Service is being strengthened further. The 1998 National Action Plan for employment

focuses on employability by further developing the successful dual apprenticeship system, as well as actions for disadvantaged youth. As a consequence, reforms should focus, in particular, on the following areas:

- the emphasis put on active labour market measures should be supplemented by a review of the benefit and assistance schemes in order to ensure that for all groups sufficient incentives exist for participating in job training and taking up job offers;
- the government's decision to lower non-wage labour costs and income taxes for especially low-paid workers, financed via increased energy taxes, is welcomed. Such moves should be continued in order to reduce labour costs further at the lowest end of the wage scale, while respecting the need for fiscal consolidation; and
- to assess the employment legislation for SMEs with a view to its impact on job creation.

## 4. Greece

Economic growth in Greece has been strong in recent years and any slowdown in 1999 is likely to be modest. Unemployment is expected to decline gradually.

### *Budgetary policy*

Budgetary policy should focus on the following:

- the target set in the budget for a government deficit in 1999 of 1.9% of GDP should be achieved. The proposed restructuring of government expenditure in favour of investment should be effectively implemented;
- the budget for 2000 should aim for a further decline in the deficit helped by a reduction in the primary current expenditure ratio to GDP in order to contribute to lowering inflation expectations. Clear and binding norms for securing expenditure control should be respected;
- in parallel, the Greek authorities should, in line with the tax law adopted in the recent past, further pursue their efforts to increase the efficiency of the tax system by combating tax avoidance and evasion; and
- the public sector should be reformed with vigour; in particular the restructuring and privatisation of public companies, should be implemented as scheduled.

Privatisation receipts should be used to contribute to a rapid reduction in the general government debt ratio.

### *Product and capital markets*

Greece has striven to liberalise its economy in the last few years. Nonetheless, efforts need to be reinforced in specific areas:

- the Greek authorities should improve their transposition record on implementing Single Market legislation, which is worse than average, particularly as regards public procurement;
- to improve productivity, the strategy of restructuring management in state-owned enterprises should be accompanied by a sustained effort to privatise;
- although the creation of new firms is encouraging, reducing further the administrative burden for registering a new company could stimulate entrepreneurship. Ideally, this would be accompanied by a strategy to develop venture capital markets, as Greek SMEs find raising finance difficult; and
- although recent measures to stimulate business R&D expenditure from its currently low level are encouraging, further measures along similar lines should be envisaged.

### ***Labour markets***

The Greek labour market is characterised by a low employment rate, stagnating unemployment and high long-term unemployment. A reform of the labour market aimed at enhancing flexibility entered into force last year. The law introduces new types of work contracts, flexible working hours and private employment offices. The 1998 National Action Plan for employment and the implementation report point to the establishment of a more general employment strategy to tackle these problems. Particular efforts have been made to address key problems affecting

young people and women, both of which have high unemployment rates. As a consequence, reforms should focus, in particular, on the following areas:

- the preventive approach of labour market policies should be reinforced. Efforts to reform training and education systems with a view to taking better account of the needs of the productive system should be further pursued; and
- further efforts should be made in terms of new types of part-time contracts and more flexible working hours.

## 5. Spain

In the Spanish economy, high and above trend growth is expected in 1999, although at a somewhat lower rate than in previous years. A further substantial decline in the still very high level of unemployment is anticipated.

### *Budgetary policy*

Budgetary policy should focus on the following:

- the implementation of budgetary policy in 1999 should ensure that the target for the government deficit of 1.6% of GDP is met, if necessary, through a further tightening of primary current expenditure, taking advantage of the better-than-expected results in 1998 and the potential for larger savings in interest payments;
- the budget for 2000 should reaffirm the targets and strategy outlined in the stability programme: i.e. a deficit of 1% of GDP based on the containment of primary current expenditure. This will allow room for strengthening government investment, given the catching-up needs of Spain. If evidence of overheating emerges, a tighter fiscal stance should be adopted; and
- control of government expenditure should be re-enforced through the planned reform of the National Budget Law; given the increasing role of territorial governments in many fields of expenditure, the existing internal stability pact

between the regions and the state should be monitored closely and respected fully.

