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PART 2

**COMMUNICATION FROM THE COMMISSION TO THE SPRING EUROPEAN  
COUNCIL**

**TIME TO MOVE UP A GEAR**

**Country chapters**

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## Explanatory note on statistical table and graphs

The statistical annex presents 14 short-listed structural indicators derived from the European statistical system. The full database of structural indicators, including data and metadata relating to the EU Member States, the acceding and candidate countries, USA, Japan and EEA/EFTA countries, is publicly available on the Eurostat structural indicators website: <http://europa.eu.int/comm/eurostat/structuralindicators>. For each EU Member State, all 14 structural indicators are presented in one table and two charts.

### The 14 short-listed indicators

<i>GDP per capita in PPS</i>	Gross Domestic Product (GDP) in Purchasing Power Standards (PPS) (EU-25 = 100)
<i>Labour productivity per person employed</i>	GDP in Purchasing Power Standards (PPS) per person employed relative to EU-25 (EU-25 = 100)
<i>Employment rate</i>	Employed persons aged 15-64 as a share of the total population of the same age group
<i>Employment rate of older workers</i>	Employed persons aged 55-64 as a share of the total population of the same age group
<i>Gross domestic expenditure on R&amp;D (GERD)</i>	Gross domestic expenditure on R&D as a percentage of GDP
<i>Youth education attainment level</i>	Percentage of the population aged 20 to 24 having completed at least upper secondary education
<i>Comparative price levels</i>	Comparative price levels of final consumption by private households including indirect taxes (EU-25 = 100)
<i>Business investment</i>	Gross fixed capital formation by the private sector as a percentage of GDP
<i>At-risk-of-poverty rate after social transfers</i>	Share of persons with a disposable income below the risk-of-poverty threshold, which is set at 60 % of the national median disposable income
<i>Dispersion of regional employment rates</i>	Coefficient of variation of employment rates across regions (NUTS 2 level) within countries
<i>Long-term unemployment rate</i>	Long-term unemployed (12 months and more) as a percentage of the total active population
<i>Total greenhouse gas emissions</i>	Index of greenhouse gas emissions and targets according to Kyoto Protocol / EU Council Decision for 2008-2012 (Actual base year = 100).
<i>Energy intensity of the economy</i>	Gross inland consumption of energy divided by GDP (at constant prices, 1995=100), measured in kgoe (kilogram of oil equivalent) per 1000 Euro
<i>Volume of freight transport relative to GDP</i>	Index of inland freight transport volume relative to GDP, measured in tonne-km / GDP (at constant prices, 1995=100)

## THE TABLE

The country-specific table presents data from 1999 to 2004 for that country and the EU-25 average. Following the last EU enlargement, the indicators on GDP per capita in PPS, Labour productivity per person employed and Comparative price levels are now expressed in relation to the EU-25 average. Therefore data are not comparable with data released in previous years, which were based on EU-15=100.

The following flags are used in the data tables:

- b break in series;
- e estimates;
- p provisional value;
- f forecast;
- : not available;
- - not relevant.

## THE CHARTS

The 14 indicators are presented in two charts and compare the actual value with the EU-25 value<sup>1</sup>, illustrating in which areas a particular Member State is performing better or worse than the European average.

The “At risk of poverty” indicator measures relative poverty in a particular country and the EU-25 average is computed as a population weighted average of individual national values. A comparison of national values with the EU-25 average can therefore be difficult to interpret, and may give a different impression than computing risk-of-poverty rates by use of a common reference threshold. During the transition to data production under the new EU-SILC regulation by all Member States with effect from 2005, indicators are drawn from national sources which are not fully harmonised and there can be breaks in the time series of comparable data. The indicators are computed using an income definition which until 2007 excludes imputed rent revenues and mortgage interest payments.

For the presentation in charts, indicators have been divided into two groups:

- First chart; those indicators for which increasing values indicate a positive trend, i.e. where a value of the indicator above 100 when compared to EU-25 is a relatively good performance;
- Second chart; those indicators for which decreasing values indicate a positive trend, i.e. where a value of the indicator below 100 when compared to EU-25 is a relatively good performance.

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<sup>1</sup> Values in the chart = Current national value / Current EU-25 value \* 100



The charts also display the two central EU targets of reaching 3 % of expenditure on Research and Development and an overall employment rate of 70 % by 2010. In the same way as the indicators are compared to the EU-value, the targets have been converted to a ratio which compares the EU target to the real EU-25 value in 2004 (or latest year available).

#### **DATA SOURCES**

All indicators were extracted from the Eurostat database on 20 December 2005. The source of the information is Eurostat in all cases except for Greenhouse gas emissions (European Environment Agency and European Topic Centre on Air Climate Change) and Gross Domestic expenditure on R&D (Eurostat and OECD).

The European Council has invited Member States to set up national targets on the employment rate and on the gross domestic expenditures on R&D as a share of GDP. The table presents national targets on these indicators in response to the invitation. The targets have been extracted from the National Reform Programs. Member States may have other related targets.

## **Assessment of national reform programmes**

## Austria

1. Over the last decade, the Austrian economy has grown in real terms by just over 2% on average annually, slightly better than the euro area. Labour productivity growth as well has been just above the euro area average. GDP per capita at 123% of the EU average in 2004 was one of the highest in Europe. The employment rate stood at 67.8% in 2004, well above the EU average. Unemployment increased for the third consecutive year to reach 4.8% in 2004, hitting young people in particular. The employment rate for older workers, around 29% in 2004, is one of the lowest in the EU.

### PART I: GENERAL ASSESSMENT

2. The Austrian National Reform Programme (NRP) identifies seven “strategic priority areas” namely sustainability of public finances; R&D and innovation; infrastructure; international competitiveness; environmental sustainability; labour market and employment; and education and training. The Commission broadly shares this analysis of the main priorities but also regards the issue of competition in services as important.
3. Overall, the NRP focuses on continuity without any radical shift in policy or providing a new medium-term vision. Most of the measures referred to are either already in place or planned for 2006. This approach can be considered adequate and realistic in a short-term perspective. However, a clearer identification of challenges ahead and a more ambitious approach to tackling them would have been welcome. In general, the NRP is based on an integrated approach and presents a largely coherent set of policy measures. However, the degree of precision in the definition of implementing measures varies widely across the different areas covered. More information would be required to allow full verification of the consistency of the financial commitments in the NRP, with the overall aim of reaching budgetary balance. The NRP announces important targets (for example for the overall tax burden and for R&D expenditure) but does not set a national target for the overall employment rate. The NRP has some information on how Structural Funds will support its implementation.
4. Consultation and efforts to develop ownership of the document have been fairly substantial. The Federal Chancellery involved several ministries in the preparation of the NRP. A wide range of stakeholders was consulted, including social partners, regions, municipalities and economic research institutes. The Austrian Parliament adopted a favourable resolution.

### PART II: ASSESSMENT BY POLICY AREA

#### Macro-economic policies

5. The NRP identifies the sustainability of public finances as the key macro-economic challenge, an analysis shared by the Commission.

6. The strategy to tackle this challenge is based on a three-pronged approach: a balanced budget over the economic cycle; lowering the tax burden to 40% of GDP by 2010 and increasing potential growth by fostering investment in research, education and infrastructure. The NRP takes stock of macro-economic measures already implemented rather than presenting new ones. It refers in general terms to expenditure cuts, cost-saving administrative reforms and improvement in the quality of public finances by shifting expenditure towards areas conducive to growth. The NRP emphasises the contribution of the latest pension reforms to ensuring financial and social sustainability. References are made to various growth and employment packages, as well as to recently introduced measures aimed at enhancing Austria's attractiveness as a business location. The programme draws attention to the fact that the ratio of public expenditure to GDP has fallen from 57% to under 50% over the last decade but acknowledges that tax reforms in 2004/2005 contributed to a temporary weakening of the budget.
7. The macro-economic section is coherent but is not detailed enough to demonstrate convincingly when a return to a balanced budget – or to the surpluses that a balanced budget over the economic cycle would require - could reasonably be expected. In this respect, the Austrian stability programme, submitted after the NRP, provided some more details on the provisions designed to improve fiscal sustainability.

#### **Micro-economic policies**

8. In relation to micro-economic policies, the NRP focuses on R&D and innovation, infrastructure investments, international competitiveness and environmental technologies.
9. For R&D investment, Austria is committed to meet a target of 3% of GDP in 2010 (2.5% for 2006, 2.35% currently), in line with the overall EU target. To this end, research funding has been increased in 2005, through both direct support measures and tax incentives. The planned increase in R&D spending seems sufficient to bring Austria to 1% of public research investment by 2010 (0.86% currently), but substantial additional efforts may well be needed to leverage investments from the private sector. The NRP recognises weaknesses in the innovation system and tackles them adequately by measures to improve access to finance for innovative ventures and strengthen the qualifications of the workforce. Although the NRP stresses the intention to implement the EU's i2010 initiative to focus ICT developments on contributing to growth and jobs, the measures specified are not comprehensive, and ICT related policies could further benefit from support in related policy areas such as innovation, research and skills.
10. The programme acknowledges that Austria, as an export oriented economy, has strongly benefited from the internal market. Measures supporting the export effort of Austrian companies such as the "Go International" initiative should bring further benefits. Austria is also taking steps to improve its regulatory environment, particularly by reducing administrative costs and boosting competitiveness. The NRP contains a commitment to further strengthen impact assessment procedures.
11. Austria's horizontal industrial policy approach is complemented by sector specific initiatives in life sciences, nano-technology and environmental technologies. The latter is consistent with the inclusion in the NRP of environmental technologies and

resource efficiency, including renewable energy. Measures, like the "klima:aktiv" programme, which provide financial support for the introduction of climate-friendly technologies in various sectors, are an important contribution to help Austria limit CO<sub>2</sub> emissions. Most of the measures to improve the business environment or to address specific SME needs are built on past experience. Planned initiatives concerning entrepreneurship are not set out in detail and doubts remain as to their likely effect in fostering an entrepreneurial culture.

12. The NRP stresses the need to improve its transport, energy and ICT infrastructure. It is essential that projects such as the Vienna-Bratislava railway link, or the Brenner-tunnel, are now realised and the NRP provides grounds for optimism in this respect.
13. The NRP does not contain a clear commitment to improve Austria's performance in implementing internal market legislation or to reduce state regulation of liberal professions.
14. The programme addresses all relevant areas of microeconomic policies except competition in services. Objectives are generally clearly set out, though specific measures are not always precisely described, which makes it difficult at this stage to assess their likely effectiveness.

### **Employment policies**

15. The employment part of the NRP focuses mainly on attracting people into employment; promoting active ageing; adaptability issues including fighting against undeclared work and promoting "flexicurity"; and on qualifications and education reforms.
16. A number of appropriate measures are proposed to attract and retain more people in employment, for example increased expenditure on active labour market policy and the strengthening of the Public Employment Service. In the context of rising youth unemployment a number of measures have been introduced, in particular to modernise and reinforce the apprenticeship system. Existing successful programmes for people with disabilities are to be continued. Although some measures to improve qualifications for women and work-life balance are mentioned, limited attention is paid in the NRP to improving availability of childcare facilities. The integration of migrants into the labour market is also only given relatively limited attention in the NRP. Previous pension reforms begun in 2003 and continued in 2005 have already strengthened incentives to work longer. Other initiatives related to qualifications and quality at work, along with reductions in statutory non-wage costs for older workers, seem likely to contribute to increasing the very low employment rate of older workers. In 2006, the government will experiment with wage subsidies to make low-paid work sufficiently attractive to disadvantaged workers.
17. Initiatives aiming at improving the adaptability of workers and enterprises rely to a large extent on social partners. Stronger emphasis is given to preventing undeclared work. An unemployment insurance scheme for self-employed people is yet to be implemented. Very moderate wage developments have contributed to competitiveness and real unit labour costs have declined since 1999. The relatively high gender pay gap is only addressed to some extent by measures to reduce the segmentation of the labour market. The rapid development of new forms of work

also calls for special attention to preserve an adequate balance between flexibility and security.

18. Austria is performing well against several EU education and training benchmarks. The NRP focuses strongly on improving education, vocational training for young people and universities, which should contribute to raising the quality of labour supply and meeting skill demands. Nevertheless, additional attention to raising reading standards and to maths and science teaching at all levels would seem necessary. Although incentives for employers and individuals to invest in training have increased and this may prove effective, the NRP does not present a fully-fledged strategy for lifelong learning.
19. The NRP sets out a comprehensive set of measures, mostly already in place, to address the employment challenges identified. The measures taken to increase the low employment rate of older workers are appropriate but given the very low base, more radical steps and a stronger commitment from all stakeholders are needed.

### **PART III: CONCLUSIONS**

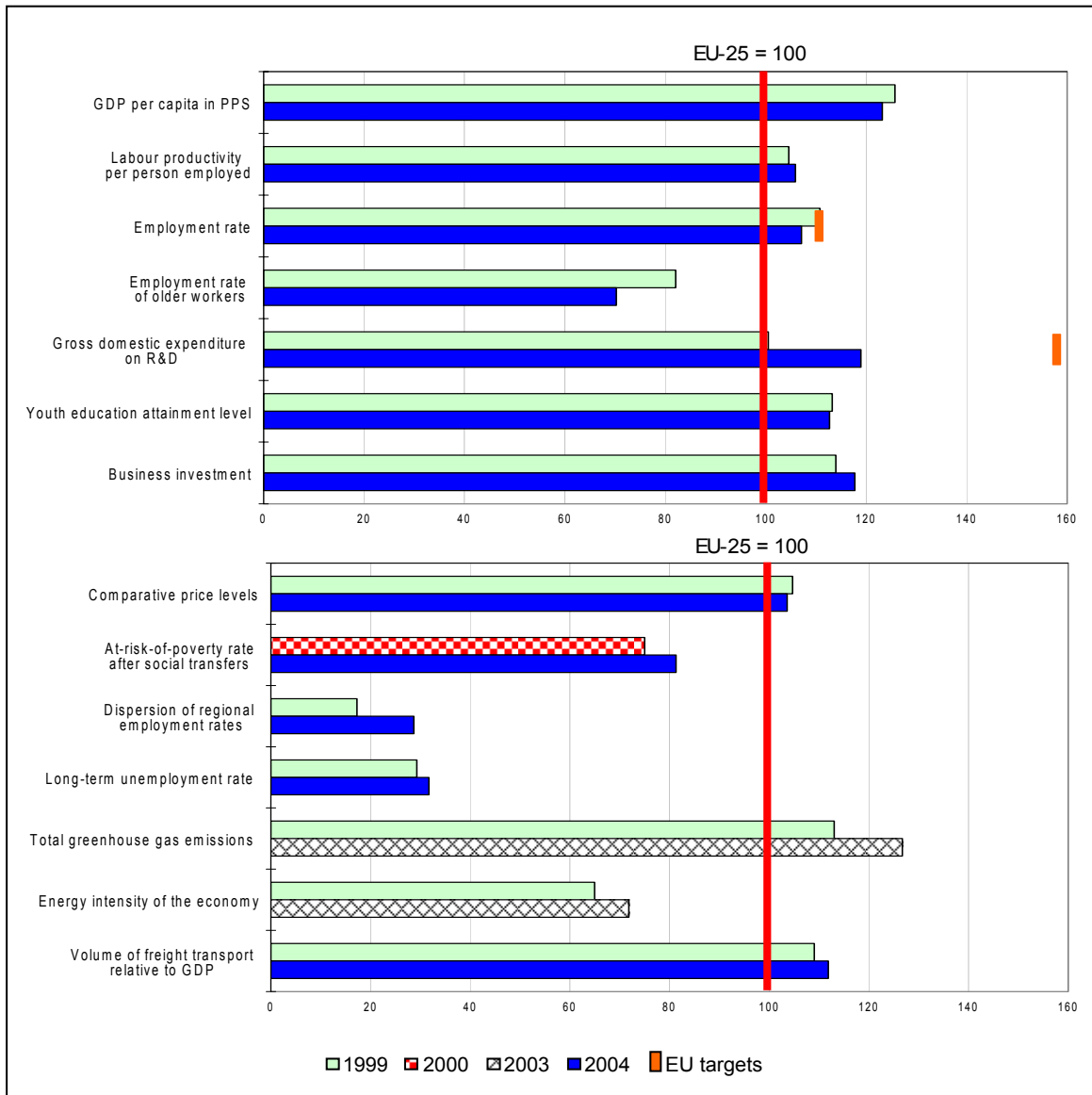
20. In line with the Integrated Guidelines, the Austrian National Reform Programme identifies and responds to the main challenges facing Austria, namely sustainability of public finances; R&D and innovation; infrastructure; international competitiveness; environmental sustainability; labour market and employment; and education and training. However competition in services has not been addressed as a main challenge. Overall, the different policy areas are well integrated within the NRP, which is coherent and for the short-term adequate and realistic. A more ambitious and longer-term approach would have been welcome.
21. Implementing measures are not always described with precision. More information would be required to assess whether the financial commitments in the NRP are fully consistent with the overall aim of reaching budgetary balance.
22. The programme's strengths include:
  - coherent strategies to boost innovation and environmental technology;
  - appropriate measures to attract and retain more people in employment, including reinforcing active labour market policy and reductions in non-wage costs;
  - initiatives to modernise and promote apprenticeships for young people.
23. Among the points requiring further attention are:
  - improving competition in services, where there are currently severe regulatory obstacles;
  - further measures to address the low employment rate of older workers and investment in the vocational training of adults.

24. Taking due account of the above, Austria is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Austria has dealt with the issues mentioned in paragraph 23. In this context, the Commission looks forward to discussions with the Austrian authorities as part of the new partnership for growth and jobs.

#### **PART IV: STATISTICAL GRAPHS AND DATA**

# AUSTRIA

	AT						2010 National target	EU-25						2010 EU target	
	1999	2000	2001	2002	2003	2004		1999	2000	2001	2002	2003	2004		
GDP per capita in PPS	125.7	126.4	122.6	120.5	121.4	123.2	3.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0	
Labour productivity per person employed	104.6	105.9	103.6	102.5	103.5	105.9		100.0	100.0	100.0	100.0	100.0	100.0		
Employment rate	68.6	68.5	68.5	68.7	68.9	67.8b		61.9	62.4	62.8	62.8	62.9	63.3		
Employment rate of older workers	29.7	28.8	28.9	29.1	30.3	28.8b		36.2	36.6	37.5	38.7	40.2	41.0		
Gross domestic expenditure on R&D	1.88	1.91	2.04	2.12	2.19e	2.26e		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe		3.0
Youth education attainment level	84.7	84.7	84.1	85.1	83.4b	86.3b		74.8	76.3	76.1	76.5	76.5	76.6		
Comparative price levels	104.7	102.0	102.6	105.2	105.7	103.6p		100.0	100.0	100.0	100.0	100.0	100.0p		
Business investment	20.4	21.3	20.9	19.4	20.2	19.9		17.9	18.3	17.7	17.1	16.7	16.9		
At-risk-of-poverty rate after social transfers	12.0	12.0	12.0	:	13.0b	13.0		:	16.0	15.0	15.0	15.0	16.0		
Dispersion of regional employment rates	2.3	2.5	2.6	2.5	2.9	3.5		13.3	13.4	13.5	13.3	12.9	12.2		
Long-term unemployment rate	1.2	1.0	0.9	1.1	1.1	1.3b		4.1	3.9	3.8	3.9	4.0	4.1		
Total greenhouse gas emissions	102.4	103.2	108.1	110.1	116.6	:		90.6	90.5	91.4	90.7	92.0	:		
Energy intensity of the economy	139.6	134.4	142.8	139.9	150.5	:		214.9	208.8	209.7	206.5	209.5	:		
Volume of freight transport relative to GDP	109.8	112.3	117.1	119.0	117.8	117.0b		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e		





## Belgium

1. After steady real GDP growth in 1996-2000 averaging 2.7%, Belgium experienced a sharp downturn. However, since the end of 2002, growth has rebounded somewhat more strongly than the euro-area average. GDP per capita was at 119% of the EU average in 2004. Labour productivity growth has been slightly below the EU average over the last decade, but the level is among the highest of the EU. Since 2000, Belgium has managed to maintain a balanced budget and to achieve a substantial reduction of the high debt ratio (97.4% in 2004)<sup>2</sup>. Employment rate is low (60.3% in 2004), especially for young and older people. The unemployment rate was at 7.9% in 2004.

### PART I: GENERAL ASSESSMENT

2. The Belgian National Reform Programme (NRP) identifies six main priorities in order to create growth and jobs: the sustainability of public finances; the reduction of labour costs; the creation of a more dynamic labour market; the stimulation of the economy through investment and reforms; strengthening the social security system; and the strengthening of synergies between environmental protection and growth. The Commission shares the NRP's analysis of the main priorities.
3. The NRP provides a fairly coherent national strategy to address the challenges, setting reasonable and consistent objectives across policy areas and presenting measures which in most instances appear relevant and adequate. The NRP could benefit from a more coordinated approach between the federal and regional governments. For the total proportion of GDP invested in R&D, the NRP sets for Belgium the target of 3% of GDP by 2010, equal to the EU-wide target. It also sets the same target as the EU as a whole for employment rate (70%), though without a precise timeframe. The programme sets out in addition a number of realistic national targets. Information on budgetary allocations or impact is scarce. In particular, the programme is not explicit on how the budgetary impact of the new initiatives will be reconciled with budgetary targets. The NRP refers only in passing to potential financial support from the EU Structural Funds. Combining measures to raise the average exit age from the labour force with measures to reduce the tax burden on labour while also building up budgetary surpluses is a particularly tough challenge.
4. Consultation and efforts to develop ownership of the document at government and administrative level have been fairly substantial. The NRP has been adopted by all Belgium's federal and regional governments, though the relevant parliaments were not involved. The drafting of the NRP was coordinated at federal level by the Prime Minister's Cabinet. Regional authorities and social partners have contributed extensively and are expected to play an important role in the implementation of many of the proposed measures. One region has elaborated a regional reform programme, attached to the NRP, whilst for other regions and communities reference to other specific programmes has been made.

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<sup>2</sup> For 2005, discussions with Eurostat on the statistical treatment of some operations have not yet been finalised.

## **PART II : ASSESSMENT BY POLICY AREA**

### **Macro-economic policies**

5. The main macro-economic challenges identified in the NRP are the sustainability of public finances, while preserving the social security system, and the improvement of the competitiveness of Belgian enterprises through strict control of the cost of labour. The Commission shares this analysis.
6. Since 2000, Belgium has managed to maintain a balanced budget and achieved a substantial reduction of its high debt ratio. The NRP sets the aim of reducing the debt ratio further by maintaining a balanced budget and gradually building up surpluses from 2007 onwards (0.3% of GDP in 2007 and 0.6% in 2008). It presents a comprehensive strategy based on fiscal consolidation aiming at financial sustainability and ensuring adequate pensions, notably through improvements to minimum pension levels and further steps to strengthen incentives to work longer. The programme also covers recent measures taken to limit the growth of healthcare expenditure but it does not fully explain how the authorities plan to achieve the budgetary surpluses announced. Increasing employment could contribute significantly to this by widening the tax base while reducing the cost of unemployment benefits, but the NRP does not assess the anticipated budgetary impact of its employment policy.
7. The NRP sets the objective of reducing the current tax burden on labour (currently at 42.6% of the wage cost) to the average of the neighbouring countries (38.4%) by 2010. The Commission supports this objective but the NRP does not comprehensively set out the measures the government will take to compensate for the anticipated loss in tax revenues (estimated at 2.2% of GDP), especially in view of the budgetary targets. The NRP also emphasises the importance of wage moderation to preserve Belgium's competitiveness. In this respect, the programme refers to Belgium's institutional context, in particular the 1996 competitiveness law and the existing system of wage negotiations, as instruments facilitating continued wage moderation. However, this system seems to be vulnerable in a context of increasing national inflation and wage moderation in the neighbouring countries.
8. Overall, the NRP sets rather ambitious macro-economic objectives. Only a few specific measures or new initiatives are presented for the period 2005-2008. The targets set will help focus policy and implementation efforts but some further fundamental choices remain to be made regarding alternative sources of revenues and/or specific measures to restrict expenditure, so as to ensure that budgetary, competitiveness and employment targets are compatible.

### **Micro-economic policies**

9. The NRP presents a wide range of priorities, including: the promotion of R&D and innovation; the improvement of market functioning; support for entrepreneurship; investments in infrastructure; and the encouragement of sustainable use of natural resources.
10. Belgium confirms its objective of reaching investment of 3% of GDP in R&D by 2010, which would involve reversing the downward trend in R&D intensity since

2001 (from 2.2% in 2001 to 1.9% in 2003). The programme intends to intensify public investment and to stimulate private investment in R&D, through supporting “competitiveness clusters”, enhanced co-operation between enterprises and strategic research centres, the promotion of innovation in SMEs, in particular by a better use of patents and through the protection of intellectual property rights. Measures are also set out to strengthen human resources in R&D in the private sector. The stimulation of research and innovation in the services sector and the use of public procurement receive relatively little attention. As regards co-operation and networking, it is not wholly clear from the NRP whether there is a strong enough strategy to encourage international cooperation through participation in cross-border projects and clusters.

11. To enhance the economic climate for investments and enterprises, the NRP stresses the need to improve market functioning. Proposals to reform competition policy include further removal of barriers to competition in services markets including in network industries, redirection of state aid towards horizontal objectives such as R&D, innovation or environment, and the reinforced role of the competition authorities. A new competition law aims at redesigning the architecture of the regulatory framework, in particular by amending the role of the Competition Council towards the sectoral regulators in network industries. It will be important to equip such regulatory bodies with adequate resources and to ensure their independence.
12. The programme also presents useful measures to expand investment in infrastructure, to attract foreign investment, to spread access to ICT through a national plan to reduce the digital divide, and to improve energy efficiency and the use of renewable energies. The reinforcement of the drive for better regulation described in the NRP, including the use of ex-ante impact assessment of new legislative proposals, can make a significant contribution to improving the business environment by reducing administrative costs. The NRP makes a commitment to improve the implementation of internal market law by intensifying efforts to reduce both Belgium’s deficit in writing EU Directives into national law and the number of infringement cases against the country.
13. Overall, the NRP presents a wide range of positive micro-economic initiatives seeking to raise Belgium's economic growth potential. The coherence of the NRP would benefit from better coordination of specific measures across the different levels of government.

## **Employment**

14. The NRP identifies two main employment priorities: first, raising employment rates, in particular by tackling youth and long-term unemployment and by promoting active ageing; and second, further reducing the high tax burden on labour. The Commission supports this choice.
15. Given the low employment rates, especially for youth, older people and women, attracting and retaining more people in employment is central to the Belgian NRP. To help achieve the employment rate targets, a “Pact Between Generations” has been agreed by the government. The Pact contains some new measures to strengthen existing active labour market measures, to tackle youth unemployment and to promote a more comprehensive active ageing strategy. The eligibility criteria for

early retirement schemes will be gradually tightened, although the impact of these measures will depend on the extent to which exceptions and alternative routes remain. The Pact seems an interesting first step to increase the employment rate of older workers.

16. As regards long-term unemployment, recent measures imposing stronger job search requirements show some early positive results and are entering their second phase covering 30 to 40 year olds. The reinforced work bonus scheme should further reduce the marginal effective tax rate for unemployed people taking up a job, which is currently the highest in the EU. The integration of ethnic minorities is identified as a priority but no new measures are proposed. Cooperation between public employment services - for example through a better exchange of vacancies - and increased language training are included in the NRP and should promote interregional mobility, which is particularly important for the Brussels region and surrounding areas. However, no information is provided on budgets or timing.
17. In order to promote the adaptability of workers and enterprises, the NRP highlights targeted reductions of non-wage labour costs. The tax wedge has been reduced substantially over the last five years but is still the highest in the EU. The goal of bringing the tax burden on labour down to the average in neighbouring countries by 2010 will require additional efforts compared to previous years. The NRP also sets out measures to better accompany the restructuring of enterprises, with a view to making early retirement a last resort. The change of legislation intended to involve temporary work agencies in fighting youth unemployment is interesting.
18. Increasing investment in human capital is an important element of the NRP. The commitment to raise private investment in training to 1.9% of the wage bill, set for 2004 but not yet reached, is reconfirmed for 2006. A "Training Agenda 2010" will include measures aiming at one in two workers receiving training every year by 2010. These plans are likely to lead to significant and necessary improvements to the results from Belgium's training policies, which until now have been rather limited. Measures announced for the recognition of informal qualifications and competencies are particularly interesting.
19. Overall, the employment strand of the NRP is based on assessing, implementing and building on measures already taken. Many initiatives with high potential are included, although their impact will need to be carefully monitored given the size of the challenges. The NRP provides a timeframe for most measures, but limited information on budgetary resources. Addressing important regional labour market disparities is left to the regional authorities, whereas a more coordinated approach might provide added value.

### **PART III : CONCLUSIONS**

20. In line with the Integrated Guidelines, the Belgian National Reform Programme identifies and responds to the main challenges facing Belgium, namely the sustainability of public finances; the reduction of labour costs; the creation of a more dynamic labour market; the stimulation of the economy through investment and reforms; strengthening the social security system; and the strengthening of synergies between environmental protection and growth. Overall, the NRP provides an

integrated national strategy to address the challenges, with clear analysis, a number of realistic targets and relevant measures.

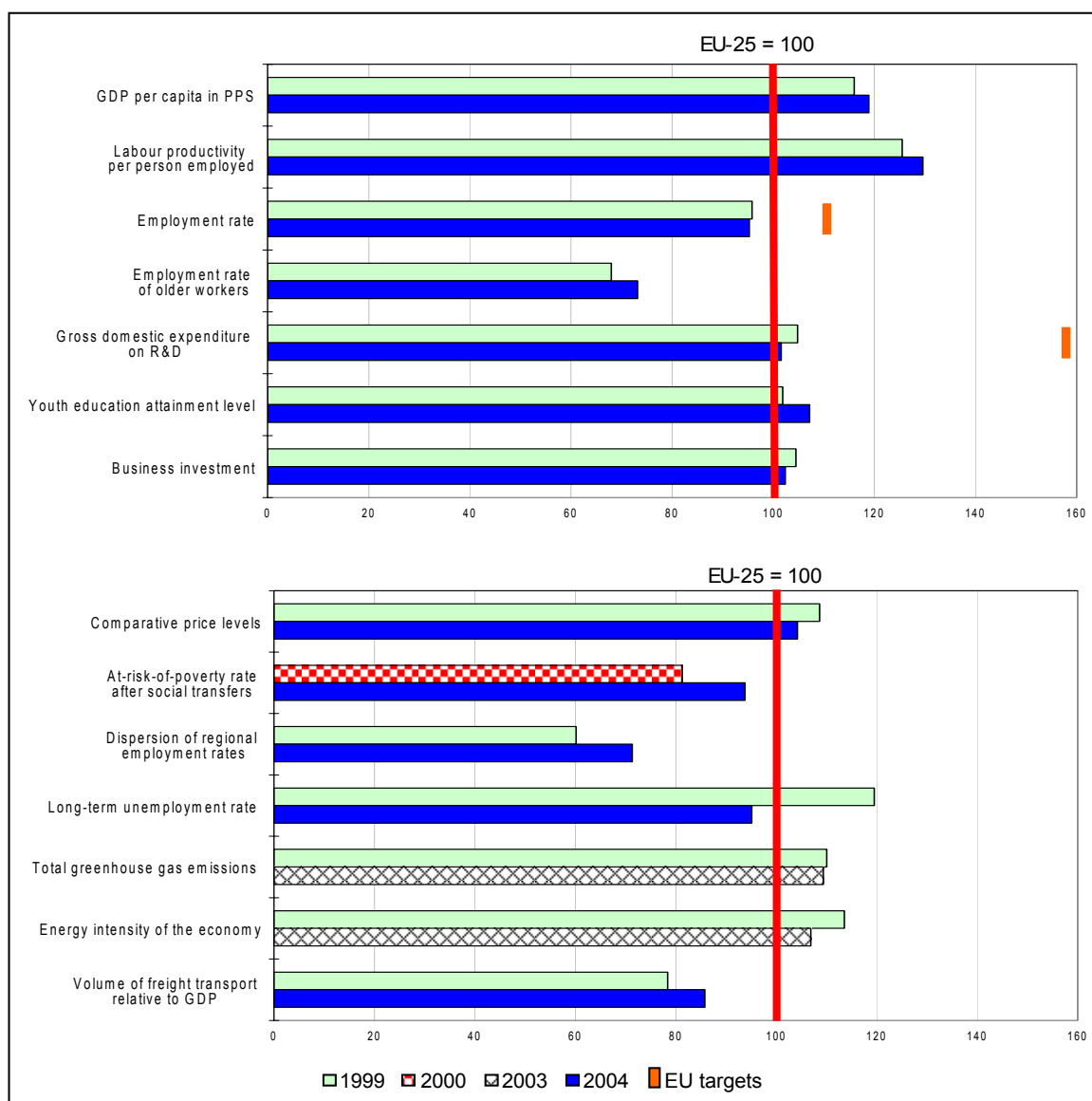
21. In some policy fields, the programme would benefit from a more coordinated approach between the federal and regional governments. It is not explicit on the financial impact of the new initiatives or on reconciling that impact with budgetary targets, particularly in so far as combining a reduction of the tax burden on labour with increasing budgetary surpluses is concerned. Effective implementation and monitoring of measures to raise the effective exit age from the labour market will be needed.
22. The programme's strengths include:
  - measures to expand investment in infrastructure, increase access to ICT and improve energy efficiency;
  - good first steps towards the development of a comprehensive active ageing strategy.
23. Among the points requiring further attention are:
  - additional efforts to bring down the tax burden on labour, to meet the target of matching the average in neighbouring countries by 2010 in the context of sustained budgetary consolidation;
  - tackling regional employment disparities.
24. Taking due account of the above, Belgium is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Belgium has dealt with the issues mentioned in paragraph 23. In this context, the Commission looks forward to discussions with the Belgian authorities as part of the new partnership for growth and jobs.

#### **PART IV: STATISTICAL GRAPHS AND DATA**

## BELGIUM

	BE							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	116.0	117.3	117.7	118.1	118.6	118.9	70.0*	100.0	100.0	100.0	100.0	100.0	100.0	70.0
Labour productivity per person employed	125.5	126.7	127.1	128.3	129.3	129.6		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	59.3	60.5	59.9	59.9	59.6	60.3		61.9	62.4	62.8	62.8	62.9	63.3	
Employment rate of older workers	24.6	26.3	25.1	26.6	28.1	30.0		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	1.96	2.04	2.17	1.99	1.92	1.93f		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	
Youth education attainment level	76.2	80.9	79.4	81.1	81.3	82.1		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	108.6	105.8	102.8	102.3	104.0	104.2p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	18.7	19.0	18.8	17.6	17.2	17.3		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	13.0	13.0	13.0	:	15.0b	15.0		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	8.0	7.9	8.0	8.0	7.7	8.7		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	4.9	3.7	3.2	3.6	3.6	3.9		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	99.7	100.6	99.9	99.0	100.6	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	244.0	236.1	228.1	213.6	223.9	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	78.9	98.1	100.0	99.1	95.0	89.7		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	

\* National target: 70% as soon as possible



# Cyprus

1. In 2004, Cyprus's GDP per capita stood at 84% of the EU average, the highest of the ten new Member States. With an average annual GDP growth rate of 4.1% in 1995-2004, Cyprus was among the best performers in Europe. Since the mid-1990s real wage growth has outpaced productivity increases, even though productivity growth has been slightly above the EU average, leading to some loss of price competitiveness. Nevertheless, unemployment is low at 5.2% in 2004. The total employment rate at 69.1% is close to the Lisbon target.

## **PART I: GENERAL ASSESSMENT**

2. The Cypriot National Reform Programme (NRP) emphasises the objective of increasing the growth potential of the economy and living standards for citizens, aiming at real convergence with the EU. It identifies challenges in the following areas: fiscal sustainability; quality of public finances; R&D, innovation and ICT; increasing the diversification of the economy; competition and business environment; environmental sustainability; infrastructure; human capital; and social cohesion. The Commission shares this analysis, though in the employment field it would give particular emphasis to lifelong learning and skills.
3. The NRP provides a clear and comprehensive overview of numerous specific measures and links them well to final objectives. It includes an ambitious and challenging target for investment in R&D, 0.65% of GDP for 2008 and an ambitious but realistic target for an employment rate of 71% by 2010. Most measures are described in detail, with an implementation schedule, and with the annual budgetary impact indicated where relevant. At the same time, the links between the overall strategy and some objectives could be explained more clearly. The role of EU Structural Funds is highlighted, but not elaborated upon, despite the importance of this funding for realising certain aspects of the Cypriot NRP.
4. Consultation and efforts to develop ownership of the document have been substantial. The NRP was formally adopted by government and discussed at parliament. It has gone through extensive consultations with social partners and will be subject to continuous dialogue in the implementation period. A monitoring and follow-up mechanism will be established under the Ministry of Finance.

## **PART II: ASSESSMENT BY POLICY AREA**

### **Macro-economic policies**

5. The main macro-economic focus in the NRP is on fiscal consolidation through expenditure restraint and increased revenues. It also targets restructuring government expenditure toward capital outlays, enhancing fiscal management and transparency. It includes reforms in health care and social insurance, and labour supply and wage moderation measures. To a large extent, the Commission shares Cyprus's point of view on these challenges.

6. According to the NRP, these measures should result in reducing the general government deficit to 1.2% of GDP and government debt to below 60% of GDP by 2008 (and a deficit of 0.9% of GDP in 2009). Most measures are described in detail. Nevertheless, measures and time-schedules regarding the delayed reform of the healthcare system (part of the package of measures to address fiscal sustainability) are only summarily indicated. On social security reform, government proposals are presented, though the precise adjustments to be made to the system are to be agreed with social partners. Their budgetary impact is left open.
7. Overall, the macroeconomic reform measures outlined in the NRP are appropriate and their full and timely implementation would clearly help address the challenges identified in the NRP.

### **Micro-economic policies**

8. There are four microeconomic key challenges referred to in the NRP: promotion of R&D, innovation and ICT; enhancing competition/improving business environment; environmental sustainability; and upgrading basic infrastructure. These are consistent with the objective of diversifying the economy and strengthening its competitive advantages.
9. The need to further increase R&D investment, in particular by private business and to promote innovation and ICT diffusion is recognised as essential to securing long-term growth. Given the low level of R&D in Cyprus, reaching the ambitious target of 0.65% by 2008 represents a considerable challenge, notwithstanding impressive public spending growth in this area in recent years. The proposed policy mix concentrates on boosting the scientific base and private R&D and developing human resources. It assembles the necessary building blocks for developing a full-scale research and innovation system, although questions remain regarding potential bottlenecks along the way and links between public and private R&D spending. The programme appropriately envisages the creation of innovation poles, along with “business incubators” to help emerging companies survive and grow during the start-up period. Some important issues, such as promoting cross-border knowledge transfer and venture capital for innovation, may deserve more attention. The clear presentation in terms of timing, costing, and measurability of the large number of measures on ICT bodes well for their effectiveness.
10. The strategy for improving investment and growth conditions by enhancing the business climate and competition must be seen against the background of a generally favourable business environment and strong competition in much of the economy. The measures proposed to enhance competition in sectors where it was absent until recently can be seen as initial steps. Introducing comprehensive evaluations of state aid and focussing on market failures is appropriate and builds on progress already made. Reducing the burden of regulation and systematically assessing its impact will be particularly important for SMEs. The proposed loan guarantee facility will help SMEs overcome financing constraints during the start-up phase. The intended amendment to the bankruptcy law is not fully clear from the NRP. The steps envisaged to increase public sector efficiency could do much to help improve the business climate, although the absence of projected funding for most of them raises questions about their effectiveness. Measures to upgrade basic infrastructure respond well to the challenge identified.



11. Given current environmental problems, the importance of environmental sustainability for growth and jobs is well recognised in the NRP, in particular with regard to the impact of environmental degradation on tourism. The policy priorities to increase energy efficiency (including the use of renewables) are set out clearly and reflected in relevant and concrete measures that promise to be effective in reaching their specified objectives.
12. For the most part, micro-economic policies are clearly described and details of timetables and budgetary impacts are included. However, more prioritisation and consideration of synergies between the key challenges would be beneficial.

### **Employment Policies**

13. The employment challenges set out in the NRP are achieving full employment, improving quality and productivity at work and strengthening social and territorial cohesion. Five priorities flow from these: promoting more effective use of domestic labour reserves; better managing economic migration; increasing the flexibility of the labour market; developing human capital; and further enhancing social inclusion. The Commission subscribes to these priorities.
14. The NRP aims to attract and retain more people in employment through a lifecycle approach involving a wide range of measures. There is high priority for implementing appropriate active labour market measures and substantial funding is allocated to this. The already high female employment rate is expected to increase to an ambitious but realistic target of 63% by 2010, through the reconciliation of work and family life, flexible forms of work, upgrading of skills and reducing the gender pay gap, which is higher than the EU average. With an appropriate legal framework already in place, the authorities are due to discuss with social partners the development of a detailed policy favouring flexible but secure forms of work, including by making part-time work more attractive for those currently inactive. Further measures to activate older workers are underway, and it has been agreed that the retirement age in the public sector will gradually increase to 63 by 2008. While the employment of Turkish Cypriots is actively encouraged, a review of the economic migration strategy is awaiting endorsement by the social partners. New legislation is expected in 2006.
15. The development of a comprehensive lifelong learning strategy to respond to the shift towards a knowledge-based economy could benefit from more clarity and focus. High priority is given to numerous measures to reform the vocational education and training systems. There is limited clarity on how these reforms will make vocational education and training, as well as the outdated apprenticeship scheme, more attractive and credible and on how they will offer vocational career paths which are alternative to general education. Reducing the relatively high rate of early school leaving is not addressed. A system of continuing education and training is well established. Measures to improve opportunities for university studies in Cyprus are expected to reduce the "brain drain". A quality certification system for training providers is proposed and will be followed by the establishment of a quality certification scheme for vocational qualifications.

16. The challenge of social and labour market integration of vulnerable groups is addressed in an integrated manner in the NRP, with appropriate initiatives targeting most groups.
17. Clear employment targets are set in the NRP, but other indicators in the field and benchmarks are scarce, thus making the evaluation of results a difficult task. Budgetary resources are earmarked, but for some important measures, notably the reform of the apprentice scheme, appear insufficient.

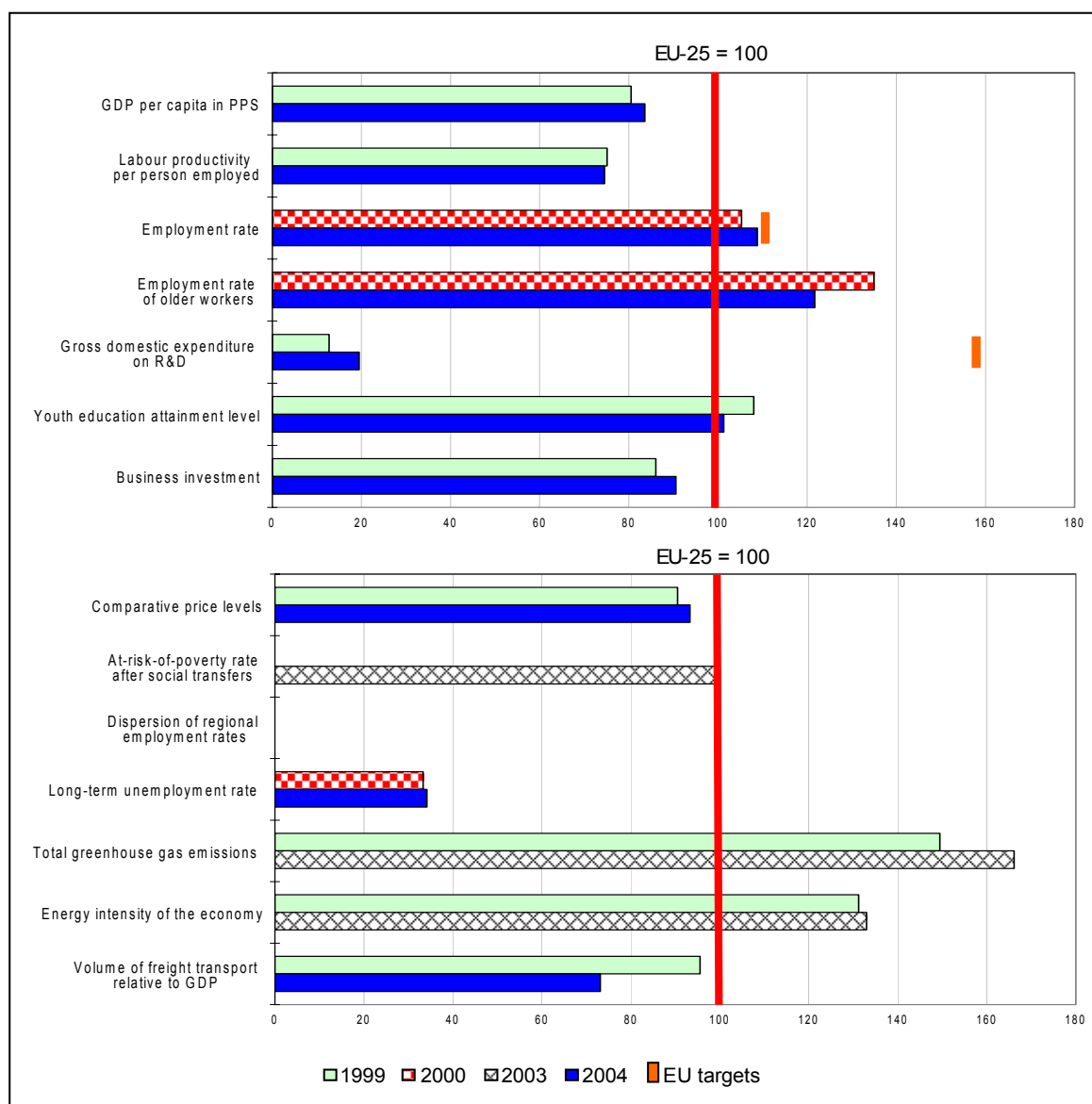
### **PART III: CONCLUSIONS**

18. In line with the Integrated Guidelines, the Cypriot National Reform Programme identifies and responds to the main challenges facing Cyprus, namely fiscal sustainability; quality of public finances; R&D, innovation and ICT; increasing the diversification of the economy; competition and business environment; environmental sustainability; infrastructure; human capital; and social cohesion, though more attention could have been paid to the development of vocational skills and lifelong learning. Overall the programme is clear, comprehensive and ambitious. However, more prioritisation in the micro-economic area will be necessary.
19. Most measures are described in detail, with an implementation schedule, and with the annual budgetary impact indicated where relevant. The extensive consultations undertaken with social partners and the clear provision for ongoing dialogue will facilitate effective and timely implementation.
20. The programme's strengths include:
  - the initiative to develop a research and innovation system;
  - the priority and funding allocated to active labour market measures;
  - efforts to further increase the already high female employment rate.
21. Among the points requiring further attention are:
  - addressing long term sustainability of the public finances, including reforms of social security;
  - measures to reduce the rate of early school leaving.
22. Taking due account of the above, Cyprus is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Cyprus has dealt with the issues mentioned in paragraph 21. In this context, the Commission looks forward to discussions with the Cypriot authorities as part of the new partnership for growth and jobs.

