



COMMISSION OF THE EUROPEAN COMMUNITIES

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PART II

**IMPLEMENTING THE RENEWED LISBON STRATEGY
FOR GROWTH AND JOBS**

"A year of delivery"

Assessment of the National Reform Programmes

Statistical Annex to the Country Fiches – explanatory notes

The statistical annex presents 14 short-listed structural indicators derived from the European Statistical System with a gender breakdown where possible.

The full database of structural indicators, including data and metadata relating to the EU Member States, the Acceding and Candidate countries, USA, Japan and EFTA countries, is publicly available on the Eurostat Structural Indicators website: <http://ec.europa.eu/eurostat/structuralindicators>. For each EU Member State, all 14 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&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)

* Indicators disaggregated by gender

The table

The country-specific table presents data from 2000 to 2005 for that country and the EU-25 average. The following flags are used in the data tables:

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

The charts

The 14 country-specific indicators are presented in two charts which compare their actual values with the EU-25 values¹, illustrating in which areas a particular Member State is performing better or worse than the European average. 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.

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 2005 (or latest year available).

Data sources

All indicators were extracted from the Eurostat database on 23 November 2006. 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).

¹ Values in the chart = Current national value / Current EU-25 value * 100

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.

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 national targets presented are those that respond to this invitation and have been extracted from the respective National Reform Programs.

Explanation of abbreviations

EU-25: European Union (25 countries)

Euro Area: Euro Area (12 countries – EUR-11 plus GR up to 31.12.2000 and EUR-12 from 01.01.2001)

Belgium

Assessment of National Reform Programme

1. Since 2002, growth has rebounded somewhat more strongly than the euro-area average, after an earlier downturn. GDP per capita is expected to be around 118% of the EU average in 2006. Labour productivity growth has been slightly below the EU average over the last decade, but the level of productivity is among the highest in the EU. In 2000, Belgium achieved a balanced budget for the first time, which it maintained until 2004. In 2005 the deficit was 2.3% of GDP, resulting from the one-off assumption of a debt worth 2.5% of GDP from the national railways, but in 2006 the general government budget should again come close to balance. The debt-to-GDP ratio has remained on a downward trend and should reach 89% of GDP in 2006 (compared to 108% of GDP in 2000). The employment rate is low (61.4% expected for 2006), especially for young and older people. The unemployment rate is forecast at around 8.6% in 2006.
2. Economic policy focuses on controlling labour costs, creating a more dynamic labour market and stimulating innovation. Measures to reduce the tax burden on labour and to strengthen the social security system need to be reconciled with the budgetary targets necessary to reduce the still high debt level and to prepare for the cost of an ageing population. Combining efforts to curtail health care expenditure with policies to increase employment could help contribute to the long-term sustainability of public finances. Removing barriers to competition in services markets (including in some network industries) would support more dynamic growth.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified six main priorities: 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 NRP also underlined the commitment to increase investment in R&D. The Commission considered in the 2006 Annual Progress Report (APR) that additional efforts were necessary to bring down the tax burden on labour, in the context of sustained budgetary consolidation, and to tackle regional employment disparities.
4. Its 2006 Implementation Report shows that Belgium is generally making good progress with the implementation of its NRP. Progress has been good on reducing the debt ratio, stabilising the downward trend in R&D intensity and in the field of administrative simplification. A number of measures have been introduced to increase the level of investment. Progress has also been made in implementing measures to increase labour supply. Progress has been less satisfactory on competition in network industries and tackling the low employment and high unemployment rate of disadvantaged groups. More progress is also needed to limit early school leaving and on reforms to revitalise the education and lifelong learning systems.

5. Belgium has launched a series of measures to respond to the commitments made by the 2006 Spring European Council. It is too early to observe results on most of these measures. Some further action has been taken to promote better regulation and reduce the administrative burden. Considerable progress has been made in reducing start-up times. As a result, the number of business start-ups has increased by 30% in Belgium between 2003 and 2006.
6. In order to strengthen the governance of the Lisbon Strategy for Growth and Jobs the Belgian federal government has involved regional authorities in drafting the progress report. The social partners and the Federal Council for Sustainable Development were widely consulted and had the opportunity to give advice on policy areas, on some of the implementing measures and on reporting. This will underpin the implementation of large parts of the NRP. The report includes several references to the contribution of EU Structural Funds. The forthcoming National Strategic Reference Framework describes a clear link between the priorities of the Lisbon Growth and Jobs Strategy, the NRP and the priority axes of the future Structural Fund operational programmes in Belgium.

PART II - ASSESSMENT BY POLICY AREA

Macro-economic policies

7. Belgium managed to maintain a balanced budget from 2000 until 2004. This was also planned for 2005, but as a result of an exceptional debt assumption from the railway company SNCB, a deficit of 2.3% of GDP was posted. The debt ratio has, however, maintained its downward trend and was 93% of GDP in 2005. The Implementation Report confirms the aim of further reducing the debt ratio through a balanced budget in 2006 and gradually building up surpluses from 2007. For 2006, reforms in the health sector appear to have been adequate in curbing the strong growth in health care expenditure. Expenditure restraint and some new taxes on non-labour income partially compensate for the budgetary impact of measures to reduce the tax burden on labour and to increase pensions, but the government has also continued to have recourse to one-off measures. The budget proposal for 2007 aims at a 0.3% of GDP surplus, but in the course of the fiscal year further steps may be necessary to reach that target. From 2008, additional policy choices will have to be made to reach the projected surpluses. Public finances would benefit from increasing the employment rate, but the Belgian authorities estimate that the net budgetary gain of current measures (the so-called Generation Pact) will be limited to 0.3% of GDP by 2030.
8. In order to preserve competitiveness and stimulate employment, further steps have been taken to enhance the fiscal environment of businesses and reduce the tax burden on labour (42.6% of wage costs in 2005) to that of the average of neighbouring countries (38.4%) by 2010. However, this tax burden remains one of the highest in the EU. In 2006, the government finalised the implementation of the 2001 tax reform programme. Further measures to cut social contributions on labour were introduced, and will gradually be implemented in 2006 and 2007. The Implementation Report also reiterates the importance of controlling labour costs for preserving competitiveness. The outcome of this depends on the upcoming inter-sectoral wage agreement for 2007-2008.

9. Belgium maintains its rather ambitious macro-economic objectives, but recent measures have increased future budgetary costs (the takeover of pension funds, real estate sale-leaseback operations, measures to increase social benefits). Therefore realising the envisaged budgetary surplus from 2007 is even more important in order to prepare for the anticipated cost of ageing. Further choices remain to be made regarding alternative structural sources of revenues and/or specific measures to restrict expenditure, so as to ensure that budgetary targets are compatible with the aim of reducing the tax burden on labour.

Micro-economic policies

10. The NRP presents a wide range of micro-economic 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.
11. In the field of R&D and innovation, some progress was made in 2006 and the declining trend in total R&D intensity appears to have stabilised. Public investments have risen and private investment has been further promoted. The creation of clusters and competitiveness poles is recognised as an important policy to establish closer links between the science base and the industrial production system. The system of fiscal incentives to reduce the costs of employing researchers has been further extended towards the private sector, including young, innovative SMEs. However, the Implementation Report suggests that reaching the target of 3% of GDP in R&D by 2010 will require more public funding, a more forward looking strategy, and a better coordinated approach at the federal and the regional levels. A set of measures are reported concerning networking, internationalisation, knowledge transfer and human resources for R&D, access to risk capital and improvements to the patent system. However, a more comprehensive approach to encouraging international co-operation, to developing cross-border projects and clusters and to attracting foreign investment is needed.
12. Belgium has implemented a number of ICT measures, particularly to promote e-government, to improve confidence in online security and to encourage the ICT industry. More information on e-Health and e-Inclusion as well as on the budget and timetable for specific measures would help assess progress. In telecommunications, the industry regulator has imposed a series of obligations on the incumbent that will enable market entry by other operators. For the markets that have not been notified yet, the complex institutional situation will require better co-operation between the regulatory authorities competent for certain aspects of infrastructures common to telecommunications and broadcasting.
13. Belgium has improved its record on transposing EU internal market directives into national law, but its deficit is still slightly above the 1.5% interim target and efforts need to be continued. There has been improvement in the transposition of measures under the EU Financial Services Action Plan, but Belgium still has a significant backlog in this respect. The public procurement package should be transposed urgently.
14. The Implementation Report illustrates measures for further liberalisation of the service sector (in particular in some network industries), aiming to give a stronger

role to competition authorities and to put in place a new allocation of responsibilities between authorities and sector-specific regulators. Some markets, where the incumbents still have a dominant position, need to be made more competitive by facilitating new entry. Efforts to improve market transparency are important in this respect. Measures to ensure independent, clearly mandated, and adequately staffed regulators must be closely monitored and reinforced where necessary. In the rail freight market, additional action by the government is needed to encourage market entry. In the gas and electricity markets, the authorities should reinforce the incentives for transmission and distribution network operators to provide better, cheaper, and more flexible services. A first step towards better functioning energy markets is the Code of Conduct to protect consumers. Better implementation of the recent voluntary performance standards for distribution network operators could improve services to network users. Authorities should improve the management of the gas infrastructure and review the system of allocation of storage capacities and the balancing rules on the gas network. Reforms to increase competition in professional services are necessary, building on the current evaluation by the competition services. Belgium is promoting the use of market-based instruments to improve energy efficiency and stimulate the use of renewable energies. A national biodiversity strategy has been developed to halt the deterioration of biodiversity by 2010.

15. A significant number of initiatives have been taken in the micro-economic field to stimulate the economy through investment and reforms. Some of the measures taken are promising but they are too recent to assess their full impact. Progress made in the field of better regulation and administrative simplification is noteworthy. No information is provided on progress made to set up a single contact point for recruiting the first employee and more focus is needed on entrepreneurship education. There has been some progress regarding R&D and innovation. To reach the objective of 3% GDP invested in R&D by 2010, more commitment from the public authorities is needed, both in terms of funding and strategy. In the services sector, in particular network industries, adequate transposition of agreed EU directives would be a first step towards better market functioning. In electricity, gas and rail markets, competition could be enhanced by better implementation of the provisions for unbundling and third party access, and by improving market transparency.