### *Product and capital markets*

Over the recent period, Spain has made serious endeavours to improve the functioning of product markets. Nonetheless, further efforts are needed in specific areas:

- despite progress in transposing Single Market legislation during 1997 and 1998, further improvement is still necessary, especially in transport;
- a large part of non-agricultural state aid takes the form of sector-specific aid. Such aids should be reduced;
- under regulatory reforms, much has been done to deregulate telecommunications, electricity, gas and air transport. A similar effort should be made in retail distribution;
- the administrative burden facing Spanish companies is high, both in terms of the number of procedures and of delays for company registration. Measures should be taken to rectify this situation; and
- the Law for the Promotion of Industrial Innovation being prepared by the Spanish government to stimulate industrial innovation is particularly welcome, given the present low share of R&D expenditure.



### *Labour markets*

Although the unemployment rate decreased by more than 2 percentage points in 1998, to reach 18.7%, Spain has one of the most difficult starting points of all Member States. Apart from high rates of youth, long-term and female unemployment, the Spanish labour market suffers from a low employment rate, a low rate of female participation and a low rate of part-time work. The 1998 National Action Plan for employment represents a significant move towards activation and prevention. Furthermore, a new law recently introduced should enhance the attractiveness of part-time work for employers and employees, while the new decentralised management model of the National Employment Institute will help improve employability. Negotiation structures have been created to actively involve the social partners in the definition and implementation of employment policies. As a consequence, reforms should focus, in particular, on the following areas:

- the high levels of long-term and youth unemployment call for a shift from passive to active labour market policies, with particular emphasis on

investment in training and education to increase human capital and adaptability as indicated in the 1998 National Action Plan for employment;

- efforts in line with the recent personal income tax reform to reduce the tax wedge, combined with further reforms of the pension system aimed at discouraging early retirement, should provide additional incentives on the supply side of the labour market, while helping to ensure the sustainability of social protection in Spain;
- recent agreements with the social partners to reduce the cost of dismissal should be reinforced in order to diminish the relative weight of temporary contracts, while enhancing part-time work and thereby introducing more flexibility in the labour market; and
- striking regional differences as regards unemployment rates indicate that the social partners should review wage formation systems with a view to adapting wage developments to productivity differentials at regional level.

## 6. France

Economic growth in France will decelerate in 1999 to about its trend rate. A further but less rapid decline in unemployment is expected.

### *Budgetary policy*

Budgetary policy should focus on the following:

- implementation of budgetary policy in 1999 should respect the target for the government deficit of 2.3% of GDP. This should be possible but it may require the French government to exploit the safety margins of the budget and, if the need arises, freeze spending;
- government expenditure in 1999 and subsequent years should be strictly controlled and any slippage should be promptly corrected. In particular, social security spending should be closely monitored. The government should rapidly announce measures that will ensure a durable compliance with the expenditure ceilings established in the stability programme; and
- the expected strengthening of economic activity in 2000 and beyond should be used to make progress towards the medium-term objective for the deficit as projected in the favourable scenario of France's stability programme.

### *Product and capital markets*

The French authorities have made efforts to deregulate and promote competition in product and capital markets. Nonetheless, further efforts are needed in specific areas:

- despite steady improvement since November 1997, France's record in implementing Single Market Directives could still be improved, particularly in telecommunications;
- the large proportion of non-agricultural state aid devoted to rescuing and restructuring firms in difficulties should be reduced. As the French authorities themselves recommend in their Report on French economic reforms, preference should be given to generic measures to improve firms' ability to adapt and innovate;
- although liberalisation of the network industries (telecommunications, post, electricity, gas, transport) is generally keeping pace with the requirements of Community legislation, faster progress could be made, particularly in the energy sector; and
- measures already taken to simplify formalities, to reduce the administrative burden on business and to encourage innovation should be closely monitored and the effort made in these areas should be continued.