### **PART IV : STATISTICAL GRAPHS AND DATA**

# CYPRUS

	CY							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	80.5	81.3	83.2	82.4	80.5	83.6	71.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	75.1	73.6	73.6	72.4	71.1f	74.5f		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	:	65.7	67.8	68.6	69.2	68.9		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	:	49.4	49.1	49.4	50.4	49.9		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	0.24	0.25	0.26	0.31	0.35	0.37p		0.65 (2008)	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	80.8	79.0	80.5	83.5	79.5	77.6		74.8	76.3	76.1	76.5	76.5	76.6			
Comparative price levels	90.5	91.3	91.9	90.9	96.5	93.3p		100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	15.4	14.3	14.1	15.2	14.3	15.3		17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	:	:	:	:	15.0	:		:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	-	-	-	-	-	-		13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	:	1.3	1.0	0.8	1.1	1.4		4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	135.4	141.6	140.7	145.1	152.8	:		90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	282.0	282.3	274.4	269.9	278.6	:		214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	96.2e	94.6e	93.9e	95.7	99.5	76.5		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e			



## Czech Republic

1. Over the period 1996-2000 economic growth in the Czech Republic averaged 1.5%, but since then growth has increased to 2.9% on average, and has been even more robust in recent years, driven mainly by investment and strong exports. Labour productivity growth has been slightly above the EU average over the last decade. GDP per capita has risen to 71% of the EU average (2004). The employment rate is slightly above the EU average at 64.2% (2004) and employment performance has started to improve. The unemployment rate is at 8.3 % (2004).

### **PART I: GENERAL ASSESSMENT**

2. The Czech National Reform Programme (NRP) identifies three main overall challenges: to continue public finance reform; to strengthen and increase industrial competitiveness while respecting the need for sustainable resources; and to increase labour market flexibility. The Commission shares this analysis of the main priorities.
3. The strategy presented in the NRP is essentially a continuation of existing policies. The 46 policy areas identified for action in the NRP are relevant and represent a set of consistent and mutually interlinked measures but there is little information on prioritisation between them. The NRP has been drafted as a brief general document with the intention of making it accessible to a wide public and intentions are described often only in general terms. In only certain areas are concrete reforms set out and information on their budgetary impact is limited, though in some cases more detail is available in specific national strategic documents. Quantitative targets are identified for public finances, for public expenditure on R&D (1% of GDP by 2010) and employment rates (66.4% for overall employment in 2008). The role of Structural Funds is specified in several parts of the NRP, in particular the employment part.
4. Consultation and efforts to develop ownership of the document have been fairly substantial, with more envisaged. In preparing the NRP, the Deputy Prime Minister for Economic Affairs was appointed as political coordinator. A governance structure was established involving relevant ministries and social partners. The NRP was discussed with the Parliament and with the social partners. The government has announced that the general public will be consulted and measures to achieve a high degree of visibility for the Lisbon process will be undertaken.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. Continuing reform of public finance is expected to contribute to macroeconomic stability and sustainable growth. The strategy proposed in the NRP outlines six priorities with respect to these objectives, with particular focus in the medium term on meeting the Maastricht criteria on budget deficits and government debt and

emphasis in the long term on safeguarding the sustainability of public finances. The Commission subscribes to the focus on these two key areas.

6. According to the NRP, the macroeconomic policies it sets out should result in decreasing the general government deficit to less than 3% of GDP and in keeping government debt below 60% of GDP by 2008, in order to be able to join the euro area by 2010. After 2008, the target is gradually to reduce deficits to below 1% of GDP. However, these objectives are not very ambitious in the light of the better than expected budgetary outcomes in 2004 and 2005. The programme refers to the main instrument of medium-term budgetary consolidation – expenditure ceilings for central government but the record on implementing these is mixed so far. The NRP recognises that the long-term sustainability of public finances is a central problem in the Czech Republic but not enough detail is presented to permit an assessment of the strategy proposed to deal with this. To improve long-term sustainability a coordinated action plan is proposed, requiring medium-term budgetary consolidation along with reforms of pensions, the health care system and the labour market. Although this coordinated approach is evidence of good intentions, insufficient detail is given on how it will be implemented in practice. There are positive measures to increase the transparency of public finances, in particular by disclosing state guarantees and contingent liabilities.
7. The fiscal strategy proposed is not very ambitious and is not supported by a clear schedule for implementation. For medium-term consolidation it will be important to ensure that the expenditure ceilings are respected and to improve budgetary planning. The long-term sustainability issue requires more specific attention and especially a clearer picture of health care and pension reforms.

### **Micro-economic policies**

8. Among numerous microeconomic priorities the following four receive most attention in the NRP: R&D and innovation; the business environment; the modernisation and development of transport and ICT networks; and sustainable use of resources. The Commission shares the view that these are key to improving economic growth and employment.
9. R&D expenditure is currently 1.3% of GDP, one half of which comes from public funds. A target has been set for public R&D investment to reach 1% of GDP by 2010, and budgetary plans reflect this targeted increase up to 2008. However, no target is included in the NRP for overall R&D intensity. Efforts covered in the NRP to stimulate private research expenditure by tax deductions have the potential to help boost competitiveness, as does a planned change to make the funding mechanism for public research institutions more favourable to industrial research. The NRP presents a thorough analysis of the current problems with the R&D system. Changing the R&D structure favouring special-purpose financing over institutional financing is envisaged. However, issues such as prioritisation in the R&D budget, improving R&D infrastructure or specific measures to deal with developing and investing in highly qualified personnel for R&D need further development. With respect to innovation policy, the NRP addresses the challenges created by insufficient infrastructure and finance in rather general terms, while the coverage of the direct support for innovation activities needs further clarification. The NRP does not

explicitly discuss measures to improve the quality of innovation support services and to strengthen innovation links between domestic and foreign-owned companies.

10. The NRP sets out a plan to enhance the business environment through better regulation and by supporting SMEs. The measures to improve regulation are focused on administrative costs and impact assessment and represent a very strong reform agenda in the area of better regulation. The NRP lists a number of ongoing SME programmes that will end in 2006 but no indication is given in the NRP itself on further action in this area.
11. In other important areas such as the modernisation and development of ICT and transport networks and the sustainable use of resources, issues are well identified in the NRP, but the measures proposed to deal with them are somewhat scattered. The NRP presents strongly focused measures to invest in broadband connections (the target of making the broadband internet available to 50% of the population by 2010 is mentioned) and stimulate the availability of online public services.
12. The ongoing micro-economic policy initiatives presented in the NRP are numerous and in general useful. However, there are certain gaps in them and it remains to be seen whether they bring solutions to the problems and challenges identified. Linkages between different policy measures should be further developed. Attention will need to be paid to ensuring the timely and full implementation of ongoing policies.

### **Employment policies**

13. The key challenge of increasing labour market flexibility is complemented by seeking greater inclusion in the labour market and improving education. Within these challenges numerous general priorities are identified. The Commission subscribes to the choice of challenges, though three issues deserve more attention: the most disadvantaged groups in the labour market; regional disparities in unemployment; and the gender dimension.
14. Labour market flexibility is given prominence in the NRP, which lists a number of useful initiatives to promote making work pay and geographical mobility. The programme includes measures such as reducing taxes for low-wage earners and reforming the social benefits system to encourage the activation of benefit claimants. The current legal provisions promoting flexible forms of labour relations (part-time work, fixed-term contracts, teleworking) are still only partly used, though the new Labour Code being discussed by the Czech Parliament is expected to allow for more operational flexibility in the organisation of work and working time arrangements and to provide greater contractual freedom in employment relationships. The practical effects of these measures, once adopted and applied, will need to be carefully assessed. The NRP recognises the modernisation of public employment services as essential for the success of employment policy, though few concrete measures are proposed in this area and the problems of limited personnel and funding remain to be resolved.
15. The NRP identifies problems of inclusion in the labour market and of potential labour market shortages and strives to address these problems by improving the inclusion of three specific groups: the young, the elderly, and women. The measures

proposed are based mainly on an extension of existing labour market policies. Particular attention is paid to active immigration policy and the inclusion of foreigners in the labour market. The NRP does not cover measures targeted at promoting the inclusion of disabled people or of resident ethnic minorities such as the Roma population, though the Czech authorities have indicated some separate information on this.

16. In the area of investment in human capital, the NRP gives particular priority to reforming curricula for primary education and to improving relations between employers and educational and professional institutions in order to better adapt education and training systems to labour market needs. There has been some progress in stimulating participation in tertiary education and lifelong learning. More effort is needed however, to implement a comprehensive lifelong learning strategy, especially in continuing education. The NRP stresses the need to increase incentives for individuals and employers to invest in training.
17. The NRP identifies a broad set of problems in the Czech labour market and attempts to address them. However, more effort will be needed to increase investment in human capital so the proposed reforms in the educational system can be fully implemented.

### **PART III: CONCLUSIONS**

18. In line with the Integrated Guidelines, the Czech National Reform Programme identifies and responds to the main challenges facing the Czech Republic, namely to continue public finance reform; to strengthen and increase industrial competitiveness while respecting the need for sustainable resources; and to increase labour market flexibility. Overall, the NRP includes some useful initiatives, notably in micro-economic policy, but in some areas lacks clear priorities and concrete measures.
19. The budgetary impact of measures is not always clearly spelled out in the NRP. It will be crucial to develop targets, time schedules for the implementation of reforms and appropriate monitoring processes for the successful implementation of the strategy.
20. The programme's strengths include:
  - important steps to improve regulation and the business environment;
  - a wide-ranging set of measures to address potential shortages in the labour market, especially with regard to making work pay and to particular groups such as the young, the elderly, and foreigners.
21. Among the points requiring further attention are:
  - securing the long-term sustainability of public finance, especially with regard to reforms of pension and health care systems;
  - more emphasis on improving human capital through lifelong learning, taking account of the most vulnerable groups, and regional disparities in unemployment;

- policies to improve R&D and innovation and in particular to develop human capital for the R&D system and improve its functioning.
22. Taking due account of the above, the Czech Republic is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way the Czech Republic has dealt with the issues mentioned under paragraph 21. In this context, the Commission looks forward to discussions with the Czech authorities as part of the new partnership for growth and jobs.

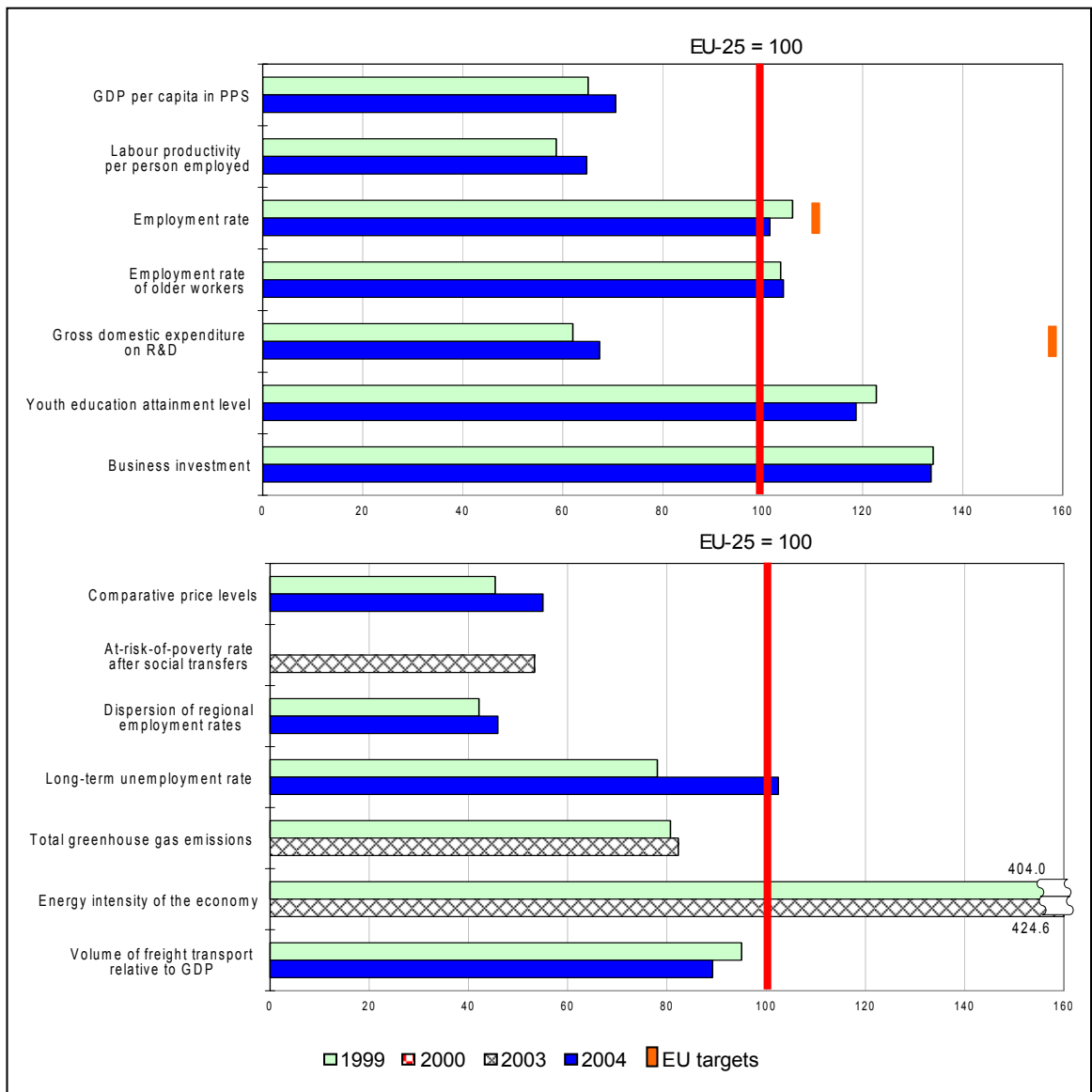
#### **PART IV: STATISTICAL GRAPHS AND DATA**



# CZECH REPUBLIC

	CZ							EU-25							
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target	
GDP per capita in PPS	65.1	64.0	65.1	66.6	68.1	70.6	66.4 (2008)  *	100.0	100.0	100.0	100.0	100.0	100.0	70.0	
Labour productivity per person employed	58.7	58.9	59.9	60.4	62.4	64.8		100.0	100.0	100.0	100.0	100.0	100.0		
Employment rate	65.6	65.0	65.0	65.4	64.7	64.2		61.9	62.4	62.8	62.8	62.9	63.3		
Employment rate of older workers	37.5	36.3	37.1	40.8	42.3	42.7		36.2	36.6	37.5	38.7	40.2	41.0		
Gross domestic expenditure on R&D	1.16	1.23	1.22	1.22	1.26	1.28		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe		3.0
Youth education attainment level	91.8	91.1	90.5	91.7	92.0	90.9		74.8	76.3	76.1	76.5	76.5	76.6		
Comparative price levels	45.4	47.2	50.3	54.7	55.5	55.0p		100.0	100.0	100.0	100.0	100.0	100.0p		
Business investment	24.0	24.7	24.3	22.9	22.7	22.6		17.9	18.3	17.7	17.1	16.7	16.9		
At-risk-of-poverty rate after social transfers	:	:	8.0	:	8.0	:		:	16.0	15.0	15.0	15.0	16.0		
Dispersion of regional employment rates	5.6	5.8	5.7	5.6	5.8	5.6		13.3	13.4	13.5	13.3	12.9	12.2		
Long-term unemployment rate	3.2	4.2	4.2	3.7	3.8	4.2		4.1	3.9	3.8	3.9	4.0	4.1		
Total greenhouse gas emissions	73.1	76.8	77.0	74.3	75.7	:		90.6	90.5	91.4	90.7	92.0	:		
Energy intensity of the economy	868.4	888.4	883.9	875.8	889.6	:		214.9	208.8	209.7	206.5	209.5	:		
Volume of freight transport relative to GDP	95.7	94.0	93.5	97.9	99.5	93.3		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e		

\* National target: 1% (2010) for the public sector



## Denmark

1. Denmark benefits from high GDP per capita (122% of EU average in 2004), productivity and employment levels. Annual real GDP growth has been some 2% on average in the last decade, while labour productivity growth per person employed has been at the speed of the EU average. The employment rate is the highest in the EU (75.7% in 2004). Employment growth has been strong since 2004 and the unemployment rate (5.4% in 2004), one of the lowest in the EU, has been further reduced.

### **PART I: GENERAL ASSESSMENT**

2. The Danish National Reform Programme (NRP) outlines four broad challenges: to prepare for the ageing of the population; reap the benefits of globalisation; strengthen the framework for improved productivity; and increase value for the users of public services. These broad challenges are translated into a number of priorities: improving competition in certain sectors; enhancing public sector efficiency; developing a knowledge society; securing environmental sustainability and energy; encouraging entrepreneurship; and increasing the labour supply. The Commission shares the NRP's analysis of the main priorities.
3. The Danish reform strategy is presented clearly and coherently. The NRP's approach is broad, ambitious, long-term and realistic. It aims to carry out existing policies and, if necessary, to reinforce them. Quantitative targets with timetables are set in some areas. The target set for R&D investment is to exceed 3% of GDP by 2010, the same level as the overall target for the EU. The employment target is to increase employment by between 50 000 and 60 000 people, corresponding to around 2% of the labour force, by 2010. The policies presented in the NRP often refer to broad lines for action and relatively few specific measures are presented. This is particularly the case for initiatives aiming at improving competition and increasing the labour supply. The NRP states, however, that further measures to raise labour supply and to strengthen education, innovation and entrepreneurship will follow on the basis of the reports and recommendations of two key advisory bodies appointed by the Government: the Welfare Commission, whose report was presented in December 2005, and the Globalisation Council, due to report in Spring 2006. The NRP also describes how EU structural funds will be used to promote the objectives.
4. Consultation and efforts to develop ownership of the document have been substantial. The NRP has been endorsed by the Government and presented to Parliament. The views of social partners, local authorities and representatives of civil society have been collected and are presented in annexes to the programme.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. The overall macro-economic aims are sound public finances, a stable exchange rate, price stability and high employment. The Commission fully subscribes to these aims.

6. The strategy to assure long-term fiscal sustainability is a continuation of the one in place for a number of years, consisting of building up government funds by saving budget surpluses in combination with increasing employment by around 2 per cent of the labour force by 2010. In the medium and long term, a higher level of employment is necessary to secure the future funding of welfare commitments. Policy to ensure fiscal sustainability in view of an ageing population continues to be based on the objective of an average annual general government budget surplus of 0.5-1.5% of GDP until 2010. On the expenditure side, a key objective is to limit the annual growth of real public consumption to 0.5 per cent up to 2010. Income taxes were cut by 0.7 per cent of GDP in 2004 and taxes will be further reduced to the extent that there is budgetary scope. Monetary policy aims at keeping the krone's exchange rate with the euro stable. This policy lays the basis for price stability in line with the euro area.
7. The implementation of the measures outlined in the programme should contribute significantly to attaining the objectives of the macro-economic strategy. However, few concrete measures are set out to achieve the increase in employment necessary for long-term fiscal sustainability.

### **Micro-economic policies**

8. The Danish government identifies as important challenges: enhancing competition in some sectors; strengthening public sector efficiency; developing a knowledge society; securing environmental sustainability and encouraging entrepreneurship. The Commission shares this analysis.
9. The NRP points to the objective of halving the number of sectors facing competition problems by 2010, in order to help bring consumer prices in Denmark, consistently the highest in the EU, more into line with the rest of the Union. Sectors currently affected by a lack of competition include parts of the construction sector, utilities, food processing and professional services. The NRP describes concretely how the authorities identify sectors facing significant competition challenges. It sets out measures to increase competition through amendments to the Competition Act and a review of competition-restricting rules. This will complement action already under way to make shop opening hours more flexible and to amend the Public Tender Act. While the measures envisaged have good potential to enhance competition, full details and clear schedules are not always given. Against this background, a swift implementation of these measures, including strengthening competition through combating cartels more effectively, would be positive.
10. The NRP also includes proposals to make public services more efficient. A planned reform will lead in 2007 to a large cut in the number of municipalities and is likely to deliver efficiency gains through economies of scale. In addition, the NRP presents measures to increase competition in the provision of public services, including enhanced competition between public and private providers.
11. Total R&D spending amounted to 2.6 per cent of Denmark's GDP in 2003, well above the EU average of 1.9 per cent. About 70 per cent of R&D spending is financed by the private sector. If Denmark maintains its current strategy and increases public R&D as intended, the 2010 target of 3 percent of GDP seems realistic. There remains scope to maximise the results of Denmark's relatively high

R&D spending in terms of further boosting productivity. In this respect, the NRP includes promising plans to better exploit technological opportunities by improving knowledge transmission between universities and the private sector, though it is not yet clear to what extent these plans will change incentives for public sector researchers to collaborate with the private sector. In addition, Denmark aims to promote e-government, use of ICT by SMEs, ICT skills and research. Broadband take-up is to be stimulated through competition, enhanced by a framework that strengthens convergence and security. The “National ICT policy initiatives”, however, lack detail.

12. The NRP makes positive efforts to decouple the link between economic growth and environmental impacts. Environmental taxes, such as the new tax on mineral phosphorous in animal feed and the reduction in tax on sulphur-free petrol, are used to ensure that prices better reflect the costs of environmental degradation for society. The 2005 energy strategy promotes energy-saving initiatives addressing in particular energy consumption in the transport sector.
13. While Danish entrepreneurship looks healthy on the basis of the indicator of business start-ups, few of the new firms develop into high-growth companies. The NRP therefore includes plans to grant certain entrepreneurs a three-year period of tax relief to provide an incentive for further growth. This is an interesting initiative and should be followed by a careful evaluation. The relatively small and illiquid stock market could hinder firm growth and the measures presented in the NRP to ease access to capital will help address this problem. An example is the Entrepreneurship Fund that provides early stage venture capital. The government aims to reduce the administrative costs of enterprises by 25 per cent between 2001 and 2010, and has developed a strategy to achieve this objective. With regard to internal market policy, Denmark’s efforts in terms of implementing internal market policy, for instance through a special task force, are encouraging.
14. The micro-economic policy initiatives in the NRP are likely to make a positive contribution to jobs and growth. In some cases, the proposed measures need to be more concrete in order to guarantee successful implementation. For example, few details are given on the timing of the measures to enhance competition.

### **Employment policies**

15. Against the background of the ageing population, the Danish NRP identifies increased labour supply through higher labour force participation as an important challenge. In addition, the NRP focuses on improving the adaptability of employees and enterprises, improving the basic school system and increasing the number of students in secondary and tertiary education. The Commission shares this analysis of the main challenge and priorities.
16. The NRP outlines a number of measures to attract and retain more people in employment in order to increase the labour supply by 2010 and beyond: tighter requirements to seek a job for immigrants who receive benefits; a lower average age for finishing tertiary education; reducing absence due to illness; increasing the average retirement age; and improved functioning of the labour market through overhauling employment policies. These measures have potential to further increase

the already high employment rates but might be insufficient to meet the challenge of a targeted increase of 50-60,000 persons in employment by 2010.

17. The Danish labour market is generally characterised by a high degree of adaptability of workers through mechanisms and measures reviewed and reinforced on a continued basis through involvement of social partners. In terms of adaptability of workers and enterprises, no specific measures have been taken so far. However, to realise national objectives for lifelong learning, the government and the social partners have established a Tripartite Task Force to reform the vocational and adult training system. This is an important first step in a long-term process. The first recommendations from this Task Force are expected in early 2006.
18. Regarding investments in human capital, the focus is again on addressing more long-term challenges and preparing Danish society for the effects of globalisation and technical change. One set of new initiatives aims at increasing the proportion of young people completing upper-secondary education by establishing more cohesion and interaction between subjects, and by improving apprenticeships and vocational colleges. Another set of initiatives aims at increasing the numbers of young people completing higher education and the speed with which they do it. Youth unemployment, which is linked to early school-leaving in particular, will be tackled through measures to ensure participation in individualised education or training. These measures are adequate and focused, with overall targets identified for 2010 and 2015, although some of those seem over optimistic.
19. Overall, the Danish employment strategy is wide-ranging and ambitious but specific measures to increase employment are so far limited, partly because the government is awaiting important advisory reports. In general, budgetary information is scarce in the employment section of the NRP.

### **PART III: CONCLUSIONS**

20. In line with the Integrated Guidelines, the Danish National Reform Programme identifies and responds to the main challenges facing Denmark, namely to prepare for the ageing of the population; reap the benefits of globalisation; strengthen the framework for improved productivity; and increase value for the users of public services. These broad challenges are translated into a number of priorities: improving competition in certain sectors; enhancing public sector efficiency; developing a knowledge society; securing environmental sustainability and energy; encouraging entrepreneurship; and increasing the labour supply. Overall the NRP's approach is broad, coherent and long-term, with ambitious and achievable objectives based on a comprehensive and clear short, medium and long-term analysis and taking account of important EU policies. Action on the recent and forthcoming recommendations of key advisory bodies is likely to lead to an increase in the number of specific reform measures proposed.
21. Clear timetables are given for some measures, but more detail and clearer implementation schedules are necessary for others. Medium-term budgetary implications are set out for most objectives.
22. The programme's strengths include:

- it aims to actively incorporate environmental aspects across different policy fields;
- measures on energy, education, improving the efficiency of the public sector and promoting R&D and innovation;
- the tax relief granted to entrepreneurs in order to provide incentives for further growth is particularly interesting.

23. Among the points requiring further attention are:

- more concrete and specific measures to increase labour supply, which may flow from the recommendations of the Welfare Commission (see above);
- more detailed measures to enhance competition;

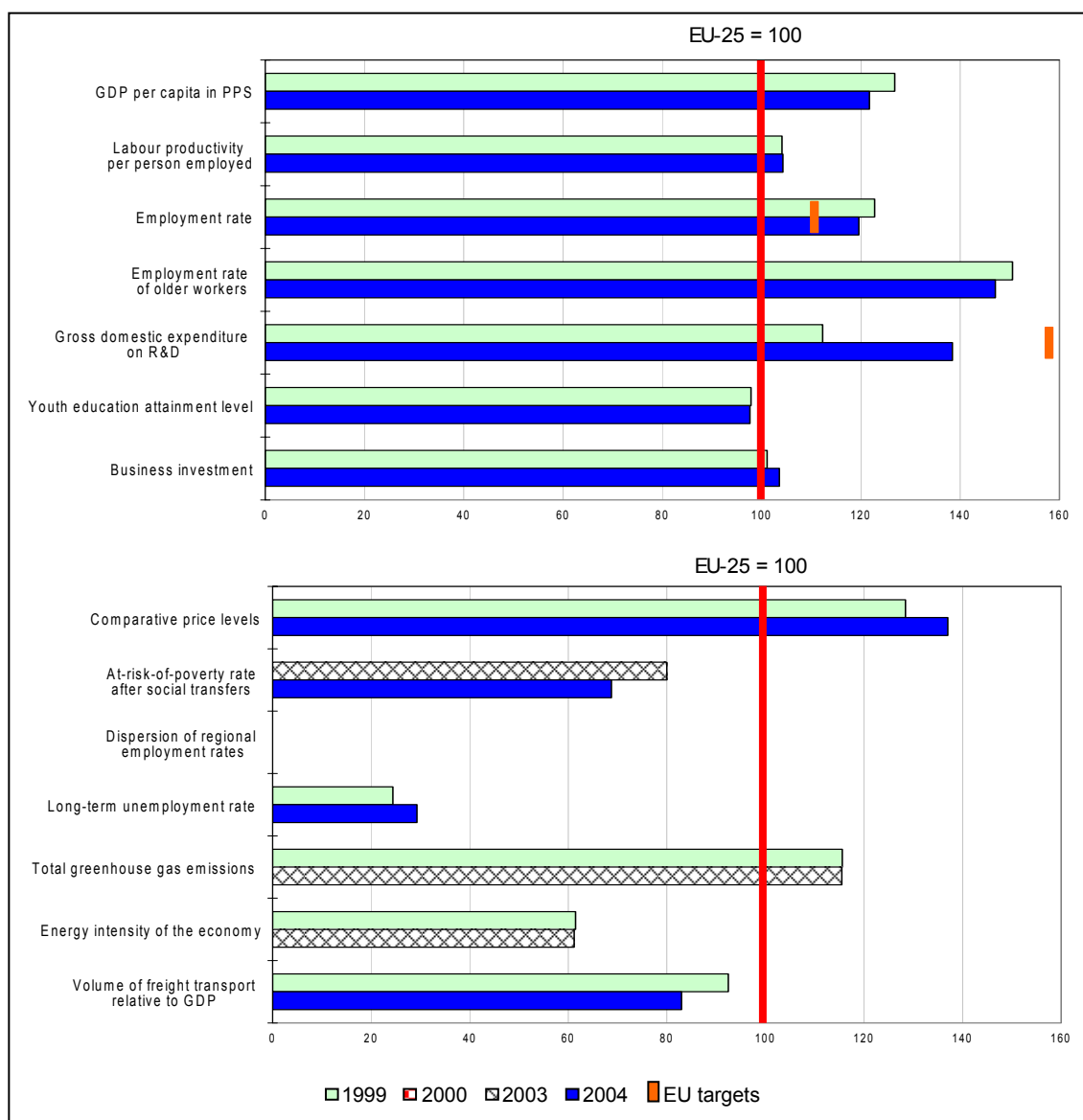
24. Taking due account of the above, Denmark is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Denmark has dealt with the issues mentioned in paragraph 23. In this context, the Commission looks forward to discussions with the Danish authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# DENMARK

	DK						2010 National target	EU-25						2010 EU target	
	1999	2000	2001	2002	2003	2004		1999	2000	2001	2002	2003	2004		
GDP per capita in PPS	126.8	126.9	125.4	121.1	120.9	121.7	3.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0	
Labour productivity per person employed	104.1	105.6	105.1	102.1	103.3	104.3		100.0	100.0	100.0	100.0	100.0	100.0		
Employment rate	76.0	76.3	76.2	75.9	75.1	75.7		61.9	62.4	62.8	62.8	62.9	63.3		
Employment rate of older workers	54.5	55.7	58.0	57.9	60.2	60.3		36.2	36.6	37.5	38.7	40.2	41.0		
Gross domestic expenditure on R&D	2.10	2.27	2.40	2.55	2.59	2.63p		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe		3.0
Youth education attainment level	73.2	69.8	78.3b	79.6	73.0b	74.8		74.8	76.3	76.1	76.5	76.5	76.6		
Comparative price levels	128.4	127.8	130.7	135.6	138.8	137.0p		100.0	100.0	100.0	100.0	100.0	100.0p		
Business investment	18.1	18.5	17.9	17.8	17.6	17.5		17.9	18.3	17.7	17.1	16.7	16.9		
At-risk-of-poverty rate after social transfers *	10.0	:	10.0	:	12.0b	11.0		:	16.0	15.0	15.0	15.0	16.0		
Dispersion of regional employment rates	-	-	-	-	-	-		13.3	13.4	13.5	13.3	12.9	12.2		
Long-term unemployment rate	1.0	1.0	0.9	0.9	1.1	1.2		4.1	3.9	3.8	3.9	4.0	4.1		
Total greenhouse gas emissions	104.7	98.1	100.2	99.1	106.3	:		90.6	90.5	91.4	90.7	92.0	:		
Energy intensity of the economy	132.1	125.0	126.6	123.8	128.2	:		214.9	208.8	209.7	206.5	209.5	:		
Volume of freight transport relative to GDP	93.1	93.0	85.5	86.2	87.7	86.8		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e		

\* Alternative computation for Denmark using income definition including imputed rent revenue and mortgage interest payments: 2003 10.0b and 2004 10.0



## Estonia

1. Estonia's economic transition to a market economy started from a very low position with respect to GDP per capita and productivity. Employment declined significantly during the transition, but drastic economic reforms have led to over 6% real GDP growth during the last decade. Rapid productivity growth has been reflected in a sharp increase in wages. As a result, GDP per capita has risen rapidly to 51% of the EU average in 2004. The employment rate in 2004 was 63%. Unemployment has fallen rapidly (9.2% in 2004).

### **PART I: GENERAL ASSESSMENT**

2. The Estonian National Reform Programme (NRP) focuses on two key challenges: first, R&D and innovation and second, employment. The Commission shares this analysis of the main priorities.
3. The strategy in the NRP is forward-looking, ambitious and linked well with existing policies. References are made to other strategic initiatives that are already being implemented or are in the pipeline. The programme is integrated and coherent across the macro-economic, micro-economic and the employment policy chapters. The NRP is structured clearly, indicating objectives and policies to achieve them, including detailed measures. For most measures a set of quantitative indicators is provided with the target values set for 2008, allowing progress to be measured. The NRP sets targets to increase R&D spending to 1.9 percent of GDP by 2010 from 0.82 percent in 2003 and to raise the employment rate to 67.2 percent in 2010 from 63 percent in 2004. The budgetary implications of the planned initiatives are only broadly defined. The presentation of the link between measures envisaged in the NRP and Structural Funds (estimated at some 4 % of GDP) is not sufficiently concrete.
4. Consultation and efforts to develop ownership of the document have been very substantial. The Prime Minister's office coordinated the preparation of the Estonian NRP and will also oversee implementation. A competitiveness working group, established for the preparation of the programme under the chairmanship of the Director of the EU Secretariat of the State Chancellery, brought together representatives of several ministries, social partners, local authorities, and civil society. The draft NRP was posted on the internet for public consultation. The programme was discussed in various parliamentary committees and the NRP approved by the EU Affairs Committee of the Parliament.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. Maintaining sound public finances and the conditions for low inflation and price stability are the core objectives for macro-economic policies. These priorities are particularly appropriate as Estonia has a currency board pegging the kroon to the



euro. Raising the employment rate is seen as a key for sustaining the economy's strong growth performance in the future and raising the living standard.

6. The NRP strongly emphasises budget balance and financial sustainability, notably through the tax system and the allocation of government spending. For the rest, reliance on market forces is considered the key condition for sustained strong growth. A business friendly tax reform, shifting the burden of taxation to consumption and environmental taxes and away from labour and income are complemented by public spending reform. If successfully implemented, this policy direction should yield important benefits for growth and employment. The Estonian NRP addresses the external account deficit in the context of the broader objective of ensuring a stable macroeconomic environment.
7. The focus of macro-economic policies and measures proposed in the NRP on fiscal sustainability and creating conditions for employment growth are fully appropriate in the context of Estonia's economic situation.

### **Micro-economic policies**

8. Estonia has identified R&D and innovation as a key challenge for sustaining strong economic growth and enhancing competitiveness. In addition to addressing this key challenge, the NRP proposes measures to improve the business environment, the functioning of markets and infrastructure. Given that the recent strong growth has been achieved largely in low-productivity sectors whose competitiveness may come under pressure in the context of globalisation, these micro-economic priorities are particularly relevant for Estonia's long-term growth prospects.
9. The NRP presents a clear diagnosis of the main weaknesses and constraints for R&D and innovation. It formulates quantified objectives and provides clear timetables for reaching them. Estonia plans to continue its efforts towards achieving investment in R&D of 3% of GDP – the target level set for the EU as a whole - by 2014, building on progress made in recent years. The intermediate objectives set (1.5% of GDP by 2008, 1.9 % by 2010) are ambitious but not unrealistic. Explicit budgetary commitments for achieving them still need to be made. Several measures aim at improving the quality of research and innovation as well as the development of human capital. More emphasis may be needed on increasing the low level of private investment in R&D to reach the overall target. The R&D and innovation strategy would benefit from clearer prioritisation. The central role of foreign direct investment (FDI) in financing R&D and fostering the transition from a relatively low-tech to a high-tech based industrial portfolio are not mentioned in the plan.
10. The objective of further enhancing the business environment and stimulating entrepreneurial culture, where Estonia has already achieved much, is addressed by measures on improving the regulatory framework, reducing the administrative cost for business and simplifying legal requirements for start-ups. Impact assessments of new legislation related to enterprise policy are also envisaged. The creation of the Estonian Development Fund in 2006 and the establishment of a network of local "business angels" will help improve access to capital for start-up companies, especially SMEs with high growth potential. The strengthening of access to finance for innovative firms is particularly important in this regard.

11. In several areas beyond the identified key challenges, the NRP proposes measures to enhance competitiveness. The planned development of the public transport infrastructure of rail and road systems and the proposed establishment of nation-wide broadband access will have a positive impact on Estonia's competitiveness. The NRP also proposes measures to improve e-services in the public sector in order to enhance communication between businesses and the administration. The pro-active competition policy envisaged along with the strengthening of competition authorities are likely to improve the functioning of product and financial markets. Important steps towards the opening the electricity market to competition are also envisaged.
12. The objectives set for environmental policy are clear and the programme identifies important links between environmental sustainability and growth potential. Moreover, planning for ecological tax reform is well advanced. The NRP recognises the energy sector as a main polluter and proposes specific reforms to improve the situation.
13. The micro-economic part of the NRP is both focused and comprehensive. The policies proposed to enhance Estonia's growth potential are presented fully and clearly in the programme and if fully implemented are likely to be effective.

### **Employment policies**

14. The NRP reflects the government's determination to address the employment challenges facing Estonia. The programme lists those challenges as a low employment rate, structural unemployment, skills and lifelong learning. It specifically addresses the issues of: long-term unemployment; the unemployment of youth and women; the high drop-out rate from school; the low quality of vocational education and training of employees; and the fragmented higher education system. Special attention is also paid to improving the adaptability of workers and enterprises. The Commission shares the NRP analysis of where employment priorities lie.
15. To attract and retain more people in employment, Estonia plans to further develop public employment services, including introducing personalised case management, and to improve the coordination between labour markets and social services. These measures are supplemented by special instruments targeting the young and long-term unemployed. Reforms of the pension system are intended to increase the employment rate of older workers. The integration of significant numbers of currently inactive people into the labour market will be necessary to reach the targeted levels for overall employment (67.2% by 2010) and for the employment of disabled people (30% by 2008). The NRP does not fully explain how these levels are to be achieved. The integration of certain categories of the inactive and unemployed, such as ethnic minorities, is not covered by the programme. In order to increase female participation to 65% in 2010, the availability of childcare services will be improved. Other measures to increase the female participation rate, including gender mainstreaming measures, are not considered in the NRP.
16. To increase adaptability, measures are announced to improve the functioning of the labour market, reduce undeclared work, modernise labour relations and improve the working environment so as to sustain productivity and workers' ability to stay in

employment longer. Shortcomings in the current legal framework for labour relations are addressed through a number of amendments to employment acts and regulation on collective agreements. The social partners' role in keeping wage developments in line with productivity improvements is insufficiently considered.

17. Despite an already high general level of education, Estonia is committed to increasing investment in human capital. Further raising the skills and education levels of the labour force to reduce structural unemployment features prominently in the programme. National targets set for the effectiveness and quality of formal education are ambitious but achievable through full implementation of the measures proposed in the NRP. Several policy measures, particularly related to vocational training and support to lifelong learning are presented in a clear and detailed way. A comprehensive lifelong learning strategy is scheduled to be formally approved by the Government by the end of the year. Attention is given to enhancing young people's employability and to reducing the drop-out rate, with the NRP focusing appropriately on improving educational quality and access.
18. Estonia makes a strong effort to meet the key challenge it sets itself of increasing employment and to address the issue of structural unemployment. By fully implementing the proposed measures the ambitious objectives can be reached.

### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the Estonian National Reform Programme identifies and responds to the main challenges facing Estonia as a fast growing economy, namely R&D and innovation and employment.. Overall, the NRP is integrated, coherent and clearly structured, with explicit links made between policy areas. Objectives are ambitious, with clear paths and detailed measures set out for achieving them.
20. For most measures a comprehensive set of quantitative indicators and targets is provided. These, along with the extensive consultation with stakeholders and the clear structures for implementation will be significant advantages in putting the NRP into practice. However, the budgetary implications of the planned initiatives are only broadly defined. More emphasis is needed on linking the measures in the NRP with the forthcoming substantial injection of structural funds and on enhancing Estonia's administrative capacity to manage the funds.
21. The programme's strengths include:
  - the importance attributed to achieving synergies between environmental sustainability and growth;
  - the credible effort to introduce ICT in the public sector, which builds on impressive existing achievements and is a good example for other countries;
  - plans to improve the working of the labour market, reduce undeclared work, modernise labour relations and improve the working environment.
22. Among the points requiring further attention are:

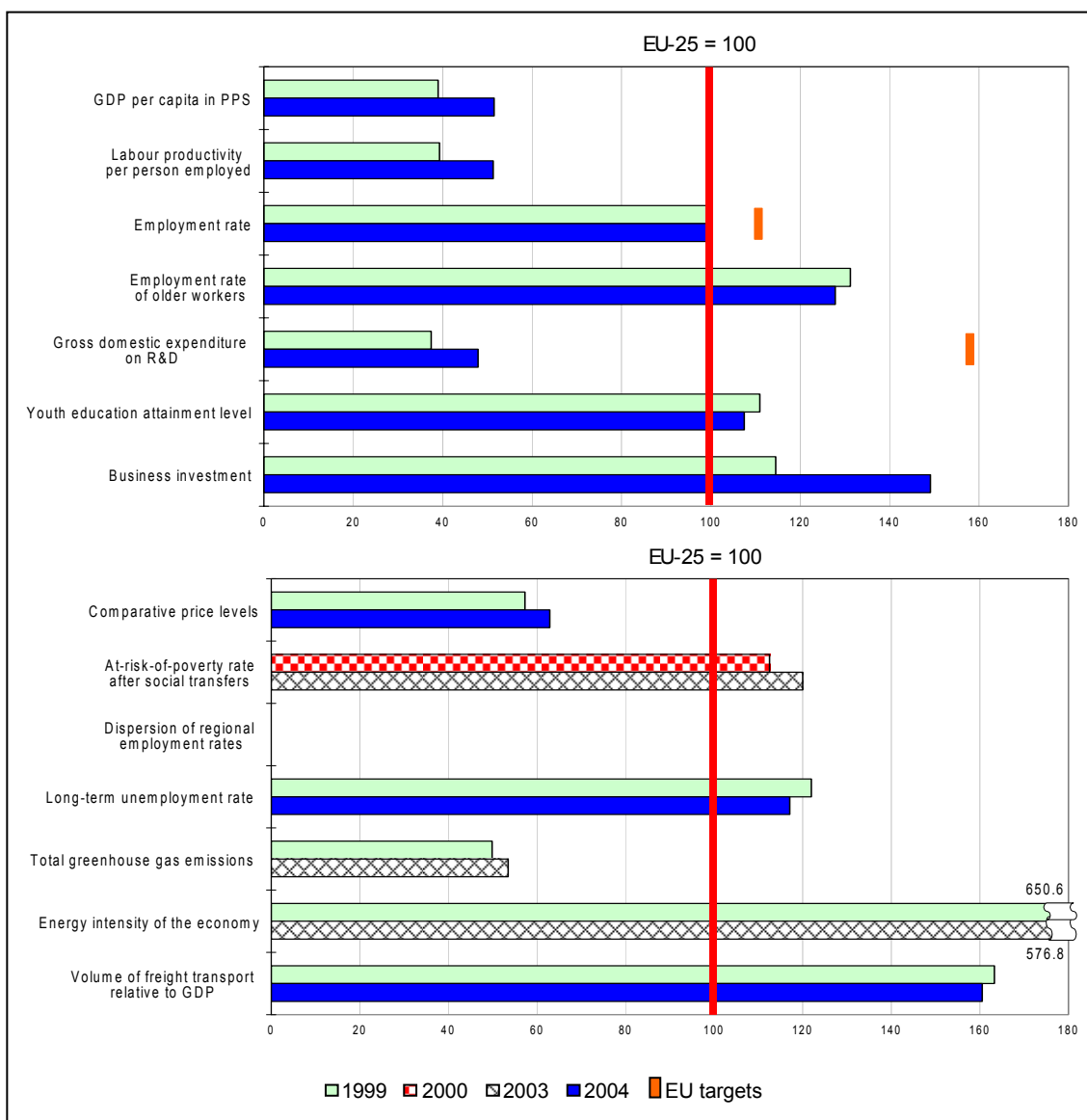
- a stronger focus on increasing private R&D investment and on the role of FDI in that context;
- further measures to develop a comprehensive active labour market policy and to improve skills in order to achieve the ambitious employment rate target set .

23. Taking due account of the above, Estonia is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Estonia has dealt with the issues mentioned in paragraph 22 In this context, the Commission looks forward to discussions with the Estonian authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# ESTONIA

	EE							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	39.0	41.2	42.4	45.3	48.5	51.5	67.2	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	39.3	42.6	43.8	46.0	48.2	51.3		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	61.5	60.4	61.0	62.0	62.9	63.0		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	47.5	46.3	48.5	51.6	52.3	52.4		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	0.70	0.62	0.73	0.75	0.82	0.91p		1.9	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	83.0	83.6	79.5	80.4	81.4	82.3		74.8	76.3	76.1	76.5	76.5	76.6			
Comparative price levels	57.3	56.8	59.7	62.1	63.2	62.9p		100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	20.5	21.7	22.9	24.0	25.5	25.2		17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	:	18.0	18.0	18.0	18.0	:		:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	-	-	-	-	-	-		13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	5.0	5.7	5.7	5.0	4.7	4.8		4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	45.2	45.4	44.7	44.9	49.2	:		90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	1398.1	1214.8	1273.0	1153.2	1208.4	:		214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	164.4	182.8	165.2	172.3	158.5	167.9		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e			



## Finland

1. After expanding at an annual rate of nearly 5% during 1995-2000, Finland's economic activity slowed with the global downturn in 2001, although growth has remained well above the EU average. Yet, growth of the labour productivity per person employed has been only slightly above the EU average over the last decade. There are, however, marked differences between sectors. GDP per capita was at 113% of the EU average in 2004. The employment rate was at 67.6%. In 2004, the unemployment rate was 8.8%, which is slightly below the EU average.

### PART I: GENERAL ASSESSMENT

2. The Finnish National Reform Programme (NRP) presents three medium-term challenges: the sustainability of public finances, improving competitiveness and productivity and improving the functioning of the labour market. There is a target of attaining balanced central government finances by 2007. These challenges are defined in a very broad sense and linked to eleven macro, micro and employment key priorities. The Commission broadly shares the NRP's analysis of the main priorities, and it also sees increasing competition, particularly in services markets, as an important challenge.
3. The NRP gives an overview of the Government's ongoing and planned policy actions. The NRP describes the main strategic orientations, while the reader is referred to the underlying policy documents for details of specific action proposed. The NRP is coherent across the different policy areas and contains a range of ambitious but achievable quantitative targets, including an annual increase in labour productivity of at least 2.5 per cent to 2010 and the creation of 100,000 new jobs by 2007, which would raise the employment rate to about 70 per cent. The longer-term objective is to raise the employment rate still further, to 75 per cent by 2011. Targets are also set for research spending, reduction of the dropout rate from school and lowering the entry age into tertiary level education and the graduation age. The NRP describes how EU Structural Funds will be used to promote the objectives.
4. Consultation and efforts to develop ownership of the document have been very substantial, in part based on the preceding broad and inclusive debate on Finland's globalisation strategy. The NRP was prepared by a group composed of the key Ministries and the Prime Minister's office, under the leadership of a Director General at the Ministry of Finance. Other Ministries, social partners, local government, the science community and independent NGOs were consulted. The NRP was presented to the Finnish parliament for information.

### PART II: ASSESSMENT BY POLICY AREA

#### Macro-economic policies

5. The overarching policy goal is to ensure the sustainability of public finances in the face of demographic change, which means that while Finland's overall macro-economic performance is quite strong, new challenges will be faced in the medium

and long term. Key priorities are controlling public expenditure, ensuring the capacity to fund welfare services and improving public sector productivity.

6. The NRP includes a well-designed strategy for boosting public sector efficiency and quality in the provision of services, through for example the public sector productivity programme for the central government, the basic services programme assessing income and expenditure for local governments and a project to reform municipal and social services structures. Other on-going measures include phasing in pension reform and the maintenance of central government spending limits. The objective is set to restore balance in central government finances under conditions of normal economic growth by 2007. The goal for local government finances is to improve the balance, but no quantified targets are given.
7. The implementation of the measures outlined in the programme should contribute to the long term sustainability of public finances and help address long term challenges arising from population ageing.