Employment

16. The NRP sets the aim of raising the employment rate, mainly by reducing non-wage labour costs, by promoting active ageing and by tackling youth unemployment. A number of measures have been taken to increase labour supply at both ends of the working age population. The most important development is last year's "Generation Pact" that introduced measures to increase the employment rate for the 55 to 64 age group (31.8% in 2005). This is a first important step towards a fundamental change in attitude on early retirement. However, according to the Study Committee on Ageing, the employment rate of older people may not have reached 50% in 2030. Therefore further attention is needed to raise the employment rate more rapidly. This would make a key contribution towards the adequacy and sustainability of pensions and public finance. A programme to encourage active job search has been set up, comprising additional assistance and training, and a tighter enforcement of availability criteria. Efforts should be strengthened to ensure all regions meet the EU

objective of offering unemployed young people training, retraining, work practice, a job or other employability measure within six months. Some measures have been taken to tackle increasing regional unemployment disparities, the second highest in the EU. The regional employment agencies have developed a broad-based mutual job vacancy exchange system. Regional disparities are also worrying in the field of education and more effort is needed. The employment and unemployment rate gaps between EU and non-EU nationals are very high. Urgent attention should be devoted to improve education performance and language skills, make better use of active labour market policies, to promote diversity in the labour market, and to implement anti-discrimination measures.

17. On adaptability of workers and enterprises, although a comprehensive approach towards developing a "flexicurity" approach is lacking, there is a clear commitment to address skills challenges, particularly for the low-skilled. Belgium is taking a more active approach in the case of company restructurings: when large scale redundancies take place a re-employment cell has to be set up. The government has adopted tax measures to encourage a more flexible use of labour, such as shift work and overtime work.
18. The target set for 2004 by the social partners, of investing 1.9% of the private sector wage bill in training, has not been achieved (it reached 1.25%). The number of people participating in training decreased slightly to 8.4% in 2005. Belgium needs therefore to reinforce efforts on lifelong learning to reach the EU target of 12.5% participation, and the national target of at least doubling the participation rate in lifelong learning among the low-skilled. Apart from incentives for companies to increase the provision of training places, there is no clear approach to increasing participation and investment in training. Measures have been taken for the recognition of competences. To develop the training agenda, the government is relying on the forthcoming negotiations among social partners on a new multi-sector agreement. Important reforms were launched recently, such as improving the image and the quality of technical education, but they are too recent to show results. It is important to reinforce the measures taken in order to limit early school leaving and thus avoid young people leaving school with limited skills.
19. The NRP identifies clearly the employment challenges and reflects the government's determination to increase the employment rate. The implementation of the measures is contributing to progress in employment growth, although the unemployment rate continues to hover around 8.4%. Sustained attention is therefore necessary to tap the employment potential of disadvantaged groups, youth and old people. Vigorous efforts are needed to limit early school leaving and to revitalise the education and lifelong learning system so that the labour market is sufficiently supplied with skills.

PART III CONCLUSIONS

20. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
21. Belgium is making good progress in the implementation and reinforcement of its 2005-2008 National Reform Programme. While there is a certain risk for the

sustainability of public finances in the context of an ageing population, overall the policy framework is appropriate. Despite moderate progress on R&D, Belgium is implementing the measures announced in the micro-economic field and reinforcing existing reforms to increase investment. The picture in the employment field is more mixed and steps are needed to achieve the EU-wide employment rate goals, in particular for older people. Belgium has launched a series of measures to respond to the commitments made by the 2006 Spring European Council.

22. Among the strengths of the Belgian National Reform Programme and its implementation are: the continued downward trend of the debt ratio; the stabilisation of the declining trend in R&D intensity; the development of clusters and competitiveness poles; the improved record on the transposition of internal market directives; further measures in the field of better regulation and administrative simplification; the policy to promote business start-ups; the measures to improve the alternate learning system; and the formal recognition of acquired skills and the quality of the technical education system are welcome.
23. The policy areas in the Belgian National Reform Programme where weaknesses need to be tackled with the highest priority are: reducing the tax burden on labour and reducing regional disparities in unemployment. Against this background Belgium is recommended to:
 - undertake further efforts to reduce the tax-burden on labour towards the average of its neighbouring countries, while continuing fiscal improvement;
 - take further measures aimed at reducing regional disparities in unemployment through active labour market policies, reintegration and education policies.
24. In addition, it will be important for Belgium over the period of the National Reform Programme to focus on: ensuring the long term sustainability of public finances; identifying further emission reduction policies and measures; improving competition in gas and electricity markets, including through independent and effective regulators and through additional measures concerning transmission and distribution operators; and increasing the employment rate for older workers and vulnerable groups, in particular by tightening the eligibility criteria for early retirement schemes and by enhancing active labour market policies.

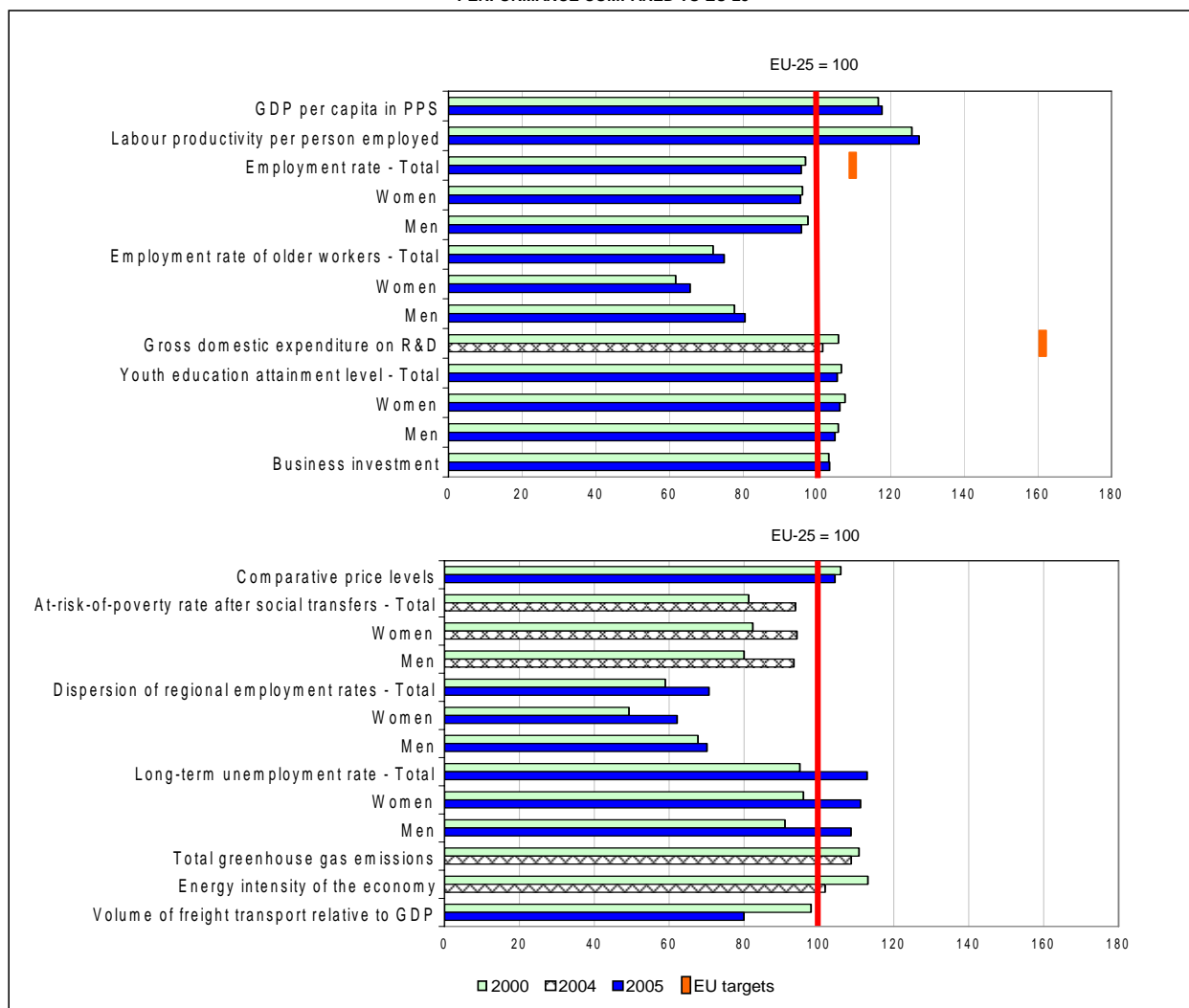
PART IV: STATISTICAL GRAPHS AND DATA

BELGIUM

	BE							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	116.7	117.2	117.5	117.9	118.7	117.7		100.0	100.0	100.0	
Labour productivity per person employed	125.8	126.2	127.5	128.3	129.0	127.8		100.0	100.0	100.0	
Employment rate							70.0*				70.0
Total	60.5	59.9	59.9	59.6	60.3	61.1		62.4	63.3	63.8	
Women	51.5	51.0	51.4	51.8	52.6	53.8		53.6	55.7	56.3	
Men	69.5	68.8	68.3	67.3	67.9	68.3		71.2	70.9	71.3	
Employment rate of older workers											
Total	26.3	25.1	26.6	28.1	30.0	31.8		36.6	41.0	42.5	
Women	16.6	15.5	17.5	18.7	21.1	22.1		26.9	31.7	33.7	
Men	36.4	35.1	36.0	37.8	39.1	41.7		46.9	50.7	51.8	
Gross domestic expenditure on R&D	1.97	2.08	1.94	1.89	1.89p	:	3.0	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	81.7	81.7	81.6	81.2	81.8	81.8		76.6	77.1	77.5	
Women	85.6	85.2	84.8	84.6	84.8	85.3		79.5	80.1	80.3	
Men	78.0	78.3	78.5	77.9	78.9	78.4		73.7	74.2	74.7	
Comparative price levels	105.8	102.8	102.3	104.0	104.2p	104.3p		100.0	100.0p	100.0p	
Business investment	18.9	18.7	17.5	17.2	17.8	18.0		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	13.0	13.0	:	15.0b	15.0	:		16.0e	16.0e	:	
Women	14.0	15.0	:	16.0b	16.0	:		17.0e	17.0e	:	
Men	12.0	12.0	:	14.0b	14.0	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	7.9	8.0	8.0	7.7	8.7	8.4		13.4	12.2	11.9	
Women	10.1	10.4	10.2	9.1	10.7	10.5		20.5	17.3	16.9	
Men	6.7	6.4	6.6	6.9	7.2	6.8		9.9	10.2	9.7	
Long-term unemployment rate											
Total	3.7	3.2	3.7	3.7	4.1	4.4		3.9	4.1	3.9	
Women	4.6	3.5	4.3	4.2	4.7	5.0		4.8	4.7	4.5	
Men	3.0	2.9	3.2	3.3	3.7	3.8		3.3	3.6	3.5	
Total greenhouse gas emissions	100.4	100.0	98.8	100.4	100.7	:		90.7	92.7	:	
Energy intensity of the economy	236.1	228.1	213.6	217.4	208.2	:		208.8	204.9	:	
Volume of freight transport relative to GDP	98.0	100.1	99.1	95.0	89.3	83.7		100.1e	104.6be	104.7e	