### *Labour markets*

The employment rate is relatively low, in particular for workers aged 55 and more. The unemployment rate, including youth unemployment, is higher than the EU average. Recent reforms have improved the employment content of growth by means of a good combination of active and preventive measures. The 1998 National Action Plan for employment has clearly addressed the prevention of youth unemployment, as well as the integration of the long-term unemployed. There are important programmes of job creation, especially in emerging community services. Also, new initiatives on life long learning are under discussion. As a consequence, reforms should focus, in particular, on the following areas:

- the increased emphasis on active labour market policies of the 1998 National Action Plan for employment should be backed up by a review of both unemployment benefit schemes (job availability requirements) and employment protection legislation. Such a review should aim at both increasing the encouragement to take up jobs or participate in active labour market measures and enhancing the incentives to create jobs;
- provided budgetary room is created, the recent policy of tax cuts at the lower end of the wage scale and the promotion of jobs in certain service areas should be continued; and
- a prominent reform of the French labour market is the gradual introduction of the 35-hour working week. The bulk of the implementation remains to be done. Special attention should be paid to the avoidance of increasing the cost of labour and to the introduction of more flexibility regarding work organisation and working time (annualisation of working time).

## 7. Ireland

Very rapid growth in the Irish economy is expected to continue in 1999, albeit not quite as strong as in the previous two years. Unemployment should decline further at a significant pace.

### *Budgetary policy*

Budgetary policy should focus on the following:

- since the public finances are already in strong surplus, the main challenge for budgetary policy is to ensure stability. Should there be evidence of wage inflation continuing to gather pace, there should be a readiness to use budgetary policy to restrain the economy; and
- the growth in government consumption should be steadily restrained from the estimated 5% volume increase in 1998 to 2% in 2001, as outlined in the stability programme.

### *Product and capital markets*

Reforms of product and capital markets are key elements of the government's economic strategy. Nonetheless, further efforts are needed in specific areas:

- Ireland should accelerate the reduction of its transposition deficit on Single Market legislation especially in transport;
- the Competition Authority should be given power to enforce directly

Articles 85 (cartels) and 86 (abuse of dominant positions) of the EC Treaty;

- liberalisation and regulatory reform of the Irish network industries generally follows progress made in EU legislation. However, telecommunications, electricity and gas supply, and domestic and international transport are dominated by state-owned companies. Telecom Eireann is being partially privatised this year. Similar initiatives to promote competition in these sectors should be considered; and
- venture capital in Ireland is very modest. This is a serious handicap to the development of Irish SMEs. However, since 1995, improvements are being made in the venture capital market and efforts in this direction should be continued. R&D expenditure is also low. In view of this, measures should be taken to create incentives encouraging venture capital and local R&D and the government could consider participating more fully to improve Ireland's R&D performance.

### *Labour markets*

Ireland has made substantial progress both in increasing the employment rate and in reducing the unemployment rate, which has been more than halved in four years. The 1998 National Action Plan for employment places most emphasis on employability, relying strongly on active policies. To address the problem of long-

term unemployment, specific preventive measures involve young unemployed and older workers, while a clear commitment has been made to raise the participation level of the long-term unemployed in training from 11 to 20 %. Reflecting such measures, but especially its recent strong growth, Ireland's unemployment rate was well below the EU average by late 1998, while its employment rate is now approaching the EU average. Long-term unemployment has fallen faster than unemployment as a whole and is continuing to decline. However, further efforts are required to reintegrate the long-term unemployed and those with low educational qualifications. As a consequence, reforms should focus, in particular, on the following areas:

- the 1999 National Action Plan for employment should place greater

emphasis on preventive measures. Furthermore measures to increase the participation rate of the long-term unemployed and the low-skilled in education and training programmes remain important;

- in line with the fourth national economic programme -- *Partnership 2000* --, adherence to the social pact plays an important role in furtherance of the wage moderation that is necessary for the maintenance of employment growth; and
- while the setting of a minimum wage can be important for addressing issues of social inclusion and poverty, potential negative effects from setting the minimum wage level too high should be avoided.

## 8. Italy

Economic growth in Italy continues to be subdued, with both domestic and external demand lacking strength, and there has not yet been any significant decline in unemployment.