### **Micro-economic policies**

8. The NRP prioritises the functioning of markets and competition; knowledge and innovation; entrepreneurship; ICT and transport networks; energy and climate policy. In general, the NRP outlines many valuable micro-economic policy measures which should stimulate growth and jobs.
9. Competition issues are a key challenge for Finland. Consumer prices are relatively high – some 25 per cent above the EU25 average in 2002 – which is likely to partially reflect a lack of competition in some sectors. The NRP points to regulations which directly prevent competition in pharmacy services, opening hours for the sale of consumables and in the transport and construction sectors. Some measures are proposed in the NRP to address these issues, including a new law on public procurement. Several ongoing research projects are analysing competition issues. The NRP does not address in detail the specific issue of ensuring that the Finnish competition authority possesses and exercises sufficient powers to speedily and decisively remove barriers to open competition.
10. Total R&D spending amounted to 3.5 per cent of Finland's GDP in 2003, well above the overall 3 per cent EU target for 2010. About 70 per cent of R&D spending is financed by the private sector. In the NRP, the Finnish government announces a target of raising total R&D spending to 4 per cent of GDP by the end of the decade. Public spending on R&D is projected to increase by 5-7 per cent each year over the same period. This commitment to research is not fully reflected in the country's performance in terms of creating innovative products and services. The NRP sets out plans to continue the process of strategic prioritisation in the allocation of research funding, as well as stronger focus on the international dimension of the research and innovation system. The NRP aims simultaneously at increasing excellence in cutting edge technological research and broadening innovation policy to the service sector.
11. The rate of business start-ups in Finland is significantly below the EU average, though the procedures and time required to set up businesses in Finland are already quite favourable by international standards. Furthermore, too few firms grow into medium-sized or large enterprises. To promote entrepreneurship and a favourable

business environment, the NRP refers to a forthcoming national action plan for better regulation and to the existing entrepreneurship policy programme. The proposed steps to reduce further the administrative cost for private businesses are promising. The reform of corporate and capital income taxes in 2005 and the ending of property tax from 2006 also appear to have potential to improve the environment for entrepreneurship and SMEs. The government also plans to invest an additional 11.5 million euro in a new type of venture capital fund.

12. To facilitate the spread and effective use of ICT, several measures are presented, such as the launch of programmes to promote the uptake of ICT in SMEs and increased broadband availability. The NRP presents plans for promoting the environmental technologies and includes a commitment to reform tax structures with a view to promoting sustainable development.
13. In view of the opportunities and challenges increased globalisation presents for its leading industries, the reform of the research and innovation system and the increase in investment set out in the NRP are appropriate and of strategic importance for Finland, even in the light of its existing strong performance in these areas. The better regulation, ICT and environmental measures are also potential sources of jobs and growth. Some of the other micro-economic policies proposed in the NRP are not set out in a way detailed enough to allow a comprehensive assessment of their potential impact. For example, it is not wholly clear how extensive the effect of the measures proposed to boost competition will be.

### **Employment policies**

14. The NRP identifies extending working life, improving the incentives of tax and benefit systems, wage formation and improving the balance between labour demand and supply as key employment priorities. The focus is on increasing labour supply at both ends of the working age population. The Commission shares this point of view.
15. To attract and keep more people in employment, Finland focuses on the retention of older workers in the labour market. The employment rate among older people has increased rapidly in recent years, and recent pension reforms should contribute to further increases in the average exit age. Nevertheless, the effectiveness of the pension reforms needs careful monitoring and more measures may prove necessary to remove remaining disincentives to stay in work. Measures for preventing exclusion, especially of young people, as well as for “making work pay” through developing the tax and benefit system have been strengthened in the 2006 budget proposal. The decentralised implementation of active labour market measures through the labour force service centres is appropriate and can help reduce structural unemployment and meet employer demand for skills, though it will need to be closely monitored to ensure effective delivery. Limited attention is given to employment-based immigration in the Programme as the Government is currently in the process of adopting a new immigration policy programme.
16. The NRP acknowledges that improving working conditions is an important precondition for further increases in productivity and the employment rate. Comprehensive programmes are being implemented to this end. Finland has a well-balanced and targeted approach to lifelong learning and has already achieved the EU benchmarks on education and training. Tackling early school leaving remains a key



priority. An overall target for the proportion of working age people participating in training is set at 60 per cent by 2008, compared to 54 per cent in 2000. To maximise the effect of this, more attention may need to be paid to workers with lower educational levels. In order to promote the occupational mobility of an ageing workforce, further measures could be taken on "learning at work" methods, as well as on the recognition of qualifications and competencies.

17. The employment measures proposed in the NRP are likely to make an important contribution to increasing the labour supply and reducing structural unemployment. However, to reach the ambitious 75% employment rate target by 2011, further measures need to be considered to encourage older workers to stay longer in employment and to integrate immigrants and disabled people into the labour market.

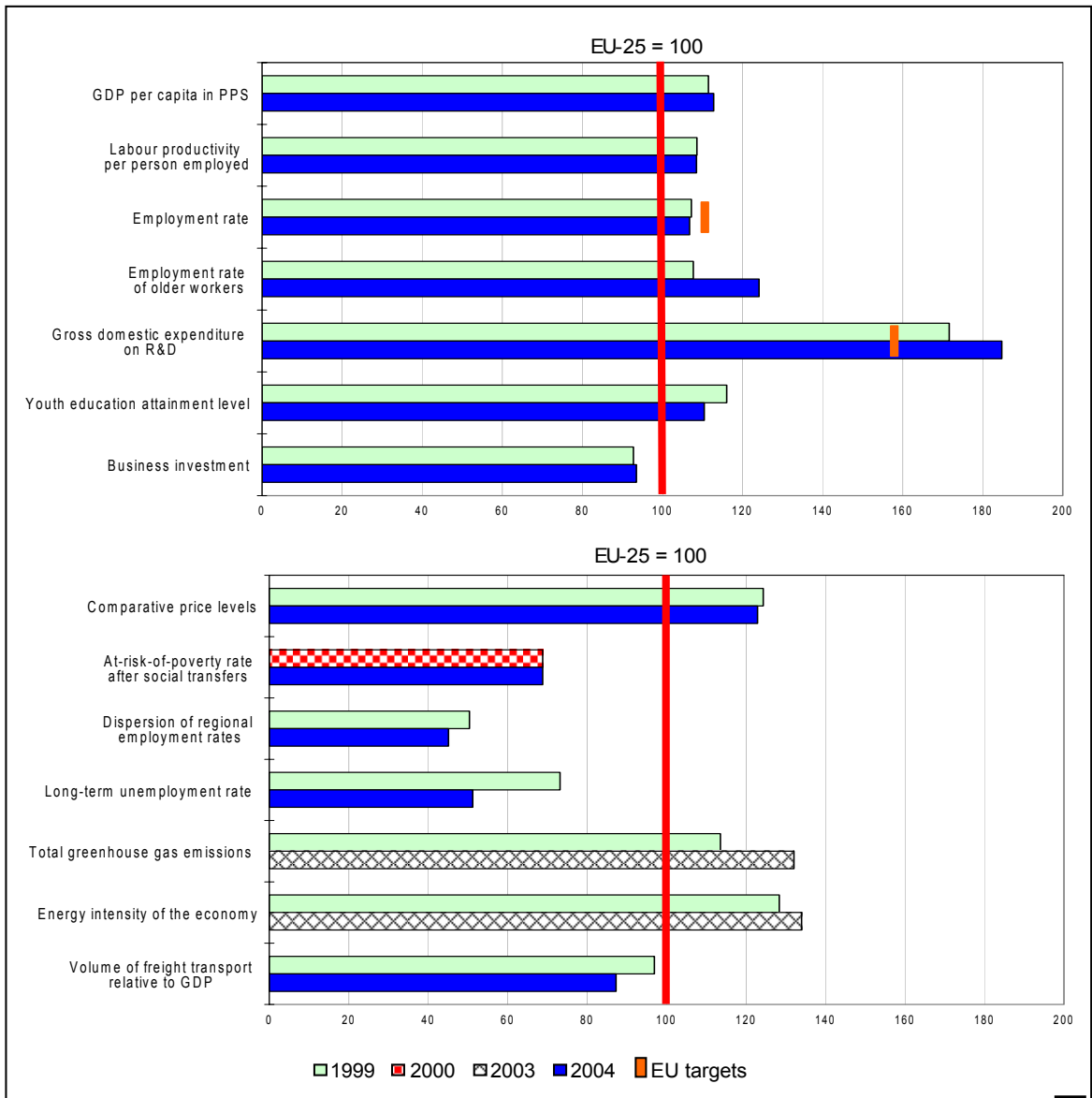
### **PART III: CONCLUSIONS**

18. In line with the Integrated Guidelines, the Finnish National Reform Programme identifies and responds to most of the main challenges facing Finland, namely three medium-term challenges: the sustainability of public finances, improving competitiveness and productivity and improving the functioning of the labour market and a target of attaining balanced central government finances by 2007. However, increasing competition, particularly in services markets, is an important challenge for Finland which is only partially addressed in the programme. Overall, the NRP is coherent and sets out ambitious yet achievable objectives and a range of concrete and appropriate policy measures to build on the recent successes of the Finnish economy.
19. The NRP includes fairly comprehensive information on timetables, targets and budgeting. The broad debate organised with stakeholders to discuss Finland's globalisation strategy and the resulting sense of ownership is likely to pay dividends in the implementation phase
20. The programme's strengths include:
  - the sense of urgency with respect to the sustainability of public finances;
  - the set of measures to promote entrepreneurship and improve the business climate;
  - the ambitious R&D investment target of 4% by 2010 and the move towards stronger specialisation of research and a wider application of innovation, in particular in the service sector.
21. Among the points requiring further attention are:
  - increasing competition in service markets;
  - further initiatives to keep older workers longer in employment.
22. Taking due account of the above, Finland is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Finland has dealt with the issues mentioned in paragraph 21. In this context, the Commission looks forward to discussions with the Finnish authorities as part of the new partnership for growth and jobs.

### **PART IV: STATISTICAL GRAPHS AND DATA**

# FINLAND

	FI							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	111.5	113.6	113.2	112.7	111.7	112.8	70.0 (2007)	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	108.6	110.1	109.4	108.4	107.4	108.5		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	66.4	67.2	68.1	68.1	67.7	67.6		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	39.0	41.6	45.7	47.8	49.6	50.9		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	3.21	3.38	3.38	3.43	3.48	3.51		4.0	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	86.8	87.8b	86.5	86.2	85.2	84.6		74.8	76.3	76.1	76.5	76.5	76.6			
Comparative price levels	124.3	123.0	122.8	124.4	125.9	122.9p		100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	16.6	17.1	17.6	16.0	15.3	15.8		17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	11.0	11.0	11.0b	11.0	11.0	11.0b		:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	6.7	6.8	7.0	6.7	6.1	5.5		13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	3.0	2.8	2.5	2.3	2.3	2.1		4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	102.9	99.7	107.6	109.7	121.5	:		90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	276.0	260.1	263.8	272.2	280.7	:		214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	97.6	99.3	94.2	95.1	91.4	91.3		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e			



## France

1. After a period of weak economic growth in the first years following the turn of the century, there was an appreciable recovery in 2004, but progress was somewhat slower in 2005. Since 2000, the French economy has grown faster than the average for the European Union (EU25). Per capita labour productivity growth is just below the European average over the last ten years, whereas hourly productivity has grown faster than the average. GDP per capita was 110% of the EU average in 2004. In the last two years, the employment rate (63.1% in 2004) has improved only slightly, but it is one point above the level of 2000. The unemployment rate has remained high (9.6% in 2004). This situation has contributed to a further deterioration in the budgetary situation in France, which is already suffering from the fact that the debt ratio has trebled in the last 20 years.

### **PART I: GENERAL ASSESSMENT**

2. The French national reform programme (NRP) is based on the concept of “social growth” and identifies three main priorities: to create the necessary conditions for strong economic growth; to reduce unemployment and increase employment; to build a knowledge-based economy. It stresses the need to consolidate the public finances, redress the employment situation and strengthen the competitiveness of business. The Commission agrees, but notes that this programme takes little account of the competition and market opening aspects.
3. The NRP takes the form of a general policy document stressing the three French priorities, with no explicit reference to the European growth and employment guidelines. It highlights the action already taken or decided on in the areas of public finance, employment policy, industrial policy and innovation and research policy. Much of this action seems relevant and liable to generate real momentum. However, the NRP does not dispel the uncertainties with regard to the prerequisite of reducing the public-sector deficit. The measures in the different areas do not always seem to dovetail and the NRP provides no information on how they are to be financed by the national budget or how the European structural funds are to be used. The NRP sets objectives for the public-sector deficit and debt but does not lay down quantified targets for employment and investment in research and development. The lack of quantified targets, impact assessments and more detailed information on how certain measures are to be put into effect limits the programme’s effectiveness as a guide to future developments and a means of shaping them.
4. Efforts have been made to consult stakeholders, but should be strengthened in order to improve ownership of the document. The NRP was drawn up as an interdepartmental exercise, technically coordinated by the Secretariat-General for European affairs, which reports to the Prime Minister, and validated by the Interministerial Committee on Europe. It was discussed in parliamentary committee but enjoyed no specific coverage in the media. It was presented to the social partners and some of their comments were incorporated into the final version. The programme will be monitored by the Economic and Social Council throughout its duration.

## **PART II: ASSESSMENT BY POLICY AREA**

### **Macro-economic policies**

5. The NRP describes consolidation of the public finances as a precondition for sustainable growth, especially in view of the problems arising from an ageing population. It aims at a government budget balance of between -1.4% and +0.1% in 2009, depending on the different growth scenarios. The programme stresses that this consolidation must proceed in parallel with boosting of the growth potential of the French economy by increasing employment levels and developing a knowledge-based economy. The Commission agrees.
6. In order to strengthen the public finances, the NRP confirms France's policy of budgetary rigour, the main features of which are as follows: debt to increase more slowly than national wealth as a result of a sustained effort to reduce public-sector deficits; control of public spending to be maintained, in particular by State economies going beyond stability of 2007 expenditure in volume terms; the statutory framework for public finance to be modernised to allow public spending to be better managed; social security reforms to be further pursued. In the short term, the advent of the health insurance reform and the reduction in unemployment insurance expenditure are expected to contribute to budget consolidation, despite an increase in local authority spending.
7. As regards the link between social security and public finance, the programme contains quantified targets for pensions reform, whereas the impact of the health system reforms remains more nebulous. These reforms are tending in the right direction, even if they are probably not sufficient in themselves to ensure long-term viability of the public finances.
8. Overall, the approach adopted in the NRP is not new and continues the efforts France has been making in recent years to reduce the public-sector deficit, partly in response to the opening of a European excessive deficit procedure. However, while the goals are clear, the Commission believes that additional measures are needed to permanently address the public-sector deficit. The recent political commitment to reducing the debt is certainly a welcome development. It is well illustrated by the announcement of a public finance conference to make all parties in the public sector aware of the need to share the burden of budgetary restraint.

### **Micro-economic policies**

9. The NRP stresses the need to improve businesses' competitiveness. It particularly emphasises a greater research effort and support for innovation and SMEs. The Commission generally agrees with this approach, though it notes that the internal market aspects are not very detailed. The NRP also mentions action taken on the environment, climatic change and energy efficiency.
10. As regards research and innovation, the programme seeks to increase private investment in R&D and the effectiveness of public research and to support the spread of innovation throughout the economy. It sets out a number of positive steps to make evaluation of public research more systematic and strengthen cooperation with business. However, it would have benefited from a more detailed approach to reform

of academic research, a bill on which is under discussion. The NRP announces a number of ambitious projects in the area of innovation: an industrial innovation agency, creation of 67 clusters of excellence (*“pôles de compétitivité”*), arrangements to give SMEs easier access to innovation. These proposals form a sound basis for supporting innovation and developing industrial policy in the coming years. The large number of players and mechanisms involved raises the issue of proper coordination. The NRP also includes measures in the ICT field to improve high-capacity communications access, network security and e-government.

11. In order to support the development of SMEs and improve the regulatory environment for business, the NRP sets out various measures geared to simplifying labour law, reducing the tax burden, providing better access to finance, disseminating information and communication technologies, pursuing local and regional development and expanding the transport and energy infrastructure. However, the NRP would benefit from more detail on improving the “quality of legislation”. This covers the policies, structures and tools which could be brought into play in order to cut back and simplify legislation and carry out more systematic assessment of the impact of new initiatives, as well as the dissemination of good regulatory practice throughout government.
12. As regards competition and opening of markets in the network industries, the NRP essentially does no more than note the legal requirement to comply with the European directives. It has little to say on the other aspects relating to competition and market opening such as regulated professions or deepening of the internal market. On the other hand, progress has been made on competition in the distributive trades and banking sectors and reforms are also planned for consumer protection.
13. In the areas of research, innovation and industrial policy, the French NRP is essentially a reaffirmation of the fairly robust measures recently taken. It is still too early to assess the outcome of such action and judge its effectiveness in the long term. A particular issue is good structuring of these arrangements to limit the risks of overlapping and/or dispersion of resources, even if they do form part of an overall scheme. The NRP is less detailed and more cautious as regards internal market issues.

### **Employment policies**

14. The focus of the NRP is on expanding the demand for labour by reducing non-wage labour costs, on increasing the supply of labour by back-to-work policies and on reforming the way the labour market functions. The Commission subscribes to these priorities but regrets that investment in human capital has not been dealt with more explicitly.
15. France has a relatively high unemployment rate and low employment rates at the two ends of the age pyramid. In order to encourage more people to enter and remain in employment, the NRP stresses greater financial incentives for returning to work, the development of assisted contracts, active labour market policy with regard to welfare payments, greater support for job-seekers and greater emphasis on their personal responsibility. As regards the latter, France has devised monitoring arrangements, with provision for imposing penalties. Integration of young people is a special priority and the NRP also highlights school drop-out prevention and wider access to

apprenticeships. The stress on integration of disadvantaged target groups represents a change in emphasis as compared with previous years. The thrust of these measures is in the right direction. It will also be important to ensure that they are coherent with future changes in the unemployment insurance and minimum income rules. As regards the employment of older workers, France has launched a policy of reforms to encourage more people over 50 to remain in or return to work. The programme favours the social dialogue approach and states that a plan of action will be agreed in consultation between the State and the social partners. Details of the measures are still to be determined in the light of the consultation process. Development of an overall strategy for employment of older people remains a vital issue for France.

16. It is particularly important for France, where there is a sharp division in the labour market between those in work and those without assured work, to ensure a match between workers' flexibility and the adaptability of businesses. In this context, the NRP highlights the introduction of the "new recruitment" contract (*Contrat Nouvelle Embauche — CNE*), which is intended to encourage hiring in businesses with up to 20 employees. An assessment of the CNE is planned for the end of 2008. Among the other prime issues for France, the NRP refers only indirectly to the question of anticipating and managing economic change. Nor does the programme contain any assessment of the impact on employment and productivity of certain particularly important measures such as lowering non-wage labour costs for the low-paid and making the working time legislation more flexible.
17. Apart from the aspects concerning access of young people to the labour market, the NRP could give fuller treatment to the need for greater investment in human capital. Measures along these lines have recently been announced. The main points that it mentions in this connection are measures concerned with gender equality, health at work and combating exclusion and discrimination. Since greater access to life-long learning remains an issue that France needs to address, especially as regards older workers and the least-skilled, the NRP could have discussed implementation of the Life-long Training Act more fully.
18. The NRP describes a set of measures to tackle certain problems characteristic of the French labour market. There is a new emphasis on persons in difficulty, in particular young people. As active labour market policy and assisted contracts come on stream, they should help to reduce unemployment in the short term. However, it is difficult to assess the scope, coherence and impact of employment policies on the basis of the NRP. It is to be hoped that dialogue between the social partners will lead to significant progress on employment of older workers.

### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the French National Reform Programme identifies and responds to many of the main challenges facing France, namely creating the necessary conditions for strong economic growth, reducing unemployment and increasing employment and building a knowledge-based economy. It stresses the need to consolidate the public finances, redress the employment situation and strengthen the competitiveness of business. It provides only a partial response to the major issues of competition and market opening and of enhancing human capital. The NRP contains several reforms and positive steps,

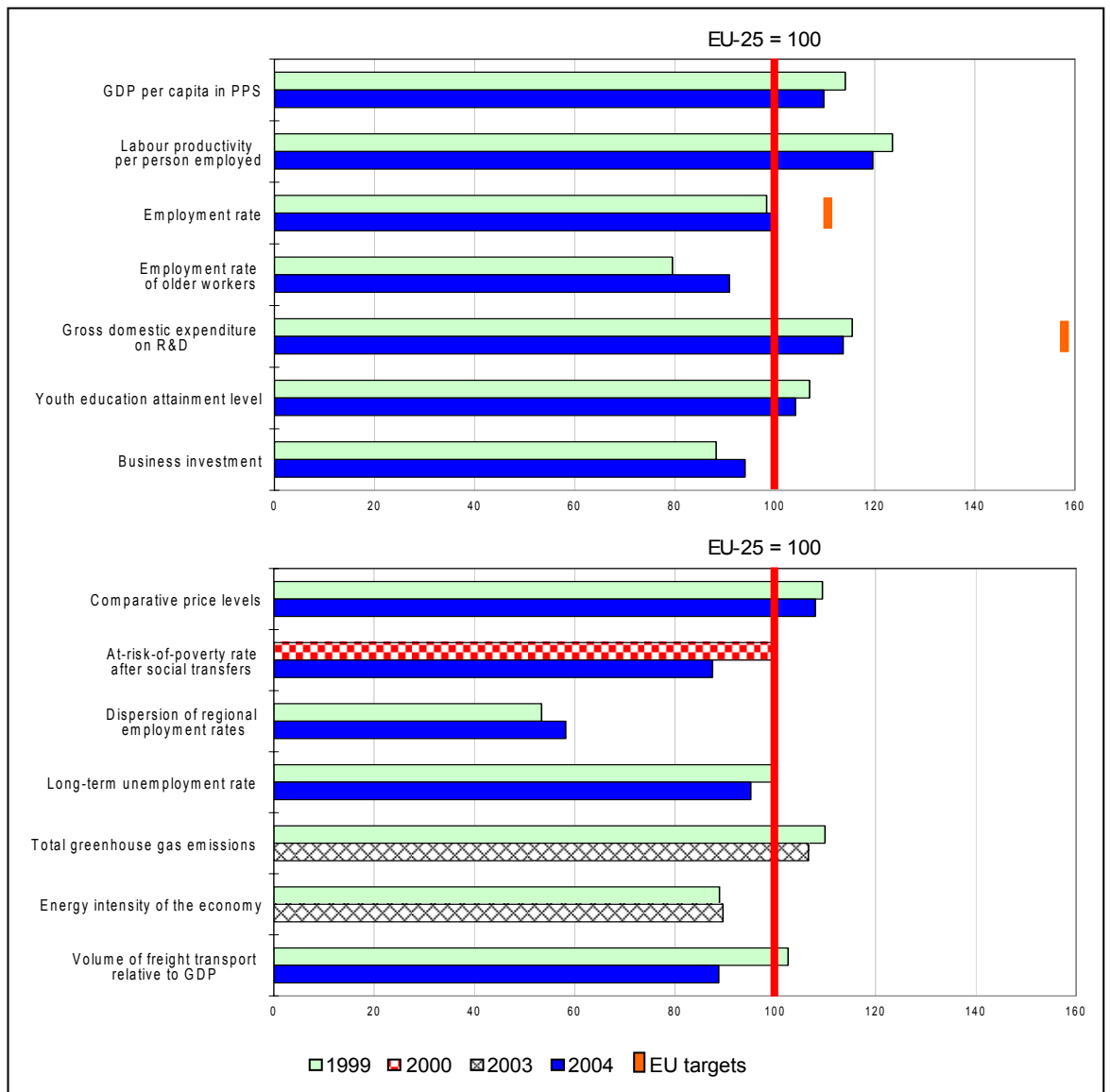
though the objectives and how they are to be attained could be set out in greater detail. The programme would also benefit from closer linkage of the different areas covered.

20. It would be desirable to clarify how the NRP relates to the European growth and employment guidelines, how the exact scope of some measures will be determined and what budgetary resources will be allocated in order to put them into practice.
21. The programme's strengths include:
  - the emphasis on employment of young people;
  - the adoption of a proactive innovation policy, especially through the development of clusters of excellence.
22. Among the points requiring further attention are:
  - permanent correction of the public debt;
  - more vigorous action to improve regulation and promote the opening of markets, especially in network industries;
  - strengthening of integrated employment strategies, e.g. as regards segmentation of the labour market, worker and business flexibility and employment of older people.
23. Taking due account of the above, France is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way France has dealt with the issues mentioned in paragraph 22. In this context, the Commission looks forward to discussions with the French authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# FRANCE

	FR							2010 National target	EU-25							2010 EU target
	1999	2000	2001	2002	2003	2004	1999		2000	2001	2002	2003	2004			
GDP per capita in PPS	114.1	114.2	114.5	112.7	111.8	109.8	:	100.0	100.0	100.0	100.0	100.0	100.0	100.0		
Labour productivity per person employed	123.5	122.9	123.2	121.2	120.9	119.6	:	100.0	100.0	100.0	100.0	100.0	100.0	100.0		
Employment rate	60.9	62.1	62.8	63.0	63.3	63.1	:	61.9	62.4	62.8	62.8	62.9	63.3	70.0		
Employment rate of older workers	28.8	29.9	31.9	34.7	36.8	37.3	:	36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	2.16	2.15b	2.20	2.23	2.18	2.16p	:	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0		
Youth education attainment level	80.0	81.6	81.8	81.7	80.9	79.8	:	74.8	76.3	76.1	76.5	76.5	76.6			
Comparative price levels	109.4	107.0	105.5	106.1	105.8	108.0p	:	100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	15.8	16.3	16.4	15.7	15.6	15.9	:	17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	15.0	16.0	13.0b	12.0	12.0	14.0b	:	:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	7.1	6.9	8.3b	8.0	7.2b	7.1	:	13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	4.1	3.5	3.0	3.1	3.7	3.9	:	4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	99.6	98.7	99.3	97.5	98.1	:	:	90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	191.0	186.6	188.3	186.1	187.6	:	:	214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	103.3	100.0	96.8	94.6	92.4	92.8	:	100.7e	100.4e	99.4e	100.3e	99.7e	104.7e			





## Germany

1. Real GDP growth in Germany averaged 2 % over the period in 1996-2000, but has fallen to half that rate since then. Over the last decade, labour productivity growth has been slightly above the EU average, and has been improving in recent years. GDP per capita stood at 109 % of the EU average in 2004. The employment rate stands at 65 % of the working age population. The employment rate of older workers (in 2004 at 41.8 %) is slightly above the EU average, but significantly below the Lisbon target (50 %). Unemployment rose by 0.5 percentage points to 9.5 % in 2004.

### PART I: GENERAL ASSESSMENT

2. The German National Reform Programme (NRP) identifies six key challenges: the knowledge society; market functioning and competitiveness; business environment; the sustainability of public finances (including sustainable growth and social security); ecological innovation; and the re-orientation of the labour market. The Commission largely shares the analysis of the main priorities, but considers that a stronger response is needed regarding competition in services.
3. The NRP provides a coherent and integrated strategy to address the challenges identified. However, in many cases, as a result of the limited time-span between the constitution of the new government and the required submission of the NRP, the programme tends to present intentions without providing further detail regarding goals, funding, and timetables. The programme would also benefit from a clearer prioritisation among the main challenges in each policy area. It presents a national R&D target for 2010 of 3 percent of GDP, compared to 2.5 percent in 2004. It does not set a target for the employment rate. The role of the structural funds is only described in passing. The plan to reduce the number of laws requiring co-decision by the *Bundestag* and *Bundesrat* has the potential to facilitate future reforms.
4. The drafting of the NRP has been coordinated by the chancellor's office. The NRP recognises that, owing to the recent formation of a new government, efforts to develop ownership of the document have been rather limited. It presents a firm commitment by the authorities to involving all stakeholders much more closely in the period ahead. The Commission recognises that the German NRP was produced under special circumstances, preventing a stronger involvement of stakeholders and constraining a more detailed elaboration. While the *Länder* contributed to the drafting, *Bundestag* and *Bundesrat* were not formally consulted. Parliamentary groups, local authority organisations and social partners received the document for information.

### PART II: ASSESSMENT BY POLICY AREA

#### Macro-economic policies

5. In the area of macro-economic policy, the programme identifies sustainability of public finances (including sustainable growth and social security) as the key challenge.

6. The NRP envisages reducing the overall fiscal deficit from 3.7 percent of GDP in 2004 to below 3 percent by 2007 and reaching structural balance afterwards. The planned measures include the phasing out of tax allowances from 2006 and raising the VAT rate by three percentage points in 2007. Part of the related revenue increase will be used to lower non-wage labour costs. The measures envisaged seem sufficient to reach the deficit target. However, the consolidation effort by the *Länder*, which are responsible for about half of the overall fiscal deficit in Germany, remains vague.
7. The NRP sets out to improve the quality of public finances by shifting from consumption to investment on the expenditure side and from direct to indirect taxation on the revenue side. This approach is appropriate in the context of the overall fiscal strategy. However, the breakdown of the intended quality shift in terms of broad budget items and timelines is not provided. Questions remain whether the envisaged reduction in the contribution rate to unemployment insurance can be partly funded as intended by efficiency gains in its administration. Further reforms in the pensions system, such as the increase in the statutory retirement age, are also intended to underpin long-term fiscal sustainability. On health, the NRP announces a future reform of financial instruments without giving details. The reform aims primarily at reducing non-wage labour costs. Moreover, statutory long-term care insurance will be adapted to demographic changes by introducing elements of a funded scheme.
8. The NRP sees the consequences of unification as a main obstacle to higher growth in Germany. It recognises that the catching-up process of the eastern *Länder* was accompanied by high unemployment and a review of regional policy is deemed appropriate. A thorough analysis of the situation is, however, not provided in the NRP and it does not substantiate how the already legislated transfers to the eastern *Länder* until 2019 can be used more effectively.
9. The macro-economic key challenge identified in the NRP is appropriate against the background of fiscal developments in recent years. The choice of priorities in this regard is shared by the Commission. If fully implemented, the proposed measures will make a significant contribution to addressing the key challenge.

### **Micro-economic policies**

10. In the area of micro-economic policy, the programme presents the key challenges of knowledge society; market functioning and competitiveness; business environment; and ecological innovation.
11. Focusing on Germany's strong international position with regard to R&D and innovation, the NRP proposes efforts to enhance further this comparative advantage by extending the knowledge society. The importance of strengthening the systems of education and life-long learning is recognised in that context. The R&D investment target (3% of GDP by 2010) is ambitious, given the stagnation in R&D spending in recent years. However, recent initiatives provide substantial additional public funding until 2011 to promote excellence in universities and large public research organisations. Regular evaluations of subsidised research will help ensure proper targeting of public R&D spending to sustain the leverage effect on private R&D. The policy mix and the strong involvement of stakeholders bode well for the effectiveness of the strategy. The intention of the *Länder* to support closer

cooperation between science, research, and businesses, if followed up by appropriate measures, is likely to reinforce existing synergies. Timing and funding of the measures envisaged in that regard are, however, not specified. The measures announced for innovation and ICT to improve incentives for inventions and provide support for their marketing will help sustain Germany's strong innovative capacity. However, the lack of detail regarding the proposed measures in this area makes their full evaluation difficult.

12. To improve the business environment through better regulation, the NRP envisages a substantial reduction in the number of federal laws on the books. The proposed systematic use of the standard-cost model should help reduce administrative costs for businesses. The creation of an independent federal monitoring institution for impact assessments and the intention of the *Länder* to introduce such systematic assessments are important steps in the right direction. However, the crucial function of municipalities in this context is not mentioned. The envisaged reduction in reporting requirements for SMEs, the creation of a web-based, one-stop agency for start-ups, and entrepreneurship education at all levels, are particularly promising for enhancement of the business environment. The financing instruments for SMEs described in the programme are suitable to strengthen framework conditions. A more competitive corporate tax system is announced for 2008, albeit without details. The switch to degressive subsidies with firm expiry dates will enhance subsidy efficiency. On infrastructure, the NRP outlines a programme to improve the efficiency of transport systems. Simplifying regulations on infrastructure planning will accelerate respective policy measures. On corporate governance, the NRP broadly describes measures already taken to enhance transparency and investor protection, while preserving the system of co-decision.
13. The NRP recognises the need to improve market functioning further. The new structure of the federal regulatory office is designed to achieve this in the area of network services. The intention to exempt investment in broadband networks from regulatory interventions for an unspecified period, in order to create investment incentives, raises regulatory and competition issues, which need to be checked on a case-by-case basis by the competent European and German institutions. Reforming the regulation of intensely regulated professional services, beyond what was partly achieved in the craft sectors, is not mentioned. On public procurement, where competition is limited, only general intentions for reform are announced. Furthermore, the NRP aims to increase the competitiveness of specific sectors through targeted R&D subsidies and the support of information networks.
14. Energy efficiency and security, as well as innovation in environmental technologies, are the components of the response to the key challenge of "ecological innovation". The strategy to achieve the clearly defined objectives in this area appears solid. It is closely linked with objectives and strategies for R&D and innovation. Ongoing and new measures aim to provide economic incentives for technological modernisation in industrial energy production and use. Targets are set for upgrading the energy efficiency of housing, the share of renewable energy in total consumption, and of biological fuels in transport. The commitment to the existing target for the reduction in greenhouse gas emissions is reaffirmed.
15. The programme addresses all relevant areas of micro-economic policies except competition in services. Addressing the key challenges decisively still promises to

contribute to enhancing the growth potential of the German economy. The proposed measures are generally relevant to the challenges. However, in many cases, only intentions are presented.

## **Employment policies**

16. The NRP focuses on the education system and lifelong learning in the context of promoting the knowledge society. It calls for adapting the labour market to the demographic challenge through structural reforms of labour market institutions, an increase in labour market participation, raising adaptability and employability and improving the reconciliation of family life and work.
17. As regards the need to attract and retain more people in employment, the further implementation of the comprehensive labour market reforms launched since 2002 and their possible adaptation after the evaluation announced in the NPR remains at the centre of the employment strategy. These reforms can make a substantial contribution to reducing unemployment. However, overcoming the administrative and financial difficulties continues to be a major challenge, especially in a context of budgetary consolidation.
18. The programme presents ambitious and clear objectives for the integration of young people into the labour market, such as ensuring that they shall not be unemployed for longer than three months and securing more apprenticeship places through the successful National Training Pact. The intention to improve the employment situation for older workers, among other measures, through an agreement with social partners, focusing on access to qualifications, appears appropriate in the light of demographic trends and the planned increase in the statutory retirement age. The response to the issue of women's participation in the labour force appears weak, given wide gender gaps regarding pay and part-time work. The NRP proposes to strengthen transfers to families but does not report on progress towards the announced increase in the number of childcare places. The commitment of municipalities is crucial in this respect.
19. With regard to improved adaptability of workers and enterprises, the measures set out to reduce non-wage labour costs would support the recent favourable trend in unit labour costs, mainly due to wage moderation. In view of the concentration of long-term unemployment among the low-skilled, the plans specified to review the tax/benefit systems and to introduce in-work benefits should be implemented without delay. The extension of the probationary period from six to 24 months may have a positive impact on labour demand, but care should be taken that it does not contribute to further labour market segmentation.
20. The NRP recognises the need to strengthen school and higher education. The proposed measures should help to improve the quality of, and access to, education from early childhood onwards, with a focus on disadvantaged and migrant children. Their successful implementation, however, depends largely on the commitment of the *Länder*. The intention to develop continuing education and training into a fourth pillar of the education system is appropriate and a rapid introduction of the planned financial instruments is desirable.

21. The NRPs priorities regarding employment are ambitious and coherent. More clarity with respect to policy implementation, including financial and administrative capacities, and close cooperation with Social Partners, *Länder* and municipalities will be important for the success of the strategy.

### **PART III: CONCLUSIONS**

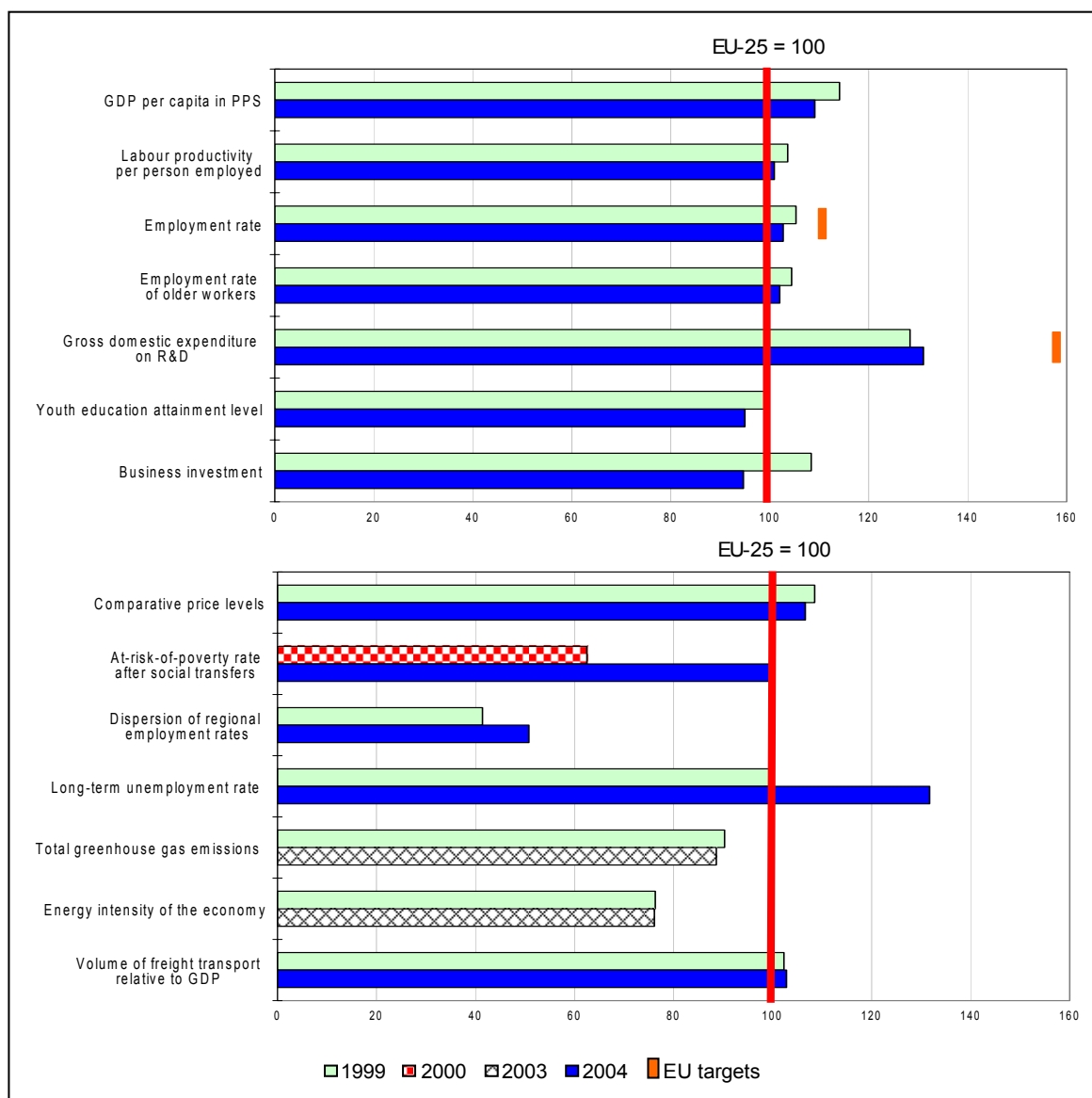
22. In line with the Integrated Guidelines, the German National Reform Programme identifies and responds to most of the main challenges facing Germany, namely the knowledge society; market functioning and competitiveness; business environment; the sustainability of public finances (including sustainable growth and social security); ecological innovation; and the re-orientation of the labour market, though competition in services is an important area only partially addressed. Overall, the NRP sets out a coherent, integrated and appropriate strategy. However, given the large number of measures included a clearer prioritisation would have been called for.
23. The NRP was drawn up under very tight deadlines, given the recent elections. This makes the limited consultation and degree of detail on objectives, funding and timetables understandable. The plan to reduce the number of laws requiring co-decision by the *Bundestag* and *Bundesrat* has the potential to facilitate the adoption of reforms. The involvement of the *Länder* and of municipalities, particularly with regard to their responsibilities in policy areas such as better regulation, education, and R&D, is not always evident from the NRP.
24. The programme's strengths include:
- measures to improve the business environment, such as regular assessment of the impacts of regulation at regional and federal level, measures to support start-ups and improve access to finance for SMEs;
  - the approach to promoting "ecological innovation", for example in the field of energy efficiency and of environmental technologies;
  - the determined approach to tackling youth unemployment.
25. Among the points requiring further attention are:
- improving competition, notably in public procurement, in professional services and in the provision of broadband networks;
  - a more comprehensive approach to improve the integration of low-qualified workers, including immigrants;
  - a more concrete and operational plan to achieve the intended increase in childcare facilities.
26. Taking due account of the above, Germany is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Germany has dealt with the issues mentioned in paragraph 25. In

this context, the Commission looks forward to discussions with the German authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# GERMANY

	DE							2010 National target	EU-25						2010 EU target
	1999	2000	2001	2002	2003	2004	1999		2000	2001	2002	2003	2004		
GDP per capita in PPS	114.1	112.5	110.5	109.2	108.9	109.1	3.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0	
Labour productivity per person employed	103.6	101.8	100.8	100.4	101.0	100.9		100.0	100.0	100.0	100.0	100.0	100.0		
Employment rate	65.2	65.6	65.8	65.4	65.0	65.0		61.9	62.4	62.8	62.8	62.9	63.3		
Employment rate of older workers	37.8	37.6	37.9	38.9	39.9	41.8		36.2	36.6	37.5	38.7	40.2	41.0		
Gross domestic expenditure on R&D	2.40	2.45	2.46	2.49	2.52	2.49e		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe		3.0
Youth education attainment level	74.6	74.7	73.6	73.3	72.5	72.8		74.8	76.3	76.1	76.5	76.5	76.6		
Comparative price levels	108.5	105.6	107.1	107.5	108.7	106.6p		100.0	100.0	100.0	100.0	100.0	100.0p		
Business investment	19.4	19.7	18.3	16.6	16.3	16.0		17.9	18.3	17.7	17.1	16.7	16.9		
At-risk-of-poverty rate after social transfers	11.0	10.0	11.0	15.0b	15.0	16.0		:	16.0	15.0	15.0	15.0	16.0		
Dispersion of regional employment rates	5.5	5.7	6.1	5.9	6.0	6.2		13.3	13.4	13.5	13.3	12.9	12.2		
Long-term unemployment rate	4.1	3.7	3.7	3.9	4.5	5.4		4.1	3.9	3.8	3.9	4.0	4.1		
Total greenhouse gas emissions	81.8	81.4	82.3	81.3	81.5	:		90.6	90.5	91.4	90.7	92.0	:		
Energy intensity of the economy	163.9	159.7	162.5	158.7	159.5	:		214.9	208.8	209.7	206.5	209.5	:		
Volume of freight transport relative to GDP	103.7	103.3	103.3	102.2	103.1	107.5		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e		



# Greece

1. Greece has experienced strong economic growth of 4.4% on average since 1999 with a labour productivity growth clearly above the EU average. GDP per capita stands at 82% of the EU average (2004). With job creation generally low, the employment rate (59.4% in 2004) remains far below the Lisbon target, particularly for women and elderly workers, and unemployment (10.5%) is still high. Greece has a high public deficit (6.6% of GDP) and the highest public debt ratio in the EU (at 109.3 % of GDP) (2004 figures).

## **PART I: GENERAL ASSESSMENT**

2. The Greek National Reform Programme (NRP) identifies key challenges in the field of public finances, employment, education and lifelong learning as well as in a very broad range of micro-economic and environmental policy areas. Modernisation of the public administration is presented as crucial for addressing these challenges and ensuring sustainable growth of the economy as a whole. The Commission broadly shares the NRP's analysis of the main priorities.
3. The NRP sets out a consistent strategy, backed up by relevant policies and measures, but more prioritisation would improve the prospects of achieving important reforms in a timely way. An immediate target is to reduce the budget deficit below 3% of GDP in 2006, compared to 6.6% in 2004. Ambitious targets are also set for employment (62.5 %) and unemployment rates (8.4 %) for the year 2008, as well as for R&D expenditure (1.5% by 2010) and public expenditure for education (5% of GDP by 2008). The programme presents numerous measures, both on-going and new, across the macro-economic, micro-economic and employment areas. Significant attention has been given to the contribution of the European Structural Funds for the implementation of the NRP, both in the current period and for the period 2007-2013.
4. Consultation and efforts to develop ownership of the document have been very substantial. The NRP was prepared under the coordination of the Minister of Economy and Finance. It was approved by the government and discussed in the relevant Parliamentary committees. Its preparation involved extensive consultations with the social partners. Regional and local authorities, NGOs and civil society were also consulted. The Greek Economic and Social Committee (OKE) has established an observatory to monitor the evolution of the reform process set out in the programme.

## **PART II: ASSESSMENT OF POLICIES**

### **Macro-economic policies**

5. Given the high public deficit and public debt ratio, the programme sets as priorities to restore fiscal balance in the short-term and to ensure the long-term sustainability of public finances. The Commission shares this analysis.



6. Although it is expected in the programme that the deficit will fall in 2005 and 2006, it remains unclear in the programme how the government deficit will be reduced in a sustainable manner below 3% of GDP by 2006 and beyond. The NRP announces structural measures both on the expenditure side (a 3.5% reduction of government consumption in nominal terms in 2006) and on the revenue side (fighting tax evasion, broadening the tax base), as well as a series of interventions to improve resource allocation and the quality of public finances. However, while the fiscal consolidation is based to a large extent on permanent measures, the NRP includes one off measures, such as the sale and extension of concession rights (airport, roads, casinos). Achieving the target presupposes that the deficit figures for 2004 and earlier years are not revised upwards and that the increasing co-financing requirements of the Structural Funds up to 2008 are properly taken into account.
7. Achieving a more durable fiscal consolidation is recognised as a challenge. The programme assumes that the expected increase in employment levels - with rather ambitious targets set in this field - will make an important contribution to sustain public finances. It also puts forward a number of reforms in the healthcare sector, such as the introduction of an information system allowing better cost control and the increased use of public private partnerships. However, the NRP does not present a comprehensive strategy for reforming the pension system to improve adequacy and sustainability. Except for in the banking sector, important measures such as reforms of early retirement, reform of the pay-as-you go system, or the development of the second pillar, are postponed to a future social agreement, with an imprecise calendar.
8. The NRP has potential for steering the process of reforming public finances in a successful direction. However, to the extent that the fiscal consolidation path outlined in the NRP is partially based on one-off measures, uncertainties remain on the medium-term deficit reduction and on the path to reduction of the debt ratio. Given the sharp deterioration of the dependency ratio and the large budgetary impact of ageing, the slow progress on pension reform is a particular concern.

### **Micro-economic policies**

9. The Greek NRP includes policies covering the following areas: structural reforms in product markets to strengthen the business environment, competition and export promotion; developing the knowledge society; improving capital markets; environment and sustainable development; regional and social cohesion; and modernisation of public administration. The Commission subscribes to the objectives of this very broad range of micro-economic policies but sees improving the business environment and competition and strengthening R&D and innovation as the first priorities in making Greece more attractive as a business location and in improving productivity levels.
10. The NRP addresses a wide-range of business environment and competition issues. To reinforce entrepreneurship, the NRP includes support for business start-ups, better access to finance for SMEs and one-stop-shops. It also seeks to contribute to a more favourable fiscal environment by reform of corporate taxation and of the investment incentives regime. The regulatory framework is to be enhanced through various measures covering issues such as land use planning, industrial zoning, public-private partnerships, bankruptcy law, e-commerce, independence for competition and regulatory authorities and a reform of opening hours. The NRP also refers to

improvements to public procurement and the regulation of public works and the wider use of impact assessment. The degree of specificity and detail varies across policy areas. With its bearing on the business environment and better regulation, the priority given to modernising public administration appears well chosen, although implementation will be a challenging task.