* National target: 70% as soon as possible

PERFORMANCE COMPARED TO EU-25



Czech Republic

Assessment of National Reform Programme

1. In recent years growth in the Czech economy has strengthened significantly, averaging 3.6% of GDP between 2001 and 2005. In 2006, the economy is expected to grow by 6%. GDP per capita is currently 76.2% of the EU average. The recent strong economic growth has positively affected the labour market with the employment rate projected to reach 67.4% in 2006, above the EU average. Unemployment is estimated to fall to 7.4% in 2006. Labour productivity has continued to increase, reaching 68% of the EU average.
2. Whilst unemployment has fallen, the proportion of long-term unemployed remains high and further falls are likely to be tempered by structural factors including the high tax wedge on employment. The current macro-economic environment gives ample opportunity to tackle the main fiscal policy challenges of: improving medium-term budgetary consolidation and achieving sustainable public finances for the long-term. Whilst measures have been undertaken to restructure taxation to favour employment and to improve budgetary control, increasing the flexibility of budgetary expenditure and respecting budgetary ceilings, would support medium-term consolidation. Major reforms of the pension and health care systems would contribute to longer-term sustainability.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified the following key 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 shared this analysis, but considered that further attention should be paid to: securing the long-term sustainability of public finance, especially with regard to reforms of pension and health care systems; improving human capital through lifelong learning, taking account of the most vulnerable groups and of regional disparities in unemployment; and policies to improve R&D and innovation and in particular to develop human capital for the R&D system.
4. The 2006 Implementation Report shows successes in certain areas but progress has been mixed. On the plus side, there has been progress on improving the business environment and reforms have been introduced to curricula for primary education and to increase participation in tertiary education. Initial progress has been made on improving the control of the budget and shifting the tax burden from direct to indirect taxes; implementing measures on better regulation; making work pay and regional mobility; supporting disadvantaged groups; and recognition, validation and certification of skills. However, no major reform of public finance has been undertaken or is currently planned. The planned R&D expenditure increase is unlikely to take place in full. The development of sufficient human capital for the R&D system depends on financing from the 2007–2013 Structural Funds. There has also been limited progress towards: increasing the use of ICT, including e-

Government; meeting the key challenge of increasing labour market flexibility; modernizing the public employment service; and developing a comprehensive education and lifelong learning strategy.

5. Progress on meeting the commitments made at the 2006 Spring European Council has been mixed. One-stop shops for setting up a business became operational in August 2006 and there are plans to ensure by the end of 2007 that young unemployed people get a new start within six months of becoming unemployed. However, the Implementation Report does not include information on progress towards establishing a single contact point for recruiting the first employee or on entrepreneurship education.
6. There is some progress on improving governance of the implementation of the Growth and Jobs Strategy. The established governance structure involves relevant ministries and social partners while parliament, the regions, and municipalities were all consulted on the Implementation Report. Measures have been taken to improve communication and consultation of the general public. Monitoring of progress is not fully developed yet, and more evaluation results will become available in the next years. Cohesion Policy funding will amount to 3.3% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The Implementation Report covers five areas of fiscal policy contributing to the stability and long-term sustainability of public finances. However, while actions have been taken or are planned in certain areas, no major reform of public finances has been undertaken or is currently under discussion.
8. The government deficit increased from 2.9% of GDP (2004) to 3.6% of GDP (2005), but that was lower than projected, due mainly to higher than anticipated growth and the carry-over of unspent funds. No significant spending cuts have been introduced in 2006. The 2007 draft budget projects the deficit to widen to about 3.8% of GDP in 2007, in breach of previously approved expenditure ceilings. This is mainly due to increases in social spending, the impact of which is estimated at some 1.2% of GDP. On the other hand, measures have been taken to restructure the tax burden and to improve control over public finances. These include reductions in corporation tax, including tax breaks for R&D investment, and reductions in personal income tax. There has also been a reduction in the number of extra-budgetary funds and institutions, which will improve the transparency and accountability of public finances. An all-party pension report was compiled in 2005, presenting a range of reform proposals and their detailed assessment by an independent group of experts, but this has not been followed up by government action.
9. The Czech Republic has one of the most rapidly ageing populations in the EU, so public finances will come under increasing pressure through the pension and health care systems. Major reforms of those systems are therefore essential for long-term public finance sustainability.

Micro-economic policies

10. The Implementation Report concentrates on the four main micro-economic areas identified in the NRP: R&D and innovation; the business environment; modernisation and development of transport and ICT networks; and sustainable use of resources.
11. Some progress has been made in the area of R&D and innovation, largely due to an increase in private R&D expenditure. Public R&D expenditure has been growing, but slower than anticipated by the NRP. However, the overall 2.06% R&D intensity target for 2010 may be difficult to meet if the public R&D expenditure from national sources is limited to 0.60% of GDP in 2009. The increased R&D expenditure will be concentrated into a set of long-term R&D priorities, which are part of the national R&D policy. Changes in the structure of public R&D expenditure favouring targeted research funding are on-going. Tax incentives for private research were introduced in 2005; a first assessment of their impact will be available by the first half of 2007. The development of human resources for R&D is considered a priority. Attention needs to be paid to the development of innovation infrastructure (business incubators, science and technology parks, technology transfer centres) that will promote cooperation between public research institutions and the private sector. In this respect, the development of links between foreign-owned and domestic companies deserves more emphasis. Enhancement of patenting and the protection of intellectual property rights remains a challenge despite efforts made. A new scheme for early stage financing for SMEs, including instruments providing risk capital and micro loans for innovative companies, is being prepared.
12. The implementation of measures to improve the business environment is on-going. Integrated impact assessments will be implemented in the course of 2007 for all new legislation. Analysis of administrative costs borne by business has been completed, but has not been approved by the government. This could hamper meeting the commitment to decrease administrative burdens by 20% by 2010. New insolvency legislation reinforcing creditors' position will enter into force in July 2007. A system of Central Registration Points (one-stop shops for setting up a business) became operational as of August 2006. It is encouraging that action is being taken by the competition authority to screen existing regulations covering some professional services and to identify areas requiring change. Transposition of EU internal market legislation into national law needs further improvement, as despite the progress made, the transposition deficit is still above the target of 1.5%.
13. Progress has been mixed on the modernisation and development of ICT and transport networks and on the sustainable use of resources. Investment in broadband infrastructure is planned, financed by Structural Funds and revenues from the privatisation of *Cesky Telecom*. The aim is to help achieve the target set in the NRP that 50% of the population takes up broadband infrastructure by 2010. Several e-Government projects have been launched and some legal acts needed to underpin further progress have entered into force, although the legislative process of the crucial act on data sharing in public administration has stalled. Further efforts are needed to build on progress in increasing computer literacy. Construction of highway and railway infrastructure is ongoing.

14. A programme for sustainable use and efficiency of resources is being prepared, but energy intensity remains very high. The measures mentioned in the Implementation Report should be resolutely applied and reinforced, if the Czech Republic is to reach the target of obtaining 8% of its electricity from renewable sources. The future of the planned fiscally neutral environmental tax reform remains at issue.
15. Overall progress in the micro-economic area has been mixed. Business environment measures are on-going, but a number of important measures foreseen by the NRP in the other key areas, namely public R&D spending plans and e-government legislation, are not fully implemented.

Employment policies

16. The Implementation Report focuses on the key challenge of increasing labour market flexibility, complemented by greater inclusion in the labour market of young, women, older workers, immigrants and improving education.
17. Economic growth has helped to attract more people into the labour market, but long-term unemployment persists. Youth unemployment has decreased, mainly as a result of stricter eligibility criteria, but measures to address this issue still need to be more coherent and innovative. By 2007, every young person is to be offered a new start – a job or training - within six months of becoming unemployed. Employment of older workers has increased, but more progress is desirable. This requires full implementation of the active ageing strategy with stronger incentives to work longer and to take up a job, better access to training to improve skills, and measures to encourage employers to recruit. Measures have been proposed to increase women's employment, in particular support for the reintegration of women after maternity leave and measures to increase the accessibility of childcare. However, these proposals still need to be approved and implemented and do not tackle the high gender pay gap. Unemployment of people with disabilities is steadily increasing, and further attention should be paid to the situation of the Roma minority. Measures taken go in the right direction but need to be strengthened. Reforms already adopted to prevent the abuse of sickness benefits now require implementation. An important range of measures has been taken to make work pay, including a tax reduction for low-wage earners, adjustments to the two bottom tax brackets of personal income tax, increases in the minimum wage and a reform of the social benefits system to encourage activation. The effect of the resulting incentives should be carefully monitored. Regional disparities in unemployment remain, and the modernisation of public employment services is advancing slowly. Active labour market policies are underfunded.
18. To improve the adaptability of workers and enterprises, measures have been taken to improve geographical mobility (liberalisation of housing rents and stimulating commuting). The new Labour Code allows for more flexibility in the organisation of work (working time accounts will be introduced) and provides greater contractual freedom in employment. The reform does not address employment protection on permanent contracts. An integrated "flexicurity" approach should therefore underpin further reform, which needs to be implemented, in cooperation with social partners and without hampering the impact of measures to make work pay and promote geographical mobility.