### *Budgetary policy*

Budgetary policy should focus on the following:

- implementation of budgetary policy in 1999 should avoid any significant slippage from the target for the primary surplus; the target for the total deficit of 2% of GDP must be respected, helped by savings in interest payments;
- the budget for 2000 should aim to re-establish the primary surplus of 5.5% of GDP indicated in Italy's stability programme. This is necessary to ensure a continued rapid decline in the general government debt ratio. The momentum of the privatisation programme should be maintained and privatisation receipts should be used to reduce public indebtedness further;
- government current primary expenditure in the current and subsequent years should be tightly controlled, in order both to respect programme targets and to allow room for the desired expansion in government investment; and
- targeting the stabilisation of pension expenditure as a percentage of GDP is welcome. Since current and future developments in pension expenditure give some reasons for concern, the

Italian government is encouraged to re-assess the reform of the pension system.

### *Product and capital markets*

Past years have witnessed continuous progress in Italy's macroeconomic adjustment. The policy agenda now needs to be focused on structural issues aimed at promoting competition and enhancing efficiency. Nevertheless, further efforts are needed in specific areas:

- Italy's record on transposing Single Market legislation has been poor and progress has been slow. Measures should be taken to rectify this situation, especially in areas such as transport and public procurement;
- the level of non-agricultural state aids is high. Efforts should therefore be made to reduce the overall level of non-agricultural state aid and improve its structure;
- liberalisation of the network industries is generally progressing in line with the requirements of Community legislation. However, transport liberalisation should be intensified, especially road and rail transport; and
- despite recent reforms, the time necessary for registering a company is still very long. Italy should set itself tougher targets and deadlines to reduce both the high number of procedures and the long time-span for establishing new businesses.

### *Labour markets*

The Italian labour market is characterised by low employment rates and high unemployment rates, in particular, very high rates of youth and long-term unemployment and severe imbalances between the North and South. The recent adoption of a tailor-made approach vis-à-vis the newly unemployed shows that efforts are being made towards preventing the drift into long-term unemployment. Furthermore, the tightening of eligibility criteria of unemployment benefit schemes and the targeting of employability measures should improve the current situation. As a consequence, reforms should focus, in particular, on the following areas:

- efforts to improve active labour market measures would need to be substantially increased in addition to recent measures concerning job-search assistance, training and apprenticeships;
- although the 1999 Budget includes tax breaks for low-income households, efforts to shift the tax burden away from labour to other tax bases should be pursued within the process of fiscal consolidation;
- such efforts have to be combined with reforms of benefit schemes to reduce the number of employed being transferred to pensions and other schemes;
- without compromising the budgetary targets, early activation and adequate unemployment benefits should ensure an increased labour supply and greater labour mobility;
- a review of employment protection legislation should also have positive results; and
- tripartite local agreements in the South introducing wage flexibility in line with lower labour productivity should be encouraged.

## 9. Luxembourg

Economic activity in Luxembourg is likely to expand robustly in 1999, although not as rapidly as in 1998. Unemployment should stay at its very low level.

### *Budgetary policy*

Budgetary policy should focus on the following:

- government expenditure should be monitored closely, so that the high government surplus does not rely just on the rapid increase in tax receipts linked to strong economic growth; and
- structural reforms, in particular regarding the social security system, should continue in order to contribute to the maintenance of sound public finances and to prepare for the challenge of population ageing.

### *Product and capital markets*

Several sectors are undergoing structural reforms in Luxembourg. However, further efforts are needed in specific areas:

- despite recent efforts to catch-up, Luxembourg has been relatively slow to implement Single Market regulations. Implementation should be stepped up, particularly in the areas of telecommunications and transport;
- in Luxembourg, regional aids account for a very large part of non-agricultural state aids, a surprisingly

high percentage for a small, prosperous country. Evaluating the necessity and effectiveness of these aids therefore seems appropriate; and

- price levels in Luxembourg are relatively moderate except in the construction sector. The country maintains an extensive system of price regulation that is unique within the European Union. The purpose of the system is to help reduce pressures on wage levels, which are indexed to the rate of inflation. The abolition of the price regulation system should be considered.