11. Most R&D and innovation measures put forward are of a spending nature, to be co-financed by the European Structural Funds. The programme sets a target to increase the level of public and private R&D expenditure to 1.5% of GDP by 2010 (from 0.61% in 2003). Some concerns remain as to whether this can be achieved and it is not clear to what extent measures put forward will prove effective, given the absence of a global framework for action and the limited absorption capacity of the economy. In spite of their reliance on the Structural Funds, R&D and innovation initiatives are not given a high priority in the planning for use of the Funds after 2007.
12. The programme addresses additional issues relevant to the Greek situation. For example, it includes action to spread the use of ICT across Greek society, economy and territory. The NRP presents a number of projects contributing to the ambition to become a regional energy hub, including the development of infrastructure and cross-border projects. The NRP also highlights, several, mostly ongoing, measures on the environment and the sustainable use of resources, although measures on ETAP and information on future financing of environmental policy are missing. The NRP does not include structural measures to speed-up implementation of Internal Market directives. On strengthening the competitive advantages of the industrial base, only broad objectives and declarations of intent are included.
13. Overall, the programme addresses micro-economic challenges coherently, although a more comprehensive strategy for R&D and innovation, addressing institutional aspects and covering both the private and public sector seems to be missing. Specific targets, timetables and data on budgetary resources are also scarce. Moreover, instead of streamlining and simplifying policy development and administration, in many cases it adds new layers and institutions to existing ones.

### **Employment policies**

14. The NRP highlights the need to increase low employment rates, in particular for women, to tackle high unemployment and to develop education and lifelong learning as central employment priorities. It also seeks to improve the functioning of the labour market and the adaptability of workers and enterprises. The Commission shares this analysis of the priorities.
15. The programme sets out a number of measures to attract and retain more people in employment, in particular in regions lagging behind. It assumes sustained levels of economic growth and therefore of labour demand in the years to come. Active labour market policies are being strengthened to support job-seekers, with significant efforts to modernise public employment services, including improving identification of labour market needs. It is still not clear, however, how these services, together with private operators, will be in a position to deliver personalised services. At the same time, possible financial disincentives for taking-up a job are being partially eliminated through employment subsidies granted for registered unemployed people. However, a more in-depth review of the impact of the tax and benefit system would

seem appropriate. Measures proposed to address high youth unemployment (26.9%), reduce gender pay gaps, and to promote older workers' participation would also benefit from greater clarity. In particular, the programme could be clearer and more ambitious in responding to the long-term challenge of population ageing, for example by raising the average exit age as part of a wider modernisation of the social protection system.

16. A number of important commitments are made to improve investment in human capital, concentrating on enhancing the quality of education and increasing participation in lifelong learning. Particularly important steps are efforts to increase public expenditure on education, measures to reduce the number of pupils dropping out of school, the adoption of a new framework law on lifelong learning and skills development measures in public administration. However, rapid and effective implementation of the measures proposed will be essential if they are to succeed. Particular attention will be needed to ensure that education and training cater better for labour market needs, and that there is better access to training for low-skilled workers, older workers and for SME staff.
17. In order to improve the functioning of the labour market and the adaptability of workers and enterprises, measures are presented to support geographical and occupational mobility, diversify working time arrangements and promote part-time work through encouraging it in the public sector and improvements in the regulatory framework. Policies in other important areas, such as non-wage labour costs, undeclared work, quality and health and safety at work, are limited or unclear.
18. Assuming continuing high growth rates and the rapid implementation of reforms, the NRP sets out ambitious commitments and targets to increase employment. The employment challenges are addressed by a combination of on-going and new measures, which will require a sustained commitment to ensure their effectiveness and realism. Delivering all of these in a relatively short timescale will be a major organisational challenge and good implementation will be crucial, in particular for the delivery of personalised services as part of the modernisation of public employment services, as well as for the reforms of the education and training systems.

### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the Greek National Reform Programme identifies and responds to the main challenges facing Greece, namely in the field of public finances, employment, education and lifelong learning as well as in a very broad range of micro-economic and environmental policy areas. Modernisation of the public administration is presented as crucial for addressing these challenges and ensuring sustainable growth of the economy as a whole. The NRP presents many appropriate policies and measures, though a strategic framework is not always clear.
20. The extensive consultation of stakeholders and the planned involvement of the Greek Economic and Social Committee during the implementation phase will facilitate putting the measures in the NRP into practice. Nevertheless, delivering the very wide range of initiatives covered in the NRP within the 2005-2008 period will require a

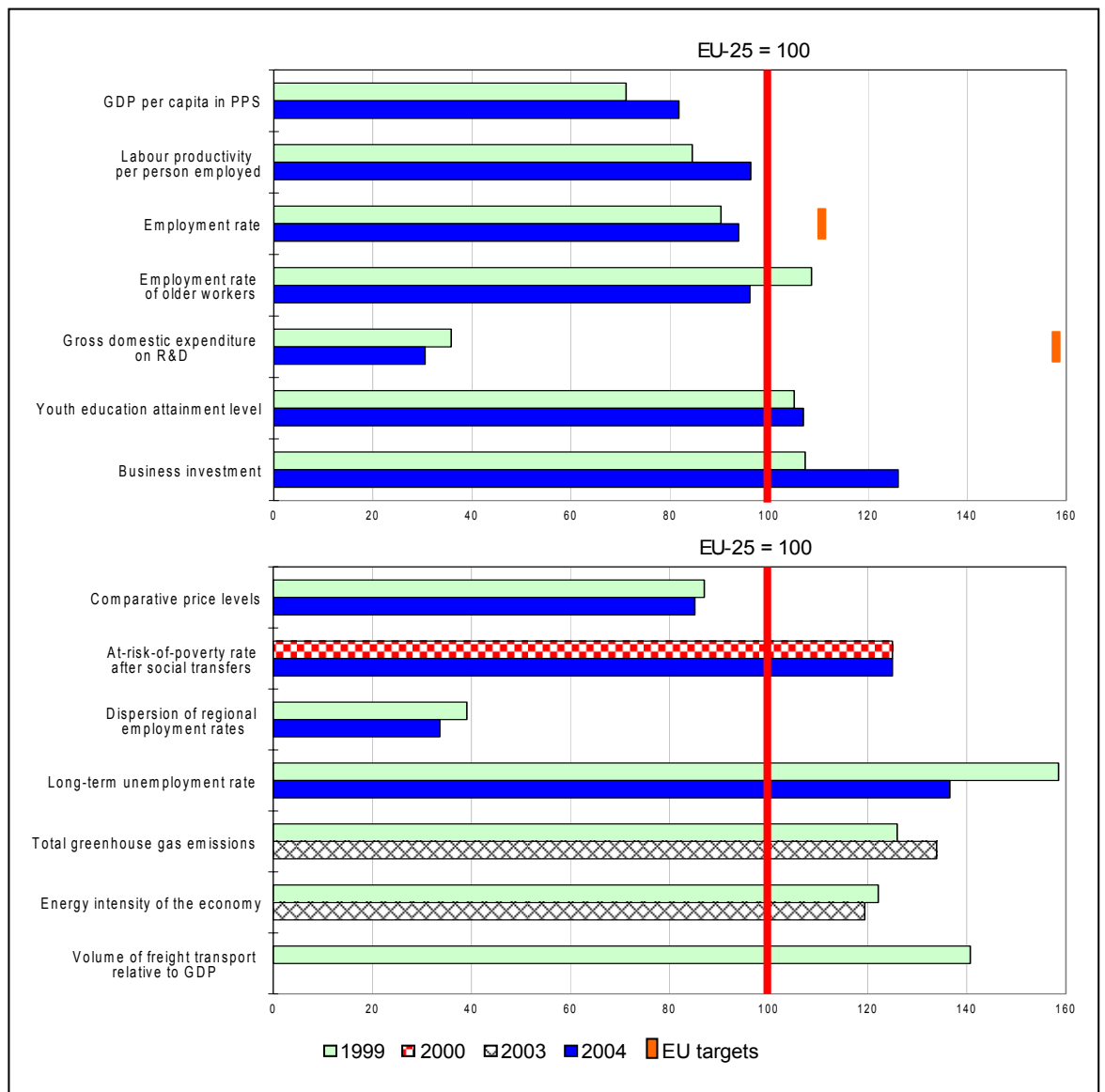
strong and sustained commitment. Specific targets, timetables and budgetary details are provided only for some initiatives.

21. The programme's strengths include:
  - strong linkage of the priorities in the NRP with current and future EU funding;
  - the systematic integration of an ICT dimension in sectoral policies.
22. Among the points requiring further attention are:
  - fiscal consolidation through the use of more permanent measures;
  - ensuring that measures for R&D and innovation cover both financial and institutional aspects and are part of a consistent strategy involving both public and private partners;
  - putting into practice modernisation of the public administration;
  - reinforcement of active labour market measures and of education and training reform.
23. Taking due account of the above, Greece is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Greece has dealt with the issues mentioned in paragraph 22. In this context, the Commission looks forward to discussions with the Greek authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# GREECE

	GR							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	71.1	71.6	72.8	76.9	80.7	81.8	62.5 (2008)	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	84.5	86.4	89.3	94.7	98.1	96.3		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	55.9	56.5	56.3	57.5	58.7	59.4		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	39.3	39.0	38.2	39.2	41.3	39.4		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	0.67	:	0.64	:	0.62p	0.58p		1.5	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	78.6	79.3	80.0	80.7	81.7	81.9			74.8	76.3	76.1	76.5	76.5		76.6	
Comparative price levels	87.0	84.0	84.5	82.2	84.5	85.1p			100.0	100.0	100.0	100.0	100.0		100.0p	
Business investment	19.2	19.5	19.8	20.2	21.5	21.3			17.9	18.3	17.7	17.1	16.7		16.9	
At-risk-of-poverty rate after social transfers	21.0	20.0	20.0	:	21.0b	20.0			:	16.0	15.0	15.0	15.0		16.0	
Dispersion of regional employment rates	5.2	5.1	4.3	3.8	3.2	4.1			13.3	13.4	13.5	13.3	12.9		12.2	
Long-term unemployment rate	6.5	6.2	5.5	5.3	5.3	5.6			4.1	3.9	3.8	3.9	4.0		4.1	
Total greenhouse gas emissions	114.1	118.5	119.6	119.6	123.2	:			90.6	90.5	91.4	90.7	92.0		:	
Energy intensity of the economy	262.5	263.6	260.6	258.0	250.1	:			214.9	208.8	209.7	206.5	209.5		:	
Volume of freight transport relative to GDP	141.7e	:	:	:	:	:			100.7e	100.4e	99.4e	100.3e	99.7e		104.7e	



# Hungary

1. Since the mid-1990s, the Hungarian economy has grown at an average annual rate of 4%, one of the highest growth rates in the EU. Labour productivity growth is also well above the EU average. However, the budget deficit (5.4% in 2004) will, instead of declining as foreseen, increase above 6% in 2005. GDP per capita is currently at 60% of the EU average. Following a temporary acceleration in 2003, employment growth turned negative in 2004 and the overall employment rate has decreased to 56.8%, far below the Lisbon target, while unemployment has increased (6% in 2004), though remaining below the EU average. Low unemployment is however coupled with a very low rate of activity (60.5% in 2004)

## **PART I: GENERAL ASSESSMENT**

2. The Hungarian National Reform Programme (NRP) identifies nine main challenges: reducing the fiscal deficit; R&D and innovation; business environment; competition; infrastructure; raising the employment and activity rate; improving the labour market situation of the disadvantaged; reducing regional labour market disparities; and enhancing human capital through better education & training. The Commission shares this analysis of the main priorities.
3. The medium-term strategy presented in the NRP aiming at a continuous catching-up with EU average GDP per head through robust economic growth and increasing employment appears realistic, but the level of ambition implied in the programme is difficult to assess, as in places, the presentation of measures is not fully clear or concrete. The programme does not fully explain how the reforms in various areas are integrated and whether there are possible synergies between them. Their overall coherence across policy areas is not always evident, for example when assessing the objectives regarding infrastructure investment against the background of aiming also for fiscal consolidation. The NRP refers to the ambitious employment rate target of 63% by 2010, as set by the Government in 2004. No target for R&D spending by 2010 is specified. For some measures, the NRP highlights support from the Structural Funds. Given the strong emphasis on development needs, the role of cohesion policy in the delivery of the “growth and jobs” agenda could have been more strongly highlighted.
4. Consultation and efforts to develop ownership of the document have been substantial. The programme has been formally endorsed by the Hungarian government. It has been subject to wide consultation with social partners and local authorities. Furthermore, a consultation conference has been organised for a wide range of key partners. In addition, the draft was available on-line for comments. The document was presented to the Employment Committee of the Hungarian parliament.

## **PART II: ASSESSMENT BY POLICY AREA**

### **Macro-economic policies**

5. The macro-economic key challenge of reducing the fiscal deficit is a central issue for the Hungarian economy. The policies and measures proposed are generally relevant to respond that challenge but they lack detail and quantified estimates of their impact. A clearer presentation of the integration and the overall coherence of the proposed measures would facilitate their assessment.
6. The strategy of ensuring long-term sustainability by complementing a gradual approach to cutting the fiscal deficit with further progress with healthcare and pension reforms addresses crucial issues for the Hungarian economy. Coupled with a planned reform of the tax regime, including a considerable reduction in the VAT rate, the measures presented seem likely to be effective in contributing to growth and employment and to improving the business climate. However, the information provided in this regard is not sufficient to assess fully the consistency of the proposed measures with the medium-term macroeconomic objectives. The absence of a clear timeline for achieving budgetary balance and the reduction of government debt makes it difficult in general to assess the macro-economic strategy.
7. While the policy objectives, strategies, and measures presented in the programme to tackle the macroeconomic key challenge can be regarded as a suitable response in principle, several questions remain unanswered owing to insufficient detail in the programme. The absence of clear timelines risks undermining the credibility and effectiveness of the strategy, in particular given the importance of careful sequencing of those measures envisaged which will have a fiscal impact.

#### **Micro-economic policies**

8. The programme identifies R&D and innovation, the business environment, competition, and the development of infrastructure as micro-economic key challenges. The Commission subscribes to these priorities.
9. The NRP recognises the importance of achieving stronger R&D and innovation and analyses many problems that need to be addressed in that regard. First is the small contribution by the private sector to overall R&D spending, which stands at a comparatively low level of 0.95 % of GDP. Regulatory problems, weak links between business and research institutions, surprisingly small spillover effects for innovation from cooperation with foreign companies, as well as the fragmentation of research activities, are all seen as key factors constraining Hungary's innovative capacity. While the R&D and innovation challenge is well presented in its various dimensions, the corresponding policy response is only in some cases clearly laid out. The NRP does not set out to a monitoring and evaluation system for the R&D and innovation strategy. To facilitate the move toward a more knowledge-based society, the inefficiencies identified in the Hungarian education system need a more concrete response. The programme fully recognises the importance of spreading the use of ICTs, but says little on how this objective can be achieved in practice.
10. Measures presented to improve the business environment in Hungary comprise the tax reform in 2006, the assessment and reduction of the administrative cost to enterprises and efforts to achieve better regulation through the introduction of impact assessments. The NRP recognises the importance for SMEs of better access to finance, although insufficient detail in the presentation of measures in this area makes assessing them difficult. The relatively low level of attention paid to practical

measures to achieve efficient bankruptcy procedures and company restructuring regulations contrasts with the programme's clear recognition of the importance of these issues. Encouraging and supporting entrepreneurship at all school levels remains an important challenge.

11. The programme proposes to increase competition in the network industries, where incumbents' market shares remain high, and in the case of the gas and electricity sectors, the switching rate is very low. However, apart from stating the general need to continue the process of opening markets and to improve the efficiency and independence of regulatory bodies, policies and implementation measures to achieve more competition are not specified.
12. While the NRP identifies the environmental challenges and corresponding budget allocations, little is said on the steps and timing for putting them in practice. The programme places a strong emphasis on the development of high-quality infrastructure, as regional disparities in this field are increasing, limiting the country's economic potential and regional competitiveness. The important budgetary implications of modernising the infrastructure are not addressed very clearly.
13. The microeconomic key challenges identified are all presented clearly and existing constraints on increasing potential economic growth in Hungary are analysed in considerable detail. The strategies, policy objectives, and measures presented to address these well-understood problems sometimes do not match the analysis in clarity and detail. This raises questions about their level of ambition and likely effectiveness.

### **Employment policies**

14. Raising the low employment and activity rate, improving the labour market situation of the disadvantaged, reducing regional labour market disparities and enhancing human capital through better education and training are the four key challenges identified for Hungary's employment policies. These priorities reflect well the country's needs in this area.
15. The NRP places strong emphasis on attracting more people to employment and retaining them. Appropriate principles are laid down for a coherent reform of the unemployment and social benefits system, with a view to boosting activity through setting more coherent incentives, for example by making unemployment benefits conditional on an active job search. Without a comprehensive review of the social benefits system, including disability benefits, the effectiveness of the proposed measures remains in doubt. Incentives encouraging active ageing need to be backed by further measures to limit early retirement and by reducing the flow of new recipients of disability pensions. Measures to reach the inactive population through the public employment service by involving municipalities and setting up, with European Social Fund assistance, an integrated employment and social services system promise to deliver results. These measures can build on progress already made with the reduction in employers' social security contributions. Improving the health situation of the population and related health care reforms could also contribute to increasing participation and employment rates. Measures to improve the situation of people with disabilities and of the Roma population and to reduce



persistent regional disparities may require stronger coordination and monitoring and closer cooperation with stakeholders.

16. The NRP shows the clear determination of the authorities to transform undeclared work into regular employment through measures instituting strong and coherent incentives and sanctions. In this respect, linking health service entitlements to contribution payments made is an important step forward. The measures proposed to reduce the tax wedge, particularly in the lower income segment, can contribute to more employment and help combat undeclared work. The impact of recent minimum wage increases on the levels of low-skill and low-wage employment needs to be closely monitored.
17. On enhancing human capital, the lifelong learning strategy adopted by the government is not described in the programme in enough detail to permit a full assessment. The measures to reduce the number of drop-outs from school, to ensure equal access to education, and to adjust education and training systems better to labour market needs, do not seem to reflect a clear strategic policy approach. The emphasis placed on upgrading skill levels may fall short with regard to the particularly disadvantageous labour market situation of low-skilled persons.
18. Building on the existing national employment strategy, the programme presents a number of important forward-looking measures aimed at increasing activity. While the clear focus on this area enhances the likelihood of the measures being effective, the policy response to the challenges in the area of education and lifelong learning deserves a similar level of attention.

### **PART III: CONCLUSIONS**

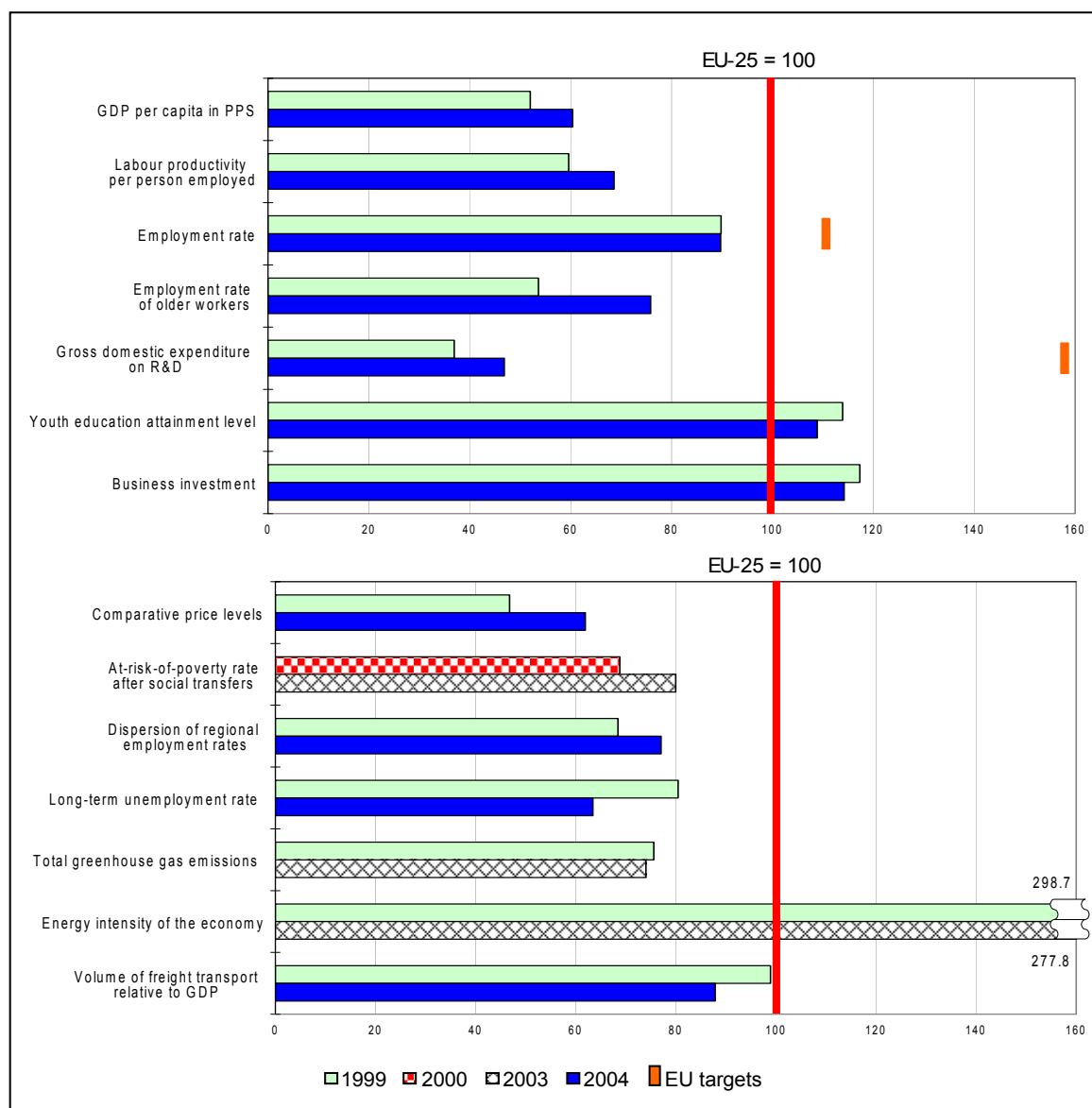
19. In line with the Integrated Guidelines, the Hungarian National Reform Programme identifies and responds to the main challenges facing Hungary, namely reducing the fiscal deficit; R&D and innovation; business environment; competition; infrastructure; raising the employment and activity rate; improving the labour market situation of the disadvantaged; reducing regional labour market disparities; and enhancing human capital through better education & training. Overall, the medium-term strategy presented in the NRP appears appropriate given the Hungarian context of aiming to push GDP rapidly towards the EU average. Nevertheless, the programme is not fully integrated, in particular with the fiscal stability strategy, and measures across the different policy areas do not always appear coherent.
20. The NRP contains a clear presentation of challenges and a frank and thorough analysis of existing problems and constraints. The wide and transparent consultation process bodes well for the implementation of the outlined policies. However, in places, the presentation of measures and particularly their medium-term budgetary impact could be clearer and more concrete.
21. The programme's strengths include:
  - measures to improve the effectiveness of the public employment service and the intention to set up an integrated system of employment and social services;
  - measures to transform undeclared work into regular employment.

22. Among the points requiring further attention are:
- strategies to ensure sustainable public finances;
  - clearer and more robust measures to enhance competition in network industries;
  - improving the business environment including SMEs' access to finance;
  - increasing the responsiveness of education and training systems to labour market needs and upgrading skill levels, particularly for low-skilled persons.
23. Taking due account of the above, Hungary is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Hungary has dealt with the issues mentioned in paragraph 22. In this context, the Commission looks forward to discussions with the Hungarian authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# HUNGARY

	HU							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	52.0	53.2	56.1	58.4b	59.6	60.4	63.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	59.6	60.9	64.6	67.1b	67.2	68.6		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	55.6	56.3	56.2	56.2	57.0	56.8		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	19.4	22.2	23.5	25.6	28.9	31.1		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	0.69	0.80	0.95	1.02	0.95	0.89		:	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	85.2	83.6	84.4	85.8	85.0b	83.4		74.8	76.3	76.1	76.5	76.5	76.6			
Comparative price levels	46.8	48.4	52.0	56.9	59.0	61.9p		100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	21.0	20.2	19.5	18.3	18.8	19.3		17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	:	11.0	11.0	10.0	12.0	:		:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	9.1	9.0	8.8	9.4	8.5	9.4		13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	3.3	3.0	2.5	2.4	2.4	2.6		4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	68.5	66.3	68.5	66.1	68.1	:		90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	642.0	600.5	588.6	579.6	582.0	:		214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	99.6	97.5b	91.8	86.9	85.4	91.9		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e			



## Ireland

1. Over the last few decades, Ireland has experienced a rapid increase in real GDP per capita and employment levels. Labour productivity growth has been well above the EU average over the last decade. In terms of GDP per capita Ireland was close to the EU average ten years ago, but now it stands at 138% (2004), the second highest in Europe. Recent employment growth has been driven by increased participation and, notably, by immigration from the new Member States, resulting in the employment rate of 66.3% and the lowest unemployment rate in the EU, at 4.5% in 2004.

### PART I: GENERAL ASSESSMENT

2. The Irish National Reform Programme (NRP) recognises that the overall challenge now for Ireland is to sustain and improve its recent good economic performance, based on taking advantage of the opportunities presented by globalisation and the internal market. The NRP therefore identifies an extensive set of priorities which can be summarised as: maintain a stable macroeconomic environment; investment in economic and social infrastructure; improve labour supply; better regulation; improve R&D, innovation and entrepreneurship; promote social inclusion and sustainable development. The Commission broadly shares the NRP's analysis of the main priorities, but identifies pension coverage as an additional area of concern.
3. The measures presented in the NRP are based on the current social partnership agreement: "*Sustaining Progress*", which will shortly be renegotiated, after which new policies will emerge. Consequently, very few new policies are for now proposed in the NRP, which presents existing policies clearly and within the well-established national strategic framework. Ireland's national target for investment R&D is 2.5% of GNP for 2013 - no intermediate targets are given. Neither are formal employment rate targets specified. The link between use of Structural Funds and the NRP priorities is not clearly presented, as the role of cohesion policy is mentioned only in the annex.
4. Consultation and efforts to develop ownership of the document have been very substantial, assisted by the fact it is based on building on policies on which there was a fair degree of existing consensus. The Department of the Taoiseach co-ordinated the overall preparation of the NRP with the Departments of Finance and Enterprise, Trade and Employment. An extensive consultation with other departments and agencies took place. The social partners were consulted in the course of preparation and the programme was considered in both houses of the Parliament. There were also bilateral discussions with a number of Member States.

### PART II: ASSESSMENT BY POLICY AREA

#### Macroeconomic policies

5. The NRP identifies three key priorities in this domain: ensuring macro-economic stability; prioritising public investment in infrastructure and other growth-promoting

expenditure; and managing anticipated long-run fiscal pressures, including those arising from the population ageing. The Commission supports this approach.

6. The NRP reiterates and reviews ongoing macroeconomic policies, in particular those aimed at achieving long-term sustainability and quality of public finances, which to an important extent are based on pension reform. The programme refers to some existing policy initiatives in the area of pension coverage, recent improvements of minimum pensions and further steps envisaged to strengthen the incentives to work longer. However, coverage remains significantly below government targets and detail is lacking on how Ireland will address the problem of a growing imbalance between income in work and in retirement. The NRP refers to the preparation of a new 2007-2013 National Development Plan, which will set out a new strategy for infrastructure, human capital and R&D investment.
7. The macroeconomic policies set out largely involve continuing the successful approach Ireland has taken in recent years and appear sufficient to underpin further growth and job creation. Attaining the stability-oriented macro-economic objectives should facilitate the implementation of the structural reforms envisaged. However, the Commission believes that more attention could be given to the issue of pension coverage as a key element behind financial and social sustainability.

### **Microeconomic policies**

8. The NRP identifies several micro-economic priorities: improving competitiveness, infrastructure, regulation and social inclusion; increasing R&D investment and efficiency; encouraging greater innovation and entrepreneurship; and sustainable development. The Commission largely supports the choice of these priorities, noting however that the NRP does not identify competition in services as a key challenge.
9. Ireland provides a comprehensive set of measures to consolidate and improve the competitiveness of its industrial base, but relatively little information is given on the measures to address comparatively high price levels in Ireland, which tend to underline the problem of overall competitiveness. Measures to enhance the transport infrastructure are described, but without references to how they are related to important ongoing projects. Better regulation measures described in the NRP include the impact assessment system now in place, the planned simplification exercise and the creation of a business forum for consultation purposes. Measures to extend and deepen the Internal Market are clearly addressed and detailed information is provided. No specific information is given on reform of the regulation of professional services.
10. Ireland's research and innovation policies build on existing measures. A key initiative mentioned in the NRP is the Science, Technology and Innovation (STI) Strategy to follow-up Ireland's 2004 R&D action plan, but no detail on the content and time schedule of the STI strategy is provided. The action plan's R&D targets for 2013 are referred to but no intermediate targets are given. Some other individual R&D initiatives are referred to but insufficient information is provided for their evaluation. A general analysis and list of on-going policy measures in the annex to the NRP reflects recent efforts to increase the scale and efficiency of research and innovation investment over the long-term. The 2005-2007 Enterprise strategy "Transforming Irish Industry" represents a major effort to address shortcomings in

innovation performance, for example regarding the creation of start-ups, “incubators” and innovation centres, as well as the availability of venture and equity capital. Measures to improve business support services for SMEs with specific focus on key sectors are presented, but here the NRP would benefit from more clarity and detail.

11. To strengthen the Irish position in the global information society, the NRP addresses various areas to stimulate ICT use, but the proposals set out are either rather vague, for example on e-government and ICT in schools, or already implemented, such as actions on broadband communication and e-business development.
12. Concrete measures to support more sustainable production and consumption patterns as well as green public procurement initiatives, such as financial support for bio fuels and renewable electricity, are presented. The Irish climate strategy, currently under revision, will be of key importance in delivering results.
13. Overall, the NRP identifies a number of important micro-economic policy priorities. The initiatives in relation to these are largely on-going initiatives and in general are producing or have the potential to produce good results. More details on new policies to address bottlenecks in infrastructure and competition in services would be helpful. Achievement of the relatively ambitious R&D target will depend on maintaining a high level of R&D investment by foreign subsidiaries and on major increases in R&D investment by Irish industry. This will require a bigger leverage effect of public funding on private investment and creation of more extensive linkages between public research and industry.

### **Employment policies**

14. Ensuring that the Irish labour force is cost competitive is a key government objective reflected in the three employment priorities: the overarching priority of higher levels of employment, improved quality and productivity at work, and social cohesion; labour supply issues, including tackling inactivity and developing a skill-based migration system; and developing a highly skilled and adaptable workforce.
15. In striving to further raise employment rates, against the background of the overall employment rate target for the EU of 70 % by 2010, Ireland will seek to improve labour supply through intensified measures to address specific target groups in the inactive population, to address remaining disincentives in the tax and welfare systems and to increase female participation. The NRP does not explain how the provision of affordable, high quality childcare services will be further developed. Greater integration of vulnerable groups is envisaged, with recent measures to support the employment of people with disabilities highlighted. The NRP also mentions the current development of a skills-based migration policy as an essential element to ensure the sustainability of economic growth.
16. With regard to adaptability of workers and enterprises, the NRP focuses on the implementation of the National Workplace Strategy, a promising initiative aimed at supporting workplace innovation, skills development and work-life balance. Apart from health and safety in the workplace, relatively little attention is paid to the issues of quality of work and poverty among employed people. The linkages between human capital and productivity are not directly addressed, though this issue is relevant for securing the long-term sustainability of economic growth.

17. The problem of improving skills in the labour force is clearly recognised in the NRP. It indicates that increased investment in human capital will focus on development of skills relevant both to enterprises and individuals and ranging from improving general skill levels to targeting more specific sectoral and occupational skills. The need to improve the position of the low skilled is recognised, though details of measures addressing this issue, especially with respect to older workers, are not presented in detail.
18. The NRP provides a comprehensive approach to reaching its employment objectives, though a ranking of priorities would be helpful. The measures set out are mostly on-going and generally sufficient to make good progress. The specific manner in which inactivity is to be addressed, the enhancement of adult participation in learning and provision of affordable and improved childcare services could usefully have received more attention.

### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the Irish National Reform Programme identifies and responds to most of the main challenges facing Ireland, namely maintaining a stable macroeconomic environment; investment in economic and social infrastructure; improving labour supply; better regulation; improving R&D, innovation and entrepreneurship; promoting social inclusion and sustainable development, though pension coverage is an important question not fully addressed. Overall, the NRP takes an integrated and ambitious approach to further reinforcing factors which have underpinned Ireland's recent economic success, based on a well-established national strategic framework.
20. Details on measures, their objectives and their budgetary implications are incomplete in some areas, including among others promoting ICT use, improving skills and enhancing childcare provision. The extensive consultations on the NRP and the level of existing consensus on many of policies presented in it will be a considerable advantage as implementation of the reforms proceeds.
21. The programme's strengths include:
  - its approach to sustaining macro-economic stability;
  - measures to enhance the quality of industrial development;
  - the emphasis on the need to integrate inactive people into the labour market, to increase female participation and to address skills development.
22. Among the points requiring further attention are:
  - ensuring policies on R&D and science and innovation investment are sufficiently robust to reach the ambitious targets set;
  - more specific measures to address pensions coverage.
23. Taking due account of the above, Ireland is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in

particular the way Ireland has dealt with the issues mentioned in paragraph 22 here-above. In this context, the Commission looks forward to discussions with the Irish authorities as part of the new partnership for growth and jobs.

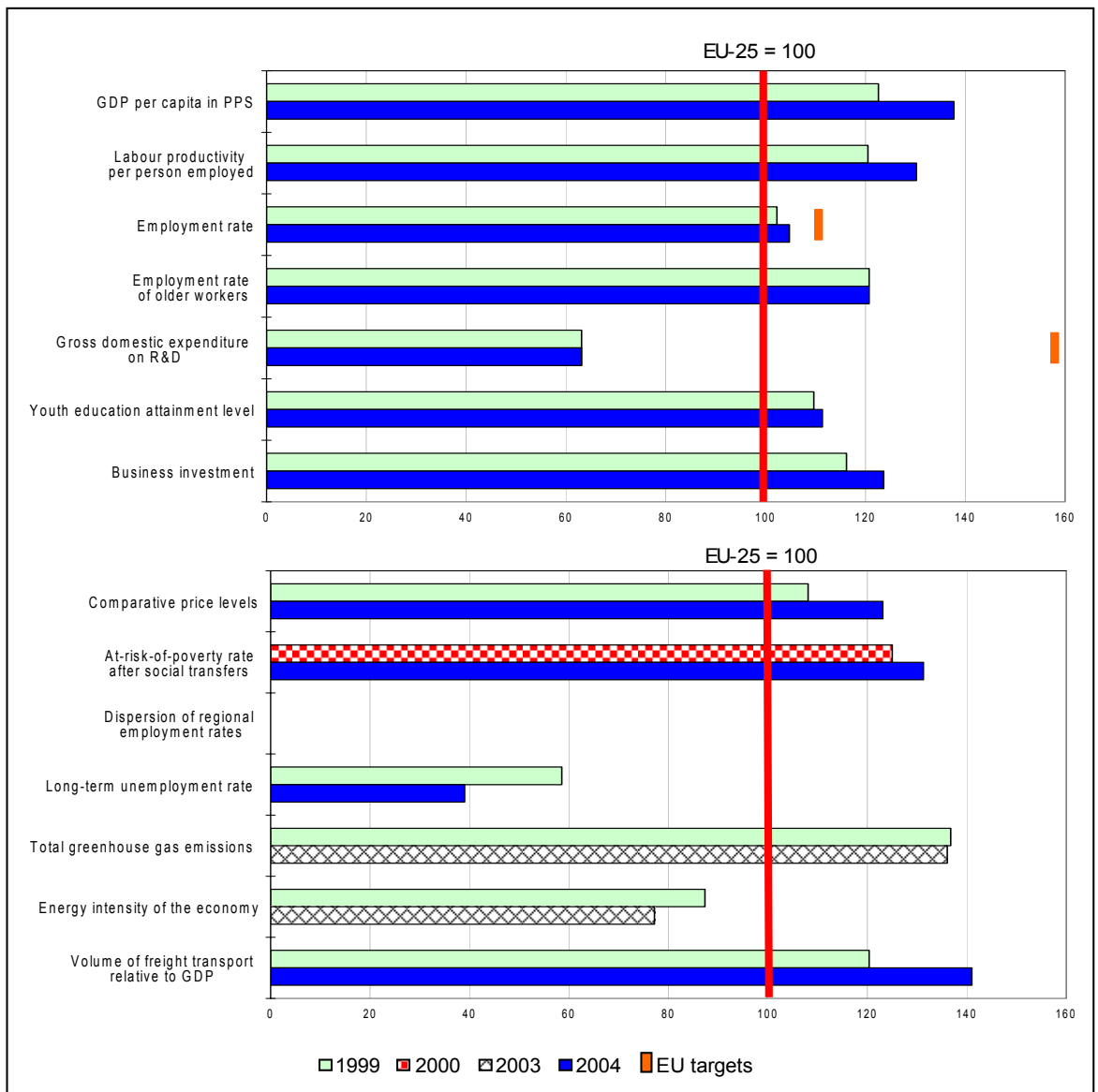
#### **PART IV : STATISTICAL GRAPHS AND DATA**



# IRELAND

	IE							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	122.6	126.8	129.4	133.5	134.7	137.7		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	120.5	122.4	124.5	128.5	129.0	130.2		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	63.3	65.2	65.8	65.5	65.5	66.3	:	61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	43.7	45.3	46.8	48.0	49.0	49.5		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	1.18	1.13	1.12	1.10	1.16	1.20	*	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	82.0	82.4	84.6	83.9	85.3p	85.3p		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	108.1	111.6	116.0	122.4	126.6	123.1p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	20.8	20.7	18.9	18.1	19.2	20.9		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	19.0	20.0	21.0		21.0b	21.0			16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	-	-	-	-	-	-	-	13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	2.4	1.6	1.3	1.3	1.5	1.6		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	123.9	127.8	131.1	128.6	125.2			90.6	90.5	91.4	90.7	92.0		
Energy intensity of the economy	187.7	175.1	172.5	166.1	161.7			214.9	208.8	209.7	206.5	209.5		
Volume of freight transport relative to GDP	121.2	132.0	125.1	135.0	141.0	147.5		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	

\* National target: 2.5% (2013) of the Gross National Product (GNP)



## Italy

1. Italy's GDP per capita in 2004 was 103% of the EU average. Between 1995 and 2004, Italian GDP grew by 1.6% per year on average, compared to 2% for the euro area. During that period the growth of productivity per person employed was also below the euro area average. In spite of low growth, robust job creation in recent years has contributed to a fall in the unemployment rate to 8% in 2004, below the EU average. At the same time, the employment rate, at 57.6% (2004) remains far below the Lisbon target. Italy has faced a reduction of its international competitiveness and has a very large public debt.

### **PART I: GENERAL ASSESSMENT**

2. Italy's National Reform Programme (NRP) highlights five priorities to boost output growth and employment: extending the area of free choice for citizens and companies (by opening up energy and services markets); granting incentives for scientific research and technological innovation; strengthening education and training; upgrading infrastructure; protecting the environment. A sixth priority, long-term fiscal sustainability, is addressed in a separate document (see paragraphs 5 and 6 below). The Commission shares this analysis but also sees general enhancement of competition in all markets, including through deepening the internal market, as a major challenge for Italy. Furthermore, the Commission believes that the challenge of increasing employment rates and reducing regional employment disparities will indeed benefit from reforms to strengthen education and training, but additional initiatives should be considered as well. These measures were presented to the Commission in a separate document.
3. The Italian programme contains many realistic and valuable measures, most of which are already planned or on-going. However, the main steps for 2005-2008 are not always accompanied by timetables or information on monitoring and evaluation procedures. There is recognition in the NRP of the importance of integration between micro-economic, macro-economic and employment policies. The programme focuses largely on the micro-economic area, while macroeconomic and employment policies are largely covered in the annexes. The estimated total cost of the programme is €46.5 billion, most of which was already included in the 2005 budget. The remaining part (€13 billion) is conditional on expected revenues deriving from sales of public sector real assets in 2006-2008. Seventy per cent of the overall funding is allocated to infrastructure. The Programme is to some extent coordinated with other policies, partly covered by the annexed background material. No targets are set for R&D spending. Cohesion policy, expected to provide a large contribution to achieving the aims of the Programme, is discussed mainly in relation to the current implementing period. General references to the possible use of financial resources from the Structural Funds 2007-2013 are made.
4. Consultation and efforts to develop ownership of the Italian NRP at government, administrative and expert level have been substantial. A new internal governance structure (Comitato Tecnico) was charged of inter-ministerial co-ordination. The results of a survey of 120 economists were taken into account. Regional authorities

and social partners had the opportunity to express their views both formally and informally. The NRP was presented to the parliament after its adoption.

## **PART II: ASSESSMENT BY POLICY AREA**

### **Macro-economic policies**

5. The NRP's five priorities for action relate mainly micro rather than to macro-economic policies. However, the programme states that the consolidation of public finances according to the plans in the economic and financial planning document for the years 2006-2009 (DPEF)<sup>3</sup> is to be considered an integral part of the Programme.
6. Those plans identify long-term sustainability of public finance as a priority, to be achieved based on the recovery of economic growth, the budgetary effects of the 2004 pension reform and medium-term fiscal consolidation. The DPEF aims to reduce the general government deficit to below 3% of GDP by 2007 (from 4.3% in 2005) and to reduce the debt-to-GDP ratio from 108% in 2005 to 101% in 2009. This is primarily thanks to an increase in the primary surplus from 0.6% to 3% of GDP over the same period. However, the Commission's analysis is that long-term fiscal sustainability in Italy would require maintaining a minimum primary surplus of around 4% of GDP, underpinned by reforms to permanently restrain public spending. The Italian NRP does not cover pensions in detail but reforms since the early-1990s have sought to address long-term sustainability by reducing future pension liabilities. In particular, the 2004 reform, to take effect from 2008, raises the retirement age, and foresees the development of the "second pillar" (funded pensions). Full implementation of that reform together with raising employment rates, in particular of women and older workers, will be important for the pensions system to combine social adequacy and financial sustainability in future.
7. In the light of Italy's high public debt, low potential GDP growth rate and the expected increase in ageing-related expenditure, the macro-economic strategy and targets might not prove sufficiently ambitious. In particular, the planning document does not adequately address the continuing increases in health care expenditure. However, the approval of the 2006 "Legge Finanziaria" represents, if fully implemented a further step towards the goals of consolidation of public finances as stated in the DPEF.

### **Micro-economic policies**

8. The Italian NRP highlights four micro-economic priorities: R&D, "free choice for citizens and companies", infrastructure and environment. It includes various initiatives to improve the business environment, including better regulation. However, the programme does not address in full challenges such as strengthening competition and deepening of the internal market.

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<sup>3</sup> Documento di Programmazione Economico-Finanziaria per gli anni 2006-2009 submitted by the government to parliament on 15 July 2005. The document is available in Italian at: [http://www.tesoro.it/Documentazione/DPEF\\_2006-2009/DPEF\\_2006-2009.pdf](http://www.tesoro.it/Documentazione/DPEF_2006-2009/DPEF_2006-2009.pdf)

9. The proposed action to boost R&D includes interesting elements, for example fiscal measures to make undertaking R&D more attractive for companies. The proposed reorganisation of the national research system should also over time help to improve R&D performance, despite limited detail in the programme on cooperation between Ministries and the regions and on fostering links between SMEs and between business and the public sector. Research and innovation resources tend to be concentrated on specific sectoral projects rather than on structural measures with a potentially broader economic impact. The programme states that the combination of measures and projects in research and innovation should enable Italy to approach the 3% of GDP goal for R&D spending. A strong commitment to achieving that objective and the 66% target for the private contribution to R&D expenditure will be necessary. The programme tackles the most important issues in ICT but without prioritising fully the measures proposed.
10. Under the theme of “free choice for citizens and companies” the Italian NRP aims to increase competition, especially through more open utilities markets (including energy) and in services, but does not give full details on how these goals will be achieved. The removal of barriers restricting competition in professional services is envisaged, even though specific implementation measures are not mentioned in detail. The programme proposes a series of specific measures to improve the business environment by improving regulation and public sector efficiency, such as simplification of existing legislation, a project on the application of the Standard Cost Model for measuring administrative costs, guidelines for consultation exercises and increasing the use of impact assessments. These initiatives are likely to contribute to reducing the burden on businesses. The newly approved framework law reforming bankruptcy legislation should also encourage entrepreneurs. Provisions for speeding up and improving the implementation of EU legislation should be specified in the NRP.
11. The NRP sets out plans for investment in upgrading road, sea and rail infrastructure by completing major projects. There are also interesting initiatives to introduce or improve IT infrastructure in schools, healthcare, tourism and public administration. The programme would benefit largely from a detailed reference to the regional dimension. The Trans-European Transport Network projects are at the centre of the strategic framework for transport policy. Little reference is however made to the railway network outside TENs, which merits improvements especially in the Southern Italy.
12. The fairly strong emphasis on environmental protection in the NRP is not reflected in the budgetary allocation for 2006-2008. The proposed measures to promote research and innovation in renewable energy would need to be specified.
13. The micro-economic chapter of the Italian NRP contains important elements, notably on boosting research and making the business environment more attractive, which have the potential to contribute effectively to growth and jobs. The infrastructure investment set out in the programme should also help the economy to function better. Overall the aim of the measures proposed constitutes the type of micro-economic reforms which, in synergy with macro-economic stability and labour market reform, could reduce Italy’s dependence on traditional sectors, help SMEs to grow and new businesses to emerge and thus help to tackle the reduction of international

competitiveness which Italy is facing. Their effective, full and timely implementation will be crucial to attain such goals.

### **Employment policies**

14. The Italian programme cites strengthening of education and training as its main employment priority. Employment is considered as “endogenous” to all the other priorities in the NRP. Other significant employment-related challenges such as employment rates significantly below the EU averages and the sharpest regional employment disparities in the EU are addressed in the annex.
15. Most of the education and training measures mentioned are already in place. The NRP covers the 2003 education and training reform (operational as from 2007-2008) and university reform. There are useful initiatives to support higher education - particularly in scientific subjects – to ease the school-to-work transition, to reduce early school leaving and to train civil servants. Further substantial information on the evaluation and monitoring of reforms, on quality assurance mechanisms to ensure common standards across regions or on training measures for low-skilled and older workers should be provided. The overall funding included in the NRP for education and training is very limited. The key role in employment policy of regions and social partners could have been better highlighted.
16. Given its approach (with employment as an endogenous element) the Italian NRP does not address directly the issue of attracting and retaining more people in employment. The focus on youth employment, female participation, childcare, active ageing, integration into work of people with disabilities or active labour market policies is addressed in the annex, as are certain specific aspects important for Italy such as flexibility and security, wage developments, geographical productivity differentials, undeclared work and non-wage labour costs.
17. As far as employment policy is concerned, the Italian NRP devotes its attention to education and training. There is cause for optimism over some of the individual measures proposed, such as the reform in the educational system. However, significantly more efforts would be certainly needed to boost educational and training levels up to the EU average, despite some positive trends. As stated, more information on other employment policies is available in other documents but the provision of some details in the NRP itself would have allowed a more coherent analysis of the links and synergies with other policy areas.