19. To increase investment in human capital, particular priority is given to the ongoing reform of curricula for primary and secondary education. Progress is less evident in improving relations between employers and education institutions. Further efforts are required to improve pathways between secondary and tertiary education, including vocational training, and to provide a wider access to general courses in order to better cope with changing skill demands. Participation in tertiary education has increased (new universities, faculties and study programmes), but more resources and better incentives for both students and tertiary education institutions are still necessary. Participation in lifelong learning remains low, especially for older workers (1.9% in 2005 and decreasing) and the low skilled (0.9% in 2005). The new law on the verification and recognition of further education (entry into force in 2007) and the National System of Qualifications are welcome. They should be complemented by a comprehensive strategy to increase access to lifelong learning. Particular emphasis should be placed on the low skilled and older workers and on increasing incentives for individuals and employers to invest in training, and on developing learning institutions.
20. Some progress has been made in the employment field but the Czech Republic must make more use of the favourable economic climate to press forward with reforms. A more complete response to the key challenge of more labour market flexibility requires an integrated "flexicurity" approach, with the active involvement of the social partners. Such an approach should further modernise and implement the Labour Code, review incentives created by the tax and benefit systems, modernise the public employment service and strengthen active labour market policies. This must be combined with the development of a comprehensive education and lifelong learning strategy that tackles the low level of skills, particularly amongst older workers.

PART III: CONCLUSIONS

21. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
22. The Czech Republic is making limited progress in the implementation of its National Reform Programme: progress in several areas is not clearly spelled out, some reforms have been postponed, while others have not been set in motion. Yet the strong economic growth should facilitate reforms. There are certain risks in the macro-economic area, particularly for medium-term budgetary consolidation and the long-term sustainability of public finances in the context of an ageing population. Although the Czech Republic is generally moving ahead relatively well in the micro-economic field, progress on R&D is moderate. In the employment area more efforts are required to respond to the key challenge of improving labour market flexibility. Progress on meeting the commitments made at the 2006 Spring European Council has also been mixed.
23. Among the strengths of the implementation of the National Reform Programme are positive measures to increase the control and transparency of public finances; to improve regulation and the business environment; to reform curricula for primary education and to stimulate participation in tertiary education.

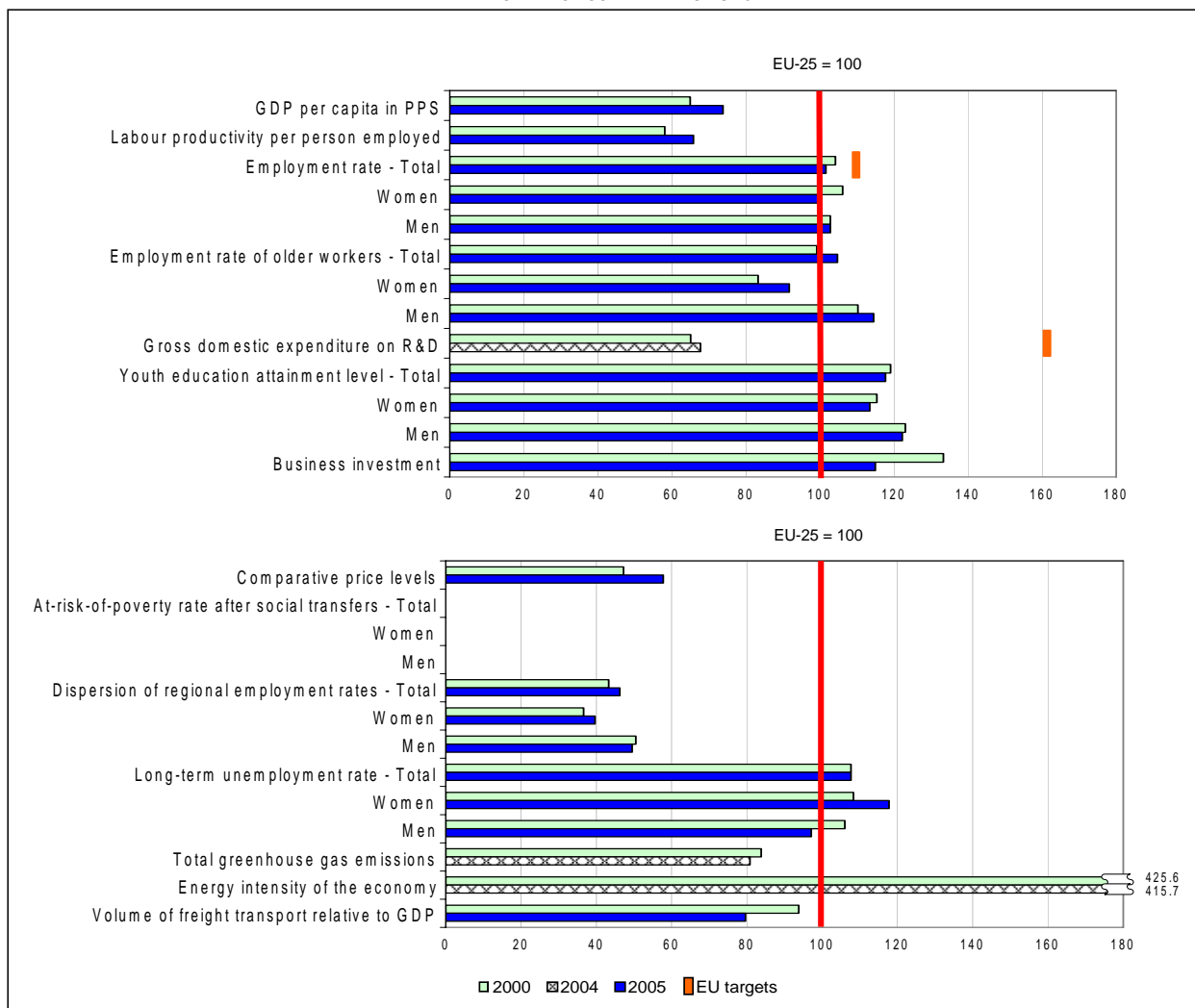
24. The policy areas in the Czech National Reform Programme where weaknesses need to be tackled with the highest priority are: the sustainability of public finances, since the 2007 budget anticipates a breach of the expenditure ceilings and an increased deficit; increasing the amount and effectiveness of public R&D expenditure; improving security and flexibility in the labour market; improving education and training and increasing participation in lifelong learning. Against this background the Czech Republic is recommended to:
- with a view to improving the long-term sustainability of public finances, take steps to implement reforms of the pension and healthcare systems, in particular on the basis of the 2005 all-party pensions report, and fix a timetable for their implementation;
 - strengthen efforts to improve collaboration between business and public R&D institutions, while keeping up the pace of increasing public R&D investment;
 - modernise employment protection, including legislation and tax and benefit systems, improve education and training systems, and provide incentives to invest in training, particularly for older workers and the low-skilled.
25. In addition, it will be important for the Czech Republic over the period of the National Reform Programme to focus on: improving the system for patenting and the protection of intellectual property rights; speeding up progress in the ICT area, including by implementing and monitoring the development of a fully enabling legal environment for e-Government; meet targets for reducing the administrative burden on enterprises; further developing access to finance for innovative companies; developing links between foreign-owned and domestic companies; introducing entrepreneurship education into the curricula; better integrating disadvantaged groups into the labour market; reducing regional employment disparities; reconciling work and family life; tackling the gender pay gap and implementing the active ageing strategy.

PART IV: STATISTICAL GRAPHS AND DATA

CZECH REPUBLIC

	CZ							EU25					
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target		
GDP per capita in PPS	64.9	65.8	67.7	68.3	70.5	73.8	66.4 (2008)	100.0	100.0	100.0	70.0		
Labour productivity per person employed	58.1	59.0	60.2	61.5	63.5	65.8		100.0	100.0	100.0			
Employment rate													
Total	65.0	65.0	65.4	64.7	64.2	64.8		62.4	63.3	63.8			
Women	56.9	56.9	57.0	56.3	56.0	56.3		53.6	55.7	56.3			
Men	73.2	73.2	73.9	73.1	72.3	73.3		71.2	70.9	71.3			
Employment rate of older workers													
Total	36.3	37.1	40.8	42.3	42.7	44.5		36.6	41.0	42.5			
Women	22.4	23.1	25.9	28.4	29.4	30.9		26.9	31.7	33.7			
Men	51.7	52.6	57.2	57.5	57.2	59.3		46.9	50.7	51.8			
Gross domestic expenditure on R&D	1.21	1.20	1.20	1.25	1.26	1.42		2.06	1.86e	1.86e		:	3.0
Youth education attainment level													
Total	91.2	90.6	92.2	92.1	91.4	91.2			76.6	77.1		77.5	
Women	91.7	91.3	92.0	91.5	91.8	91.1		79.5	80.1	80.3			
Men	90.7	89.8	92.4	92.8	91.0	91.3	73.7	74.2	74.7				
Comparative price levels	47.2	50.3	54.7	55.5	55.0p	57.8p	100.0	100.0p	100.0p				
Business investment	24.4	24.5	23.6	22.1	21.3	20.0	18.3	17.1	17.4				
At-risk-of-poverty rate after social transfers													
Total	:	8.0	:	8.0	:	:	16.0e	16.0e	:				
Women	:	8.0	:	9.0	:	:	17.0e	17.0e	:				
Men	:	7.0	:	7.0	:	:	15.0e	15.0e	:				
Dispersion of regional employment rates													
Total	5.8	5.7	5.6	5.8	5.6	5.5	13.4	12.2	11.9				
Women	7.5	7.7	7.0	7.4	6.6	6.7	20.5	17.3	16.9				
Men	5.0	4.7	5.1	4.9	5.1	4.8	9.9	10.2	9.7				
Long-term unemployment rate													
Total	4.2	4.2	3.7	3.8	4.2	4.2	3.9	4.1	3.9				
Women	5.2	5.1	4.6	5.0	5.3	5.3	4.8	4.7	4.5				
Men	3.5	3.4	3.0	2.9	3.4	3.4	3.3	3.6	3.5				
Total greenhouse gas emissions	76.0	76.2	73.4	75.2	74.9	:	90.7	92.7	:				
Energy intensity of the economy	888.4	883.9	875.8	891.2	851.8	:	208.8	204.9	:				
Volume of freight transport relative to GDP	93.9	93.5	97.5	98.7	92.8	83.4	100.1e	104.6be	104.7e				

PERFORMANCE COMPARED TO EU-25



Denmark

Assessment of National Reform Programme

1. Denmark enjoys high GDP per capita (124.6% of the EU average in 2006), 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 around the EU average. The employment rate is the EU's highest (76.6% in 2006). Employment growth has been strong in the last few years and the unemployment rate (3.8% in 2006), has been further reduced and is now the lowest in the EU.
2. The Danish economy is at present performing strongly. Due to sound macroeconomic policies and a strategy aimed at fiscal sustainability in the long term, which during 2006 was further strengthened, Denmark is also well placed to confront the long-term challenge posed by the ageing of the population. This success builds on a high overall employment rate and the “flexicurity” labour market approach combining flexible rules for hiring and dismissal with active labour market policies, relatively high unemployment benefits and strict enforcement of eligibility rules. However, employment rates for older workers and immigrants are significantly lower than overall levels. Moreover, the average number of hours worked is still relatively low compared with the EU average and productivity could be improved.