### *Labour markets*

The overall performance of the Luxembourg labour market is among the best in the EU. Low unemployment rates coexist with high employment growth rates. The latter has mainly been achieved due to a large share of cross-border commuters, who count for almost one third of employees. However, the Luxembourg labour market performance is weak with regard to the low employment rate of women and older workers. As a consequence, reforms should focus, in particular, on the following areas:

- the 1998 National Action Plan for employment envisages measures to remedy this situation by, *inter alia*, on the job training in firms and the creation of additional childcare facilities. This could also help reduce



the imminent risk of overheating through rapid wage increases in this fast-growing economy.

## 10. The Netherlands

After several years of rapid expansion, the Dutch economy is expected to slow in 1999 to about its trend rate. Nevertheless, the already low unemployment is likely to fall further.

### *Budgetary policy*

Budgetary policy should focus on the following:

- any deterioration in the budgetary position in 1999 should be limited and should not lead to a general government deficit exceeding the budget target of 1.3% of GDP, taking advantage of the better-than-expected result for 1998. In particular, some increases in expenditure planned in the 1999 budget should, if necessary, be reconsidered; and
- the very limited planned reduction in the deficit to 1.1% of GDP in 2002 in the context of the cautious scenario of the Dutch stability programme should in any case be considered as a minimum objective and the Dutch government is encouraged to achieve better budgetary results.

### *Product and capital markets*

The Netherlands is a good example of a country in which important product market reforms have already taken root. However, problem areas remain, particularly in the non-traded sectors such as construction and some services where competition is relatively weak. In this context, further efforts are needed in specific areas:

- although the Netherlands has a generally good record in transposing Single Market directives, its transposition deficit is concentrated in a small number of sectors, particularly transport. With a view to enhancing competition, transposition should be stepped up;
- important reforms were made to competition policy in 1998 and their efficiency should now be assessed. This includes the innovative Dutch 'Competition, Deregulation and Legislative Quality Project' (MDW operatie), launched in 1994. Central to the 'MDW operatie' is the intensification of competition and the removal of regulatory obstacles wherever possible. Such obstacles continue to hinder business start-ups, in spite of the important measures already taken (reducing both the administrative costs and number of steps needed to set-up a business). The implementation of such measures should be strictly followed;
- liberalisation of the public transport sector is still little advanced and reforms in this area should be speeded up; and
- in the retail sector, shop-opening hours have been extended but spatial planning regulations continue to be a constraint and should be reviewed.

### ***Labour markets***

Due to comprehensive structural reforms and sustained economic growth, the Dutch labour market performance is one of the best in the EU, both in terms of employment increases and unemployment reductions. Nevertheless, the share of long-term unemployment in total unemployment is still high. Personalised integration plans may be effective tools in preventing youth and long-term unemployment. The government's continued efforts to reduce taxes on low wages and to reduce the share of the working-age population dependent on benefits deserve to be recognised, although there is still a large number of persons on disability benefits. Furthermore, the social partners take the interests of unemployed outsiders to a

great extent into account. The privatisation of the sickness benefit system has helped reduce sickness-related absence from work. As a consequence, reforms should focus, in particular, on the following areas:

- the tax burden on average wages remains one of the highest in the EU. Continued efforts are therefore needed to reduce the overall tax burden on labour; and
- further efforts seem to be required to ensure sufficient incentives in benefit and assistance schemes to encourage take-up of job offers and to increase the effective labour supply, in particular, among older workers.

## 11. Austria

Austria is likely to experience a slowdown in economic growth in 1999 to about its trend rate, allowing the already low unemployment rate to remain broadly stable.

### *Budgetary policy*

Budgetary policy should focus on the following:

- tight control of government expenditures is needed in order to ensure that the recent adaptation of family taxation does not lead to a build-up of pressures on the budget and that the target of 2% of GDP for the government deficit in 1999 is met;
- for the years beyond 1999, the Austrian government should do its utmost to overachieve, as in the past, the budgetary targets set in the stability programme and ensure that the general government debt ratio is kept firmly on a downward path; and
- while the net tax relief provided by the recently adopted tax reform is to be welcomed, significant savings on the expenditure side will be necessary in order not to compromise the objective of a further reduction in the deficit from 2000 onwards.