### **PART III: CONCLUSIONS**

18. In line with the Integrated Guidelines, the Italian National Reform Programme identifies and responds to many of the main challenges facing Italy, namely extending the area of free choice for citizens and companies (by opening up energy and services markets); granting incentives for scientific research and technological innovation; strengthening education and training; upgrading infrastructure; protecting the environment. A sixth priority, long- term fiscal sustainability, is addressed in a separate document. However, a wider coverage in the NRP of the approach to increasing employment rates and reducing regional employment disparities would have allowed it to present a clearer strategy covering all policy areas and the links

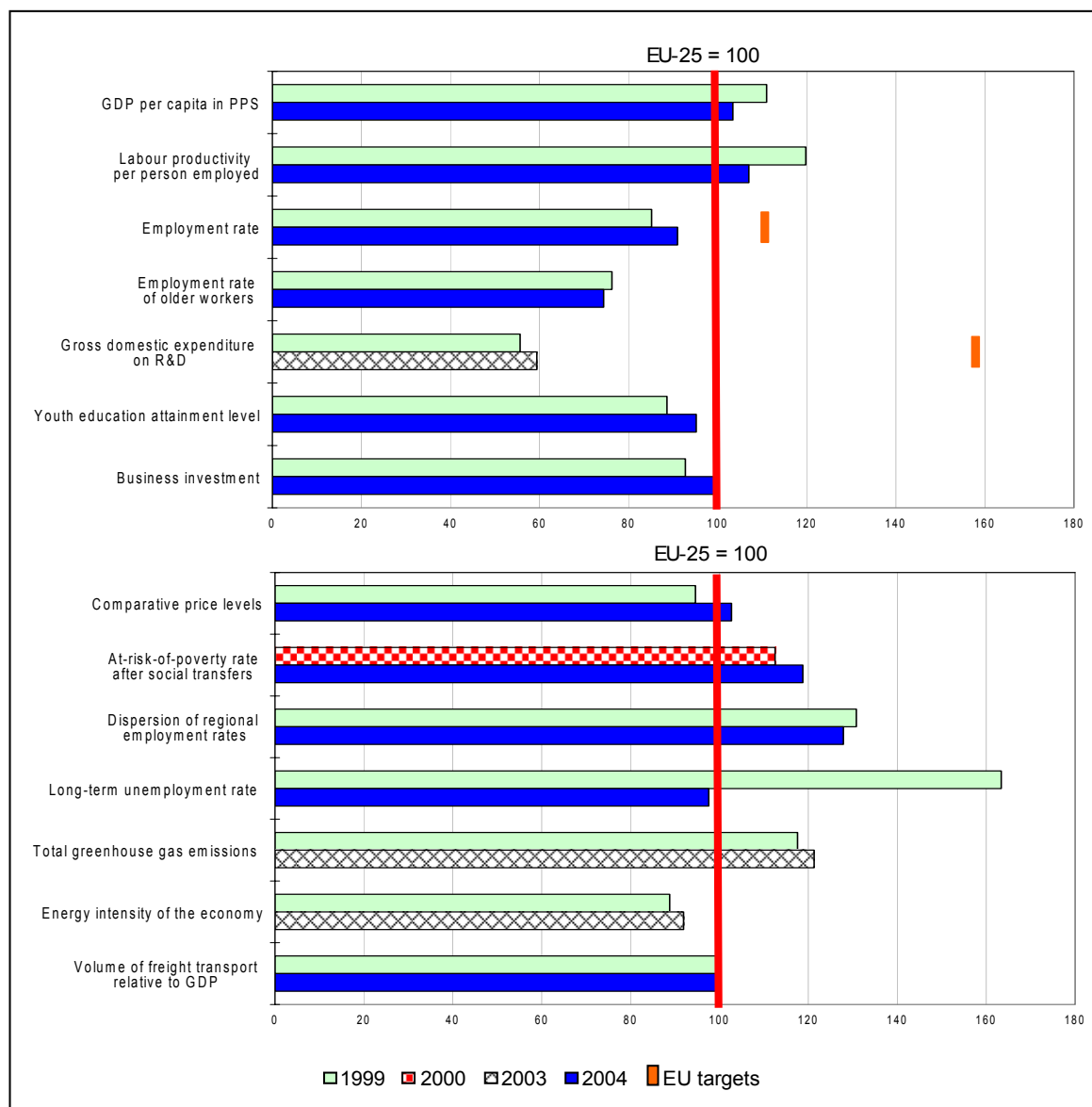
between them. Competition and regional issues are major challenges for Italy but are addressed only in a limited way in the NRP.

19. Targets, timetables and details on monitoring and evaluation procedures are often not provided in the NRP. The distribution of implementing responsibilities between different Ministries and between central government and regional and local authorities is not always clear.
20. The programme's strengths include:
  - measures to improve the regulatory environment for business, notably reducing administrative costs and reform of bankruptcy legislation;
  - certain measures aimed at improving educational performance, in particular in higher education.
21. Among the points requiring further attention are:
  - further efforts to achieve fiscal sustainability;
  - stronger and more specific measures to boost competition, particularly in network industries and services;
  - increasing labour supply and raising employment rates, including tackling regional disparities.
22. Taking due account of the above, Italy is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Italy has dealt with the issues mentioned in paragraph 21. In this context, the Commission looks forward to discussions with the Italian authorities as part of the new partnership for growth

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# ITALY

	IT							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	111.0	110.0	109.7e	107.6e	105.5f	103.4f		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	119.8	118.4	115.5	111.7	108.9	107.0		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	52.7	53.7	54.8	55.5	56.1	57.6b	:	61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	27.6	27.7	28.0	28.9	30.3	30.5b		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	1.04	1.07	1.11	1.16	1.14	:	:	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	66.3	68.8	67.0	69.1	69.9	72.9		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	94.6	94.0	95.5	97.9	102.3	102.7p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	16.6	17.4	17.3	17.9	16.6	16.9		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	18.0	18.0	19.0	:	:	19.0b		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	17.4	17.5	17.1	16.7	17.0	15.6		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	6.7	6.3	5.7	5.1	4.9	4.0		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	106.5	108.0	109.0	108.7	111.6	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	190.9	186.9	184.0	184.1	192.6	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	100.9	102.1	100.9e	102.6e	93.4e	104.4be		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	



## Latvia

1. Supported by one of the highest productivity growth rates in the EU, real GDP in Latvia has grown at an annual average rate exceeding 7% since 2000. GDP per capita rose to 43% of the EU average in 2004, still the lowest in the EU. This contrast with much slower progress in the labour market – the total employment rate (62.3% in 2004) remains 1% below the EU average and the unemployment rate has only recently fallen below 10%. Imbalances, as evidenced by high inflation and a wide external account deficit, persist.

### **PART I: GENERAL ASSESSMENT**

2. The Latvian National Reform Programme (NRP) identifies five main economic policy directions: securing macro-economic stability; stimulating knowledge and innovation; developing a favourable and attractive environment for investment and work; fostering employment; and improving education and skills. The Commission shares the NRP's analysis of the main priorities.
3. The NRP builds on a number of national programmes already in place. There is in general coherence between macro-economic, micro-economic and employment areas but the NRP envisages very ambitious reforms in many sectors. This raises doubts over whether the ambitions set out are fully realistic. The programme links each Integrated Guideline to specific measures and, where appropriate, includes the planned contribution of EU Structural Funds. Some measures are set out in detail, while others are broader lines for action. Action plans and funding commitments have been set for most guidelines. National targets are set for 2010 for employment rate (67%) and for R&D investment (1.5% of GDP).
4. Consultation and efforts to develop ownership of the document have been substantial. A clear internal governance structure has been established to ensure inter-ministerial coordination. The parliament was consulted. Regional and local government bodies will be responsible for implementing some of the proposed reforms and participated in debate during the drafting of the NRP. Social partners and other stakeholders will be involved in the implementation process where appropriate and were consulted during the drafting process, along with civil society.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macroeconomic policies**

5. The objective of macro-economic stability is to be reached by meeting four key challenges: fulfilment of the Maastricht criteria on the government budgetary position; the introduction of the euro; strengthening fiscal discipline and budgetary planning procedures; and balancing budgetary discipline with improving social conditions. The Commission subscribes to these objectives.
6. Policies for wage developments, pensions and income taxation are described in detail, but there are in many other cases no clear timelines or analysis of budgetary



implications. The NRP does not deal with savings-investments imbalances that are at root of the current account deficit or with the rapid expansion of credit that is contributing to inflationary pressures. Fiscal policy aims at maintaining a sustainable budgetary position and achieving a balanced budget position in the long rather than medium term.

7. The Commission believes that the macro-economic policy initiatives described in the NRP could contribute to the sustainable economic development of Latvia.

### **Microeconomic policies**

8. The Latvian NRP presents two micro-economic priorities: (i) stimulating knowledge and innovation and (ii) developing a favourable and attractive environment for investment and work. The Commission's analysis is in line with this.
9. The Latvian NRP demonstrates clear ambition to move towards a more knowledge-based economy by substantially increasing public investment in research and innovation. To reach the objective for public R&D spending of 1.1% of GDP by 2008, public investments will be increased by 0.15% GDP each year. Many new R&D measures are presented, though not in detail. The strategic framework seems incomplete, and specific targets for the results of the various measures are set only in certain cases. Creating conditions for increased cooperation between research institutes and businesses is an important part of the policy mix not covered comprehensively in the NRP. The main instrument to promote industrial research is the technology agency, which may need to be complemented by other tools in order to meet the ambitious goals for overall R&D spending. The programme outlines policies to improve technology transfer through technology/business incubators. A mechanism is set out for seed capital and promotion of clusters: this seems to be an effective response to the need for increased co-operation between stakeholders in the innovation system, though no details are given on the budget and scope of this measure.
10. ICTs are mentioned as an important tool to strengthen the knowledge-based economy. Measures to widen their use are focused on five areas: e-government; e-learning; development of internet access points; improvement of internet security; and the extension of broadband infrastructure to remote and rural areas. The Commission supports this choice of priorities but a more detailed implementation plan and a more precise budget allocation would be helpful in assessing the likely results. The NRP presents a general outline of a support programme for patent applications and protection. Within a context of sustainable growth, the NRP gives a high priority to the promotion of renewable energy, supported by a limited number of measures on environmental technology.
11. Regarding the business environment, implementation focuses on measures to support SMEs and includes access to finance and support for participation in international events. The NRP sets out a general outline of a limited number of new measures for the development of competitive markets. These aim to improve the functioning of the internal market by stronger market surveillance, promote the free movement of services, reform public procurement rules, widen use of e-procurement and further develop e-government. The NRP contains a comprehensive set of measures to

improve the road and railway infrastructure. However, no details are provided on energy infrastructure measures.

12. The programme covers all key micro-economic topics and proposes measures that are often well focused. Detail on implementation is not always provided. Latvia would benefit from a more integrated research and innovation strategy to absorb effectively the planned increase in public investment and to turn it into growth and jobs. Increased use of market-based instruments in both R&D and environmental policy may be needed to achieve the objectives outlined in those areas. Measures to promote entrepreneurship in education could be strengthened.

### **Employment policies**

13. The Latvian NRP broadens the overarching strategic objectives of fostering employment and improving education and skills into four key employment challenges: reducing regional disparities in employment and unemployment; reducing undeclared work; tackling the high unemployment risk for the young, persons after child-care leave and people with poor knowledge of Latvian; and matching education and skills to labour market requirements. The Commission supports this choice of priorities, which the NRP addresses mostly through continuing and refining existing policies.
14. The NRP addresses the marked regional disparities in employment mainly through supporting business start-ups, infrastructure and geographical mobility. The role of local governments and social partners, as well as the importance of local employment plans are highlighted. However, no information is provided regarding the measures envisaged to address the sharp rural-urban divide.
15. The NRP provides a comprehensive set of measures to prevent undeclared work and improve the adaptability of the labour market. The administrative capacity of the State Labour Inspectorate and the role of the social partners will be reinforced to ensure compliance with health and safety and labour legislation and to combat undeclared work. The Commission supports this choice of measures and looks forward to their effective implementation.
16. There is a wide range of measures to strengthen labour supply. Measures to attract more people to the labour market concentrate mainly on registered job-seekers and to a much smaller extent on the other inactive people who wish to work. The NRP focuses on policies covering the life-cycle approach, inclusive labour markets and meeting labour market needs. It lists comprehensive measures to prepare the young for the labour market and sets out a strategy to promote inclusive labour markets, including reinforcing active labour market policies, unemployment prevention, childcare and social services. Measures are foreseen for non-Latvian speakers and disabled people. The NRP does not place planned increases in the minimum wage in the context of possible risks to job creation for the low-skilled. Despite the increase in the tax-free threshold, the tax wedge for the low paid is still high, which contributes to an unemployment trap. Inflation is eroding efforts to make work pay. The policy objective to reduce the “at-risk-of-poverty” rate to 11% by 2008 is ambitious in these circumstances.

17. Efforts to match education and skills to labour market requirements seek to increase the attractiveness of professional education, engineering and natural sciences through modernising the establishments where these options are offered, increasing subsidised study places in engineering and natural sciences and providing access to study loans and grants. Strengthening co-operation with employers will help in designing training programmes and will improve forecasting of future needs. Although the NRP mentions early school leaving and improving access to education at all levels, few details are provided on specific action. The NRP provides very limited information on progress expected in developing and implementing a lifelong learning strategy. Further assessment of labour supply issues, including labour emigration, is important for Latvia in dealing with potential bottlenecks in its transformation to a knowledge-based society.
18. Overall, the NRP presents a comprehensive overview of the current approach to tackling labour market challenges. The lack of implementation details in some cases makes it difficult to assess the likely effectiveness of the measures. Areas seeming to require further attention are reducing inactivity, the urban-rural divide, mismatch of education and skills with labour market demand and developing a comprehensive lifelong learning strategy.

### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the Latvian National Reform Programme identifies and responds to the main economic challenges facing Latvia, namely securing macro-economic stability; stimulating knowledge and innovation; developing a favourable and attractive environment for investment and work; fostering employment; and improving education and skills. Overall, the NRP is coherent and ambitious and takes a broad approach to addressing the difficult challenges of economic transition and structural adjustment.
20. Budgetary information is included for most areas. However, details on the implementation and timing of measures, for example on disseminating ICTs, reducing urban-rural wealth disparities and on some aspects of education and training reform, are often lacking.
21. The programme's strengths include:
  - the focus on R&D and ICT and the reforms envisaged in these areas;
  - the measures aiming at improving transport infrastructure;
  - measures to promote inclusive labour markets.
22. Among the points requiring further attention are:
  - a clearer and stronger commitment to achieving macro-economic stability including by stepping up fiscal consolidation ;
  - policies to stimulate partnerships between research and education institutions and businesses;

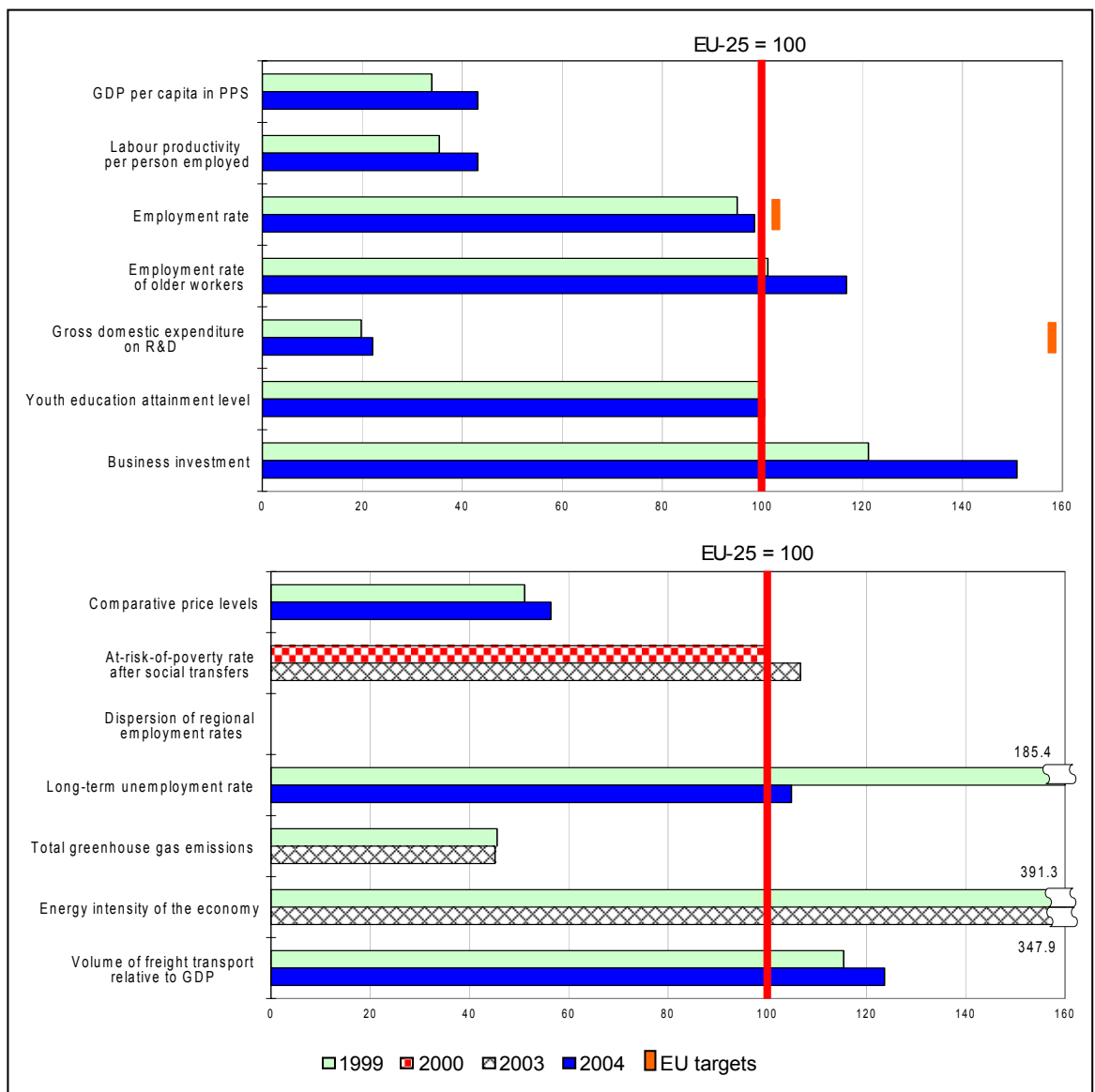
- stronger measures to adapt education and training to labour market needs and to develop and implement a coherent lifelong learning strategy.

23. Taking due account of the above, Latvia is invited to implement its NRP with vigour. The Commission 2006 progress report on the implementation of the NRP should cover in particular the way Latvia has dealt with the issues mentioned in paragraph 22. In this context, the Commission looks forward to discussions with the Latvian authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# LATVIA

	LV							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	33.9	35.1	36.9	38.4	40.5	43.1	67.0 1.5 (2008)	100.0	100.0	100.0	100.0	100.0	100.0	70.0
Labour productivity per person employed	35.4	38.0	39.2	40.0	41.2	43.1		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	58.8	57.5	58.6	60.4	61.8	62.3		61.9	62.4	62.8	62.8	62.9	63.3	
Employment rate of older workers	36.6	36.0	36.9	41.7	44.1	47.9		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	0.37	0.45	0.41	0.42	0.38	0.42		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	
Youth education attainment level	74.6	76.8	70.3	73.2b	74.0	76.9		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	51.1	57.5	58.2	57.6	55.4	56.4p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	21.7	23.2	24.0	22.8	23.2	25.5		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	:	16.0	:	16.0	16.0	:		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	-	-	-	-	-	-		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	7.6	7.9	7.2	5.7	4.3	4.3		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	41.3	39.2	42.3	41.9	41.5	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	840.9	756.0	816.5	750.3	728.8	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	116.2	120.2	120.1	122.5	133.4	129.3		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	



## Lithuania

1. Lithuania has been experiencing rapid economic growth since 1996, supported by the second highest labour productivity growth rate in the EU. Over the period 2001-2004 real GDP growth averaged 7.9%. However, GDP per capita was only 48% of the EU average in 2004. Domestic demand has accelerated rapidly in the last three years, overtaking exports as the driver of economic growth and leading to higher external account deficits. The employment rate is at 61.2%. Unemployment fell sharply from 12.7% in 2003 to 10.9% in 2004.

### **PART I: GENERAL ASSESSMENT**

2. The Lithuanian National Reform Programme (NRP) sets three key national priorities: (1) macroeconomic policies to sustain fast growth of the economy and a stable macroeconomic environment; (2) microeconomic policy to promote the competitiveness of Lithuanian companies; (3) employment policy to promote employment and investment in human capital. The Commission shares this analysis.
3. The NRP sets out an ambitious forward-looking strategy, while building on a number of national programmes already in place. Although the sections on macro-economic, micro-economic and employment policies contain cross-references, in terms of content it is not clear that they are consistent. Several targets are set for 2010 and for 2005-2008, including ambitious targets for overall employment (68.8% in 2010) and investment in R&D (2% of GDP in 2010). The presentation of measures, however, varies in the level of detail. This sometimes makes a full appreciation difficult of how measures will contribute to growth and jobs and of whether they are sufficient to respond to the challenges identified or to meet the targets set. While the preparations for the next programming period for the Structural and Cohesion Funds are described, it is not entirely clear how a coherent approach with the NRP will be achieved in practice.
4. Consultation and efforts to develop ownership were very substantial. Lithuania has established an ad-hoc inter-ministerial committee to ensure coordination and ownership of the NRP within the government. Steps were taken to involve key stakeholders. The parliament was involved in the preparation of the plan, the social and economic partners were consulted, civil society was invited to comment on the draft NRP and a conference was held in September. The NRP also attributes to the social partners a role in implementing certain measures but does not set out in detail what specific tasks or responsibilities this would involve.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. In a context of accelerating wage growth and inflation, the NRP aims to maintain high productivity growth through tax and labour market reforms, together with the promotion of R&D and innovation activities. Those activities are expected to be underpinned, to a certain extent, by foreign direct investment. The NRP also

acknowledges the importance of an efficient allocation of bank credit for macro-economic stability and highlights the need for reforms of the pension and healthcare systems to guarantee the sustainability of public finances in the long term. The Commission largely shares Lithuania's point of view on these priorities.

6. The macro-economic strategy builds on the policies implemented in previous years. Monetary and fiscal policies will aim for participation in the eurozone in 2007. The most important macro-economic measures outlined in the NRP are reforms in pension and healthcare systems, the promotion of flexible wage setting and tax reform. These will be accompanied by microeconomic and labour market reforms that should strengthen competitiveness and productivity. The programme presents some detailed measures for tax reform but very little on measures to attract foreign direct investment or in relation to financial stability. Most of the macro-economic measures are difficult to assess fully as they are presented only in general terms: further measures to increase employment rates and the retirement age would contribute to the future adequacy and sustainability of pensions.
7. Lithuania plans to meet the conditions for participation in the euro by a sustainable fiscal policy and timely legal and administrative preparations. In the short to medium term, the NRP projects a reduction in general government deficit from 2.3% of GDP in 2005 to 1.5% in 2007, which from the point of view of the Commission, is realistic. However, reducing the deficit further to 1.3% of GDP in 2008 might be considered optimistic without measures to compensate for the decrease in the personal income tax. Furthermore, the budgetary targets presented in the NRP involve a more expansionary fiscal stance which would make fiscal policy less supportive of price stability. On the other hand, the latest update of Lithuania's Convergence Programme, submitted to the Commission in December 2005, presents lower general government deficit targets. The NRP also highlights an increase in competition as a factor that should help to keep inflation down but does not set out clear measures in this respect. The Commission would be interested in learning more about plans to strengthen competition in network industries. The inflation projection of 2.1% for 2006 is considered optimistic, particularly in view of the acceleration of wage growth that is predicted in the NRP.
8. Overall, however, the macro-economic strategy presented in the NRP seems realistic provided the reforms envisaged are implemented in full.

### **Micro-economic policies**

9. The NRP identifies the promotion of competitiveness as the key priority. The Commission shares this view and would stress the importance of infrastructure, R&D and innovation policies.
10. Infrastructure remains a key problem and Lithuania devotes considerable financial resources to connecting its energy network with West European networks and modernising transport (road and rail). Here the focus is on environmentally sustainable forms of transport, for example multimodal transport systems and the creation of "rail Baltica", linking Lithuanian railways with rail networks in Western Europe. The NRP envisages activities in three areas of information and communication technologies: citizens' use of ICT, e-government and the use of ICT

in the economy. Funding efforts concentrate on broadband infrastructure, where the Structural Funds are to play an important role.

11. The government plans structural reforms to boost R&D. Investment both in public and private sectors, knowledge transfer and the reform of the education system are key points, aiming at strengthening the public science base and upgrading the innovation system. Lithuania will need to increase considerably public sector spending on research, if it wants to reach the target of 1% of GDP by 2010 (from about 0.5% in 2002), and also has a very ambitious target for private sector research investment. Substantial efforts to leverage private sector spending will be needed to achieve the ambitious overall 2% target for research investment (0.68% in 2003).
12. The NRP contains many measures to improve innovation performance. The Business Innovation Programme tries to provide a coherent national research and innovation strategy. While the development of clusters is well covered, little priority is given to efforts to increase intellectual property. Furthermore, a reliable national statistical system is not yet – despite recent efforts – fully developed in Lithuania. Such a system could be used for industrial research and innovation monitoring purposes.
13. Overall, the NRP conveys a sense of where the government sees the key priorities and how it tries to address them, though assessing policies in detail is not easy because the description of measures is not always very precise. This is also the case in a number of other important areas such as the internal market, competitive markets, better regulation, or policy on SMEs, which represent 99.3% of Lithuanian enterprises.

### **Employment Policies**

14. The key priorities are boosting employment and investing in human capital. The challenges referred to include: responding to the rapid ageing of the labour force; reducing high long-term and youth unemployment; ensuring that the labour force has the skills employers need; reducing labour market imbalances between sectors and regions; and the need to boost productivity and participation in education and lifelong learning. The Commission shares this analysis and the resulting choice of priorities.
15. Measures to attract and retain more people in employment focus on promoting a lifecycle approach to work, improving health care, strengthening labour market institutions and social partnership. Key targets are set, including an ambitious overall employment rate target (68.8% in 2010, 61.2% in 2004). To retain older workers in employment, the scope for part-retirement and increasing the pension age are to be analysed with a view to rising the pension age to 65 by 2026. Social inclusion measures have a strong emphasis on disabled people and there is a clear reference to the national action plan on social inclusion. There is a varied and appropriate policy mix on youth employment, with youth organisations involved in delivery. Whilst general healthcare is covered, health and safety at work is not, though relevant prevention measures could improve productivity. The development of the network of vocational guidance centres is a step towards better meeting employers' needs in terms of skills.



16. To improve adaptability, Lithuania intends to take a number of initiatives that the Commission considers generally appropriate. These include: the implementation of unemployment prevention programmes; the promotion of flexible forms of employment; strengthening measures against undeclared work; the promotion of labour mobility; increasing investment in training and the reduction of labour taxation. However, the description of these policies in the NRP is not very detailed and targets are not set. In particular, it is doubtful whether the policy response to the challenge of labour mobility will prove sufficient, despite its importance given existing regional disparities. The NRP envisages a reduction of the income tax rate and an increase in the minimum wage, but it is not entirely clear from the document whether there is a comprehensive overall approach to ensuring employment-friendly developments in labour costs and wage setting.
17. The NRP covers investment in human capital exhaustively, but not entirely systematically, which makes it difficult to identify the priorities. Lithuania has a lifelong learning strategy, which is mentioned along with measures to develop teachers' skills, improve learning conditions in schools, enhance vocational guidance and training curricula, develop the national system of qualifications and establish quality assessment. The low-skilled and those with special educational needs receive particular attention. Regarding higher education, strong emphasis is put on increasing efficiency by creating centres of excellence, promoting entrepreneurship and developing self-government. Important national targets are set. The target for participation in lifelong learning (10% in 2010) would, if achieved, represent a significant improvement compared with the present situation (6.5%).
18. Overall, the analysis of the employment situation is sound and the priorities chosen respond to the key challenges. Important and ambitious targets are set. However, many measures are not yet sufficiently concrete, their link to the objectives is not always apparent. More quantitative indicators would clarify their expected impact. The financial resources mentioned, when identified, mainly refer to the current Structural Funds programme.

### **PART III: CONCLUSIONS**

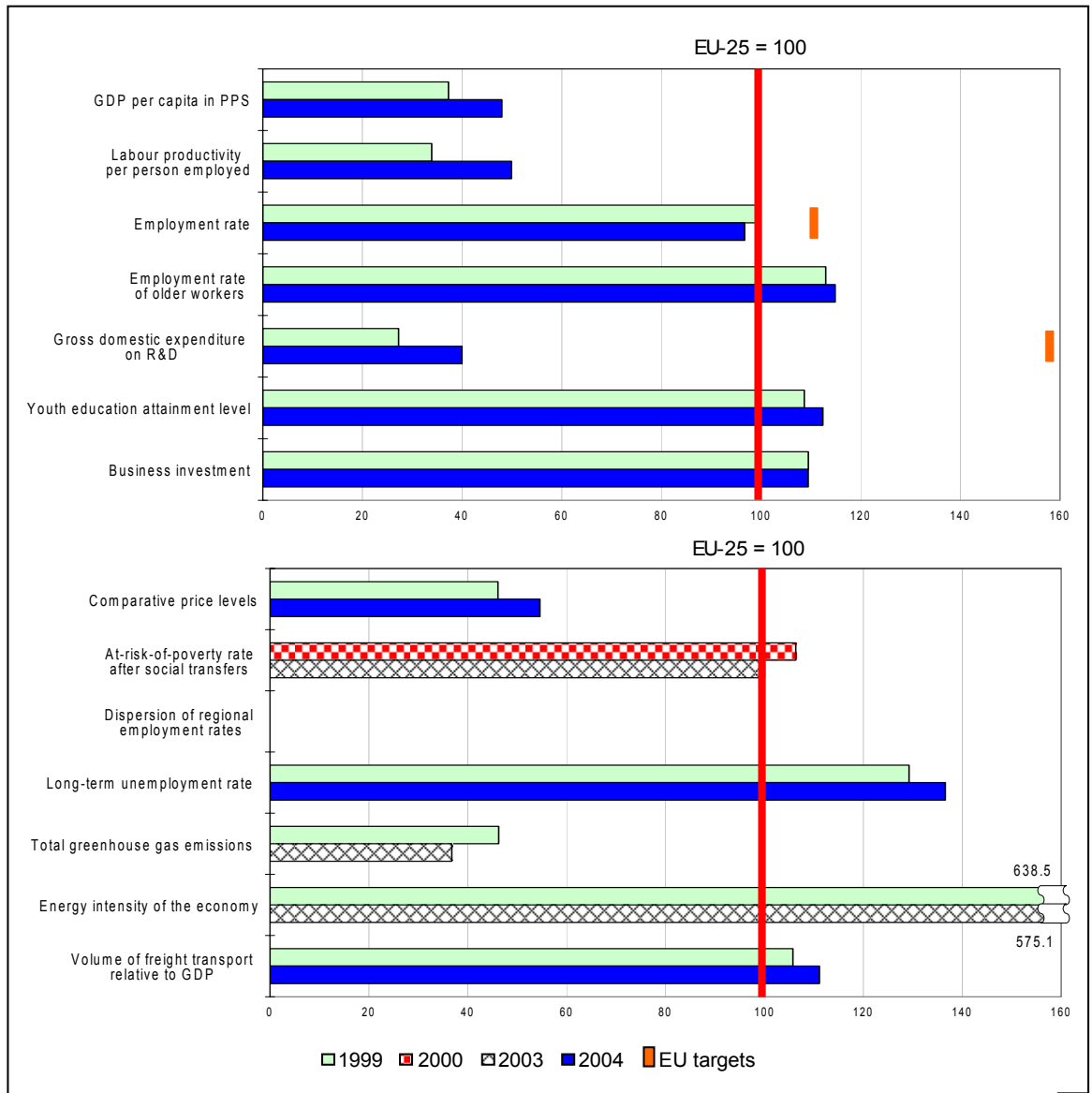
19. In line with the Integrated Guidelines, the Lithuanian National Reform Programme identifies and responds to the main challenges facing Lithuania as an economy seeking to maintain high growth in order to reach EU average levels of per capita income, namely (1) macroeconomic policies to sustain fast growth of the economy and a stable macroeconomic environment; (2) microeconomic policy to promote the competitiveness of Lithuanian companies; (3) employment policy to promote employment and investment in human capital. Overall, the NRP is ambitious and builds on existing policies. However, coherence between policy areas is not always clear.
20. Implementation will be facilitated by the Lithuanian authorities' efforts to launch a public debate about the reform agenda and to involve stakeholders, including in ensuring that structural funding is used effectively. Nevertheless, the detail given in the NRP on the content, funding, timing and monitoring of measures is in many cases insufficient to allow a complete assessment of their likely effectiveness.

21. The programme's strengths include:
- the attention and financial resources devoted to improving transport and energy infrastructure, including by better international connections;
  - the focus on raising youth employment rates;
  - the attention given to improving skills.
22. Among the points requiring further attention are:
- strengthening the science and technology base, including by increasing public sector spending on R&D to reach the ambitious target set for 2010;
  - additional efforts to strengthen innovation systems;
  - further reinforcement of active labour market policy and of the promotion of labour mobility.
23. Taking due account of the above, Lithuania is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Lithuania has dealt with the issues mentioned in paragraph 22. In this context, the Commission looks forward to discussions with the Lithuanian authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# LITHUANIA

	LT							2010 National target	EU-25						2010 EU target	
	1999	2000	2001	2002	2003	2004	1999		2000	2001	2002	2003	2004			
GDP per capita in PPS	37.3	38.3b	40.3	42.1	45.5	48.0	68.8	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	33.9	41.2b	45.1	45.1	47.4	49.9		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	61.7	59.1	57.5	59.9	61.1	61.2		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	40.9	40.4	38.9	41.6	44.7	47.1		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	0.51	0.59	0.68	0.67	0.68	0.76		2.0	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	81.3	77.9b	81.2	79.3b	82.1	86.1			74.8	76.3	76.1	76.5	76.5		76.6	
Comparative price levels	46.1	51.6	53.0	54.6	54.9	54.6p		100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	19.6	16.3	17.9	17.4	18.2	18.5		17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	:	17.0	17.0	17.0	15.0	:		:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	-	-	-	-	-	-		13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	5.3	8.0	9.2	7.2	6.1	5.6		4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	41.9	40.9	40.0	38.5	33.8	:		90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	1372.2	1208.4	1256.8	1272.7	1204.8	:		214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	106.5	109.7	98.2	117.6	119.1	116.2		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e			



## Luxembourg

1. Growth of Luxembourg's GDP in 2004 was only half that of 2000, but remains strong at 4.5%. During this period, there was a considerable slowdown in productivity growth. GDP per capita was 227% of the EU average in 2004. The employment rate (61.6% in 2004) remains slightly below the EU average, while the unemployment rate is at an historic high (4.8% in 2004, 2.7 points up on 2001) and a form of structural unemployment seems to be emerging. A characteristic feature of Luxembourg is that a very large part of the working population consists of frontier workers, who represent 40% of jobs filled and more than two thirds of new jobs.

### **PART I: GENERAL ASSESSMENT**

2. Luxembourg's national reform programme (NRP) adopts a strategy resting on the twin pillars of full employment and innovation, while emphasising the need to maintain the existing social model. The programme identifies five priorities for action: a high-quality education and training system, an economy integrated into the European and international context, an attractive economic environment, a stable macro-economic framework and adherence to the principles of sustainable development. The Commission agrees with these priorities. However, certain important issues, such as that of older workers, might have been given greater prominence.
3. The NRP represents a relevant approach, at least in principle, to the policies needed to meet these challenges. However, it does not provide a basis for assessing exactly what impact some measures will have, since it does not specify how they are going to be put into effect. To a large extent, the measures described are at the planning stage or are expressions of intent on the part of the government. The programme sets an R&D investment target (3% of GDP in 2010) but fails to lay down quantified targets for employment or provide a timetable for putting the main measures into practice. There is only brief mention of the link between the strategy formulated and the contribution of the European structural funds.
4. Significant steps have been taken to place consultation procedures on a firm footing and ensure ownership of the document. Production of the NRP was coordinated by the Minister for Economic Affairs and Foreign Trade on behalf of the government. An ad hoc committee was formed, with representation from the main ministries concerned. The competitiveness monitoring unit attached to the Ministry of Economic Affairs assists the "Lisbon coordinator" in his work. There was extensive consultation on the programme between the government, Parliament and the social partners. The latter will be directly involved in its implementation.

### **PART II – ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. The NRP identifies two main macro-economic issues: economic stability, to be achieved by reducing the public-sector deficit, and longer-term economic and

budgetary sustainability, which is linked to the social and financial viability of the social security system. The Commission agrees.

6. In 2004, Luxembourg for the first time ran a budget deficit, amounting to -2.3% of GDP in 2005. The NRP thus emphasises the government's commitment, reflected in the 2006 budget, to reducing the government deficit to -1.8% in 2006. The NRP states that this effort will continue in 2007 and 2008, without indicating how this will be done. It also stresses that consolidation measures of a more structural nature will be required in the longer term.
7. As regards the second issue, the NRP confirms the government's intention to continue adapting the social security system to the needs of the population while ensuring sustainability of the existing social model. It reviews the main steps recently taken to this end, but does not contain any new measures.
8. Apart from the objectives and action announced in the 2006 budget, the NRP thus does not put forward any new detailed measures to address the two issues identified in the macro-economic field.

### **Micro-economic policies**

9. The programme identifies three main micro-economic issues: innovation, the economic environment and sustainable development. The Commission agrees that this choice is a good reflection of the country's needs.
10. Research and innovation are presented as essential priorities of the programme, a major aim being diversification and reorientation of the economy towards leading-edge sectors. The stated goal is for R&D investment to reach 3% of GDP in 2010. This is ambitious, given that the current level is 1.8% of GDP and the public sector's share of research is among the lowest in the EU. Much will depend on the ability to boost the public resources devoted to research and innovation while ensuring an increase in the level of private investment. Achieving this goal will also require a special effort in terms of the institutional capacity to monitor and assess programmes. The NRP provides for greater support for human resources development in these areas and emphasises the development of innovative clusters and support for innovating businesses. These measures are tending in the right direction. However, more specific measures seem to be needed in several areas, such as patents and access to finance.
11. In order to improve the economic environment, the programme emphasises the creation of specialised clusters of excellence geared to particular sectors. It also mentions action to improve high-capacity network supply. It emphasises the need to create a better regulatory and administrative context by simplifying procedures and developing e-government. Specific measures for SMEs are also planned, e.g. to promote entrepreneurship among young people and to improve the bankruptcy laws. Luxembourg should also speed up implementation of internal market directives in the areas of finance, energy and the liberal professions.
12. In pursuit of sustainable development, the programme stresses that the environment and competitiveness are complementary concerns. There are many measures focused on improving the energy efficiency of the various economic sectors and on the use of

renewable energy sources. Targeted subsidies and more consistent use of “green” public contracts are planned in order to achieve this. There are also plans for sustainable transport infrastructure better able to cope with the cross-border commuter traffic. On the other hand, the proposed measures with regard to climate change and environmental taxes seem to lack detail. All that is planned at present is research into taxes.

13. Overall, the micro-economic priorities set out in the NRP are along the right lines. However, the measures described often lack precision and this programme thus affords no assurance that they will be put into practice.

### **Employment policies**

14. The NRP spotlights the need for economic redeployment and better anticipation and management of economic restructuring and identifies two main employment issues: ensuring greater labour market participation by residents and improving the take-up and quality of the education and training systems. The Commission agrees.
15. There is strong job creation in Luxembourg, many of the new jobs being taken by frontier workers. In order to encourage more residents to participate in the labour market, the programme puts forward a fairly balanced set of measures. The NRP first aims to improve the effectiveness of the guidance, information and monitoring services and of active labour market policy by modernising the employment service and tackling job-seekers’ cases more quickly. It also emphasises promoting a “culture” of forward management of employment to reduce inactivity and forestall withdrawals from the labour market. All stakeholders are urged to contribute and the government proposes to set up a scoreboard, partly based on the Lisbon indicators. Finally, the NRP seeks to allow better reconciliation of work and private life through better physical, legal and financial security at work — including better risk prevention, reform of the labour inspectorate, equal pay and combating of stress and harassment — or by adapting social security systems to improve the incentives for returning to work or continuing in it. However, these measures as a whole remain somewhat unspecific and certain important themes are not given enough prominence: these include older workers, handicapped workers and social exclusion.
16. As regards improving the take-up and quality of the education and training systems, the NRP offers a limited response. Some important features of the previous national action plans for employment, such as the overall training strategy and the draft schools legislation, are not mentioned in the NRP. In addition, fairly cursory attention is paid to important subjects such as school drop-out prevention or integration of immigrant children. However, the NRP does include new and welcome departures such as greater training opportunities for young people, with the development of holiday jobs and voluntary service; creation of a quality assurance mechanism for the education and training systems; the development of arrangements for validating formal or non-formal competences.
17. In order to make the Luxembourg economy more adaptable, the NRP stresses the ability to anticipate economic restructuring and the promotion of new forms of employment such as part-time work, teleworking, home working and working time accounts. It also stresses the need to ensure that pay is linked to productivity gains, maintaining, and if necessary adapting, the current arrangements for index-linked

pay. In this connection, the NRP expresses a concern to ensure that private and public players shoulder their responsibilities, while maintaining a balance between modernisation and safeguarding of the national social model.

18. Overall, the NRP provides a appropriate response to the two issues it identifies, underlining the need to make work more attractive, improve the effectiveness of active labour market policy, develop better forward management of employment and make greater efforts to promote the accreditation of skills. However, the measures described are often lacking in detail, while continuity with the previous national action plans for employment and social inclusion is not clearly established.

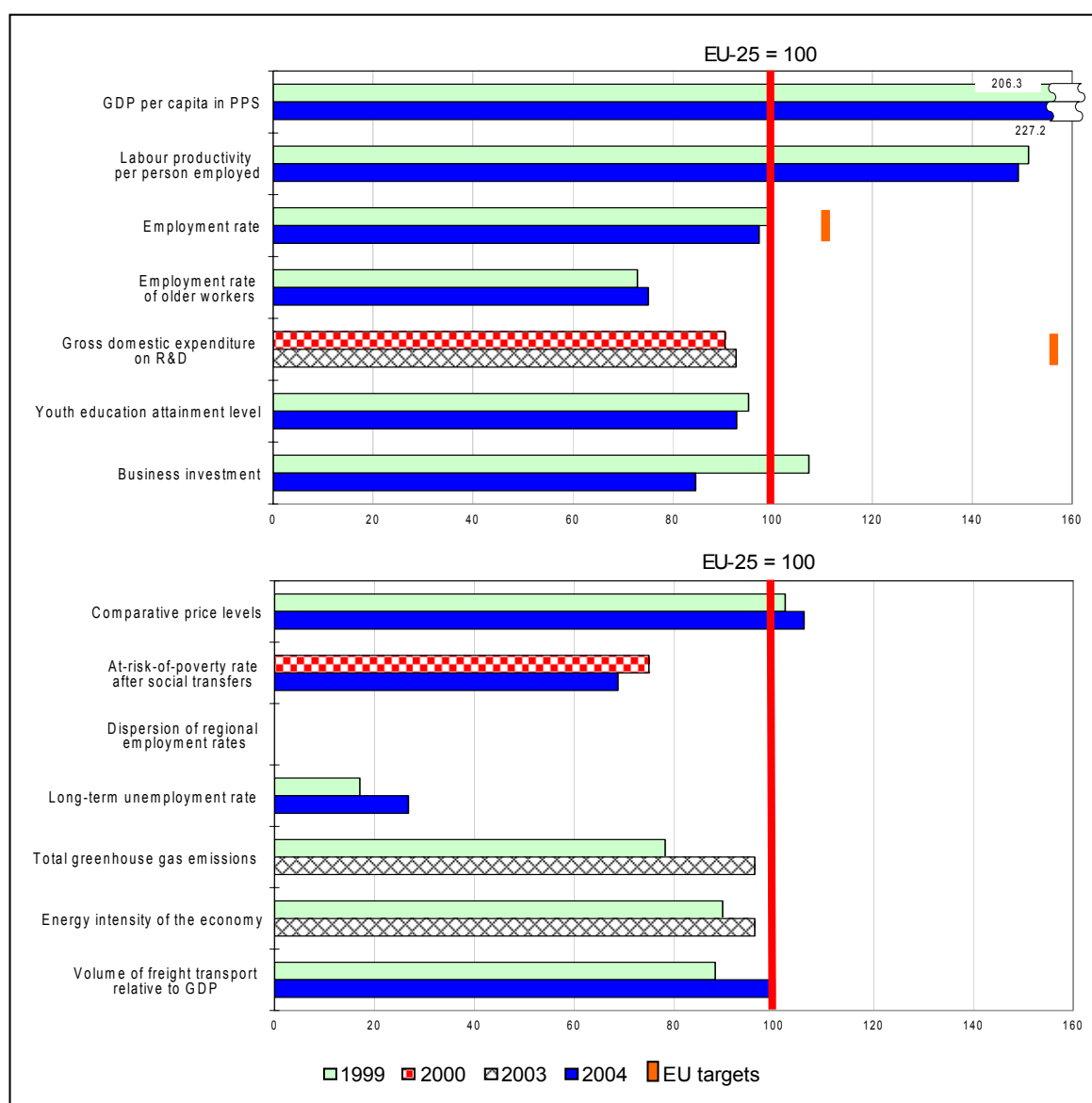
### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the Luxembourg National Reform Programme identifies and responds to the main challenges facing Luxembourg, namely a high-quality education and training system, an economy integrated into the European and international context, an attractive economic environment, a stable macro-economic framework and adherence to the principles of sustainable development. Overall, the programme is coherent, but the present lack of clear objectives, timetables and indicators makes it difficult to assess how effective it is likely to be.
20. The planned involvement of the social partners and other major stakeholders in implementing the NRP could make it easier to put the proposed reforms into practice.
21. The programme's strengths include:
  - the attention paid to specialised technological clusters;
  - the measures relating to complementarity of the environment and competitiveness, in particular as regards energy efficiency;
  - the initiatives on forward management of employment, active labour market policy for jobseekers and certification of skills.
22. Among the points requiring further attention are:
  - implementation of the ambitious research and innovation objectives;
  - in the field of employment, the need to address the position of older and handicapped workers.
23. Taking due account of the above, Luxembourg is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Luxembourg has dealt with the issues mentioned in paragraph 22. In this context, the Commission looks forward to discussions with the Luxembourg authorities as part of the new partnership for growth and jobs.

### **PART IV : STATISTICAL GRAPHS AND DATA**

# LUXEMBOURG

	LU							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	206.3	216.2	210.3	210.0	219.1	227.2f	3.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0
Labour productivity per person employed	151.3	154.4	144.6	141.8	146.2	149.2		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	61.7	62.7	63.1	63.4	62.7	61.6		61.9	62.4	62.8	62.8	62.9	63.3	
Employment rate of older workers	26.4	26.7	25.6	28.1	30.0	30.8		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	:	1.71	:	:	1.78	:		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	
Youth education attainment level	71.2	77.5	68.0	69.8	71.0	71.1		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	102.3	100.9	102.9	102.5	105.3	106.1p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	19.2	16.9	18.4	16.8	14.9	14.3		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	13.0	12.0	12.0	:	10.0b	11.0		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	-	-	-	-	-	-		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	0.7	0.6	0.6	0.8	0.9	1.1		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	70.9	74.7	76.9	84.9	88.5	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	192.9	186.6	190.7	196.7	201.5	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	88.9	96.5	106.4	107.3	109.0	104.8		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	





## Malta

1. After strong expansion at an annual average of 5% during 1994-2000, the Maltese economy practically stopped growing over 2001-2004, reflecting intensive industrial restructuring and deteriorating international competitiveness. Labour productivity growth has been well below EU average during the same period. GDP per capita has grown less than in the rest of the EU during that period and stood at 69% of the EU average in 2004. Malta's employment rate is only 54%, despite significant potential gains that could be achieved from the development of human capital. The unemployment rate was 7.6% in 2004.