PART I: GENERAL ASSESSMENT

3. The Danish 2005-2008 National Reform Programme (NRP) outlines four broad challenges: to prepare for the ageing of the population; to reap the benefits of globalisation; to strengthen the framework for improving productivity; and to increase value for the users of public services. These broad challenges lead to a number of priorities: ensuring fiscal sustainability, improving competition in certain sectors; enhancing public sector efficiency; developing the knowledge society; securing environmental sustainability and energy; encouraging entrepreneurship; and increasing the labour supply. These challenges and priorities remain valid and are restated in the 2006 Implementation Report. In its 2006 Annual Progress Report (APR), the Commission identified as areas needing further attention more concrete and specific measures to increase labour supply and more detailed measures to increase competition.
4. The Implementation Report shows that Denmark has made very good progress during 2006 in implementing and strengthening further its reform strategy across all policy areas, notably in preparing for the ageing of the population and reaping the full benefits of globalisation. Public finances are on a sound path. A Welfare Agreement (see also “Employment policies” section below) was reached in June 2006 focusing in particular on increasing long-term labour supply, on improving the quality of education and increasing the quantity and quality of R&D. Progress has also been good on improving the business environment and increasing environmental protection. Already extensive active labour market and lifelong learning policies have been further reinforced. There has been promising initial progress on boosting

competition and on strengthening initial education and training, though implementation remains at an initial stage. There has been modest progress on addressing increasing current labour shortages and on increasing labour supply in the medium-term.

5. Denmark is also responding well to the commitments made by the 2006 Spring European Council. For example, 2010 targets for public (1% of GDP) and overall (over 3%) investment in R&D have been set. There has been progress on improving the business environment through one-stop shops and measures for entrepreneurship education are being expanded.
6. Efforts to develop ownership of the Denmark's extended reform strategy have been substantial. The Welfare Agreement is based on a report by an independent group of experts, the Welfare Commission, which presented its proposals in December 2005. The views of social partners, local authorities and representatives of civil society were collected and the parties to the Welfare Agreement represent a large majority of the Danish parliament. As part of an ongoing dialogue on issues related to the overall reform agenda for Growth and Jobs, the government also regularly discusses topical issues with the Lisbon Coordination Committee, a national committee with representatives from various ministries and stakeholder organisations which has final competence for coordination. The National Strategic Reference Framework for the investment of Structural Funds is broadly in line with the NRP, addressing the core issues such as innovation, transfer of knowledge, use of new technology and development of human resources.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The NRP identified sound public finances, a stable exchange rate, price stability and high employment as key challenges in the macro-economic area. To achieve this the macro-economic strategy centres on assuring long-term fiscal sustainability, consisting of building up government funds by saving budget surpluses in combination with increasing employment by around 2% of the labour force by 2010. Policies aimed at fiscal sustainability continue to be based on the objective of an average annual budget surplus of 0.5-1.5% of GDP until 2010. On the expenditure side, the limit to the annual real growth of public consumption will be doubled to 1.0% as from 2007, which may have an effect on the government's budget surplus target. To constrain consumption growth, in particular by local governments, the government is maintaining a tax freeze, meaning that no tax rate may be increased and some individual taxes have been frozen in nominal terms. Monetary policy aims at maintaining the krone's narrow intervention margins within ERM2, thus laying the basis for price stability in line with the euro area.
8. The Implementation Report indicates important progress on long-term fiscal sustainability, with targets being met. The only exception is the government's own target for the growth rate of public consumption. Measures agreed in the context of the Welfare Agreement are well-designed and likely to be effective and will further improve the ability of Denmark to confront the macro-economic implications of its ageing population, by better balancing the number of years spent working with the

number of years spent in education and retirement. This will further contribute to sustainability as, by extending working lives, it will also broaden the tax base and limit future pension expenditure.

9. Its macro-economic strategy is serving Denmark well. Owing to successive budget surpluses and a rapid reduction of government debt, Denmark is at low risk as concerns long-term sustainability of public finances. The effect of the Welfare Agreement will further reinforce Denmark's position in this respect. In the medium term, up until 2015, however, the effect of reform measures on increasing labour supply and thus the economy's growth potential appears rather more limited and to fall short of the objective defined in the NRP.

Micro-economic policies

10. Denmark identified five important challenges in last year's NRP: enhancing competition in certain sectors; strengthening public sector efficiency; developing a knowledge society; and securing environmental sustainability and encouraging entrepreneurship. The Commission shared this analysis.
11. Denmark has made encouraging progress in improving competition. The target of halving the number of sectors affected by a lack of competition by 2010 seems realistic. Amendment of the Competition Act, as announced in the NRP, is underway. The Competition Authority and relevant ministries have proposed reinforcing available instruments for investigating cartels, such as a leniency programme and the possibility for the Competition Authority to impose fines. While concrete measures for dealing with cartels are being implemented, more detail on other initiatives would have been useful. For example, some sectoral taxation practices that may impede competition and allocative efficiency are not addressed.
12. Denmark's R&D and innovation record is very good. Total R&D spending amounted to 2.5% GDP in 2004, well above the EU average of 1.9% GDP. To boost public R&D, Denmark this year consolidated its public research system and decided on a budgetary framework to implement a range of expected measures. In this context, a number of measures are planned to ensure high quality university research, such as targeted funding and the merging of some universities and sectoral research institutions to enhance efficiency. To stimulate private R&D, Denmark has announced measures to boost technology transfer from public research to private enterprises, to improve interaction between the public and private sector and to reinforce university governance. In addition, new measures have been launched to enhance innovation in environmental technologies. Promising steps are announced to promote access to ICT for all and ICT-led innovation throughout the private and public sectors. It is expected that, if Denmark maintains its current strategy, the 2010 R&D target of 3% of GDP will be reached.
13. New initiatives have been announced to improve public sector efficiency. Public services will be exposed to competition and the use of result-oriented wages will be extended. Moreover, a reduction in the number of municipalities will take place on 1 January 2007. It is envisaged that this will improve efficiency and the quality of services.

14. Measures for new business start-ups include one-stop shops for business support, regional entrepreneurship centres and the availability of more venture capital finance. Most of the measures are yet to be implemented. Denmark has improved its efforts to promote entrepreneurship education, but detail on the state of play in introducing entrepreneurship in school curricula is missing. Denmark's regulatory simplification programme is characterised by a strong emphasis on the reduction of the administrative burden. According to government figures, administrative burdens on businesses were reduced by 5.1% between 2001 and 2005. Denmark carries out impact assessments for all new legislative proposals, and has a well-established tradition of consulting with the social partners.
15. Competition in the energy sector has increased as markets have been liberalised gradually over a number of years. To further improve the functioning of the energy market, measures to increase (cross-border) electricity interconnection supply are needed. There is encouraging progress on environmental technologies, water consumption, and energy savings. Forthcoming measures such as a development and demonstration programme for more efficient energy technologies look promising and it is positive that the potential use of market-based instruments for promotion of energy savings and sustainable energy are being examined. However, Denmark will have to identify further emission reduction policies and measures in order to meet its burden sharing target.
16. Overall, Denmark has made good progress in implementing measures to address the key challenges that were identified in the area of microeconomic policies. These measures will further improve Denmark's business climate and the economy's competitiveness.

Employment policies

16. The Danish NRP identifies increased labour supply through higher labour force participation as the principal employment challenge. It also emphasises 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 shared this analysis of the main challenges and priorities.
17. Denmark is seriously addressing the key challenge of increasing labour supply. The Welfare Agreement reached in June 2006 includes a future revision of the voluntary early retirement scheme, including by raising the eligible age by two years phased in from 2019-2022. The reform raises the statutory retirement age by two years and introduces a future indexation mechanism for both early and statutory retirement age based on life expectancy. In addition, the Welfare Agreement also includes measures to be implemented immediately on active labour market policy, education and vocational training. These reform measures are likely to address an important part of the required long-term increase in the labour force by 2040. However, they will only result in a moderate increase in medium and short-term labour supply and they will not effectively address the mounting labour shortage which is being reported. Some measures have been taken to address this, but further initiatives are needed to strengthen incentives to work, notably measures aiming at increasing the average amount of hours worked and exploring and tapping the considerable work force potential in older workers and immigrants.