### *Product and capital markets*

Several measures have been taken to promote competition and entrepreneurship in Austria. However, further efforts are needed in specific areas:

- Austria should accelerate transposition of Single Market directives into domestic law in transport and public procurement;
- the Austrian cartel law (dating from 1988) is not in line with Community law. However, the government intends to reform the present law and create an independent Cartel Office. These reforms should be put in place as soon as possible;
- efforts should be continued to reform public services and the deregulation process of utilities should be accelerated;
- shop-opening hours should be liberalised further;
- recent Austrian initiatives to simplify the procedures necessary to start a new business such as the development of 'one-stop shops' should be continued and expanded to include all registration procedures; and
- measures should be taken to develop and facilitate access to venture capital.

### ***Labour markets***

A key element of the relatively high employment and low unemployment rates in Austria is the traditional consensus approach of the social partners, helping to smooth out the effect of business cycles on the labour markets and also to adjust ex post to wage agreements which turn out to be harmful for growth. One weakness is the low activity rate, and rising unemployment, among older workers. As a consequence, reforms should focus, in particular, on the following areas:

- the 1998 National Action Plan for employment represents a further move towards a more active labour market approach, supported by a substantial increase in budgetary resources. The new 1999 National

Action Plan should make clear how the targets will be met;

- the difficulty in retaining older workers in activity suggests in particular the need for a review of the relatively generous early retirement conditions;
- special emphasis need to be paid to low wage and low skilled workers, as their share among the unemployed recently started rising; and
- recent reforms to encourage part time work and increase the working time flexibility during the year (annualisation of working time) should support the rather successful labour market performance in Austria relative to most other EU countries.

## 12. Portugal

Although economic growth in Portugal is expected to slow in 1999, it will remain close to the trend rate and should allow a further decline in unemployment.

### *Budgetary policy*

Budgetary policy should focus on the following:

- the implementation of budgetary policy in 1999 should ensure that the target for the government deficit of 2.0 % of GDP is fully met; the opportunity presented by the favourable economic growth conditions and the budgetary outcome in 1998 could be used to bring the deficit down further; lower interest payments should also be used to improve the deficit;
- the budget execution should pay close attention to primary current expenditure, especially health expenditure and the government's wage bill, in order to generate an efficient and permanent budgetary consolidation; if evidence of overheating will emerge, a tight fiscal stance should be adopted;
- the structural reforms with a direct impact on the budget outlined in the stability programme (e.g. standardisation of accounting systems and multi-annual programming of current expenditures) should be swiftly implemented to achieve better budgetary control and to improve expenditure efficiency; and

- where possible and necessary, more intense introduction of private-public partnerships in health care systems, which are already applied in some cases in Portugal, and tightening the eligibility criteria of pensions should cope with demographic trends, without significantly increasing the tax burden on labour.

### *Product and capital markets*

Developing economic integration has helped improve the functioning of product markets in Portugal. However, further efforts are needed in specific areas:

- Portugal's Single Market transposition record is poor and little legislative progress has been made since November 1997. Measures should be taken to rectify the situation, especially in areas such as public procurement, telecommunications and transport;
- the level of non-agricultural state aids is relatively low. However, a still significant part of this aid is devoted to restructuring and sector-specific measures. Efforts should therefore be made to reduce the share of these aids;
- the anti-trust legislation is currently being reviewed with the aim of bringing it into line with the EU legislation. This reform of

competition law should be implemented as soon as possible;

- liberalisation of the network industries, which is generally progressing in line with the requirements of Community legislation, should be pursued further.
- in the retail distribution sector, new restrictions have been placed on the establishment of large retail outlets in order to deal with concentration problems in the sector. However, it is questionable whether such restrictions are the appropriate way to tackle the problem;
- administrative requirements to create a business are complex and can take a very long time. The Portuguese government should make a priority of simplifying and speeding up procedures; and
- efforts should be made to develop a venture capital market and to improve innovative activity.