### PART I: GENERAL ASSESSMENT

2. The Maltese National Reform Programme (NRP) identifies five broad themes as key challenges: sustainability of public finances; competitiveness; the environment; employment; and education and training. The Commission broadly shares the NRP's analysis of the main priorities, though it would tend to place more emphasis on competition issues, addressed in the NRP as one of several areas under the key challenge of competitiveness.
3. The programme presents the individual challenges comprehensively and bases future strategy and the large number of new measures on an analysis of the current situation. It is well structured with a clear timeframe and budgetary implications for most measures. However, an overall strategic vision integrated across all policy areas and justifying and linking the choice of themes, priorities, objectives and measures is present only to a limited extent. The NRP specifies an ambitious employment target of 57 percent by 2010, but does not set an overall target for R&D expenditure. The policy objectives presented are appropriately ambitious, though the reform measures outlined may not be fully sufficient to deliver them. Synergies among the measures are not clearly identified, which may raise difficulties in implementation. The coherence of measures across policy areas is not systematically addressed. The NRP states that priorities for the use of Structural Funds are currently being prepared in a separate document.
4. Consultation and efforts to develop ownership of the document have been very substantial. The programme was produced by a coordination team in the Office of the Prime Minister, which will also plan and monitor implementation, and approved by the Cabinet. The final programme was presented to the parliament after a wide consultation process including a launch conference and a public consultation document. There were meetings with social partners and the government intends to pursue the dialogue with them and with other stakeholders during the implementation phase.

### PART II: ASSESSMENT BY POLICY AREA

#### Macro-economic policies

5. Fiscal sustainability through reducing public sector expenditure on the one hand and measures to foster economic growth on the other is the key challenge referred to in the macro-economic part of the programme. Priorities to address it include ensuring the sustainability of pension and healthcare systems and reviewing the tax framework. The Commission subscribes to this general approach.
6. The policy objectives and targets set out are coherent with previous government commitments. Reaching them would mean good progress towards addressing the fiscal sustainability challenge successfully. The strategy to limit the role of the government in the economy and to stimulate private sector activity is appropriate for Malta. However, the prioritisation between the various sets of measures is not sufficiently clear and they do not seem fully integrated. Potential synergies between them may be missed as a consequence. Furthermore, budgetary implications of the macro-economic measures are not spelled out. In some cases, such as the tax and pension reforms, the absence of a clear time schedule raises questions about the effectiveness of the overall macro-economic strategy.
7. The policy objectives and measures are relevant and would seem to constitute a strong response to the macro-economic key challenge if fully implemented. But as no information is provided on timelines and budgetary impact of several important measures a full assessment of the reform package in the macro-economic area is difficult.

#### **Micro-economic policies**

8. Competitiveness and environment are identified as priority themes in the programme. The competitiveness challenge comprises the sub-categories of enterprise, tourism, and infrastructure. These priorities are appropriate for enhancing the growth potential of the Maltese economy, although a stronger focus on competition issues would be justified.
9. As response to the competitiveness challenge, enterprise policy adopts a strong sectoral focus and many of the planned measures aim at strengthening specific areas of economic activity. The issue of building closer links between sectors with strong Foreign Direct Investment and the rest of the economy is not taken up in the NRP. While the programme acknowledges current heavy administrative costs for businesses, it is not clear whether measures in the NRP to increase the efficiency of public administration will respond adequately to that problem, though the proposed creation of a Better Regulation Unit is a useful step, in particular if one of its roles is to perform systematic impact assessments of new regulations. The limited measures to enhance competition include the opening of the electricity market and the privatisation of yacht marinas.
10. Research and innovation policy has a low profile in the NRP. While a target for public R&D investment of 0.2 percent of GDP is presented for 2007, the NRP does not include an integrated R&D strategy aiming at an overall R&D target for 2010. Although the need for a strategy on innovation is recognised, the schedule and process for developing one is not clearly set out. The programme highlights the objective of furthering the use of ICT but adds little detail. In view of these

weaknesses, the effort on R&D and innovation may not be sufficient to make a substantial contribution to business competitiveness.

11. Malta has placed the environment high on its reform agenda. Almost two-thirds of the funding envisaged in the NRP is allocated to a detailed action plan of environmental measures. The substantial attention paid to this issue is particularly appropriate for Malta, in its own right and also given the importance of tourism for the economy. However, the link between environmental policies and competitiveness is not presented in the programme. Regarding infrastructure, the potential role of transnational cooperation in reducing the problems arising from Malta's peripheral position is considered mainly through the use of sea ways.
12. The proposed objectives and measures are largely relevant in the light of the challenges and priorities identified. An overall strategic approach that integrates policy objectives and measures across themes is, however, not spelled out. In a few cases, primarily in areas dealt with under the competitiveness challenge, the proposed measures may be insufficient to achieve the policy objectives.

### **Employment policies**

13. The employment level and education and training are identified in the NRP as key challenges. The programme stresses that an effective response is crucial for economic growth and the sustainability of public finances. The priorities identified for employment policies are appropriate in view of the labour market situation in Malta.
14. Reforms set out in the NRP seek to attract and retain more people in employment and to expand labour supply, mainly by increasing employment rates for women and older workers, which are particularly low at 33.7% and 32.6 % respectively. The proposed measures target these groups and, by changing the impact of the current tax and benefits systems, aim at setting the appropriate incentives to increase participation. Making unemployment benefits conditional on participation in a mixture of training and community service is an important step in that direction and should also help increase the mobility of labour. While the approach is generally sound, reviewing comprehensively the incentives resulting from the tax and benefit system is still not a sufficiently high priority, given the Maltese labour market situation. The NRP expresses the Maltese authorities' intention to closely involve the social partners during the implementation process and this should increase the effectiveness of the strategy.
15. Meeting the challenge of improving education and training, and generally increasing investment in human capital is seen as a crucial priority in the programme. The policies set out in the NRP in this field are appropriate and focus on raising general educational levels, reducing the number of school drop-outs and higher participation in training and lifelong learning, in particular for the low-skilled. The measures envisaged to achieve these aims build on the implementation of reforms already initiated in the compulsory education system. They are complemented by a coherent set of new measures aiming at ensuring the quality and comprehensive provision of education. These include formally involving the relevant stakeholders in monitoring the match between the demand for skills on the labour market and the supply. The

initiative to provide for the certification of all forms of competencies achieved through learning, including training in basic computer skills and teacher training, can help make the labour market more efficient.

16. The NRP complements in a number of ways efforts to improve the adaptability of workers and enterprises. It sets out plans to provide employees with support to help them cope with changes in employment conditions. It also includes initiatives to manage economic migration and to enhance generally the capacity of individuals - and therefore of the economy - to absorb the impact of economic restructuring. The measures proposed to help make employment practices more flexible, such as lower tax rates for part-time work and tele-working, are appropriate to improve labour mobility. Nevertheless, reducing administrative costs and the tax burden on labour are not directly addressed.
17. The objectives and measures set out are coherent and sufficient to achieve progress towards addressing the key challenges. A fully comprehensive review of the incentives provided in the labour market by the tax and benefits system could be valuable in ensuring that the effectiveness of the overall employment strategy is maximised.

### **PART III: CONCLUSIONS**

18. In line with the Integrated Guidelines, the Maltese National Reform Programme identifies and responds to the main challenges facing Malta, namely sustainability of public finances; competitiveness; the environment; employment; and education and training. Overall, the NRP is clear and based on a good analysis of the current situation, with ambitious objectives and concrete measures. However, those measures do not in all cases appear sufficient to achieve the objectives, prioritisation is limited and integration and coherence across policy areas is not always evident.
19. The programme contains clear information on budgets and time schedules for measures in the micro-economic and employment fields, though this is not the case for the macro-economic section. Implementation will be facilitated by the clear and inclusive governance structure and the continuity envisaged.
20. The programme's strengths include:
  - the emphasis on improving human capital by raising educational levels and participation in training and lifelong learning;
  - the emphasis given to environmental sustainability.
21. Among the points requiring further attention are:
  - strengthening competition and improving the quality of the regulatory system;
  - reducing the tax burden on labour and making work more attractive through a comprehensive review of the tax and benefit system.
22. Taking due account of the above, Malta is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in

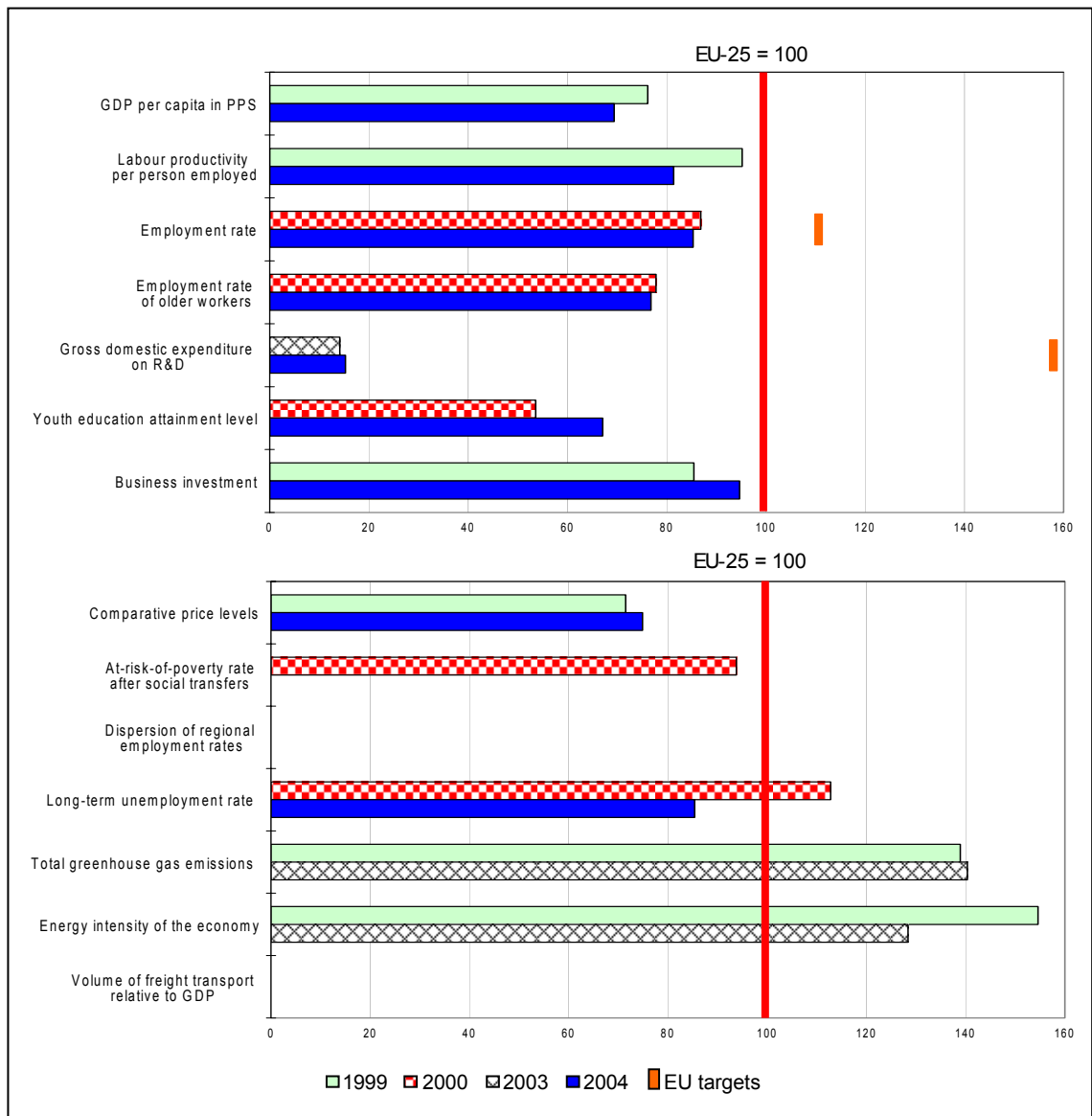
particular the way Malta has dealt with the issues mentioned in paragraph 21. In this context, the Commission looks forward to discussions with the Maltese authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# MALTA

	MT							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	76.2	76.3	72.7	72.6	71.7	69.4		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	95.2	87.9	83.5	84.7	84.6	81.4		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	:	54.2	54.3	54.4	54.2	54.0	57.0	61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	:	28.5	29.4	30.1	32.5	31.5		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	:	:	:	0.28	0.27	0.29	*	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	:	40.9	40.1	39.0	43.0	51.4		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	71.5	74.8	75.5	73.7	74.4	74.9p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	15.3	18.1	15.8	11.0	14.3	16.0		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	:	15.0	:	:	:	:		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	-	-	-	-	-	-		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	:	4.4	3.7	3.4	3.3	3.5		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	125.9	129.0	124.4	129.7	129.1	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	332.3	303.2	266.6	263.9	269.0	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	:	:	:	:	:	:		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	

\* National target: 0.2% (2010) for the public sector



## the Netherlands

1. Real GDP growth was booming in the Netherlands in 1996-2000, averaging 3.7% annually. Labour productivity growth, however, was close to the EU average. Economic growth in the Netherlands came to a near standstill in 2002 and only recovered somewhat in 2004, to 1.7%. GDP per capita at 125% of the EU average in 2004 was one of the highest in Europe. The overall employment rate declined slightly to 73.1 % in 2004, while continuing to exceed the Lisbon target. Unemployment rose to 4.6%. The share of part-time employment in the overall employment rate is very high.

### PART I: GENERAL ASSESSMENT

2. The Dutch National Reform Programme (NRP) places particular emphasis on improving labour supply. The other key challenges it identifies are: achieving faster growth in labour productivity, in particular by strengthening R&D, innovation and education; and improving price competitiveness, in particular by containing labour costs. The Commission shares the NRP's analysis of the main priorities.
3. The National Reform Programme is clear. There is coherence between the macro-economic, micro-economic and employment policy chapters. The policies presented build on a number of key reforms already in progress or announced. Quantitative targets have been adopted for many guidelines, although these are sometimes less ambitious than previous policy goals. The ambitious target for private sector investment in R&D is expressed relative to other EU Member States rather than in quantitative terms and there is no target set for R&D overall or for employment rate. The Programme refers to recently approved funding of € 2.3 billion for knowledge, innovation, education, mobility and environmental projects, but only for the latter does the NRP provide detailed funding information for specific initiatives, though the Dutch authorities have also recently submitted limited additional information on the specific funding for innovation and education. The National Reform Programme also sets out the intention to concentrate any 2007-13 EU structural funding on innovation, knowledge and human capital.
4. Consultation and efforts to develop ownership of the document have been substantial. The Secretary-General of the Ministry of Economic Affairs, as Chairman of the Central Economic Committee, took overall responsibility for drafting the programme, which was approved by the Dutch Council of Ministers. Social partners were consulted and a partial consensus reached. Their own contribution to the Strategy for Growth and Jobs is in a separate document<sup>4</sup>. Regional and local government bodies will be responsible for implementing some of the proposed reforms and were involved in the drafting through standing consultation bodies. The NRP was discussed in parliament.

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<sup>4</sup> [http://www.stvda.nl/uploads/nota\\_20050900\\_engels.pdf](http://www.stvda.nl/uploads/nota_20050900_engels.pdf)

## **PART II: ASSESSMENT BY POLICY AREA**

### **Macro-economic policies**

5. The NRP refers to objectives in four broad macro-economic policy areas: promoting economic stability; maintaining a sustainable budgetary position; improving coherence between macroeconomic, structural, and employment policies; and ensuring employment-friendly wage developments. The Commission subscribes to these objectives.
6. The NRP does not set out new macro-economic measures but refers to a number of policies that have been or are being implemented. The most important are efforts to curb the budget deficit (from 3.2% in 2003 to a projected 1.8% in 2005), a new surveillance scheme for pension funds and the introduction of new health insurance and disability schemes by 2006. Together with recent moderation in wages in sectors where pay levels are agreed collectively by the social partners, these measures are expected to contribute to the recovery of growth and employment expected in 2006. The NRP refers to the fact that open economies such as the Netherlands are very sensitive to external factors. When the performance of its main trading partners and activity in the EU as a whole recovers, positive effects of recent reforms should be reinforced. However, global developments, particularly higher oil prices, may act as a brake.
7. The policies outlined in the Dutch NRP appear sufficient to improve the macro-economic situation.

### **Micro-economic policies**

8. Improving labour productivity growth by boosting innovation and R&D is one of the key challenges addressed in the Dutch NRP. There is a range of measures to improve the business climate, but strengthening competition could have been addressed more comprehensively.
9. The Programme contains a set of policies for stimulating R&D and innovation, including tax incentives, changes to curricula, funding reforms in the university system, innovation contracts with companies and a scheme for innovation vouchers for SMEs. It notes the need for better use of investment in industrial research. The NRP states that €660 million have been allocated so far to stimulate R&D and innovation. Further funds are also expected and the assumption is that improving competition and the general climate for investment will also contribute to reaching R&D and innovation objectives. The NRP acknowledges the need for more highly qualified researchers and to strengthen cooperation between universities and businesses but does not set out an overall strategy or a clear timetable.
10. The target of privately-financed R&D expenditure matching the EU average as a proportion of GDP in 2007 and being in the EU top five in 2010 is ambitious. Given that private R&D intensity in the Netherlands declined over the 1997-2003 period to 0.99 %, it is likely that achieving it would require a doubling of expenditure by 2010. The Dutch NRP does not set an explicit target for public or total R&D expenditure,



although it indicates that private sector expenditure should be at the level of the five best performing Member States.

11. The programme seeks to boost innovation by building up critical mass in key areas. Sector-specific policies and incentives for the development of clusters and “innovation poles” are set out. Synergies with international clusters are not specifically mentioned in the NRP. Measures are proposed to improve diffusion of new technology among SMEs and through public procurement and to address ICT priorities such as e-government, improved use of the internet and the EU’s i2010 strategy on focusing ICT developments on contributing to growth and jobs. There is limited information on implementation in the NRP itself.
12. There are new initiatives to improve the business and investment climate, complementing ambitious policies in place. Special loans for enterprises to participate in European aircraft and space industries and in shipbuilding are proposed. The NRP also contains promising measures to complete and strengthen the Internal Market, including targets for implementing EU Directives, with mechanisms to achieve them. There is a commitment to stop adding additional national provisions when Directives are written into national law. Financial market supervision will be streamlined. Competition will be stimulated by new legislation on public procurement and by enhancing supervisory powers.
13. Specific measures are set out to improve the regulatory environment by improving licensing and continuing good progress towards the target of reducing regulatory costs for businesses by 25% between 2002 and 2007. SME-friendly policies include facilitating start-ups and improving access to credit and tax reductions. Measures to improve infrastructure are relatively limited, do not address in detail high quality cross-border transport links such as high-speed rail and concentrate on relieving domestic bottlenecks, though cooperation with Belgium and France in energy transport is referred to. There will be new investment (€700 m) in environmental projects, including improving air quality. The NRP contains quantitative targets for emissions and sustainability but no time plan for realisation. Measures focus on the promotion of environmental technologies.
14. The Commission’s assessment of the micro-economic chapter is generally positive. New policies on the business environment and on better regulation appear likely to build further on a successful track record. The measures to stimulate R&D and innovation are sensible but may be insufficient to achieve the target – top five in the EU by 2010 – set for private R&D investment, or to improve total R&D intensity to the extent needed. Timetables for implementing measures are not always given in the NRP.

## **Employment**

15. The Dutch programme identifies labour supply as a principal employment challenge both in terms of integrating those outside the labour market and increasing the relatively low average number of hours worked, in particular by those currently working part-time. Enhancing productivity growth through investment in human capital, as well as moderate wage development, are also identified as priorities.

16. There are significant measures to increase financial incentives to work for recipients of social and disability benefits, older workers and the unemployed, including from 2006 new disability and unemployment benefit schemes with tightened eligibility requirements. The duration of unemployment benefit will be reduced from five years to three years and two months. The national interim target for older workers (40 % working at least 12 hours weekly by 2007) is reiterated in the NRP and there are continued efforts to raise the effective exit age from the labour market. For example, tax advantages will no longer be offered for schemes providing pre-pensions before the age of 65. The intention stated in the NRP of combining making work financially attractive with proactive policies to help people to find jobs is appropriate. But successful delivery will depend on the agencies and municipalities which implement active labour market policies offering effective job search support and on the establishment of monitoring mechanisms. For example, currently only 37% of adult unemployed people are offered a new start (training, etc) during the first year of unemployment. So far, municipalities have tended to focus on those benefit recipients easiest to help back into the labour market, leading to a slight decline in the number of benefit recipients. However, the sustainability of this reintegration effort is yet to be determined.
17. Policies to increase the employment of women, despite the presence of a national target (65% working at least 12 hours weekly by 2010), are rather limited, centering on tax reforms, improving the supply of affordable child care and better reconciliation of work and private life. These may not be sufficient to stimulate a widespread transition from part-time to full-time work as they do not fully tackle the marginal tax burden on the second income or the gender pay gap. No overall employment rate target has been set for 2008 or 2010, although the NRP reiterates the government's commitment to helping achieve the 70% overall target for the EU. Neither does it mention the existing national target for youth (not more than double the overall unemployment rate), though there is an integrated approach to support for disadvantaged young people. The programme acknowledges that the employment rate target for ethnic minorities of 54% will not be attained in 2005, but addresses this issue only to a limited extent.
18. To increase the adaptability of workers and enterprises, wage moderation in line with the "Tripartite Autumn Agreement" between the social partners and the government will be complemented by changes in employment protection legislation. The greater responsibility given to the social partners on health and safety at work and risk prevention should help improve quality at work and productivity. To improve human capital, the Dutch NRP concentrates on reducing early school leaving to 8% by 2010, raising the educational attainment of 22-year-olds, and creating better links between education and the labour market. However, the NRP acknowledges that national targets are ambitious and difficult to reach, despite substantially increased efforts. Initiatives by the Dutch authorities and the social partners appear to have good potential for building on the already relatively high adult participation in lifelong learning.
19. The employment policies in the NRP are extensive, coherent and reflect the government's determination to increase labour supply. Successful implementation will depend on strong cooperation between government, implementing agencies, municipalities and social partners and on effective monitoring. Appropriate assistance to reintegrate people in the job market will be needed, as well as a stronger

focus on vulnerable groups such as recipients of social and disability benefits, long-term and low-skilled unemployed and ethnic minorities.

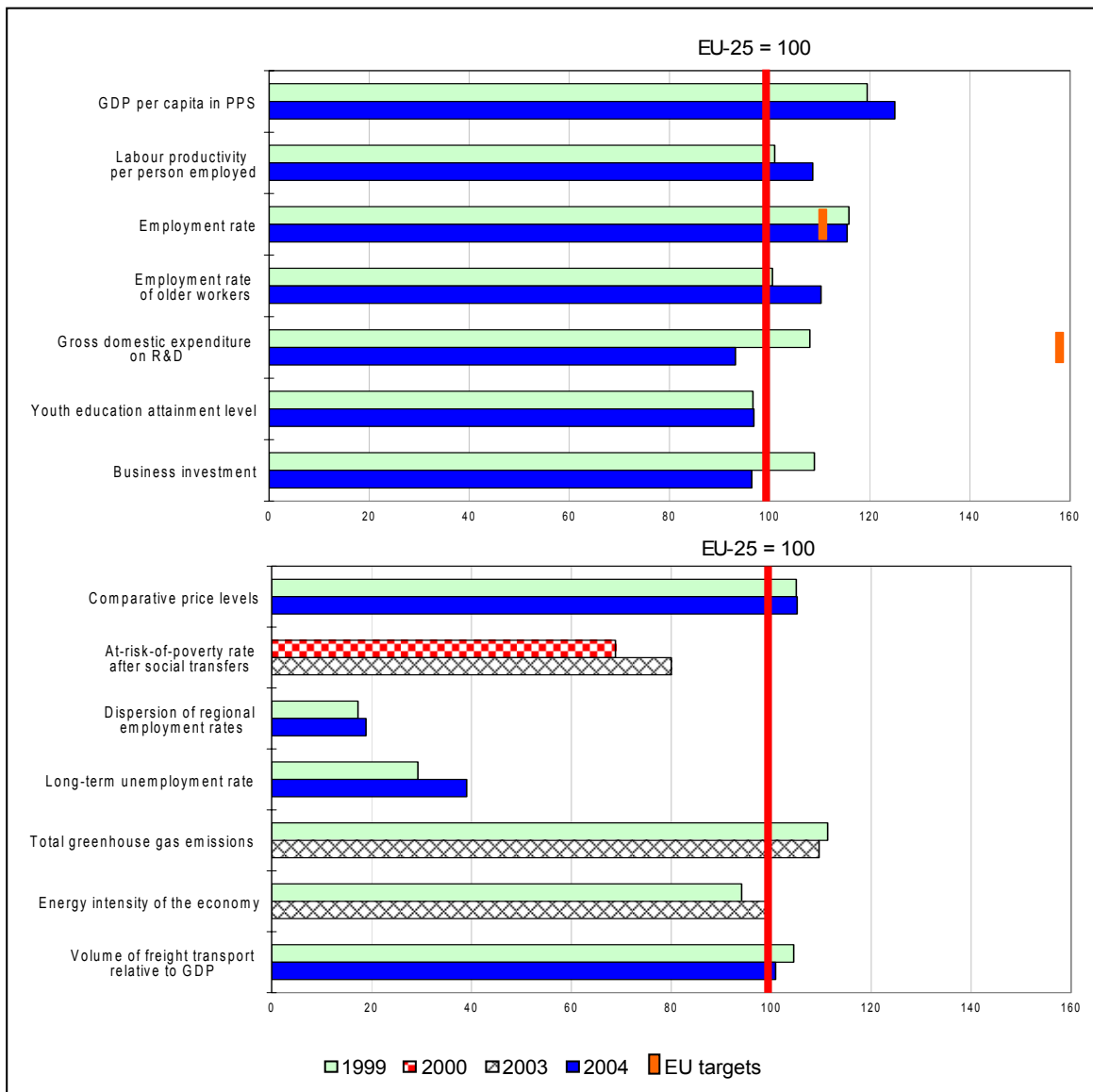
### **PART III: CONCLUSIONS**

20. In line with the Integrated Guidelines, the Dutch National Reform Programme identifies and responds to the main challenges facing the Netherlands, namely improving labour supply, achieving faster growth in labour productivity, in particular by strengthening R&D, innovation and education; and improving price competitiveness, in particular by containing labour costs. A more developed policy for R&D as well as measures to strengthen competition, thereby improving the resilience of the economy, would be appropriate. Overall the NRP is clear and coherent and in several areas shows ambition and originality.
21. The involvement and commitment of social partners in many of the reforms is likely to facilitate implementation. In some areas, such as innovation and active labour market measures, only limited detail on funding, implementation schedules and evaluation is provided.
22. The programme's strengths include:
  - initiatives to reduce regulatory burdens on businesses, which have recently inspired other Member States to develop policies along similar lines;
  - measures to increase financial incentives to work for recipients of benefits;
  - efforts to raise the effective exit age from the labour market.
23. Among the points requiring further attention are:
  - enhanced measures to increase the number of hours worked by part-time workers;
  - further efforts to facilitate the integration of ethnic minorities into employment.
24. Taking due account of the above, the Netherlands is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way the Netherlands has dealt with the issues mentioned in paragraph 23. In this context, the Commission looks forward to discussions with the Dutch authorities as part of the new partnership for growth and jobs.

### **PART IV : STATISTICAL GRAPHS AND DATA**

# NETHERLANDS

	NL							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	119.5	120.2	127.6b	125.9	125.3	125.0		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	101.0	101.6	107.7b	106.5	107.0	108.6		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	71.7	72.9	74.1	74.4	73.6	73.1	:	61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	36.4	38.2	39.6	42.3	44.3	45.2		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	2.02	1.90	1.81	1.72	1.76	1.77p	:	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	72.3	71.7	72.1	73.3	74.5	74.2		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	105.0	104.2	104.0	105.3	106.6	105.2p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	19.5	19.0	17.9	16.4	15.7	16.3		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	11.0	11.0p	11.0p	11.0p	12.0p	:		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	2.3	2.2b	2.3p	2.2	2.3	2.3		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	1.2	0.8	0.6	0.7	1.0	1.6		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	100.8	100.4	101.1	100.2	100.8	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	202.1	198.5	200.7	201.1	208.7	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	105.2	98.9	96.8	94.9	96.0	105.5		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	



## Poland

1. Over the period 1996-2000 economic growth averaged 5.1%, but was followed by a sharp economic downturn in 2001–2002 which triggered a rapid deterioration in the fiscal accounts. Nevertheless, more recently Poland has experienced an export-led upswing. GDP per capita exceeded 49% of the EU average in 2004 and was the third lowest in the EU. Labour productivity growth has been well above the EU average over the last decade. Labour market conditions have recently been improving slowly. At 18.8% in 2004, the unemployment rate is still the highest in the EU and the employment rate (51.7% in 2004) the lowest.

### **PART I: GENERAL ASSESSMENT**

2. The Polish National Reform Programme (NRP) sets as the main policy objective maintaining a high economic growth rate fostering job creation, while respecting the principles of sustainable development. To achieve this, the NRP identifies six main priorities: consolidating public finances and correcting their management; developing entrepreneurship; making enterprises more innovative; developing and modernising infrastructure and ensuring a competitive environment in network industries; creating and sustaining new jobs and reducing unemployment; and improving the adaptability of workers and enterprises by investing in human capital. The Commission shares this analysis of the main priorities.
3. The NRP focuses on continuity but also introduces some shifts in on-going policies. Its assessment of areas where improvements are needed is comprehensive and frank. There are in general coherence and cross-references between macro-economic, micro-economic and employment strands but the degree of precision in the definition of implementing measures varies widely. Main steps for 2005-2008 are not accompanied by indications of which institutions are responsible. Neither are timetables, budgetary implications or information on monitoring and evaluation procedures provided, making it difficult to assess the practicability of proposed solutions. However, the Polish authorities have indicated that as part of the new government's work programme they are preparing much of this information. No target is set for the overall employment rate. Quantified assumptions are made for 2008 (no target is set for 2010) for R&D spending (1.65% of GDP compared to 0.58% in 2004) and for the unemployment rate (14.6% compared to 18.8% in 2004). However, the measures presented do not appear sufficient to meet them. The role of the Structural and Cohesion Funds - that are and will continue to be a major source for public investments in the coming years - is mentioned but the NRP gives only general guidance on how they will be used to fulfil the Lisbon agenda.
4. There were wide consultations on the first draft of the NRP, with parliament, social partners and civil society. Owing to the recent formation of the new government, efforts to develop ownership of the final version of the NRP have inevitably been rather limited. While the Commission recognises these special circumstances, cooperation with stakeholders will need to be reinforced as the NRP is implemented and updated.

## PART II: ASSESSMENT BY POLICY AREA

### Macroeconomic policies

5. The NRP identifies one key challenge in the area of macroeconomic policies: the consolidation and better management of public finances. The Commission supports this choice.
6. The NRP outlines a number of reform initiatives. The main measures are first, social security reforms, including reform of early paths out of the labour market and of the farmers' special social security system and second, stricter monitoring and reductions of extra-budgetary expenditure managed by special government agencies. The NRP also points to the continuation of changes to the healthcare system as an important element in stabilising public finances. In addition, the programme envisages a further decentralisation of public finances and a reduction in state aid aimed at financing increased spending on R&D, job creation and the environment. The NRP does not contain any macroeconomic outlook integrated with the proposed reforms– though the new government is preparing one as part of its update of the Convergence Programme – or consider the effects of the expected inflow of EU funds reaching up to 4% of GDP. No targets for the general government deficit are set. The proposed 4-year nominal anchor covers the state budget only. The programme is silent about the budgetary impact of the planned measures, including those which may entail significant short-term spending. For example, the programme does not estimate the cost of its extensive ambitions for improving housing and infrastructure, introducing comprehensive monitoring of medical prescriptions or of a comprehensive computer system for administering the state budget. The Ministries responsible are understood to be preparing such costings now.
7. The approach to the sustainability of public finances is broad and covers the appropriate areas. However, the limited detail provided on the macro-economic and budgetary impact of reforms makes it difficult to assess the realism of the overall strategy.

### Microeconomic policies

8. The NRP identifies developing entrepreneurship, increased innovation by companies, infrastructure development and upgrading and ensuring a competitive environment in network sectors as key microeconomic challenges. The Commission broadly shares this view, though a stronger and more general emphasis on competition policy, where the NRP concentrates largely on network sectors, would be appropriate.
9. There is a range of initiatives in the NRP to improve the business environment and develop entrepreneurship. These have positive potential, including in improving the competitiveness of the manufacturing sector, if integrated into an industrial policy strategy. A “one-stop-shop” system for the registration of new businesses, an *e-platform* for businesses and a system to identify administrative costs are useful steps. Improvements in the impact assessment system (OSR) are also set out but the approach to Better Regulation needs to be further developed. The plan to rationalise commercial jurisprudence is appropriate, though more ambitious measures to accelerate proceedings, to reduce their costs and to remove legal uncertainties are necessary. Reform of regulations covering professional services is not fully

addressed in the NRP. Since access to finance is a chronic problem for Polish SMEs, the initiatives proposed to improve this are valuable, though more specific attention for technology-based start-ups would be useful. Areas not dealt with in the NRP include improving the transparency of tax procedures, reducing fiscal uncertainty, implementing Internal Market law and building on existing efforts to promote entrepreneurship to citizens through the education system, where entrepreneurship is already part of the curriculum for secondary schools. The NRP explicitly mentions the goals of redirecting state aid expenditure towards horizontal objectives while reducing the overall level of state aid. This is particularly necessary in relation to shipbuilding, steel and coal-mining, without, however, hampering the necessary restructuring processes in these sectors.

10. The assumption of reaching R&D intensity of 1.65% by 2008, from the very low current base, is ambitious but is only supported to a very limited extent by detailed proposals for concrete measures linked to performance indicators. The NRP correctly identifies a lack of business innovation as the principal weakness of Polish innovation performance. The measures to improve this are based on changes to regulation and on encouraging private funding. More emphasis on reforming public sector R&D and innovation support, in line with clear research priorities, as well as on upgrading technical skills, is necessary. Finally, the programme addresses only in a limited way the role of foreign-owned companies in the innovation system and the decline in patenting.
11. The NRP sets out in general terms a range of initiatives to improve transport, energy and housing infrastructure. The national and regional programmes will have to be coordinated closely with regulatory measures in order to bring maximum benefits: simplification of investment processes is particularly important. The opening of network markets presented in the NRP will increase competition, but the detail provided is not sufficient to assess its likely impact, in particular in electricity and telecommunications. While the NRP highlights the link between environmental technologies and increased competitiveness, setting out in more detail measures to support such technologies and the use of economic instruments to internalise external costs would allow a better assessment of their likely effect. Similarly, ICT initiatives are not precisely described. Poor housing is identified as a factor in social exclusion, unemployment and lack of labour mobility. The extensive initiatives to address this are not presented in detail or costed.
12. The micro-economic measures in the NRP would, if fully implemented, boost the business environment, innovation, entrepreneurship and infrastructure. The likely extent of that effect is unclear in the absence of details on the measures or on targets, timetables, implementation mechanisms and budgetary impacts.

### **Employment policies**

13. Creating and sustaining jobs and reducing unemployment, along with improving the adaptability of workers and enterprises by investing in human capital are among the main priorities of the NRP. The Commission subscribes to this.
14. Measures to attract and retain more people in employment focus on changes in active labour market policies, including measures to improve labour market services and to make public employment services more effective. The efforts envisaged to improve

labour market information (including statistics) should allow better targeting of labour supply to meet the economy's needs. Measures are proposed to integrate disadvantaged persons and disabled people into employment. To retain older workers in employment, efforts to reform access to early retirement schemes will continue. Gradual reforms envisaged to increase flexibility in the retirement age and to equalise the retirement age of women and men could contribute to increasing the employment of older people, thus strengthening the adequacy and sustainability of pensions. However, their successful delivery will depend on the result of a public consultation and on overall developments in the labour market. More resolute steps are needed to reduce the very large number of inactive people, to raise the employment rate and to meet the ambitious assumption of reducing unemployment to 14.6%. Cutting youth unemployment is considered a priority and the programme builds on existing policies but given the scale of the challenge new measures are needed. The issues of undeclared work, the creation of alternative jobs in rural areas, the reconciliation of work and family life and the emigration of qualified workers are not addressed. The NRP does not refer to strengthening territorial cohesion, reducing regional disparities or to the marked urban-rural divide.

15. To improve the adaptability of workers and enterprises, planned reforms concentrate on reducing the tax burden on workers with the lowest incomes and on increasing flexibility and differentiation in forms of employment. These initiatives are appropriate but described only in general terms which make it difficult to judge their likely effect. Widening the use of flexible forms of employment is raised in the NRP but is not fully backed-up by specific measures making them financially attractive. Issues of health and safety at work are not covered, though relevant prevention measures could improve productivity. Still incomplete industrial restructuring processes, which may entail job losses in coming years, also need special attention. The issue of occupational and geographical mobility, is addressed only partially.
16. In terms of investment in human capital, the NRP aims to improve the education and training system, better match education and training programmes with labour market needs and increase participation in lifelong learning, in cooperation with social partners. Measures to remove barriers to access to education, particularly those resulting from poverty and disability, include the development of distance learning and of vocational counselling systems. A strategy for lifelong learning is to be developed and implemented. However, a fully-fledged strategy for vocational training is not visible in the programme, despite the fact that over half of employers do not invest in employees' training.
17. The employment challenges are well identified in the NRP but proposed measures seem too modest both in scope and scale given the extent of the problems facing the Polish labour market. The lack of implementation details makes it difficult to assess the likely effectiveness of the measures, though the Polish authorities intend to add some of the necessary material in their Annual National Action Plan for Employment.

### **PART III: CONCLUSIONS**

18. In line with the Integrated Guidelines, the Polish National Reform Programme identifies and responds to the main challenges facing Poland, namely consolidating



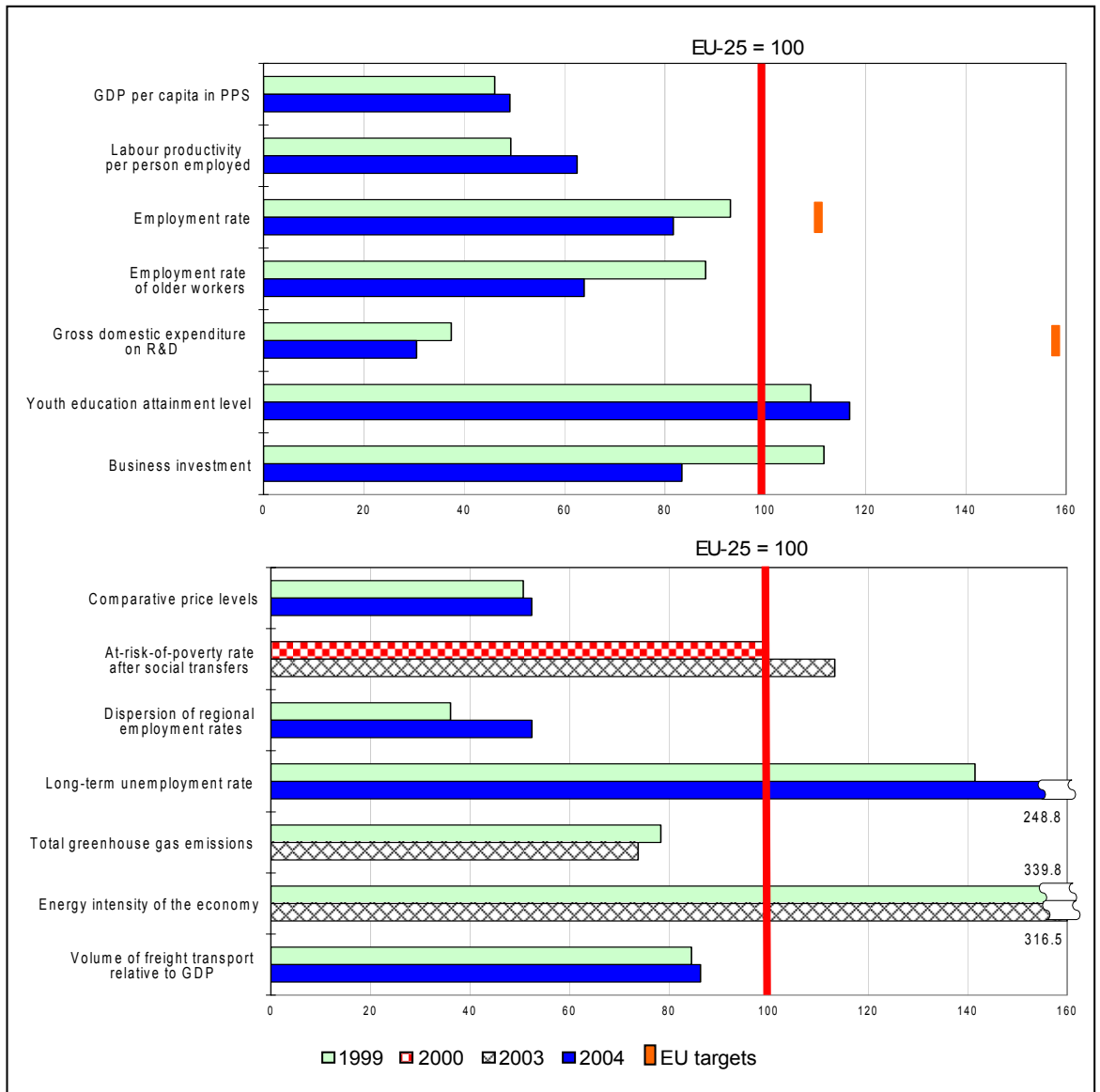
public finances and correcting their management; developing entrepreneurship; making enterprises more innovative; developing and modernising infrastructure and ensuring a competitive environment in network industries; creating and sustaining new jobs and reducing unemployment; and improving the adaptability of workers and enterprises by investing in human capital. It is based on a coherent analysis and states the intention to take a wide range of ambitious and appropriate measures. However, many are described only in the most general terms and are not yet situated within a comprehensive strategy establishing clear priorities for early action.

19. The NRP was drawn up under very tight deadlines, given the recent elections. Targets, timetables, budgetary information and details on monitoring and evaluation procedures are in general not provided. The links with Structural Funds and the distribution of implementing responsibilities is not always clear.
20. The programme's strengths include:
  - some initiatives aimed at improving the business environment by reducing administrative costs and improving SME's access to finance;
  - the focus on improving education, training and lifelong learning.
21. Among the points requiring further attention are:
  - more emphasis on competition, on reinforcing public sector R&D and innovation;
  - a comprehensive strategy for infrastructure investment and on environmental protection;
  - a more robust approach to raising employment rates and addressing regional disparities.
22. Taking due account of the above, Poland is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Poland has dealt with the issues mentioned in paragraph 21. In this context, the Commission looks forward to discussions with the Polish authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# POLAND

	PL							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	46.1	47.0	46.3	46.6	47.2	49.1		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	49.3	51.6	50.6	51.9	59.9	62.5		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	57.6	55.0	53.4	51.5	51.2	51.7	:	61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	31.9	28.4	27.4	26.1	26.9	26.2		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	0.70	0.66	0.64	0.58	0.56	0.58	:	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	81.6b	87.8	88.6	88.1	88.8	89.5		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	50.7	56.3	62.9	59.5	53.4	52.4p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	20.0	20.5	16.8	14.9	14.5	14.1		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	:	16.0	16.0	17.0	17.0	:		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	4.8	6.9b	7.2	7.3	7.2	6.4		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	5.8	7.6	9.3	10.8	10.8	10.2		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	71.0	68.3	67.7	65.5	67.9	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	730.2	680.2	673.5	654.2	663.1	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	85.1	82.9	81.0	81.7	83.1	90.3b		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	



## Portugal

1. From a high annual average 4% in the period 1995-2000, economic growth declined to only 0.5% per year between 2001 and 2005. This reflects the necessary unwinding of imbalances in the economy, in particular in government finances (a general government deficit of some 6% of GDP in 2005) and the external account. GDP per capita was 75% of the EU average in 2004, and labour productivity the lowest in the euro area. The recent economic slowdown has led to a decline in the employment rate (67.8% in 2004) and an increase in unemployment (6.7% in 2004).

### PART I: GENERAL ASSESSMENT

2. The Portuguese National Reform Programme (NRP) is built on four strategic objectives: the strengthening of budgetary consolidation, fostering economic growth, increasing overall competitiveness and reinforcing social, territorial and environmental cohesion. In order to achieve these strategic objectives a few key policy areas are identified, the majority concentrating on the micro-economic area: economic growth and sustainability of public finances; public administration reform; competitiveness and entrepreneurship; R&D and innovation; territorial cohesion and environmental sustainability; market efficiency; qualifications, employment and social cohesion. The Commission shares the analysis of the key policy areas.
3. The programme identifies clearly the main weaknesses affecting the Portuguese economy. It reviews many recently initiated policy measures. While some measures are presented in detail and with ambitious quantified targets, others are less specific, and would benefit from more detail on timing and sources of funding. This could be partly attributed to the fact that the NPR started to be prepared by a government empowered only a few months before; since the submission of the NRP some of its measures have been further detailed and implemented. Measures vary considerably in importance and relevance. Integration between the different areas could be enhanced. Furthermore a better treatment in the NPR of the modalities for its implementation and monitoring would have allowed to better assess whether the measures will be sufficient to address the key challenges. Addressing in a proper way the NPR's internal governance and in particular how its implementation is monitored is essential for the success of the NPR. The NRP defines as a key target an employment rate of 69% by 2008. While not setting an explicit quantified target for total investment in R&D, it aims to double public and to triple private R&D expenditure by 2010, thus setting an implicit target of around 2% of GDP, against the background of the overall 3% target for the EU. The NRP should specify more clearly the role of Structural Funds in providing support.
4. Consultation and efforts to develop ownership of the document have been fairly substantial. A new ad hoc team, coordinating a network consisting of representatives of all Ministers, was established at Cabinet level under the authority of the Lisbon-coordinator, reporting directly to the Prime Minister. Both the Economic and Social Council and the Parliamentary Committee for European Affairs were consulted and had a specific session on the draft programme.

## PART II: ASSESSMENT BY POLICY AREA

### Macro-economic policies

5. The NRP identifies two key policy areas in the area of macro-economic policy. The first is enhancing economic growth and promoting the sustainability of public finances. The NRP restates Portugal's commitment to the fiscal consolidation strategy, adopted earlier this year and attached to the NRP. The second is the reform of public administration. Both these challenges are relevant for Portugal.
6. Fiscal consolidation is crucial for Portugal to return to sustained economic growth. Based on a favourable economic outlook, the NRP identifies a key target as achieving a general government deficit below 3% of GDP by 2008. The most important measures for fiscal consolidation are the Central Government Restructuring Programme (*PRACE*) and changes in the social security schemes for various categories of government employees. Other measures concentrate on strengthening the expenditure control framework. The programme mentions concern over the long-term sustainability of public finances given the ageing population and acknowledges the importance of reforms in social protection to improve sustainability and fairness. Recent initiatives, notably changes in civil servants' retirement rules and on curbing early retirement, have positively contributed to address this problem. The programme recognises, however, that further measures might need to be adopted to assure the sustainability of social security and for the authorities' fiscal targets to be reached..
7. The reform of the public administration mainly refers to changes in the relations with individual citizens and enterprises, and to issues of internal organisation. While the selection of areas for action seems appropriate, the measures envisaged are not presented in a detailed manner, which makes it difficult to assess them.
8. The reform measures in the area of macro-economic policy outlined in the NRP are promising steps in relevant areas. Their implementation should both support growth and improve the sustainability of public finances. In addition, they would help curb Portugal's heavy net external borrowing. However, while some measures are described in detail, the programme does not quantify their expected impact on growth and public finances.

### Micro-economic policies

9. The micro-economic part of the NRP is divided among four "transversal policies": competitiveness and entrepreneurship; R&D and innovation; territorial cohesion and environmental sustainability; and market efficiency. The Commission agrees that these are priority areas, and would particularly emphasise the need to ensure adequate levels of competition in network industries.
10. The NRP deals with science and technology measures largely on the basis of the government's "Technological Plan". It sets ambitious objectives to bring Portugal close to the EU average in scientific and technological capacity and contains many useful measures in this regard. However, the coordination of policy design and of implementation is not explicitly addressed and the NRP would benefit from more specific information on how to achieve most of the science and technology targets.