18. The reforms announced in the Welfare Agreement will further improve Denmark's already sophisticated flexicurity approach. To further reinforce active labour market policies, Denmark has pursued efforts to tighten the eligibility criteria for unemployment benefits by strengthening active job search requirements. To further boost lifelong learning, promising reforms to the vocational and adult training system, with a particular focus on addressing the problems of the low-skilled, are due to be implemented in cooperation with social partners in 2007.
19. To improve the primary and secondary school system, a number of measures have been initiated. Total expenditure on education still remains about 50% higher than the EU average, though international surveys show that the educational performance only ranks average on a number of key indicators. The measures include more tests, improved teacher training and an action plan to improve pupils' reading skills. To increase the number of students in secondary education initial vocational education and training programmes have been reinforced. Measures have also been taken to raise the number of students in tertiary education. So far there are no visible results of these measures and it remains to be seen whether their scope is sufficient to reach the ambitious medium-term targets.
20. Overall, the employment strategy is comprehensive, ambitious, long-term and realistic. The new Welfare Agreement is likely to be effective in addressing an important part of the long-term challenges caused by ageing, although it will take time to be fully implemented. Policies aimed at increasing labour supply in the medium term are needed to improve the economy's growth potential and prevent shortages in the labour market. These policies must target labour supply by older workers and immigrants and incentives to work should be put in place to increase the average number of hours worked.

PART III: CONCLUSIONS

21. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
22. Denmark is making very good progress in the implementation of its National Reform Programme and the 2006 Spring European Council conclusions. Denmark has with the June 2006 Welfare Agreement further strengthened its reform strategy in terms both of macro-economic and employment policy and has made very good progress in reaching a national consensus on reforms. Denmark has also made progress on micro-economic policies, including in the area of competition.
23. Among the strengths of the Danish National Reform Programme and its implementation are: the comprehensive, integrated nature of the reform strategy, which is a benchmark for other Member States; the combination of a medium and long-term approach, reinforced by consistently taking into account stakeholder input; the "flexicurity" based approach to the labour market; the overall macro-economic strategy aimed at long-term fiscal sustainability, including expenditure restraint, fiscal surpluses and a rapid reduction of government debt; and the sound measures aimed at increasing labour supply in the long term, in particular the agreement to defer early retirement.

24. It will be important for Denmark over the period of the National Reform Programme to focus on: measures aimed at increasing labour supply over the medium term, up until 2015, including further initiatives to improve incentives to work and additional steps to integrate older workers and immigrants into the labour market; following through proposed reforms in competition law and ensuring that new competition powers are vigorously exercised by the relevant authorities; additional measures in energy interconnection supply, in order to improve the functioning of the electricity and gas markets; identifying further emission reduction policies and measures; reinforcing existing well-targeted measures to improve primary and secondary education and increase the number of students finalising upper-secondary or tertiary education, as these may not be sufficient to reach the ambitious targets set.

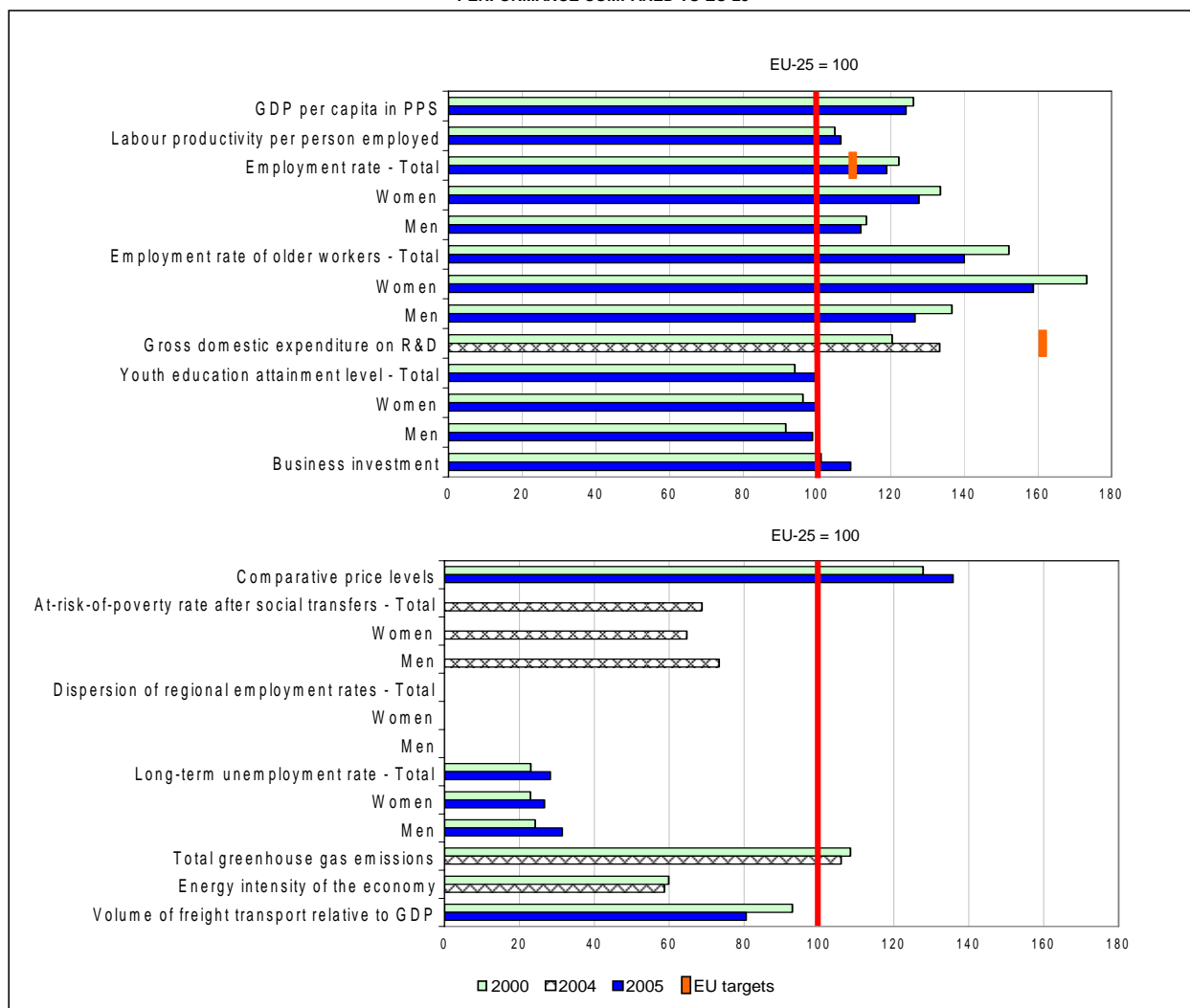
PART IV: STATISTICAL GRAPHS AND DATA

DENMARK

	DK							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	126.2	124.9	121.4	120.8	121.5	124.2		100.0	100.0	100.0	
Labour productivity per person employed	104.9	104.4	102.0	103.2	104.2	106.5		100.0	100.0	100.0	
Employment rate							:				70.0
Total	76.3	76.2	75.9	75.1	75.7	75.9		62.4	63.3	63.8	
Women	71.6	72.0	71.7	70.5	71.6	71.9		53.6	55.7	56.3	
Men	80.8	80.2	80.0	79.6	79.7	79.8		71.2	70.9	71.3	
Employment rate of older workers											
Total	55.7	58.0	57.9	60.2	60.3	59.5		36.6	41.0	42.5	
Women	46.6	49.7	50.4	52.9	53.3	53.5		26.9	31.7	33.7	
Men	64.1	65.5	64.5	67.3	67.3	65.6		46.9	50.7	51.8	
Gross domestic expenditure on R&D	2.24	2.39	2.51	2.56	2.48p	2.44p	3.0	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	72.0	78.4b	78.6	76.2b	76.2	77.1		76.6	77.1	77.5	
Women	76.5	81.7b	82.6	78.5b	78.1	80.5		79.5	80.1	80.3	
Men	67.5	74.8b	74.3	73.8b	74.3	73.8		73.7	74.2	74.7	
Comparative price levels	127.8	130.7	135.6	138.8	137.0p	135.8p		100.0	100.0p	100.0p	
Business investment	18.5	17.9	17.8	17.9	17.9	19.0		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers*		10.0		12.0b	11.0			16.0e	16.0e		
Women				12.0b	11.0			17.0e	17.0e		
Men				11.0b	11.0			15.0e	15.0e		
Dispersion of regional employment rates											
Total	-	-	-	-	-	-	-	13.4	12.2	11.9	
Women	-	-	-	-	-	-	-	20.5	17.3	16.9	
Men	-	-	-	-	-	-	-	9.9	10.2	9.7	
Long-term unemployment rate											
Total	0.9	0.9	0.9	1.1	1.2	1.1		3.9	4.1	3.9	
Women	1.1	1.0	1.0	1.0	1.3	1.2		4.8	4.7	4.5	
Men	0.8	0.8	0.7	1.2	1.1	1.1		3.3	3.6	3.5	
Total greenhouse gas emissions	98.3	100.5	99.4	106.8	98.2			90.7	92.7		
Energy intensity of the economy	125.0	126.6	123.8	126.1	120.3			208.8	204.9		
Volume of freight transport relative to GDP	93.0	85.5	86.2	87.6	86.9	84.3		100.1e	104.6be	104.7e	

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

PERFORMANCE COMPARED TO EU-25



Germany

Assessment of National Reform Programme

1. Real GDP growth in Germany averaged 2% over the period in 1996-2000. It fell to half that rate by 2005, before recovering to an expected rate of 2.4% in 2006. Over the last decade, labour productivity growth has been slightly above the EU average, and has been improving in recent years. GDP per capita is foreseen at 109% of the EU average in 2006. Employment is projected to increase to a rate of 65.8% of the working age population in 2006. Employment of older workers has continued to rise, reaching a rate of 45.4 % in 2005, which is above the EU average. Unemployment is forecast to fall to 8.9 % in 2006.
2. Germany's economic performance is held back by a high level of structural unemployment and sluggish productivity growth. To sustain growth and job-creation, economic policy is confronted with the task of tackling these structural bottlenecks, while consolidating public finances to ensure long-term sustainability.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified 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 reform of the labour market. In its 2006 Annual Progress Report (APR) the Commission pointed out that a stronger response was needed regarding competition in services, integration of less qualified workers, and an increase in childcare facilities.
4. Germany is making some good progress in implementing its NRP, especially in the macro- and micro-economic fields. Progress is particularly strong in improving the business environment, where various better regulation measures have been implemented. On the key challenge of employment policies, implementation has moved ahead, but further work remains to be done on tackling high structural unemployment, including for priority categories. There remain, however, concerns over access to some telecommunications markets, over bringing less qualified workers into the labour market, and in the field of childcare.
5. Germany is responding reasonably well to the commitments made at the 2006 Spring European Council. An ambitious yet realistic target for investment in R&D has been set (3% of GDP by 2010). Steps have been taken towards creating a one-stop shop for business start-ups, though the process is not yet complete, and to widen entrepreneurship education. However, the Implementation Report does not refer to progress on creating a single contact point for hiring the first employee. Germany has set an objective of ensuring no young person remains unemployed for more than three months, which would go further than the Spring European Council commitment, but this has not yet been fully achieved.