### ***Labour markets***

Although the overall unemployment rate is much below the EU average, long-term

unemployment is above the EU average, and unemployment among the unskilled is relatively high. Given this situation, and the ongoing restructuring of the Portuguese economy, the 1998 National Action Plan for employment envisages enhanced education and training, as well as an improved co-ordination between both systems. As a consequence, reforms should focus, in particular, on the following areas:

- measures to improve education and training should be accompanied by an adequate benefit system to ensure appropriate incentives to participate in these active measures and to take up job offers; and
- a number of laws aimed at improving the performance of the labour market have been implemented in the past few years, including the easing of dismissal and job assignment rules and the introduction of higher working time flexibility. This policy should be pursued further with a view to enhancing labour market flexibility.

### 13. Finland

After several years of rapid growth, the Finnish economy is expected to expand more slowly in 1999. But further progress in reducing unemployment is expected.

#### *Budgetary policy*

Budgetary policy should focus on the following:

- while taking into account the impact of the economic cycle, the government surplus should be improved further so as to cope with the rapidly ageing population and the pressure that this will impose on the social security accounts;
- priority needs to be given to the reduction in central government deficit, given its still unbalanced position and the need to reduce further the central government debt ratio;
- further fiscal consolidation should be based on a reduction in government expenditure (in percentage of GDP) which would also create room for the needed reduction in the high tax burden, especially aimed at supporting job creation; and
- the stability programme set annual ceilings on central government expenditure. Whereas the ceilings for the years 2000-2002 are non-binding, they should be firmly respected in the budget laws for those year.

#### *Product and capital markets*

The progress of structural reforms has been important in Finland. However, competition problems persist in sheltered sectors such as services and construction. Further efforts are needed in specific areas:

- despite significant reforms to extend the powers of the competition authority, they should also be given the power to enforce Articles 85 (cartels) and 86 (abuse of dominant positions) of the EC Treaty; and
- because the Finnish public sector is comparatively large, areas where public and private enterprises compete to provide services should be closely monitored. Efforts made to create a competitive environment in those areas should be continued.

#### *Labour markets*

Both employment and unemployment rates are higher than the EU average. The labour force participation rate among older workers is very low. The 1998 National Action Plan for employment is a combination of preventive and curative action, contributing to a reduction of the stock of the unemployed while increasing the employment rate. The government is aware of the incentive problems of the tax-benefit system and has taken several steps to improve the current situation. These measures have been successful to some extent. As a consequence, reforms



should focus, in particular, on the following areas:

- in order to improve the employment content of growth, measures should be directed at a reduction of the overall tax burden on labour;
- benefit and assistance systems need to be reviewed with the aim of increasing job availability, making job search more effective, and ensuring sufficient incentives to take up a job offer; and
- given the impact of ageing on future labour supply, pension systems should be strengthened by reviewing the conditions for access to early retirement and the possibilities for more flexibility as regards the retirement age.

## 14. Sweden

Economic growth in Sweden is likely to slowdown in 1999, but a further gradual decline in unemployment is expected.

### *Budgetary policy*

Budgetary policy should focus on the following:

- the government should adhere to its announced policies since these are expected to achieve the government's budgetary targets of a rising government surplus;
- the government should ensure the maintenance of the tight expenditure control on which its budgetary outlook is heavily reliant; and
- given the high burden of taxation in Sweden, the government should seek ways of reducing the burden further while ensuring the achievement of its budgetary targets.

### *Product and capital markets*

Sweden has a good record of reforms to goods and capital markets. However, further efforts are needed in specific areas:

- there are competition problems (high prices and high concentration ratios) in the retail and wholesale distribution and construction sectors. Measures should be taken to improve the situation. In particular, the Swedish competition authority should be given the power to enforce Articles 85 (cartels) and 86 (abuse of dominant positions) of the EC Treaty;

- the Swedish public sector is comparatively large, so the authorities' efforts to improve its efficiency are particularly appropriate;
- Sweden is among the Member States that have undertaken the most comprehensive reforms of utilities liberalisation in the Union. In spite of efforts to ensure equality amongst the different suppliers, further efforts should be taken to ensure that dominant firms do not constitute a potential threat to market efficiency. Further measures to increase competition and to promote new entry in these sectors should be envisaged; and
- regulations limiting the establishment of grocery stores reduce competition in retail distribution.