More information could be provided to help in assessing the scale of the expected interventions or the strategic vision behind individual measures. Making investment more effective would require development of the research and innovation system and closer integration of science and industry policies, among other things in order to avoid bottlenecks in human resources. Monitoring and evaluation mechanisms could be given more attention, for example in the promotion of private investment in R&D and innovation. Stimulation of private R&D is dealt with by a mix of complementary measures (risk capital, tax credits, and thematic support programmes), but it is unclear whether this is sufficient to create enough absorption capacity and avoid crowding out private financing.

11. It should be specified how some of the measures proposed to improve competition in services, particularly in network industries such as telecommunications and energy, will address the problem. Most measures in the energy sector concern the writing of EU Directives into national law. No deadlines are set for the integrated energy market in the Iberian Peninsula and no timetable is given for opening the gas sector to competition. With regard to financial services, the NRP mentions the implementation of the measures in the EU Financial Services Action Plan and envisages a reinforcement of the Guarantee Fund and adapting the legal framework for risk capital. The process of gradually introducing competition into postal services will be supervised by a regulatory body in the period 2006-2008.
12. Synergies between environmental protection and growth are addressed by seeking energy efficiency and by increasing the share of renewables. But measures to promote environmental technologies are limited. Better regulation measures concern mainly the reduction of administrative costs and no explicit reference is made to impact assessment and stakeholders' consultation. Improving the implementation of EU law is mentioned. Introduction of entrepreneurship training in secondary schools is planned. Widespread access and use of ICTs is presented as a priority, both as a tool to cut red tape in public administration and to foster regional development and enhance productivity.
13. The NRP announces a vast set of micro-economic policy measures associated with ambitious objectives. However, it is difficult to discern the strategic priorities. The measures differ greatly in importance, relevance and details on costs and timing. There is insufficient information on implementation and monitoring mechanisms.

### **Employment policies**

14. The employment chapter is based on the National Action Plan for Employment. "Qualifications, Employment and Social Cohesion" is a key policy area in the NRP. The Commission supports the top priority given to enhancing qualification levels.
15. The NRP proposes a comprehensive set of education and training measures with very ambitious targets. Due to serious structural weaknesses in qualification levels, the priority given to investment in human capital and to lifelong learning is appropriate. The proposed expansion of the double certification system at secondary level can strongly contribute to improving skills and reduce early school leaving. Further efforts are required to improve the efficiency and labour market relevance of education and training. The involvement of the social partners will be crucial to the success of the ambitious measures to certify acquired skills and to increase the

qualifications of the adult population. Measures to boost vocational training relevant to company-specific needs, should be strongly pursued.

16. Employment is addressed through policies to attract more people to the labour market and promote the adaptability of workers and enterprises. Targets for full employment by 2010 have been set and appear to be realistic. The measures to attract and retain more people in employment focus on increasing the employability of the young, disabled people, increasing female participation, promoting active ageing, and modernising public employment services. The increasing number of long-term unemployed and the gender pay gap in the private sector require further attention. Most of the measures rely heavily on the efficient and effective provision of public employment services in close contact with the social partners. The NRP could be more specific on how this is going to be achieved. Adaptability is pursued through measures to improve the anticipation and management of restructuring and the reform of labour relations. Measures on critical issues such as labour market segmentation, modernisation of work organisation, labour cost developments and productivity and quality at work are not proportionate to the challenges ahead. Some measures correctly address flexibility, but with little emphasis on security. This response may lead to imbalances and may weaken the effectiveness of the approach to adaptability.
17. Social cohesion is a fundamental component of the employment challenge. The “at-persistent-risk-of-poverty rate” and the inequality of income distribution are the highest in the EU, justifying this concern. However, the NRP would greatly benefit from a focused approach on fighting poverty and only partially addresses the challenge by including measures for the disadvantaged and socially excluded among other items such as education, active labour market policies. The NRP also refers to major actions to improve the sustainability and fairness of the social protection system, notably pension and healthcare. Mainstreaming of gender equality is identified as a priority but is scarcely addressed.
18. The ambition of some measures is encouraging, but in many cases there is little information on the means and instruments for implementation and on how the crucial involvement of the social partners will work in practice.

### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the Portuguese National Reform Programme identifies and responds to the main challenges facing Portugal, namely the strengthening of budgetary consolidation, fostering economic growth, increase overall competitiveness and reinforcing social, territorial and environmental cohesion. In order to achieve these strategic objectives a few key policy areas are identified, the majority concentrating on the micro-economic area: economic growth and sustainability of public finances; public administration reform; competitiveness and entrepreneurship; R&D and innovation; territorial cohesion and environmental sustainability; market efficiency; qualifications, employment and social cohesion. . The NRP presents a large number of measures. Many of the measures proposed appear promising, but there is considerable variation in importance and relevance. Strategic priorities, detail and integration between the different policy areas could be further enhanced.

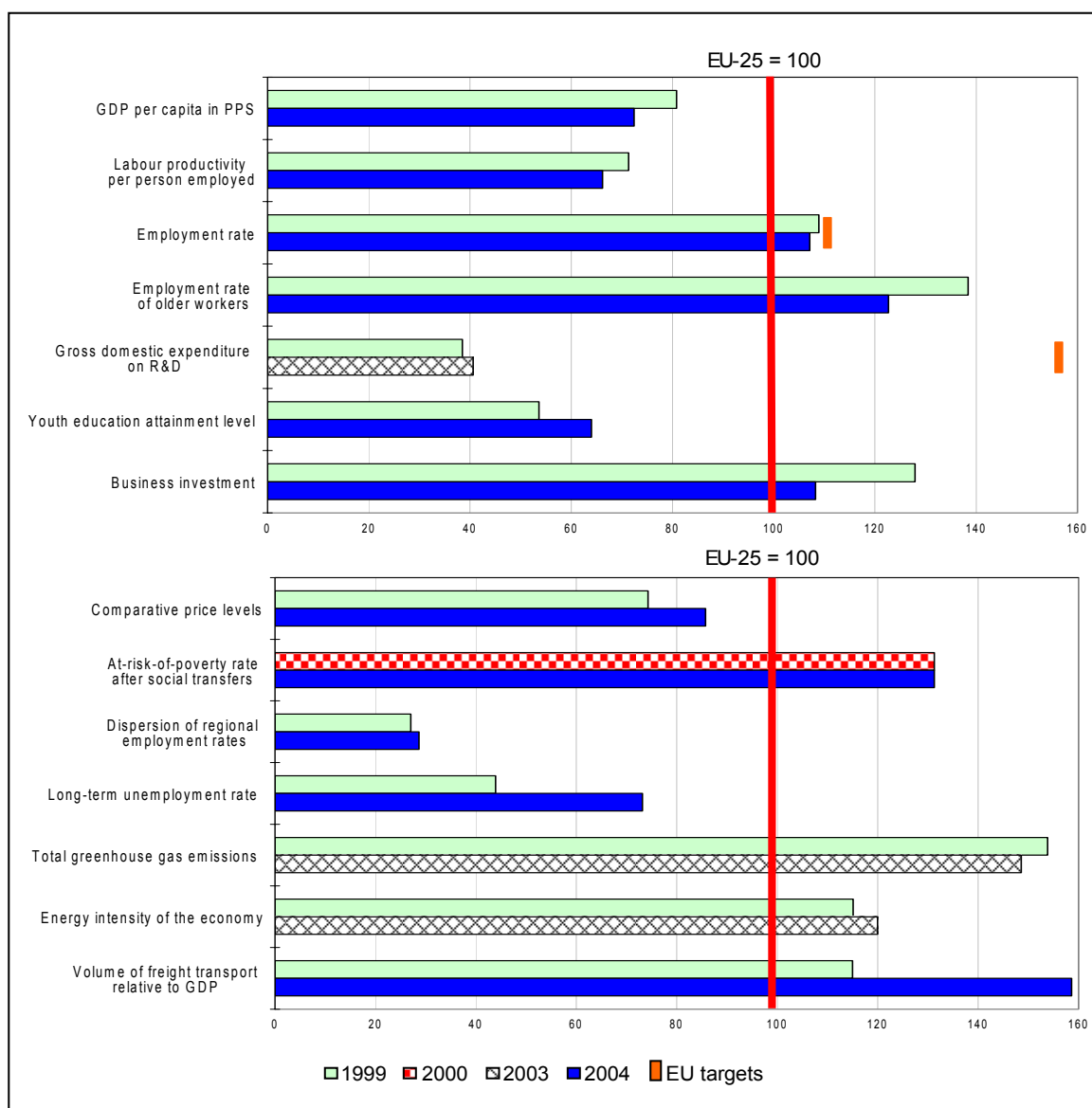
20. The NRP does not provide extensive information on the implementation and monitoring progress or on the implications for public finances and only in certain cases are objectives clear. It is therefore difficult to assess whether the measures will be sufficient to address the key challenges.
21. The programme's strengths include:
- the priority given to addressing shortcomings in science and technology through the Technological Plan;
  - the focus on investing in human capital, with ambitious measures throughout the NRP.
22. Among the points requiring further attention are:
- addressing the sustainability of the public finances;
  - stronger measures for effective competition in network industries, in particular telecommunications and energy;
  - more emphasis on promoting the adaptability of workers, notably the low-skilled, and of enterprises by modernising work organisation, while ensuring a less segmented labour market.
23. Taking due account of the above, Portugal is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Portugal has dealt with the issues mentioned under paragraph 22. In this context, the Commission looks forward to discussions with the Portuguese authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# PORTUGAL

	PT							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	80.8	80.9b	80.1	79.6	72.9b	72.4f	70.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	71.3	72.4b	71.8	71.5	66.1bf	66.2f		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	67.4	68.4	69.0	68.8	68.1	67.8		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	50.1	50.7	50.2	51.4	51.6	50.3		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	0.72	:	0.85	0.80e	0.78	:		*	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	40.1	42.8	43.5	44.2	47.7	49.0		74.8	76.3	76.1	76.5	76.5	76.6			
Comparative price levels	74.3	73.4	74.6	76.2	87.3b	85.7p		100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	22.9	23.4	22.7	21.1	19.0	18.3		17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	21.0	21.0	20.0	20.0p	19.0p	21.0b		:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	3.6	4.3	3.5	3.8	3.9	3.5		13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	1.8	1.7	1.5	1.7	2.2	3.0		4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	139.4	135.0	136.8	144.3	136.7	:		90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	247.4	241.5	243.9	254.7	251.3	:		214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	115.8	114.5	124.2	122.8	114.9	165.9b	100.7e	100.4e	99.4e	100.3e	99.7e	104.7e				

\* National target: 1% (2010) for the public sector





## Slovakia

1. The average annual real GDP growth rate equalled 3.7% over the period 1996-2000. Labour productivity growth was well above the EU average. Slovakia has recorded even sharper GDP growth since then, with 5.5% in 2004. GDP per capita was at 52% of the EU average in 2004. However, strong economic growth has not been reflected in the labour market performance in 2004, when the employment rate stood at 57%. The unemployment rate remained the second highest in the EU at 18.2% in 2004, particularly hitting young people. The employment rate for older people, at around 26.8% in 2004, is one of the lowest in the EU, but rising.

### **PART I: GENERAL ASSESSMENT**

2. The Slovak National Reform Programme (NRP), which was preceded by a National Competitiveness Strategy, aims at equalling the living standards of Europe's most advanced economies, through a competitive and diversified market economy with social balance, environmental responsibility and eurozone membership. To this end, it identifies four key challenges: information society; R&D and innovation; business environment; and education and employment. The Commission shares the NRP's analysis of the main priorities.
3. The NRP tries to integrate the different policy strands in a sound and responsible way, given the necessity for sometimes difficult policy choices. It outlines a coherent national strategy aimed at increasing the competitiveness of the country, building on several important recent reforms in the areas of public finances, taxation, pensions, healthcare, and labour market. The policy measures set out mainly concentrate on the employment and micro-economic areas. A few national targets have been set (general deficit, employment growth and unemployment rate) but not in relation to the EU targets on R&D and the overall employment rate. The target for annual employment growth of 1-2% appears achievable. The target for reducing the registered unemployment rate to under 10% by 2010 appears less ambitious given that the current level of registered unemployment is considerably lower than under the Eurostat definition referred to in paragraph (1). The NRP is less precise on the regional dimension as well as on the programme for investing the expected major inflow of structural funds.
4. Consultation and efforts to develop ownership of the document have been fairly substantial, though the role of local and regional authorities is not mentioned in the programme. The NRP was developed under the leadership of the Office of the Government and the Ministry of Finance. All the relevant ministries participated in the process, together with social partners, academic representatives and members of the Parliamentary Committee for EU Affairs.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. The macroeconomic part of the NRP mainly focuses on achieving long-term sustainability of public finances by 2010 and entry into the eurozone in 2009, as well as contributing to raising employment rates. The Commission subscribes to these macro-economic priorities.
6. The fiscal policy challenge is translated into a short-term goal of reducing the general government deficit, excluding pension reform cost, to below 3% of GDP in 2006 and of meeting the same target, including the cost of the pension reform, in 2007. The NRP contains only limited details about the measures on fiscal and monetary policy, usually without timetables or budgetary analyses, instead referring readers to the update of the convergence programme. The reforms already adopted in the areas of pension, healthcare, tax and public finance management are mentioned. The NRP reiterates the government's intention to achieve the fiscal policy goals by allocating additional public revenues primarily to faster reduction of the deficit.
7. The Commission's analysis of reforms already undertaken and in progress is generally positive but further measures may be necessary to meet the fiscal targets mentioned above.

### **Micro-economic policies**

8. The Slovak programme identifies the business environment, R&D and innovation and information society as the key challenges in the micro-economic area. The Commission shares this view.
9. The NRP recognises the need to create a favourable business environment in order to ensure long term competitiveness. The efforts mentioned towards establishing an integrated system of impact assessment and to make improve and expand consultation are promising but require completion. The programme also contains an interesting initiative to audit barriers to business in 2006. Efforts are made to reduce and redirect state aid from sectoral state aid assistance to horizontal priorities, including R&D and SMEs. A proposal to increase access to finance by setting up a stock exchange with the participation of neighbouring countries is interesting, though the NRP remains vague on the project and its participants. The NRP announces measures to improve law enforcement in 2006, though there is no information on implementation of the new bankruptcy law. The policy measures to improve the links between indigenous and foreign-owned companies are not fully developed and more could be done to improve businesses support services specifically targeted at SMEs. There is no indication of measures aimed at reducing the deficit in writing EU Internal Market legislation into national law.
10. The NRP lists a quite comprehensive range of planned actions targeting R&D and innovation, focused on three priorities: developing and supporting highly qualified scientists; research of international quality, adequately linked with the business sector; and effective public support for R&D and innovation. Despite the low starting point in terms of overall investment in R&D (0.58% of GDP in 2003), the NRP does not set national targets. It could focus more explicitly on R&D and innovation in SMEs (including early stage financing), on increasing the impact of the high level of foreign direct investment on R&D and innovation and on more and better leveraged public spending on R&D and innovation. A stronger emphasis on applied R&D

together with an improved patenting regime would be needed to strengthen the bridge from sciences and technology towards innovation.

11. The strong emphasis on the role of ICTs in education, digital literacy, e-government and broadband infrastructure is appropriate, as well as the commitment to introduce ICT-based methods in public administration management. Full implementation of these initiatives could provide a range of benefits in terms of human capital, improving the business environment and job creation.
12. The NRP proposes interesting measures to deal with certain aspects of the micro-economic challenges identified, but does not present an integrated strategy catering for different types of businesses. The action planned addresses crucial weak points in the Slovak R&D, ICT and innovation system. However, it remains to be seen whether the measures are sufficient to reverse current negative trends. A reinvigorated commitment to advance the implementation of planned policy measures and particular attention to their early evaluation will be indispensable.

### **Employment policies**

13. Four key priorities are identified by the Slovak authorities in the field of employment, namely: achieving a high employment rate; modern educational policy; coping with demographic changes and social inclusion. The Commission's assessment coincides with this.
14. In order to support employment growth, attract and retain more people in employment, the NRP puts forward an extensive set of policy measures, focusing on: reduction of the tax burden for those on low incomes; simplification of administrative procedures linked to employment and self-employment; support for geographical mobility; and active labour market policy measures for disadvantaged job seekers. Although the mobility measures and housing policy are well established and linked together, they might not be sufficient to resolve the significant regional employment disparities. The high level of structural unemployment and the gender pay gap, which remains among the highest in the EU, deserves more attention in the programme. The NRP includes several measures aimed at creating inclusive labour markets. However, some groups require more attention, such as disabled people, large families and Roma. The measures put forward to respond to demographic changes in Slovakia do not include support for "active ageing".
15. A long-term objective to further reduce the tax and social security burden is set, with priority given to low-income earners. However, the NRP does not formulate a strong commitment to reform the overall system of social contributions. Increased flexibility for enterprises in hiring staff is planned, whilst support for flexible working arrangements is limited. The NRP proposes to continue with labour inspection measures in order to reduce undeclared work, but little attention is given to reduction of the tax wedge. Although the Labour Code in 2003 transferred the responsibility for wage setting to company level, the NRP recognises the need for more commitment by the social partners in setting up the wage bargaining mechanism. In-company training needs more specific attention, also in connection with the use of Structural Funds.

16. The NRP considers education policy a top priority in the light of young people's often poor levels of key skills and the low rate of adult participation in training. It refers to the new law on education to be adopted in 2006, which if fully implemented has potential to be effective in improving human capital over time. The planned educational reform is focused on all levels of the system and covers ICT use, foreign language training, lifelong learning and education for disadvantaged children. The priorities in education policy are clearly defined, with a short reference to the future use of Structural Funds. . More emphasis could be put on cooperation with the private sector in the reform of secondary and higher education and to promoting entrepreneurship education in general.
17. The NRP presents a wide set of measures aimed at addressing the employment challenges identified. However, more developed responses to some issues would be warranted - in particular structural unemployment, regional employment disparities, investment in in-company training, and the integration of vulnerable groups into the labour market. More developed policies are also needed to tackle long-term unemployment and youth unemployment.

### **PART III: CONCLUSIONS**

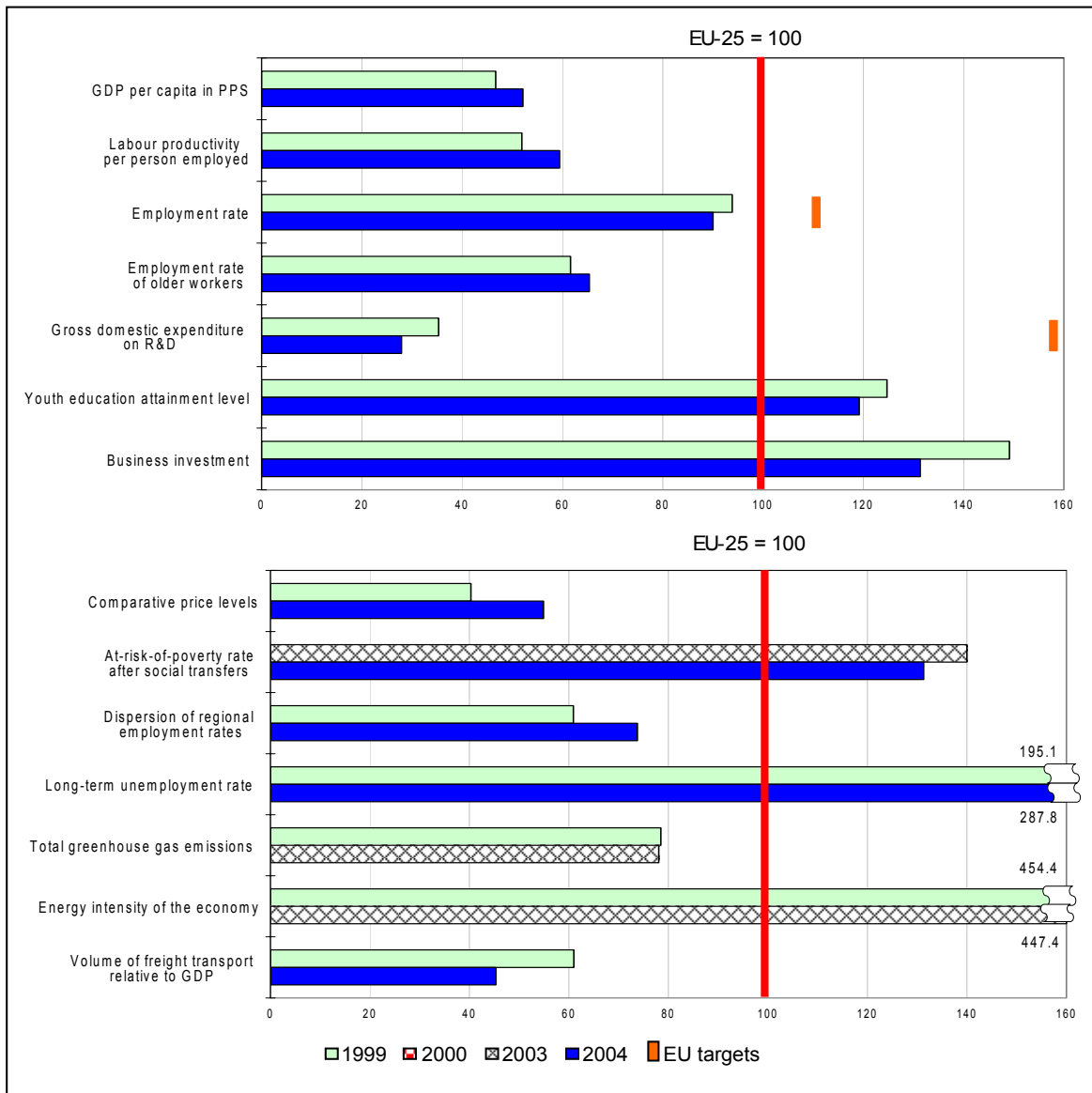
18. In line with the Integrated Guidelines, the Slovak National Reform Programme identifies and responds to the main challenges facing Slovakia, namely information society; R&D and innovation; business environment; and education and employment. Overall, the NRP builds on recent reforms. However, it is not always clear that measures presented are sufficient to meet the objectives set out.
19. The level of detail given on the various policy initiatives varies widely. The data provided is insufficient to allow an assessment of whether the financial commitments for individual initiatives are consistent with the target for the general budget deficit. In order to facilitate implementation, more should be done to foster the participation of all stakeholders and ensure efficient monitoring and evaluation.
20. The programme's strengths include:
  - measures to improve the business environment including plans to introduce an integrated system of impact assessments;
  - the priority given to developing the use of ICT, including in education;
  - the comprehensive set of measures supporting employment growth.
21. Among the points requiring further attention are:
  - stimulating R&D and innovation;
  - tackling regional disparities and structural unemployment;
  - the issue of integration of vulnerable groups, such as disabled people and the Roma.

22. Taking due account of the above, Slovakia is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Slovakia has dealt with the issues mentioned in paragraph 21. In this context, the Commission looks forward to discussions with the Slovak authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# SLOVAKIA

	SK							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	46.7	47.3	48.2	50.6	51.7	52.1		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	51.9	54.4	55.6	58.7	58.7	59.4		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	58.1	56.8	56.8	56.8	57.7	57.0	:	61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	22.3	21.3	22.4	22.8	24.6	26.8		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	0.66	0.65	0.64	0.58	0.58	0.53	:	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	93.3	94.5	94.4	94.0	94.1	91.3		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	40.3	44.1	44.6	44.6	50.5	54.9p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	26.7	23.1	25.7	24.3	23.1	22.2		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	:	:	:	:	21.0	21.0p		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	8.1	9.1	8.3	7.3	7.6	9.0		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	8.0	10.2	11.4	12.2	11.4	11.8		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	71.1	66.6	73.6	72.8	71.8	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	976.5	955.9	1015.8	976.0	937.3	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	61.4	54.0b	49.7	46.8	47.6	47.4		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	



## Slovenia

1. The Slovene economy has experienced robust GDP growth averaging 3.9% over the last decade. GDP per capita reached 79% of the EU average in 2004. Even though labour productivity has grown faster than the EU average, it remains well below the EU-15 average. Inflation, which has been one of the main concerns since 2000, is now approaching the EU average. While the employment rate is slightly above the EU average (65.3% in 2004) and the unemployment rate is one of the lowest (6.0% in 2004), the labour market is characterised by low employment of older workers and high youth unemployment.

### **PART I: GENERAL ASSESSMENT**

2. The Slovene National Reform Programme (NRP) identifies, in line with the “Slovenia’s Development Strategy”, five development priorities: a competitive economy and faster growth; a knowledge-based society; an efficient state; a modern social state and higher employment; and sustainable development. These priorities are subdivided into a number of more concrete objectives. The Commission shares the NRP’s analysis of the main priorities.
3. In order to address the above challenges, the NRP presents a comprehensive set of largely appropriate measures. It is very wide in scope and as a result the prioritisation is sometimes difficult to discern. Some reform measures are concrete, backed up with quantified targets and specific deadlines, while others appear to be only general aims. Ambitious targets are set for total R&D investment (3% of GDP by 2010, in line with the overall target for the EU) and employment (raising the overall employment rate from 65.3% to 67% by 2008) as well as in other key areas. However, as targets do not always bear a close link to specific measures, it is difficult to assess the general level of ambition and feasibility of the plan. The NRP does not elaborate on the budgetary implications of the measures it outlines. While the document stresses that the success of the reforms hinges on appropriate support from the EU budget, the links between the NRP priorities and the use of Structural and Cohesion Funds are not very explicit.
4. Consultation and efforts to develop ownership of the document have been very substantial. The government endorsed the programme, which closely corresponds to the framework document “Slovenia’s Development Strategy”. This strategy has been widely debated in public involving the tripartite Economic and Social Council, local authorities and the media. A discussion on the NRP is planned in parliament and may lead to adjustments. A new government office headed by a Minister without portfolio has been set up to co-ordinate the implementation of the reforms and a monitoring procedure will be developed.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. With a view to adopting the Euro in 2007 as the key priority, the NRP identifies macro-economic policies geared to achieving, as key priorities, nominal convergence and sustainable fulfilment of the Maastricht criteria related to inflation, long-term interest rate and exchange rate stability, as well as criteria regarding public finances. It seeks to achieve a balanced budgetary position by 2010 and cites as crucial in this respect reducing the scale of public expenditure, reforming the tax system, renewing the social agreement to keep wage policy stringent and encouraging prolonged activity on the labour market. The Commission supports this choice of goals. The expected relatively favourable macro-economic growth conditions in 2005 and 2006, with the economy growing slightly above potential, offer the opportunity to speedily proceed with reforms.
6. The policy measures to be applied to enhance the long-term sustainability of public finances remain largely unspecified in the NRP, without clear schedules for action. They can thus be seen as constituting merely broad lines for action. This lack of firm plans and of detail makes it difficult to assess the credibility of objectives for reducing general government expenditure and making public spending more flexible, while ensuring the stability of general government revenue. The NRP refers to the gradual abolition of the payroll tax by 2009 as well as the simplification of the direct tax regime and the possible introduction of a flat tax rate in 2007. There is a risk that these tax reforms could impinge on the general government balance, should the revenue shortfall due to the abolition/reduction of certain taxes not be off-set with curbs on expenditure. The NRP does not cover the details of the reform package designed to cut the high share of fixed spending commitments, currently still accounting for more than 80% of total outlays.
7. The programme presents a comprehensive approach to respond to the challenge of successfully introducing the Euro. However, policy measures put forward for improving public finances remain vague and do not allow an assessment of the feasibility of the strategy in the longer term.

### **Micro-economic policies**

8. The NRP addresses competition, R&D and innovation, business environment, better regulation, and foreign direct investment as key microeconomic challenges. The Commission's analysis is in line with this.
9. The competition challenge is addressed through a wide range of measures. The proposal to strengthen the legal basis for the Competition Protection Office is useful, but the on-going measures are needed to strengthen its staffing and financing need to be implemented. The proposed privatisation measures are not accompanied by a detailed timetable. Details are also missing on the proposals for stimulating market entry and removal of abuse of dominant position in those segments of the telecom sector with weak competition. There is nothing on reform of regulation in the professional services sector. Further proposals for increasing cross-border electricity transmission capacity, so as to increase competition in the domestic market, would be useful.
10. On R&D and innovation, a very heterogeneous set of measures has been proposed that are not sufficiently integrated to ensure the development of a coherent and successful national research and innovation system. In particular, the NRP does not



sufficiently address the key issue of improving the contribution from the private sector to R&D. Other issues requiring attention are encouraging cross-border knowledge transfer, increasing protection for intellectual property rights and the role of public procurement. An ambitious target to increase investment in R&D as a proportion of GDP to 3% by 2010 is set but does not seem realistic. The target for private R&D is not concrete enough. Whilst the initiative to increase public funding of R&D and to redirect it gradually towards technological research constitutes an important step, this needs to be combined with an increased concentration of efforts in a limited number of priority areas with sufficient critical mass. ICT measures such as the development of wireless broadband, improved ICT education, support for people buying computers and focus on e-content in Slovenia are appropriate.

11. With respect to business environment, the NRP addresses pertinent issues. The measures to simplify legislation, to reduce state aid, lighten the tax and administrative costs to enterprises and set up a structure to steer this process are serious efforts to improve regulation. The introduction of mandatory impact assessment is important step but reflection is needed on appropriate structures and consultation practices. The programme also includes appropriate measures to encourage entrepreneurship. These include improved SME access to finance, notably through the establishment of risk capital funds, and the promotion of entrepreneurial skills.
12. Although the penetration of foreign direct investment (FDI) into the Slovene economy has been low, the NRP recognises its importance and sets a quantitative target. Further privatisation should attract a significant proportion of foreign capital but the links between FDI and the privatisation strategy are not coherent. The NRP proposes measures to strengthen the industrial base that will have a positive impact on industry and will improve attractiveness for FDI. The importance given to supporting the internationalisation of SMEs is also positive.
13. The NRP focuses on important major transport initiatives which can make a significant contribution to competitiveness. However, these initiatives have to be implemented in order to improve infrastructure for railways and other forms of public transport and to manage congestion. The focus on improved environmental and spatial planning policy is appropriate and these policies need to be closely integrated to ensure that the tourism potential of the economy is realised. More emphasis on environmental technologies, energy efficiency and the use of renewables would be helpful.
14. Overall, the NRP provides a convincing response to the main micro-economic challenges identified and encouraging progress is being made on better regulation. However more action will be needed to meet certain challenges, such as improving the interaction between research activities and industry, strengthening the Competition Protection Office and increasing effective competition in the electricity market.

### **Employment policies**

15. A knowledge-based society, a modern social state and higher employment are among the priorities of the NRP. The Commission's analysis of the employment and education related challenges facing Slovenia is in line with this.

16. Ambitious targets for 2008 are set for attracting and retaining more people in employment. The target for the overall employment rate is 67%, up from the current 65.3%, and the target for older workers is 35%, compared to 29% currently. These are combined with less ambitious targets for the unemployment rate (from 6% to 5.5%) and female employment rate (2 percentage points above the EU 15 average). The intention to complement a gradual increase in retirement age with an active ageing strategy and integrated programmes for older workers is a positive development. Measures on the promotion of youth employment largely concentrate on improving employment opportunities for university graduates and preventive measures to reduce the drop-out rate from schools. The NRP sets the target of ensuring that graduates and post-graduates seeking a first job find employment within six months of completing their studies. Activation measures are foreseen to help tackle the high youth unemployment. However, the poor performance in terms of activation and prevention raises concerns over the approach. In this context, the stated intention of modernising public employment services and encouraging the development of private employment agencies is helpful. Among disadvantaged groups, only disabled people are targeted while action against discrimination is narrowly focused on gender.
17. Increased flexibility in the labour market is the main instrument put forward in the NRP to promote adaptability of workers and enterprises. All regulations hindering flexibility will be revised. The NRP recognises the need for a balance between flexibility and security but remains unspecific on how this goal will be achieved. Special attention needs to be paid to the low-skilled, older workers and workers threatened by the restructuring of some sectors. Measures increasing geographical mobility are constructive. However, no measures to prevent undeclared work are included.
18. Slovenia is performing well in education and lifelong learning relative to several EU benchmarks. The reforms in higher education and the preparation of a new lifelong learning strategy are the most important measures mentioned in this respect but attention needs to be given to achieving a minimum critical size for new universities. The NRP also states aspirations to promote private investment in human capital and increase access to lifelong learning for low skilled workers. However, concrete action to realise these aims is not specified.
19. The structural weaknesses of the labour market are well identified in the programme. Key labour market reforms are set out, aiming to increase flexibility, reduce the tax burden on labour and reform the system of social transfers. Overall, the NRP addresses the right priorities. However, the major reforms announced are not yet sufficiently well defined to permit an assessment of their probable results and many individual measures are too vaguely presented for their feasibility to be determined.

### **PART III: CONCLUSIONS**

20. In line with the Integrated Guidelines, the Slovene National Reform Programme identifies and responds to the main challenges facing Slovenia, namely a competitive economy and faster growth; a knowledge-based society; an efficient state; a modern social state and higher employment; and sustainable development. Overall, the NRP

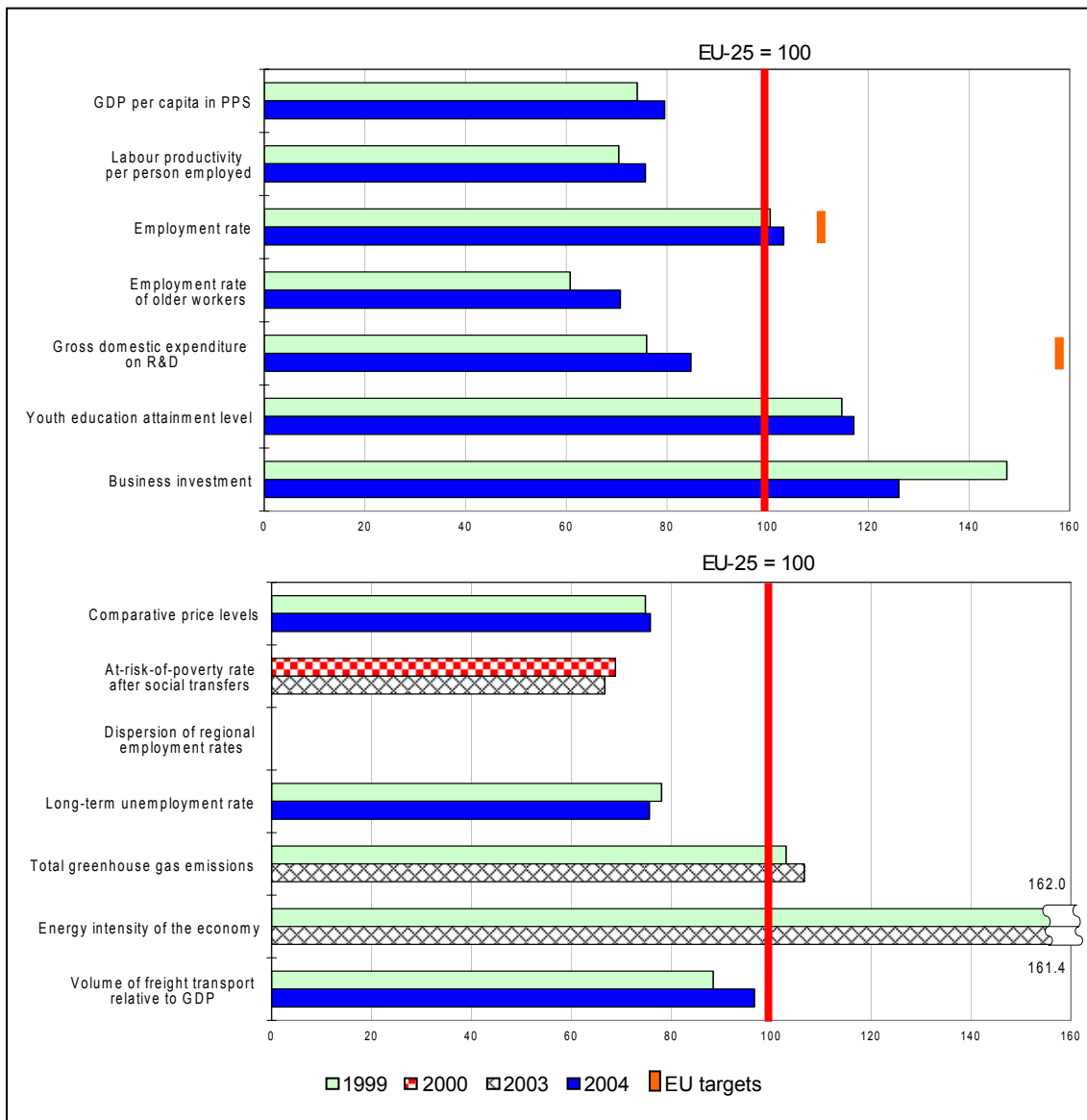
is comprehensive and the wide range of measures presented is generally appropriate, although clearer prioritisation would have been welcome.

21. There are quantified targets and specific timetables only for some of the reforms presented. Better links between targets and specific measures would allow a better assessment of the ambition and feasibility of the plan. The budgetary implications of the measures proposed are not covered in detail. However, the wide public consultation and the clear arrangements for coordinating implementation and monitoring are likely to be a significant advantage in putting the NRP into practice.
22. The programme's strengths include:
  - measures to improve regulation, including by simplifying legislation and lightening the administrative costs to enterprises;
  - efforts to support the development and internationalisation of SMEs, including by improving their access to finance.
23. Among the points requiring further attention are:
  - stronger measures to ensure the long term sustainability of pension systems and to promote active ageing;
  - a more coherent strategy for R&D and innovation, in particular improving the contribution from the private sector to R&D.
24. Taking due account of the above, Slovenia is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Slovenia has dealt with the issues mentioned in paragraph 23. In this context, the Commission looks forward to discussions with the Slovene authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# SLOVENIA

	SI							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	74.1	73.2	74.2	74.9	76.3	79.5	67.0 (2008)	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	70.4	70.2	71.6	71.4	72.9	75.7		100.0	100.0	100.0	100.0	100.0	100.0			
Employment rate	62.2	62.8	63.8	63.4	62.6	65.3		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	22.0	22.7	25.5	24.5	23.5	29.0		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	1.42	1.44	1.56	1.53	1.54e	1.61e		3.0	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	85.8	87.0	85.9	90.0	90.7	89.7			74.8	76.3	76.1	76.5	76.5		76.6	
Comparative price levels	74.8	73.1	73.2	75.5	77.9	75.8p			100.0	100.0	100.0	100.0	100.0		100.0p	
Business investment	26.4	22.5	21.2	19.8	20.5	21.3			17.9	18.3	17.7	17.1	16.7		16.9	
At-risk-of-poverty rate after social transfers	:	11.0	11.0	10.0	10.0	:			:	16.0	15.0	15.0	15.0		16.0	
Dispersion of regional employment rates	-	-	-	-	-	-			-	13.3	13.4	13.5	13.3		12.9	
Long-term unemployment rate	3.2	4.0	3.5	3.4	3.4	3.1	4.1		3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	93.3	94.0	98.6	99.3	98.1	:	90.6		90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	348.1	341.7	349.6	344.6	338.1	:	214.9		208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	89.0e	87.6e	88.5	84.0	87.1	101.1	100.7e		100.4e	99.4e	100.3e	99.7e	104.7e			



## Spain

1. Over the last decade, Spain experienced annual average real GDP growth above 3% and a sustained pace of catching-up to GDP per capita of 98% of the EU average in 2004. As a result of strong job creation, the employment rate (61.1% in 2004) has increased significantly, but remains far below the Lisbon target, especially for women, while unemployment (11% in 2004) has considerably decreased over recent months. Low productivity growth, which during the last decade has been below the EU average, coupled with persistently high inflation is damaging competitiveness.

### **PART I: GENERAL ASSESSMENT**

2. The Spanish National Reform Programme (NRP) presents two overarching policy objectives related to growth and employment: completing the real convergence of Spain with the EU-25 in terms of per capita income and increasing the employment rate to 66% by 2010. In order to achieve these two main objectives, the programme identifies seven key policy areas: budgetary stability; R&D strategy; a better environment for business; the achievement of higher competition; infrastructure development; a better functioning of the labour market; and better education and human capital. The Commission shares this analysis of the main priorities.
3. The Spanish NRP is ambitious and focuses on the most urgent challenges facing the country. The programme sets out a fairly comprehensive strategy to address Spain's economic and employment challenges, although the selection of priority measures for the period 2005-2008 is not always clear and some of the measures remain vague. Quantified targets are set for R&D spending (2% of GDP by 2010) and for the overall employment rate (66% by 2010). The target for the employment of women is 57% by 2010. An extensive set of indicators is provided to help monitor implementation. However, details on timetables and budgetary implications are limited making it difficult to assess the practicability of measures; for instance, how Spain envisages using EU Structural Funds to help reach the objectives in the programme for the period beyond 2007.
4. A clear internal governance structure has been established to ensure inter-ministerial coordination and governmental ownership of the programme. There is a call to reinforce regional governments' involvement during implementation of the programme. They have been invited to appoint "Lisbon coordinators" and draft their own programmes. Also positive is the announced involvement of stakeholders at the monitoring and evaluation stages of the programme. However, the programme provides limited information on the level of involvement and consultation of other stakeholders during its development as well as on efforts to consult and raise awareness of civil society at large.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. On the macro-economic side, reinforcing macroeconomic and budgetary stability is considered paramount to support real GDP convergence, which is a top priority of the NRP.
6. The NRP sets the target of real GDP per capita reaching 100% of the EU-25 average by 2010 (no indication is given for 2008). This target is easily attainable as real GDP per capita increased from 92.8% of the average EU-25 in 2000 to 98% in 2004. All measures presented in the NRP are expected to contribute to the overall convergence process.
7. The main quantified target is to reduce the ratio of public debt to 34% of GDP by 2010 (38% in 2008). This confirms existing commitments and policies to reduce public debt, a key aspect of which is the reform of the General Budgetary and Stability Law. The aim is to ensure greater budgetary stability over the economic cycle, to increase transparency of public accounts and to improve co-ordination with regional and local administrations. Other policy areas important for the sustainability of public finances, such as health care and pensions, are referred to but the effectiveness of on-going reforms is difficult to assess on the basis of the NRP. In the case of healthcare, success will depend on further cooperation with the regional governments.
8. Overall, the macro-economic policies outlined in the NRP appear suitable. They build on the good performances that have been achieved, notably in terms of fiscal consolidation.

### **Micro-economic policies**

9. The programme identifies four key policy areas for action in the micro-economic area: setting up a R&D and innovation strategy; improving the business environment; achieving greater competition; and developing infrastructure.
10. Concerning the R&D and innovation strategy, the research investment objective is ambitious (2% of GDP by 2010) but achievable if Spain sustains current increases in public research investment (with an objective of a 25% minimum annual increase) and succeeds in mobilising private expenditure, including through the financial participation of regional governments. The programme puts forward a wide array of measures, with quantified objectives and clear timetables. In particular, reforms of the legal and administrative framework for R&D, the new monitoring and evaluation system and the new “Plan Avanz@” to improve take-up of ICT are useful steps. Widening the use of ICT is also highlighted as a driver for modernising public administration. Further efforts would seem needed to ensure that SMEs and new firms have the capacity to engage in R&D activities and benefit from innovation.
11. With respect to improving the business environment and achieving greater competition, the new measures proposed appear appropriate, although detailed information on implementation is limited. Particular consideration is given to better regulation and achieving greater efficiency in public administration, although the plan does not discuss better regulation challenges in detail. Some important issues related to competition are not sufficiently addressed, in particular as far as the retail sector and the electricity market are concerned. For example, for the latter, improving interconnection with neighbouring countries is essential.

12. As regards infrastructure and sustainable development, the NRP refers to the Strategic Plan for Infrastructures and Transport and identifies a very complete set of objectives for road and rail networks for 2020, but does not set intermediate targets. Increased energy efficiency and decreased CO<sub>2</sub> emissions are also presented as overarching objectives.
13. Overall, the list of micro-economic policies put forward in the NRP appears relevant and should contribute to increasing productivity growth. However, except for R&D and infrastructure, it is difficult to assess the exact scope and likely impact of the measures based on the programme. The specific needs of SMEs deserve greater attention.

### **Employment policies**

14. Together with convergence in income per capita, increasing the employment rate to 66% by 2010 is the overarching objective of the NRP. Raising female employment is considered crucial in this respect and the NRP sets a target of increasing the employment rate of women from 48.3% in 2004 to 57% by 2010. The programme also seeks to address the segmentation of the labour market caused by the proportion of fixed-term contracts, which is the highest in the EU. Increasing investment in human capital through better education and skills is also considered a key priority to sustain employment and productivity growth. The Commission supports all these objectives.
15. In order to attract and retain more people in employment, measures focus on increasing the participation of women, older workers, young people and disadvantaged groups, including migrant workers. These measures include the revision of incentives for early retirement, an income tax reform and increasing the number of places in public childcare facilities, as part of a wider endeavour to modernise the social protection system. The objective of increasing public care facilities for children under three by 2% a year is helpful but would seem insufficient given the size of the challenge. While the high level of youth unemployment is considered a priority, the programme builds on existing policies and no new measures are presented. It also sets the target of reducing the current youth unemployment rate to close to the EU average by 2010 (from 22.1% to 18.7%).
16. The NRP includes measures to reduce the use of fixed-term contracts through a review of different contract types and their respective costs. These, along with measures to promote self-employment and improve health and safety at work, would constitute a first step in addressing the segmentation of the labour market. However, overall progress in improving the functioning of the labour market and the adaptability of workers and enterprises will depend on the outcome of current dialogue between social partners. Particular attention is given in the NRP to the collective bargaining agreement signed by the social partners in March 2005, which covers wage moderation. Measures to develop the market for rental housing seem likely to facilitate geographical mobility.
17. Measures to foster human capital are taking shape through a recently-adopted framework Law on education and a new joint system for occupational and continuous vocational training, due for adoption on January 2006. Action focuses on preventing learning problems in primary education, better integrating children of

immigrant origin in schools, developing the use of foreign languages and ICT, supporting higher education reforms and developing lifelong learning. Important commitments are made, although for most measures without funding being specified. The commitment to halve early school leaving by 2010 seems realistic. It will require a significant effort to achieve the objectives of 80% of 24-year-olds completing upper secondary education and of increasing the share of population in continuous training from 5.2% to 12.5% by 2010.

18. Overall, the programme reinforces the employment objectives set in previous national action plans for employment, at least in so far as most of the fairly ambitious but realistic targets are concerned. Measures would in general benefit from greater clarity, including more consideration of regional disparities, more specific information on action to raise female employment and clearer references to budgetary means. Success will depend to a large extent on the results of the on-going process of social dialogue.