6. Responsibility for the NRP and its implementation is now dealt with at ministerial level, and the consultation process has been improved by involving a large number of stakeholders. The 2006 Implementation Report provides most of the information needed to assess implementation of Germany's reform agenda, though budgets and timelines have not always been given, and aggregate budgets for the regional level would have been useful. The reduction of the number of laws requiring co-decision by the *Bundestag* and *Bundesrat* may facilitate and accelerate the reform if complemented by the announced revision of fiscal relations between the federal and state level. According to the draft National Strategic Reference Framework for 2007-2013, Germany's Structural Funds expenditure is consistent with the renewed Growth and Jobs Strategy.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The NRP identified sustainability of public finances (including sustainable growth and social security) as the key challenge. The measures announced in the NRP have been implemented, and helped by a strong economic recovery, a government deficit below 3% of GDP will be reached in 2006, one year ahead of the 2007 deadline set by the Council. Without further measures, however, progress towards achieving the medium-term objective of a balanced budget is likely to be slow.
8. The NRP set 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. A reduction of the corporate income tax rate has been announced. On the expenditure side, the Federal Employment Agency is making progress in using its resources more efficiently.
9. In November 2006, the government adopted a draft law by which the statutory retirement age will be raised in steps to 67 years, from 2012 onwards. Although exemptions to the higher age limit are being granted to a considerable extent, the move will enhance the long-term sustainability of public finances. Some budget items and timelines in the Implementation Report are not sufficiently clear, in particular regarding the health care system, for which the NRP foresaw a financial reform and higher efficiency in service provision through more competition. The main points for reform in the health care system, as listed in the Implementation Report and in the draft law, contain elements aiming at improving efficiency and fostering competition, but further clarifications are needed to assess how the proposed "health care pool" (*Gesundheitsfonds*) would meet these objectives. Measures to adapt the statutory long-term care insurance to demographic changes by introducing elements of a funded scheme, announced in the NRP for summer 2006, have not yet been drafted but are announced for the course of 2007. The reduction of non-wage labour costs resulting from the reduction in the contribution rate to the unemployment insurance will partly be offset by an increase of contributions to the health and pension systems, so that the impact on employment will be lower than expected. The German government has recently taken measures to reduce contributions to unemployment insurance below the levels it had announced in the NRP.

10. The Implementation Report lists several measures designed to support the catching-up process of the eastern *Länder*. Further detail would be welcomed on measures to increase the effectiveness of the initiatives already in place.
11. Germany has in general made good progress with the implementation of measures responding to its macro-economic key challenge. It is too early to assess results, especially as regards the health care system, and to assess whether they will be sufficient both to ensure long-term fiscal sustainability and to reduce non-wage labour costs.

Micro-economic policies

12. The NRP presented as key challenges; knowledge society; market functioning and competitiveness; business environment; and ecological innovation.
13. There has been good progress on R&D and innovation policies, notably the "Excellency Initiative", to bolster the position of top universities, the "Pact for Research and Innovation (2006-2010)", and the "High Tech Strategy", adopted in August 2006. Additional federal spending commitments have been made to reach the R&D investment target of 3% GDP by 2010. Reaching the target will mainly depend on the leverage effect of federal R&D spending on expenditure by businesses and the *Länder*. The Implementation Report also mentions new measures at regional level to promote innovation through closer cooperation between science, research and businesses, particularly in the area of ICT. An information society initiative iD2010 was decided upon in November 2006.
14. Considerable progress has been made in improving the business environment through better regulation. Legislation due to be adopted in 2006 will reduce administrative costs, particularly for SMEs. A standard cost model is being adopted, on the basis of which further targets for reduction of administrative costs will be set by mid-2007. Following a screening of federal legislation, an independent body for impact assessments (*Normenkontrollrat*) has become operational. Reporting requirements for SMEs are being reduced at federal level. A web-based information tool (*Startothek*) has been created as a first step towards establishing a one-stop-shop for company start-ups. The issues of "hiring the first employee" and reducing start-up times have been partly addressed. Some progress is visible regarding entrepreneurship education. The simplification of regulations on infrastructure planning is well under way, supporting the investment climate.
15. The federal regulatory office for network services has been given additional powers to improve incentives, review price setting and to address remaining problems such as the high market concentration, lack of transparency and vertical foreclosure in the energy markets. Since January 2006, the office has also been in charge of rail transport and ensuring non-discriminatory access to the rail infrastructure. Concerns remain regarding the intention not to introduce regulation which would open certain new markets, for example modern broadband networks, to competition, as well as the delay in effectively regulating wholesale bitstream access in other words the ability of competitors to offer their clients broadband products based on wholesale access to certain digital services provided by the incumbent). Regarding public procurement, the recent transposition into national law of the relevant EU Directives is a first step towards simplifying and modernising the German public procurement framework. In

the field of professional services, Germany has taken steps to relax the rules governing lawyers and architects, but significant restrictions remain in these and other heavily regulated professional services, as well as in the crafts sector.

16. The response to the key challenge "ecological innovation" was a strong point of the NRP, and good progress towards the well-defined objectives has been made. It is expected that the targets for greenhouse gas emissions will be reached, provided that remaining measures are implemented. However the market-oriented approaches to improving energy efficiency and diversity, mentioned in the NRP, are not described in the Implementation Report.
17. Overall, Germany has made good progress on the micro-economic key challenges, especially in the areas of knowledge society, business environment, and ecological innovation. However, the weak points referred to in the 2006 APR regarding the functioning of markets and competition have not been fully followed up.

Employment policies

18. The NRP focused on the education system and lifelong learning in the context of promoting the knowledge society. It called for: raising adaptability and employability; an increase in labour market participation; adapting the labour market to the demographic challenge through structural reforms of labour market institutions; and for improving the reconciliation of family life and work. The 2006 Implementation Report sticks to the challenges identified in the NRP.
19. Given the high level of unemployment among the low-skilled, the report announces more qualification measures for this target group and a review of the tax and benefit system. In the NRP an extension of the probationary period for new employees was proposed but this proposal was coupled with a proposal to abolish simple unconditional fixed-term contracts and subsequently both were dropped.
20. Major difficulties remain with respect to the effectiveness of the employment services in dealing with unemployed people who are hard to place, especially the long-term unemployed. The NRP objective that no young person should be unemployed for more than three months has not yet been met, and demand for apprenticeships by far outstrips vacancies for such positions. The design of measures aiming at a higher employment rate of older workers has been improved, but there should be more focus on prevention. The announced agreement with social partners to improve the qualifications of older workers has turned into an agreement to raise awareness and exchange good experiences about older workers' employment. Regarding participation of women in the labour market, and the reconciliation of work and family life, some progress has been made in the provision of childcare infrastructure, but the number of childcare places is still low. Important challenges such as the high gender pay gap are not addressed directly. Increased attention has been given to the integration of immigrants, including an announced "national integration plan" to improve the school education and vocational qualifications of young migrants.
21. The Implementation Report refers to various initiatives aiming at improving the educational system. The approach seems appropriate and should be closely monitored in close cooperation with the Länder, given their responsibility in the field

of education. A new expert forum is announced to develop recommendations for improving life-long learning, but no explicit reference is made to the plans of the NRP to develop vocational qualification for adults into a fourth pillar of the German educational system and to create a legal framework for improving the financing of adult vocational training.

PART III: CONCLUSIONS

22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
23. Germany is making good progress overall in the implementation of its National Reform Programme, and especially on the macro- and micro-economic key challenges and priority actions. It is moving forward more slowly in the field of employment. Germany is also responding reasonably well to the commitments made at the 2006 Spring European Council.
24. Strengths of the reforms in 2006 include the progress in the area of consolidation and sustainability of public finances, as well as the implementation of various better regulation measures, such as the web-based information tool "*Startothek*" for business start-ups and the establishment of an independent council at federal level for impact assessment (*Normenkontrollrat*). Other strengths are evident in the field of knowledge society (R&D and innovation), as well as in the higher visibility given to measures for the integration of older unemployed people.
25. The policy areas in the German National Reform Programme where weaknesses need to be tackled with the highest priority are: improving the long-term sustainability of public finances; improving competition, notably in professional services and new broadband markets; and tackling structural unemployment. Against this background, it is recommended that Germany:
 - improve long-term sustainability of public finances by continuing fiscal consolidation, leading to debt reduction, and by implementing the health care reform with a view to keeping expenditure growth in check and strengthening efficiency in the health sector;
 - improve competition in product and services markets, notably by continuing to relax restrictive rules governing many liberal professions and effectively regulating wholesale bitstream access;
 - tackle structural unemployment including by integrating the low-skilled into the labour market through better access to qualifications, pursuing the proposed tax-benefit reform and by providing more effective employment services for the long-term and young unemployed.
26. In addition, it will be important for Germany over the period of the National Reform Programme to focus on: ensuring that health care reform makes the health system more efficient; improving public procurement procedures; removing barriers to competition in the rail sector and in gas and electricity networks, where unbundling