### *Labour markets*

Total employment has been falling throughout the 1990s as a result of weakened economic activity, although showing some recovery in 1998 and still remaining above the average employment rate for the EU. The employment of women is concentrated in a limited number of sectors, especially in health and social services. Sweden stands above the EU averages as regards female and part-time employment rates. The unemployment rate was below the EU average in 1998. The Swedish labour market policy rightly puts emphasis on investment in human capital, through

employment training and skill development in the workplace. It has emphasised active labour market measures, which have, however, proved to be less effective in circumstances of high unemployment. As a consequence, reforms should focus, in particular, on the following areas:

- the government's plans to reduce the number of people in subsidised jobs and labour market programmes and, instead, to focus the programmes more precisely and to promote job creation in private firms should be encouraged;
- given the disincentives that stem from the very high tax burden on labour, in

particular, on low and medium wages in combination with generous welfare benefits, the government's aim to use the budgetary room for manoeuvre for reducing taxes on labour with a priority for low and medium-paid workers is also welcome; and

- further reviews of benefit and assistance schemes in order to clarify eligibility criteria, introduce gradually rising demands on the unemployed, strengthen the supervision of the administration and ensure efficient incentives to take up a job offer should strengthen and balance the efforts in taxation and activation schemes.

## 15. United Kingdom

Economic growth in the United Kingdom in 1999 is likely to be lower, falling below trend. This may lead to a gradual rise in unemployment from a relatively low level.

### *Budgetary policy*

Budgetary policy should focus on the following:

- announced expenditure plans should be strictly adhered to, so that the government's fiscal rules – on average over the cycle, borrowing only to invest and not to finance current expenditure, and keeping the net public debt ratio at a stable and prudent level – can be respected. As a consequence, the medium-term objective of the public finances broadly in balance can be achieved, as projected in the budget for 1999/2000; and
- the government should take corrective action promptly if there is evidence of a deterioration in the government balance which cannot be explained by the economic cycle.

### *Product and capital markets*

Since the 1980s, the UK has undertaken considerable reforms of its product markets. Nonetheless, areas of weakness in competitiveness remain. As a result, further efforts are needed in specific areas:

- although the UK has a relatively good record in transposing Single Market

legislation, little progress has been made over the recent period and further efforts are necessary, particularly in the area of transport;

- in the area of competition policy, recent reforms have reinforced the power of the Office of Fair Trading. The enforcement of these reforms should be strictly applied; and
- growth of small business, innovation and R&D expenditure (especially R&D by SMEs) are all relatively weak in the UK. The UK has a highly developed venture capital market, but only a small share of such funds go to early-stage business. The government adjustment of the tax structure in favour of SMEs and alteration of laws on insolvency and bankruptcy should help redress the situation.

### *Labour markets*

The labour market reforms pursued in recent years have contributed much to the improved employment and unemployment performance of the UK. At 71%, the UK's employment rate is among the highest in the EU, while the unemployment rate fell from over 10% in 1992 to around 6% in 1998. The New Deal and the Welfare to Work initiatives should lead to an improved performance among the young and adult long-term unemployed groups and to a start in addressing investment in educational skills. As a consequence, reforms should in particular focus on the following areas:

- the emphasis in 1998 the National Action Plan for employment on active labour market policy should be accompanied by continued efforts to lower marginal effective tax rates on low-paid workers; and
- further efforts are planned or have recently been put in place to deal with regional unemployment differences

and to address the issue of social inclusion. In this context, the full implementation of new initiatives relating to self-employment at a local level and the promotion of affordable child care should prove helpful. It remains to be seen whether further action along the lines of these programmes will be needed.

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# DOCUMENTS

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