### **PART III: CONCLUSIONS**

19. In line with the Integrated Guidelines, the Spanish National Reform Programme identifies and responds to the main challenges facing Spain, namely budgetary stability; R&D strategy; a better environment for business; the achievement of higher competition; infrastructure development; a better functioning of the labour market; and better education and human capital. Overall, the NRP is ambitious, coherent and fairly comprehensive. It builds appropriately on existing policies, although prioritisation between measures could be improved.
20. An extensive set of indicators is provided to help monitor implementation. However, timetables, budgetary implications and clear links with the use of EU funding are often missing, making it difficult to assess the practicability of measures. It will be important to involve stakeholders in implementing the NRP, thus spreading ownership beyond governmental circles.
21. The programme's strengths include:
  - continuing efforts on achieving greater budgetary stability over the economic cycle;
  - the comprehensive R&D and innovation plan set out;
  - the complete set of objectives for road and rail networks in the Strategic Plan for Infrastructures and Transport.
22. Among the points requiring further attention are:
  - competition issues, in particular in the retail and electricity sectors, for example by improving interconnection with neighbouring countries.
  - the segmentation in the labour market, the need to increase female employment;
23. Taking due account of the above, Spain is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in

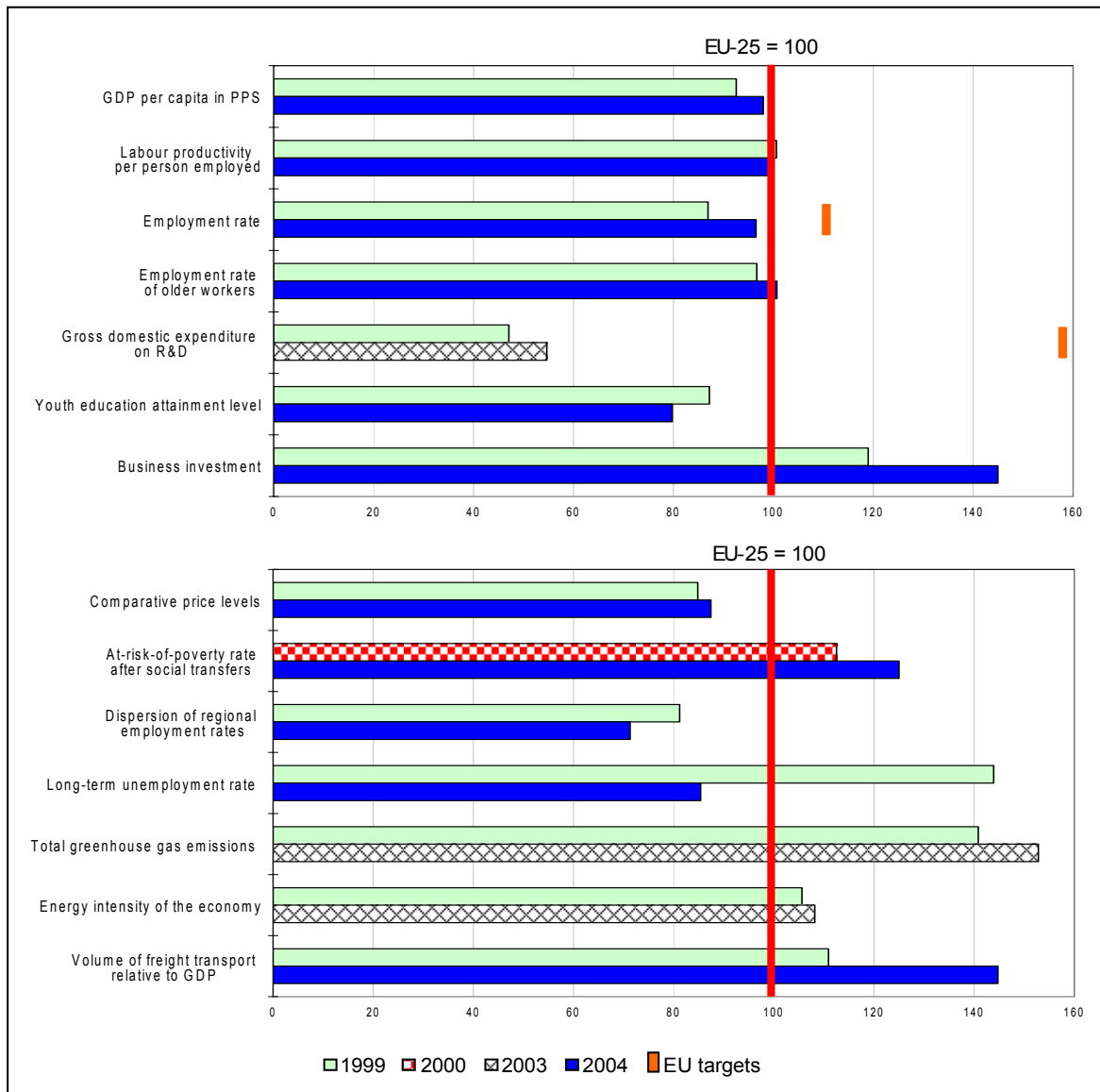


particular the way Spain has dealt with the issues mentioned in paragraph 22. In this context, the Commission looks forward to discussions with the Spanish authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

# SPAIN

	ES							EU-25								
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target		
GDP per capita in PPS	92.6	92.8	93.5	95.6	97.8f	98.0f	66.0	100.0	100.0	100.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	100.6	98.2	97.9	99.3	100.5	99.9		100.0	100.0	100.0	100.0	100.0	100.0		100.0	
Employment rate	53.8	56.3	57.8	58.5	59.8	61.1		61.9	62.4	62.8	62.8	62.9	63.3			
Employment rate of older workers	35.0	37.0	39.2	39.6	40.7	41.3		36.2	36.6	37.5	38.7	40.2	41.0			
Gross domestic expenditure on R&D	0.88	0.91	0.92	0.99	1.05	:		2.0	1.87e	1.89e	1.93e	1.93e	1.92e		1.90pe	3.0
Youth education attainment level	65.2	65.9	64.8	64.0	62.1	61.1		74.8	76.3	76.1	76.5	76.5	76.6			
Comparative price levels	84.8	85.0	85.1	85.0	86.6	87.4p		100.0	100.0	100.0	100.0	100.0	100.0p			
Business investment	21.3	22.8	22.6	22.7	23.5	24.5		17.9	18.3	17.7	17.1	16.7	16.9			
At-risk-of-poverty rate after social transfers	19.0	18.0	19.0	19.0b	19.0	20.0b		:	16.0	15.0	15.0	15.0	16.0			
Dispersion of regional employment rates	10.8	10.7	10.0	9.3	9.0	8.7		13.3	13.4	13.5	13.3	12.9	12.2			
Long-term unemployment rate	5.9	4.8	3.9	3.9	3.9	3.5		4.1	3.9	3.8	3.9	4.0	4.1			
Total greenhouse gas emissions	127.6	133.0	132.6	139.3	140.6	:		90.6	90.5	91.4	90.7	92.0	:			
Energy intensity of the economy	227.0	227.0	225.4	226.3	226.6	:		214.9	208.8	209.7	206.5	209.5	:			
Volume of freight transport relative to GDP	111.7	117.7	122.5	135.4	137.1	151.4		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e			



## Sweden

1. Sweden is in a good position with respect to GDP per capita (118% of EU average in 2004), productivity and employment levels. Real GDP growth has been slightly below 3% on average over the last decade. Labour productivity growth has been just above the EU average. The employment rate is one of the highest in the EU (72.1% in 2004). However, over recent years employment growth has been weak and employment rates have declined, while unemployment (6.3% in 2004) has increased.

### **PART I: GENERAL ASSESSMENT**

2. The Swedish National Reform Programme (NRP) puts a strong emphasis on sustainable development and integrates this theme into the social, economic and environmental policies set out. The NRP does not explicitly set clear priority areas but emphasises high labour market participation and hours worked and promotes a knowledge-based economy with environmentally efficient production processes. The Commission broadly supports this approach but also regards competition in services as a key area for attention.
3. The strategy of the NRP is broad, guided by the notion of sustainable development. The NRP spells out long-term ambitions under each guideline, emphasises continuity with existing policies and appears realistic. Timetables for implementing measures are not in most cases given and budgetary information is not always complete. The NRP does not always provide a full strategic vision and more priority setting would improve this. Some measures still need to be made more concrete. The NRP mentions ambitious targets for employment rate (80% for 20-64 year olds) and for publicly financed R&D (the annual target of 1% of GDP). No overall national target for investment in R&D is mentioned in the NRP, but at 3.75% of GDP (2004) recent investment has been high, against the background of the overall target for the EU of 3%. Relatively little new policy is set out in the section dealing with competition in services. Measures already proposed in the 2006 budget are described in more specific terms than those for subsequent years, although the NRP signals many reports and studies in the pipeline that may lead to interesting additional measures during those years. The NRP also describes how EU structural funds will be used to promote the objectives.
4. Consultation and efforts to develop ownership of the document have been fairly substantial. The Programme was formally endorsed by the Government and presented to Parliament for discussion. Meetings to consult social partners, including local and regional public authority employers, and civil society were arranged.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

5. The macro-economic strategy presented in the NRP is a continuation of policies already in place for a number of years. The strategy aims for sound public finances, low and stable inflation and wage setting in line with productivity. The NRP

acknowledges that, in the medium to long term, reaching a high level of employment and hours worked in the economy are important to sustain public welfare commitments, a view shared by the Commission.

6. The macro-economic strategy implies that fiscal policy will continue to be set within a general government budget surplus objective of 2% of GDP on average over the economic cycle and within rolling 3-year nominal expenditure ceilings. The NRP emphasises the continued need for social partners to set wages in a responsible way, supported by the national mediation office. The general government budget balance is forecast to remain in surplus over the period, but below the 2% objective. Were it to do so, the funds that could be built up would be an important element in meeting the budgetary demands created by the ageing of the population.
7. The NRP mentions ongoing investigations into the efficiency of the welfare insurance systems and the appropriateness of the way responsibilities are divided across different levels of government. The proposals based on this work may prove to be important for the long-term provision of public welfare services. The NRP mentions that the government intends to conduct a general overview of the tax system taking into account changes both in that system and in the economy as a whole since the 1990/91 reform. This work may also yield important efficiency benefits contributing to growth and incentives to work.
8. Overall, there is no urgent macro-economic challenge for Sweden and the stability-oriented framework is well designed. There is nothing in the short-term outlook that appears likely to prevent Sweden continuing to achieve its macro-economic policy objectives.

### **Micro-economic policies**

9. The micro-economic policy priorities are R&D, innovation, and ICT diffusion. The business environment and strengthening competition policy are cited as the key areas for action. The NRP sees the knowledge-based economy as its main objective.
10. R&D, innovation and ICT diffusion are identified by the government as key challenges in the context of the national “Innovative Sweden strategy”. The NRP sets clear priorities in these areas and shows a readiness to finance them. These priorities are: strengthening the role of industrial research institutes as a bridge between science and industry; improving the commercialisation of R&D; and strengthening research and training of researchers. Concerted measures to improve the intellectual property regime are set out. While the NRP contains some measures for SMEs, there would be scope for further measures focusing on research-driven and innovative SMEs, particularly encouraging links with larger firms. On ICT, the objective of a recently adopted law is a sustainable information society for all, to be complemented by a national action plan on electronic procurement and an increase in R&D investment on ICT.
11. To increase entrepreneurship, weak by international comparisons, the government plans to create a more competitive business environment. An action programme to reduce administrative costs to enterprises is being implemented, including a target to reduce such burdens arising from tax legislation by 20% by 2010. More targets will be set in 2006. Improving the use of impact assessment is mentioned, but without

information on specific implementation measures. Six sectoral industrial strategies are proposed to strengthen the competitiveness of the industrial base. Improving co-operation between industry, government, and universities at national and regional level will play an important role in this. The implementation of the long-term strategic framework on transport infrastructure, including a prioritised Trans-European Transport Network project, will contribute to links between major Swedish cities and the rest of Europe. The NRP envisages that Sweden's competitiveness increasingly will build on environmentally-friendly production processes. In particular, measures for green electricity certificates, financial support for wind power, investment programmes for renewables and energy efficiency in the construction and renovation of buildings are included.

12. The NRP acknowledges the need to strengthen competition policy and a government appointed commission is looking into streamlining the legal framework governing competition cases. No specific measures to remove barriers to entry in services markets are set out. While the NRP acknowledges that Sweden will need to adjust national rules to future EU legislation, it makes no specific commitments or initiatives to increase competition in key service sectors.
13. As regards the efficiency of the public sector, the e-government proposals are appropriate, but lack a precise timetable for implementation. No concrete measures are presented in the NRP to encourage outsourcing and benchmarking in the public sector or to strengthen the prevention of direct procurement contravening EU law.
14. The Commission's assessment of the innovation and ICT strategies is positive. Additional micro-economic measures could usefully be taken to promote a more effective market for services and improve the efficiency of the public services. The emphasis on sustainable development in the micro-economic chapter, and in particular the series of measures that will increase energy efficiency and improve the environment can help drive growth over time.

### **Employment Policies**

15. The NRP identifies increased labour supply through higher labour force participation and more working hours as a high priority given the ageing population and the current high level of welfare services. The Commission shares this view.
16. To attract more people into employment, Sweden maintains its commitment to achieve as soon as possible its existing targets on employment rate (80% for 20-64 year olds) and unemployment rate (4%). The main priority is a reinforced active labour market policy to tackle the recent increases of youth, long-term and overall unemployment, and to help the young, immigrants and disabled persons into work. The NRP recognises the need to improve the integration of immigrants into the labour market and to tackle discrimination given the high employment gap between immigrants and native born Swedes (16 percentage points). The NRP proposes a number of measures, including rehabilitation and work-based solutions, to reduce sick leave and entrants into disability pension – some progress has been made on this already. However, the large number of people already on disability pensions receives less attention and makes more active measures necessary for these people. A better balance between incentives and a substantial social safety net in the tax and benefit

systems remains a challenge, in view of a persistently high unemployment trap and a high tax wedge on labour.

17. Plans to address the adaptability of workers and enterprises mainly relate to issues such as the right to full-time employment, the use of temporary employment, subsidies for mobility and preventing undeclared work. With the currently high gender pay gap (16% unadjusted), the future action plan to eliminate gender-based wage discrimination is a positive move.
18. Sweden exceeds all the EU benchmarks for investment in human capital. The NRP focuses on the need to develop further improve quality throughout the education system and to increase equality in levels of attainment. The government's target that at least 50% of 25-year olds should begin higher education seems challenging but achievable. The NRP is weak on skills development in the workplace and participation in lifelong learning by the low-skilled, is currently lower than participation by men and women with higher skills, remains a priority.
19. Overall, the NRP provides a fairly ambitious yet not entirely complete response to the challenge of increasing labour supply. The NRP addresses most of the key areas but would have deserved a more in depth consideration of issues like unemployment and inactivity traps, maintaining a continued high labour supply of older workers and reducing the number of people on disability pensions.

### **PART III: CONCLUSIONS**

20. In line with the Integrated Guidelines, the Swedish National Reform Programme identifies and responds to most of the main challenges facing Sweden, emphasising namely high labour market participation and hours worked and promoting a knowledge-based economy with environmentally efficient production processes. However, competition in services is a key issue only partially addressed in the NRP. Overall the programme is broad, builds appropriately on existing initiatives and recent economic successes and sets out clear and realistic long-term ambitions. It includes many innovative measures underpinned by a strong effort to reinforce the three pillars - economic, social and environmental - of sustainable development. The programme's strategic vision and practicability could be enhanced by more prioritisation.
21. Timetables for implementing measures are not in most cases given and budgetary information is not always complete. Some measures could be described further. The NRP refers to various reports and studies that may give rise to further initiatives in the second half of the 2005-2008 implementation period.
22. The programme's strengths include:
  - the high priority and the associated funding commitment for promoting R&D, innovation and ICT;
  - the comprehensive approach to integrating environmental and energy aspects in the production process;

- measures to reduce unemployment, including reinforced active labour market policies.

23. Among the points requiring further attention are:

- enhancing competition in services;
- increasing labour supply, including by addressing incentives in tax and benefit systems.

24. Taking due account of the above, Sweden is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way Sweden has dealt with the issues mentioned in paragraph 23. In this context, the Commission looks forward to discussions with the Swedish authorities as part of the new partnership for growth and jobs.

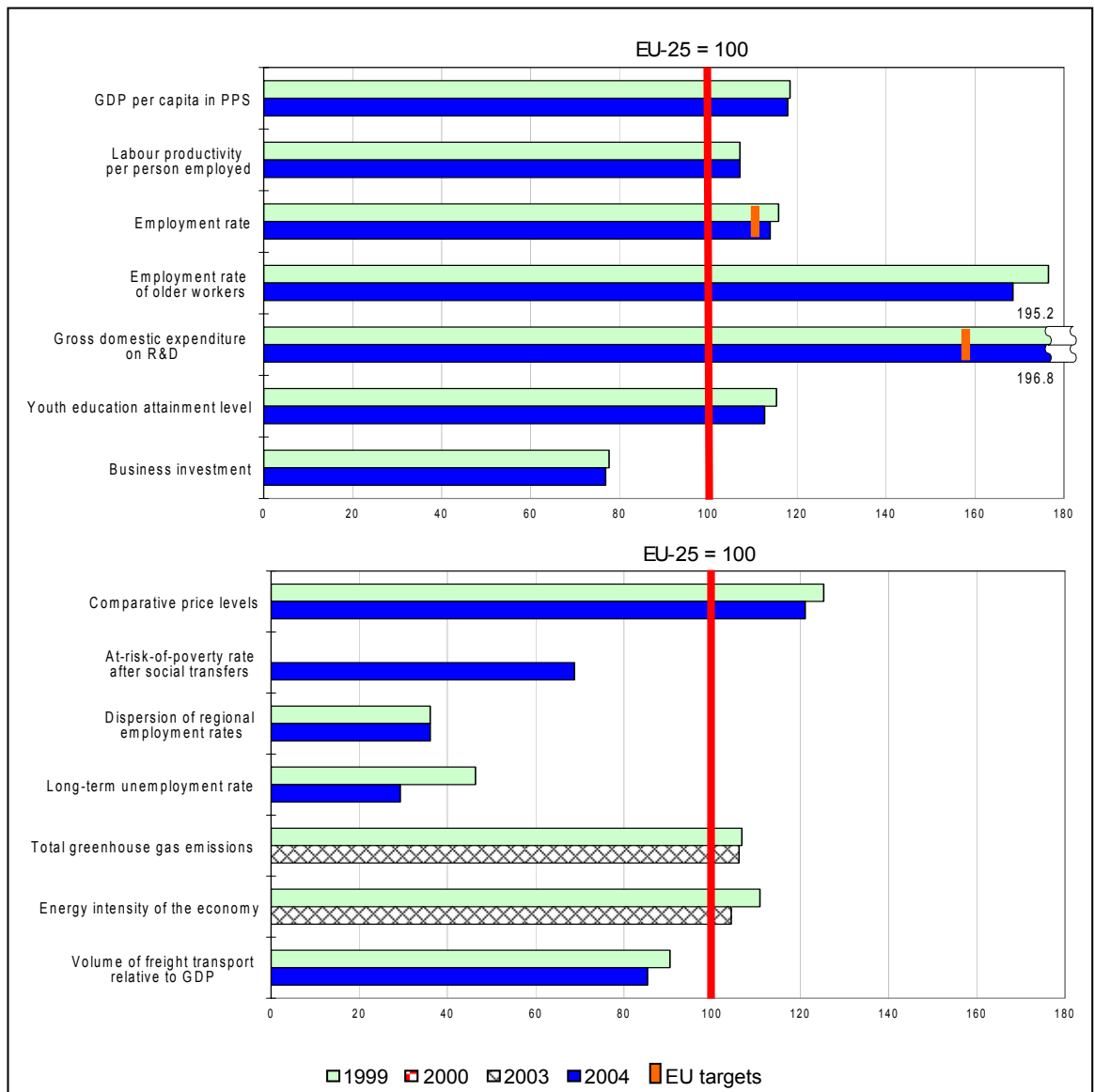
#### **PART IV : STATISTICAL GRAPHS AND DATA**

# SWEDEN

	SE							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	118.4	119.6	115.7	114.2	116.4	117.9		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	107.1	107.3	103.2	102.1	104.6	107.1		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	71.7	73.0	74.0	73.6	72.9	72.1	*	61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	63.9	64.9	66.7	68.0	68.6	69.1		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	3.65	:	4.27	:	3.98	3.74	**	1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	86.3	85.2	85.5b	86.7	85.6	86.3		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	125.3	126.7	117.0	121.1	124.0	121.1p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	13.9	14.7	14.3	13.3	12.9	13.0		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	8.0	:	9.0	11.0b	:	11.0b		:	16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	4.8	4.5	4.2b	4.6	4.3	4.4		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	1.9	1.4	1.0	1.0	1.0	1.2		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	96.7	93.0	94.4	96.1	97.6	:		90.6	90.5	91.4	90.7	92.0	:	
Energy intensity of the economy	238.2	215.0	228.9	224.3	218.6	:		214.9	208.8	209.7	206.5	209.5	:	
Volume of freight transport relative to GDP	91.1e	93.1	88.8	90.6	90.8	89.3		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	

\* National target: 80% for the population aged 20-64

\*\* National target: 1% (2010) for the public sector





## United Kingdom

1. The United Kingdom's real GDP grew 3.2% on average in 1996-2000, well above the EU average, with GDP per capita at 117% of the EU average in 2004. GDP continued to grow relatively well with favourable labour market outturns. Labour productivity growth has been a bit faster than the EU average. The employment rate at 71.6% is high and exceeds the Lisbon target. The unemployment rate has been broadly stable and is at an historic low (4.7% in 2004).

### PART I: GENERAL ASSESSMENT

2. The UK National Reform Programme (NRP) sets out broad policy priorities: maintaining fiscal sustainability in the face of demographic challenges; building an enterprising and flexible business sector; promoting innovation and R&D; widening opportunities for the acquisition of skills; increasing innovation and adaptability in the use of resources; and ensuring fairness through a modern and flexible welfare state. The Commission broadly shares the NRP's analysis of the main priorities but notes that improving transport infrastructure is also an important challenge in some regions.
3. The UK has already made considerable progress in structural economic reforms and the NRP largely reflects existing strategies. Some potential synergies between different policies are not addressed. The NRP presents a series of measures that are likely to build on to the successful structural economic reforms already undertaken in the UK through further opening markets, encouraging employment and improving the business environment. However, a number of other important challenges remain such as the fiscal balance, the efficiency of public expenditure, the quality of transport infrastructure, skill levels, pension reform and R&D policy. The UK already exceeds the employment rate target of 70% set for the EU as a whole. The NRP refers to a target of 80% for the long term, although there is no target for 2010. In addition, the government has set an R&D investment target of 2.5% of GDP for 2014, against the background of the overall target for the EU of 3% by 2010. The UK sets no target for that date, but will review progress to the UK's own target and calibrate policy on an annual basis. The role of Structural Funds in supporting the NRP is not fully explained.
4. Consultation and efforts to develop ownership of the document have been rather limited. The UK NRP was issued by H.M. Treasury. Some consultation took place, for example with the devolved administrations responsible for Scotland, Northern Ireland and Wales, but wider consultation could have strengthened the integration and ownership of the NRP. Annexed to the NRP is a joint declaration with the Irish Government on North/South cooperation to promote growth and jobs throughout the island of Ireland. A short stakeholder consultation was undertaken over the summer to gauge general interest in the Lisbon Strategy.

### PART II: ASSESSMENT BY POLICY AREA

#### Macro-economic policies

5. In terms of macroeconomic strategy, the NRP focuses on efficiency improvements to public expenditure and new initiatives for pension provision. Improving the structural fiscal balance is a challenge for fiscal policy not addressed in the NRP.
6. On the quality of public finances, the government has set an ambitious target to improve the efficiency of public spending, involving redirecting some £20bn (€29bn or 1.7% of GDP) to priority spending areas by 2007/08. The redeployment of resources to frontline health services should increase their effectiveness, but more emphasis could be given to reducing sickness costs for businesses. The NRP could have specified in more detail the monitoring mechanism and the incentives for efficiency improvements, especially in some cases where achieving savings might be particularly challenging. The 2007 Comprehensive Spending Review is expected to assess further the effectiveness of central government expenditure.
7. On public and private pension provision, the NRP reviews a number of existing policy initiatives. The low level of public pension provision is one of the determinants of the favourable long-term outlook for UK public finances. However, projected public and private pension provision appears insufficient to avoid a growing imbalance between income in work and in retirement, despite recent reforms. The report from the Pensions Commission published on 30 November 2005 suggests a possible way forward for further pension reforms.
8. Improving the structural fiscal balance is a remaining challenge. The macro-economic framework underpinned a significant fiscal consolidation in the late 1990s but the fiscal situation has deteriorated since 2002. There is a risk that revenues will continue to be below initial projections so that the deterioration of the structural balance might not be reversed sufficiently.
9. The Commission's overall analysis of the macro-economic chapter of the UK NRP is that the reforms to large areas of public expenditure, provided the necessary further efforts are made to deliver them, should provide significant efficiency benefits. On pensions, it is too early to tell whether current policy deliberation will lead to the extensive revisions necessary. The NRP gives insufficient attention to the improvement of the structural fiscal balance.

### **Micro-economic policies**

10. The UK authorities have identified R&D and innovation and the encouragement of entrepreneurship as key micro-economic challenges. The Commission broadly shares this analysis but also identifies the quality and efficiency of the transport infrastructure as a key theme because of its importance for productivity growth.
11. The mix of measures for R&D and innovation broadly matches the longer term UK policy priorities, as identified by recent strategic reviews such as the Lambert report on business-university links. In particular, the 10-year Science and Innovation Investment Framework can help rectify a period of consistent under-investment. The NRP, however, mainly describes existing schemes and measures. Further policy initiatives will be needed in order to achieve the government's 2.5% R&D target for 2014. A timetable and intermediate investment targets for 2008 and 2010 are missing, and few details are given on the expected impact of the proposed measures on business R&D investment and innovation. The development of innovation

clusters linked to universities and cross-border knowledge transfers are issues that could be examined in more detail.

12. Funding of railway infrastructure has been substantially increased and the London congestion charge has proved successful. However, the NRP would be enhanced by more measures to improve other specific transport needs outside London and the South East, particularly accessibility to local employment opportunities. The NRP contains interesting policies on innovation for improved energy and resource efficiency, but more could be done to increase energy efficiency and to promote environmental technologies.
13. Concerning the business environment, the UK identifies encouraging entrepreneurship and better regulation as key priorities. The NRP mentions a number of recent SME initiatives, some implemented successfully using significant support from Structural Funds. Nevertheless, more could be done to reduce the time period for business VAT registration, to tackle the recent decline in entrepreneurship among ethnic minorities and to achieve the very ambitious target set for female entrepreneurship. Current better regulation initiatives include: improvements to regulatory impact assessment guidelines, cross-government initiatives to reduce administrative costs and measures to simplify legislation and tax administration.
14. UK competition policy appears to be working well and contributes to the development of an open and dynamic internal market. The on-going market reviews by the Office of Fair Trading (OFT), particularly that on public subsidies, will assist in maintaining and further improving this, as will the independent review of legal services. The UK's review of the Financial Services and Markets Act allows for the speeding up of the implementation of the EU Financial Services Action Plan.
15. On the microeconomic challenges, whilst clear progress is being made in some areas from a strong policy base, additional policy initiatives will be required to ensure the achievement of the UK government's own R&D target for 2014 and in order to sufficiently improve the quality and efficiency of transport infrastructure.

### **Employment policies**

16. The UK NRP refers to the aspiration of raising the employment rate to 80% over the long term, but sets no targets for 2008 and 2010. Raising employment is to be achieved through increasing employment opportunity for all, removing barriers to participation and 'making work pay'. Increasing skills in the workforce, particularly at low and intermediate levels, is identified as key to productivity growth. The UK also recognises other on-going concerns, especially over labour market integration of vulnerable groups.
17. Key to achieving this ambitious target for attracting and retaining more people in employment will be the integration into the labour market of vulnerable groups such as incapacity benefit claimants, disabled people, lone parents, some ethnic minority groups, older people and those from areas of high deprivation. Barriers to participation in work are addressed through individually tailored support to increase employability and help people find jobs as well as by skills improvement and additional measures to 'make work pay'. As the focus of activation measures shifts to harder to reach groups, success will depend upon ensuring the continued capacity of

public employment services to intervene flexibly according to the needs of individuals, in the context of substantial administrative efficiency savings, as well as on the strength of private sector labour demand. In addressing the particularly large number of people inactive for reasons of ill-health or disability, a pilot scheme “Pathways to Work” is showing encouraging results. The scheme combines employment advice, health support and financial incentives to take up work. Notwithstanding considerable recent improvements in the availability and affordability of childcare, further progress on both aspects is needed for all parents to have a real choice to work.

18. On adaptability of workers and enterprises, there is a clear commitment in the NRP to drive productivity improvements by addressing skills challenges, particularly for low-skilled adults, and enhancing human capital. Growing emphasis is placed on the responsibilities of employers and individuals to invest in education and training, supported by incentives. The dovetailing of national/regional skills strategies and newly-created Sector Skills Councils will be vital in ensuring effectiveness. Reforms to secondary curricula seek to provide more flexible learning pathways and reduce high levels of early school leaving, to improve qualification levels and eliminate skill mismatches.
19. Overall, the employment approach is well-balanced and focused on achieving results in areas of identified weakness and piloting solutions. Against the background of the already high employment rate of 71.6%, the initiatives to engage various groups in the labour market are likely to make a positive contribution.
20. The commitments made in the NRP to address the skills challenge are indispensable in order to improve the situation on the ground. Though concerted efforts have been made to address issues such as the low level of job retention and the working poor through the introduction of the national minimum wage and child and working tax credits, further efforts are still required.

### **PART III: CONCLUSIONS**

21. In line with the Integrated Guidelines, the UK’s National Reform Programme identifies and responds to the main economic challenges facing the UK, namely maintaining fiscal sustainability in the face of demographic challenges; building an enterprising and flexible business sector; promoting innovation and R&D; widening opportunities for the acquisition of skills; increasing innovation and adaptability in the use of resources; and ensuring fairness through a modern and flexible welfare state.. Overall the NRP is coherent and contains many concrete, ambitious and original measures appropriate to build on successful structural reforms already undertaken, though integration across different policy areas is not always fully evident.
22. More detail on timetables, monitoring and evaluation methods would be necessary to allow a comprehensive assessment of the likely effectiveness of the measures proposed. Involving stakeholders in the implementation phase will be important in order to increase ownership and the effective application of policies on the ground.

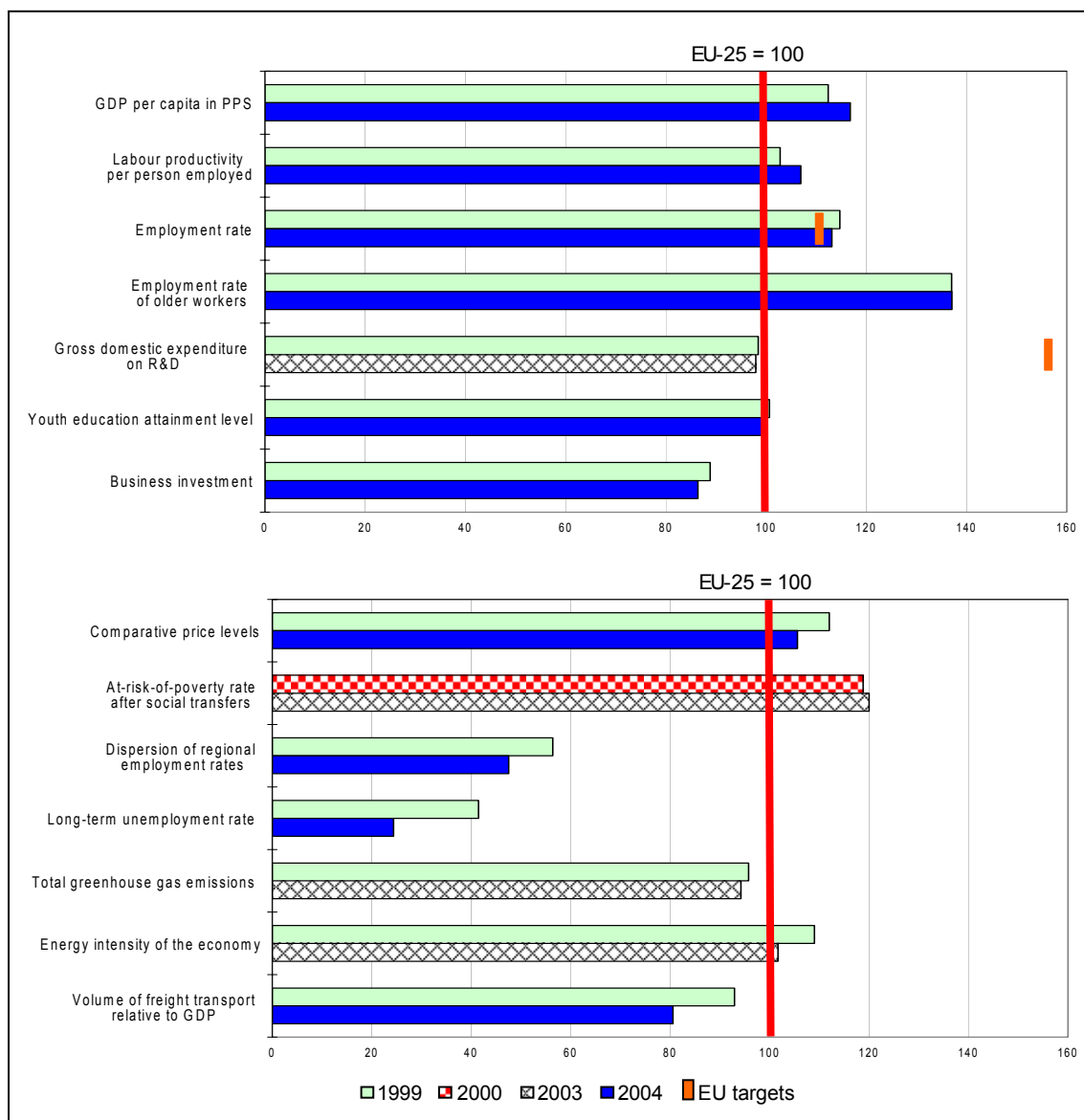
23. The programme's strengths include:
- the better regulation initiatives;
  - the "Pathways to Work" pilot initiative to assist incapacity benefit claimants to re-enter the labour market;
  - policies on competition and entrepreneurship.
24. Among the points requiring further attention are:
- budgetary consolidation, in the light of the need to upgrade transport infrastructure and to ensure an adequate pension system;
  - additional policy initiatives to boost R&D and improve transport infrastructure;
  - efforts to address skills challenges and to improve employment prospects for the most disadvantaged.
25. Taking due account of the above, the UK is invited to implement its NRP with vigour. The 2006 progress report on the implementation of the NRP should cover in particular the way the UK has dealt with the issues mentioned in paragraph 24. In this context, the Commission looks forward to discussions with the UK authorities as part of the new partnership for growth and jobs.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

## UNITED KINGDOM

	UK							EU-25							
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target	
GDP per capita in PPS	112.4	113.1	113.7	116.6	116.7	116.8f	* 2.5 (2014)	100.0	100.0	100.0	100.0	100.0	100.0	70.0	
Labour productivity per person employed	102.8	104.1	105.5	108.0	107.3	106.9		100.0	100.0	100.0	100.0	100.0	100.0		
Employment rate	71.0	71.2b	71.4	71.3	71.5	71.6		61.9	62.4	62.8	62.8	62.9	63.3		
Employment rate of older workers	49.6	50.7b	52.2	53.4	55.4	56.2		36.2	36.6	37.5	38.7	40.2	41.0		
Gross domestic expenditure on R&D	1.84	1.84	1.89	1.89	1.88	:		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe		3.0
Youth education attainment level	75.3	76.4	77.0	77.2	78.1	76.4		74.8	76.3	76.1	76.5	76.5	76.6		
Comparative price levels	112.0	117.3	114.3	110.7	103.8	105.6p		100.0	100.0	100.0	100.0	100.0	100.0p		
Business investment	15.9	15.7	15.2	15.1	14.3	14.6		17.9	18.3	17.7	17.1	16.7	16.9		
At-risk-of-poverty rate after social transfers	19.0	19.0	18.0	18.0	18.0	:		:	16.0	15.0	15.0	15.0	16.0		
Dispersion of regional employment rates	7.5	7.1	6.8	6.6	6.1	5.8		13.3	13.4	13.5	13.3	12.9	12.2		
Long-term unemployment rate	1.7	1.4	1.3	1.1	1.1	1.0		4.1	3.9	3.8	3.9	4.0	4.1		
Total greenhouse gas emissions	86.8	86.7	88.3	85.7	86.7	:		90.6	90.5	91.4	90.7	92.0	:		
Energy intensity of the economy	234.3	227.3	223.7	214.5	213.1	:		214.9	208.8	209.7	206.5	209.5	:		
Volume of freight transport relative to GDP	93.6	89.6	87.2	85.5	84.8	84.3p		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e		

\* National target: 80% following the national definition



## **Euro Area**

1. Since the launch of the Lisbon strategy in 2000, the annual growth rate for the euro area averaged 1.8% per year, lagging behind its main competitors. Hourly productivity rose 1.2% yearly between 1999 and 2003 and exhibited a declining trend. The employment rate rose from 60.6% in 1999 to 63% in 2004, whereas unemployment declined just marginally, from 9.1% in 1999 to a still high 8.9% in 2004. Employment rates for older workers and for women remained particularly low, at 38.6% and 54.5% in 2004.

### **PART I: GENERAL ASSESSMENT**

2. The euro area is more than just the sum of its parts. Membership to the Economic and Monetary Union (EMU) places a particular premium on effective policy coordination to ensure fiscal discipline and structural reforms that enhance the capacity for absorption of asymmetric shocks and to preserve price stability, low interest rates and the euro's exchange rate. In this respect, the Integrated Guideline No. 6 calls on the euro area Member States to contribute to a dynamic and well-functioning EMU.
3. The National Reform Programmes (NRPs) of the euro area countries rightly place particular emphasis on sustainability of public finances and the need to boost labour productivity through R&D, innovation and an attractive business environment and on increasing employment and participation rates. On the other hand, some important challenges such as competition in services appear to have been omitted in many NRPs.
4. The euro area countries present rather comprehensive and mostly forward-looking and consistent strategies. However, their in-depth assessment is made difficult due to limited level of detail on measures, targets, timetables and resources involved. Only some euro area programmes present quantitative targets for R&D or employment rates. Possible budgetary implications of reforms are in most cases missing. Moreover, the Programmes widely rely upon already foreseen measures which amount to just incremental improvements, rather than highly ambitious new strategies.
5. The NRPs also generally demonstrate the commitment of the national governments to the renewed Lisbon strategy. All the governments have adopted the Programmes and invited parliaments to discuss them. Social Partners were involved to some degree, whereas this was rare as regards local and regional authorities.

### **PART II: ASSESSMENT BY POLICY AREA**

#### **Macro-economic policies**

6. The euro area needs coordinated policies that achieve and maintain sound and sustainable macro-economic positions thereby contributing to a policy-mix which helps its economy to become more dynamic and resilient. Since national interest rate

and exchange rate instruments are no longer available, particular emphasis is necessary on achieving and maintaining sound budgetary positions over the cycle which will provide sufficient budgetary margin to help absorb through the working of automatic stabilisers the impact of cyclical fluctuations. Fiscal discipline is also a precondition for promoting long-term growth as well as creating the capacity to respond to future fiscal policy challenges stemming from population ageing.

7. The Programmes identify fiscal discipline, both short-term budgetary stability and long-term sustainability of public finances, as their main challenge in the area of macro-economic policies. Other challenges considered in the NRPs are efficiency of public administrations and quality of public finances, including reforms of social security and pension schemes as well as health care reforms. Nonetheless, the measures proposed to achieve the budgetary consolidation are often not sufficiently detailed thereby involving risks as regards the targets to be achieved and the timetables envisaged.
8. The fiscal consolidation strategies highlighted in the NRPs are typically expenditure-based. In general fiscal consolidation is embedded in a broader structural reform effort. The budgetary implications of the actions envisaged in other policy areas, such as employment and social policies, are seldom spelled out. To some extent one-off measures to support the process of budgetary consolidation (such as the privatisation of state assets) have been presented. A number of measures have been launched to reform pension schemes, health care and social security systems. Concerning policies for improving the quality of public finances, the euro area members typically refer to national strategies for strengthening infrastructure, human capital and R&D investment.
9. The euro area deficit is estimated at 2.9% in 2005 and according to the Commission services' autumn 2005 forecast, the deficit is expected to diminish again marginally in 2006, based on unchanged policies, and to stabilise in 2007 in the context of a moderate economic recovery. Accordingly, the upward trend in the debt ratio would continue, albeit at a diminished pace. Despite recently announced measures to strengthen the adjustment, overall, the measures announced are unlikely to significantly improve the situation. A number of Member States will still have budgetary deficits above the reference value in 2007.
10. The Programmes often neglect to take into account, and thereby give due priority, to reforms that, justified at national level, can also enhance the ability of the euro area as a whole to adjust smoothly to shocks and the changing economic environment. Some of the reforms envisaged can be expected to reinforce such resilience, for example, through support for easier matching of demand and supply in the labour market, more adaptable workforce and 'better regulation' initiatives to foster business dynamism. However, attention should be paid too to the importance of wage developments, wage flexibility and wage differentiation and to product market reforms that will increase competition and will improve the functioning of the Internal Market.

#### **Micro-economic policies**

11. Comprehensive structural reforms in product, services and capital markets are particularly important for the euro area to increase its adjustment capacity. Moreover,



in the view of the persistence of growth differences across some euro area Member States structural reforms are necessary to boost the responsiveness of the economy through changes in prices (the so-called competitiveness adjustment mechanism).

12. Promoting R&D and innovation are singled out in the euro area programmes along with improving business environment and entrepreneurship. Further key challenges are the strengthening of competition and the opening up of markets. The efficiency of public administrations, upgrading infrastructures and promoting ICT investment and use are identified to a lesser degree. The Commission generally subscribes to these priorities though notes that the competition challenge, notably in services and network industries, is not treated well enough.
13. R&D expenditures in the euro area stand at around 2% of GDP, thus significantly short of the EU-wide objective of 3%. In terms of public R&D expenditures, the Programmes foresee further increases in spending and outline measures to increase efficiency of public research. To achieve the overall objective on R&D, it is crucial to enhance more private spending in R&D. Several Programmes intend to use tax incentives and/or to make the regulatory or institutional framework more supportive for innovation, in particular among SMEs. Several Programmes also propose to identify and support clusters and innovation poles, although cross-border cooperation between them is not addressed.
14. The Programmes acknowledge the need for better business environment for companies and in particular, for SMEs. Measures to improve business environment include better regulation, easier market entry and exit, tax reforms, reforms of public administration, diffusion of ICT and upgrading infrastructures. These measures, together with those in the labour markets, are likely to lead to some reduction in costs for business and contribute positively to economic dynamism.
15. A well functioning and competitive Internal Market is particularly important for the euro area as a whole inasmuch as it will enhance its capacity to adjust smoothly to asymmetric shocks. The Programmes should address more explicitly how to reduce current transposition deficits and the number of pending infringement cases. Likewise more concrete measures should aim to increase effective competition in services and network industries and remove the significant remaining barriers in these sectors.
16. Microeconomic measures go broadly in the right direction, particularly the measures to boost R&D or to improve business environment, including better regulation. It is also however not clear whether the measures proposed to raise business R&D will be sufficient to achieve the stated objectives. In addition, the essential issues of increasing competition and improving the Internal Market have not been given appropriate attention.

### **Employment policies**

17. Achieving more and better jobs and better responsiveness of labour markets is another major contribution to make the euro area more resilient to asymmetric shocks. This requires encouraging higher labour participation, especially among women and older people, increased adaptability of workers and enterprises, and more and better investment in human capital.

18. The Programmes in the euro area aim at raising employment and labour force participation and tackling high (structural) unemployment. They are relatively scattered and generally address the groups with low employment/high unemployment, namely youngsters, females and older workers. One measure frequently proposed is a reform of the tax and benefit. Overall, the challenges identified in the NRPs with respect to retaining and attracting more workers correspond reasonably closely to those resulting from the Commission's analysis.
19. Some Member States envisage measures to strengthen adaptability. Steps are envisaged in the direction of loosening employment protection for new work contracts, geographical and occupational mobility, and easier job placement. Overall, however, more comprehensive reforms leading to greater responsiveness of labour markets through adaptation of employment legislation and the effectiveness of active labour market policies are paid insufficient attention in the programmes (i.e. the concept of flexicurity).
20. Enhancing the quality of human capital through improving education and upgrading skills, including the long-life learning strategies, are also considered to be important. Reforms of the education system find a prominent place as precondition for boosting labour productivity. The Programmes develop less on measures to boost investment in education, training for adults, and life-long learning, despite their potential for greater productivity and adaptability of the current labour force.
21. The measures have indeed a potential to contribute to increasing labour utilisation, adaptability and improving human capital. Nonetheless, the strategies put insufficient emphasis on important, though arguably difficult measures: for instance, linked to flexicurity, including changes of employment legislation, and achieving a rapid breakthrough in human capital investment.

### **PART III : CONCLUSIONS**

22. The National Reform Programmes of the countries in the euro area are broadly supported by the Commission as they address some main economic challenges for the euro area as a whole. However, further reinforcement of measures in several areas is deemed necessary to achieve a more substantial impact to address the quite sizeable challenges ahead.
23. The Programmes lay out rather comprehensive and forward-looking strategies. However, their degree of concretion varies considerably and reference to monitoring procedures are very often missing. The Commission notes, in particular, the need for more details on synergies and best sequencing of reforms and their budgetary implications.
24. The strengths of the Programmes of the countries in the euro area include:
  - Measures to ensure the sustainability of public finances in the longer term, through increases in effective pension retirement age;
  - Measures to improve regulatory environment and cut administrative costs on businesses;

- Measures to provide financial and other incentives to increase labour supply.
25. Among the points requiring further attention for a better functioning of the euroarea are:
- the need to reinforce the long-term sustainability of public finances, in particular by reverting the upward trend in the debt ratio, in line with the revised Stability and Growth Pact.
  - R&D and innovation policies need to be enhanced in order to achieve the desired objectives;
  - challenges of competition in services and in network industries and the need of a better functioning of the Internal Market are not treated sufficiently;
  - the importance of increased adaptability deserves greater attention, including wage developments, flexicurity, and investment in training for adults.

#### **PART IV : STATISTICAL GRAPHS AND DATA**

## EUROZONE 12

	EU-12							EU-25						
	1999	2000	2001	2002	2003	2004	2010 National target	1999	2000	2001	2002	2003	2004	2010 EU target
GDP per capita in PPS	109.0	108.5	108.5	107.6	107.2f	106.6f		100.0	100.0	100.0	100.0	100.0	100.0	
Labour productivity per person employed	109.3	108.0	107.6	106.8	106.5f	106.0f		100.0	100.0	100.0	100.0	100.0	100.0	
Employment rate	60.4	61.5	62.2	62.4	62.6	63.0		61.9	62.4	62.8	62.8	62.9	63.3	70.0
Employment rate of older workers	33.9	34.4	35.2	36.5	37.9	38.6		36.2	36.6	37.5	38.7	40.2	41.0	
Gross domestic expenditure on R&D	1.90e	1.90e	1.90e	1.90e	1.90e	1.89pe		1.87e	1.89e	1.93e	1.93e	1.92e	1.90pe	3.0
Youth education attainment level	71.5	72.8	72.2	72.6	72.5	72.9		74.8	76.3	76.1	76.5	76.5	76.6	
Comparative price levels	101.6	99.9	100.3	101.1	102.9	102.7p		100.0	100.0	100.0	100.0	100.0	100.0p	
Business investment	18.3	18.8	18.3	17.6	17.3	17.5		17.9	18.3	17.7	17.1	16.7	16.9	
At-risk-of-poverty rate after social transfers	15.0e	15.0e	15.0	15.0	14.0	17.0			16.0	15.0	15.0	15.0	16.0	
Dispersion of regional employment rates	13.3	12.9	12.7	12.1	11.5	10.5		13.3	13.4	13.5	13.3	12.9	12.2	
Long-term unemployment rate	4.5	3.9	3.6	3.6	3.9	4.0		4.1	3.9	3.8	3.9	4.0	4.1	
Total greenhouse gas emissions	98.1e	98.6e	99.6e	99.6e	100.7e			90.6	90.5	91.4	90.7	92.0		
Energy intensity of the economy	192.0	188.6	190.0	184.9	188.2			214.9	208.8	209.7	206.5	209.5		
Volume of freight transport relative to GDP	104.1e	104.7e	104.5e	105.3e	103.6e	109.7e		100.7e	100.4e	99.4e	100.3e	99.7e	104.7e	