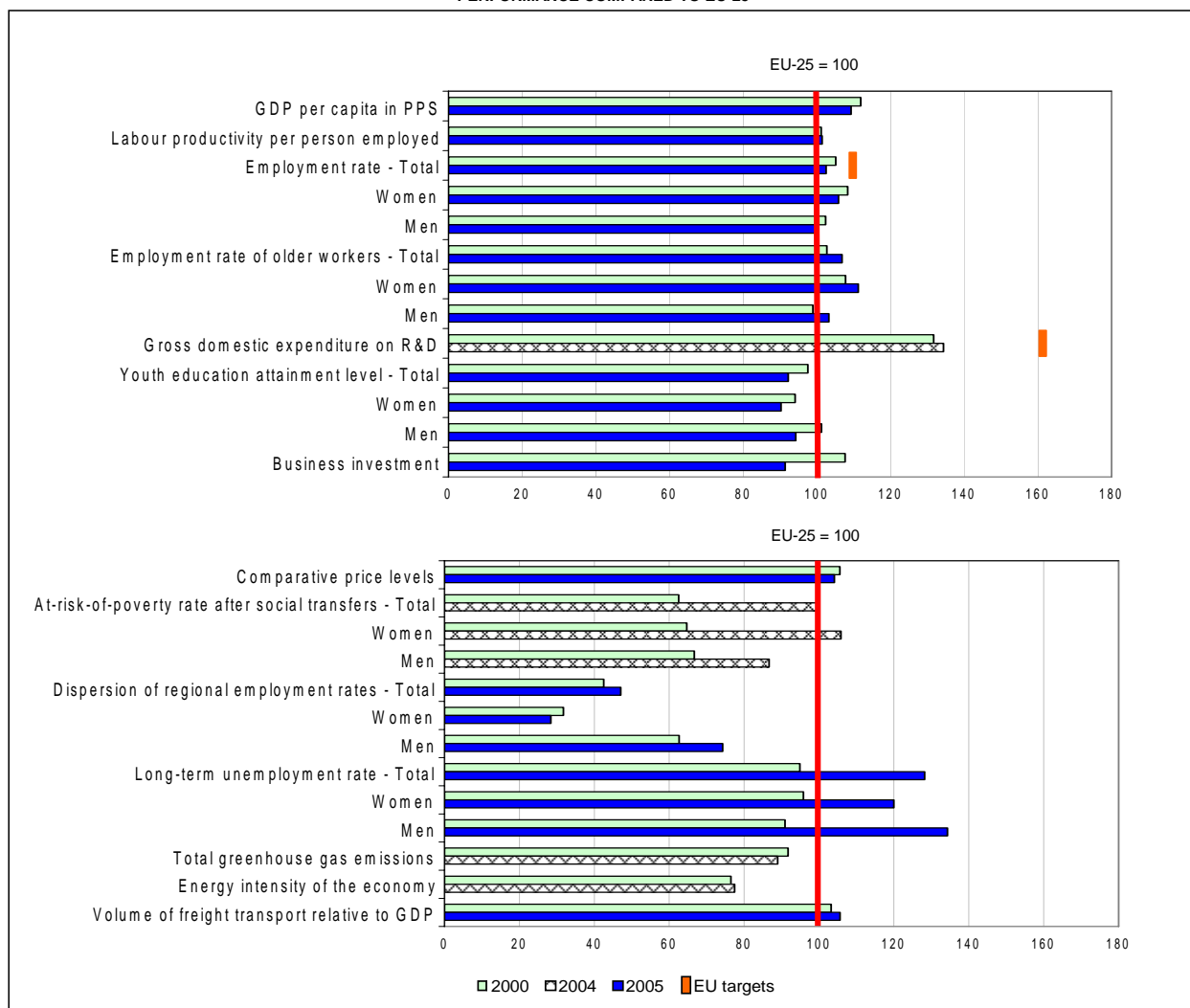
has been ineffective; speeding up business start-ups and facilitating hiring the first employee; building on existing measures to improve lifelong learning, including by developing adults' vocational training into a fourth pillar of the educational system; increasing the provision of childcare facilities.

PART IV: STATISTICAL GRAPHS AND DATA

GERMANY

	DE							EU25					
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target		
GDP per capita in PPS	111.9	110.0	108.5	108.1	108.0	109.3	:	100.0	100.0	100.0	70.0		
Labour productivity per person employed	101.2	100.1	99.6	100.2	99.7	101.4		100.0	100.0	100.0			
Employment rate													
Total	65.6	65.8	65.4	65.0	65.0	65.4b		62.4	63.3	63.8			
Women	58.1	58.7	58.9	58.9	59.2	59.6b		53.6	55.7	56.3			
Men	72.9	72.8	71.8	70.9	70.8	71.2b		71.2	70.9	71.3			
Employment rate of older workers													
Total	37.6	37.9	38.9	39.9	41.8	45.4b		36.6	41.0	42.5			
Women	29.0	29.4	30.6	31.6	33.0	37.5b		26.9	31.7	33.7			
Men	46.4	46.5	47.3	48.2	50.7	53.5b		46.9	50.7	51.8			
Gross domestic expenditure on R&D	2.45	2.46	2.49	2.52	2.50	2.51e		3.0	1.86e	1.86e		:	3.0
Youth education attainment level													
Total	74.7	73.6	73.3	72.5	72.8	71.5b			76.6	77.1		77.5	
Women	74.8	73.6	73.8	73.4	74.2	72.5b			79.5	80.1		80.3	
Men	74.6	73.6	72.6	71.6	71.5	70.4b	73.7		74.2	74.7			
Comparative price levels	105.6	107.1	107.5	108.7	106.6p	104.1p	100.0		100.0p	100.0p			
Business investment	19.7	18.3	16.7	16.2	16.0	15.9	18.3		17.1	17.4			
At-risk-of-poverty rate after social transfers													
Total	10.0	11.0	15.0b	15.0	16.0	:	16.0e		16.0e	:			
Women	11.0	:	18.0b	17.0	18.0	:	17.0e		17.0e	:			
Men	10.0	:	13.0b	13.0	13.0	:	15.0e		15.0e	:			
Dispersion of regional employment rates													
Total	5.7	6.1	5.9	6.0	6.2	5.6	13.4		12.2	11.9			
Women	6.5	6.5	5.9	5.7	5.9	4.8	20.5		17.3	16.9			
Men	6.2	6.8	7.0	7.1	7.6	7.2	9.9	10.2	9.7				
Long-term unemployment rate													
Total	3.7	3.7	3.9	4.5	5.4	5.0b	3.9	4.1	3.9				
Women	4.6	4.6	4.8	5.2	6.1	5.4b	4.8	4.7	4.5				
Men	3.0	3.0	3.3	3.9	4.8	4.7b	3.3	3.6	3.5				
Total greenhouse gas emissions	83.2	84.1	82.8	83.3	82.5	:	90.7	92.7	:				
Energy intensity of the economy	159.7	162.5	158.7	161.0	158.8	:	208.8	204.9	:				
Volume of freight transport relative to GDP	103.3	103.3	102.3	103.2	108.0	110.6	100.1e	104.6be	104.7e				

PERFORMANCE COMPARED TO EU-25



Estonia

Assessment of National Reform Programme

1. Estonia's 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 real GDP growth of over 7% annually during the last decade. Rapid productivity growth has been reflected in a sharp increase in wages. GDP per capita has risen swiftly to an estimated 65.3% of the EU average in 2006. The employment rate is estimated to increase to 68% in 2006. Unemployment is expected to fall from 7.9% in 2005 to 5.4% in 2006.
2. Estonia is reaping the benefits of bold and comprehensive structural reforms during the early years of transition, which have increased the economy's responsiveness to market forces and its international openness. A sound budgetary position has helped promote a growth and employment-friendly environment, attracting also substantial private investment from abroad. While the fundamental reforms of the early years drove entire groups out of the labour force, as reflected in low participation and high inactivity rates, recent years have been marked by strong job creation and a swift reduction in unemployment. Certain sectors now face labour shortages, exacerbated by emigration, such that labour supply is a major bottleneck for further catching up with EU average GDP. The booming economic activity has pushed up the current account deficit and been accompanied by increasing inflationary pressures.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified two key challenges: R&D and innovation, and employment. The Commission's 2006 Annual Progress Report (APR) confirmed these priorities but pointed out that more needed to be done to increase private R&D investment, particularly through foreign direct investments, as well as to develop further active labour market measures and to improve skills, in order to achieve the ambitious employment target set.
4. Against the background of a stable macro-economic environment, Estonia is making good progress with the implementation of its NRP, including addressing its key challenges. Public R&D expenditure has been greatly increased in 2006. R&D financed by business is also reported to be growing. Despite all of the appropriate steps taken, given the high growth of GDP, it will be difficult to increase R&D expenditure faster than GDP, and the target set for 2010 (1.9% of GDP) remains therefore a serious challenge. The connection of the Estonian and Finnish electricity grids is expected to increase security of supply and create a more efficient electricity market. There has been good progress with measures which will contribute to environmental protection. Some improvements have been made to the business environment, although it will be important to complete the implementation of further measures scheduled in this respect. While a proactive competition policy is scheduled for 2007, it remains unclear to what extent progress has been made regarding governance structures. On employment, Estonia has implemented a wide

range of measures that have supported good labour market performance. The employment rate has increased and enabled Estonia to set a more ambitious target for 2010. Some progress has also been made in raising the skills level of the labour force, although in view of Estonia's low labour productivity, further measures are needed to reinforce existing efforts to enhance education, lifelong learning and active labour market policies. Estonia is experiencing difficulties in implementing measures to increase the flexibility of the labour market.

5. Estonia is responding positively to the commitments made by the 2006 Spring European Council. The measures being taken to facilitate the start-up and financing of innovative SMEs, while not yet complete, will help to improve the business environment. In the employment field, the relevant targets have been adjusted and education, social and active labour market measures are being carried out. The new Labour Market Services and Benefits Act entitles young unemployed people to a job, apprenticeship, additional training or other employability measure within six months. The target to reduce early school leaving has been incorporated in the NRP, but the one for the training of older workers has not. There have been several important steps in the energy field.
6. Progress on governance is good. A new Strategy Office in the State Chancellery has been set up to oversee implementation of the NRP. In order to strengthen ownership, the government has continued to consult widely with stakeholders. The Implementation Report was sent for information to the Parliament and approved by the Government. In contrast with the NRP, the Implementation Report contains detailed information on the budgetary costs of measures for 2005, 2006 and 2007. The report makes systematic reference to the use of cohesion policy instruments which is particularly important since the vast majority of activities in the report are (co-)financed through those cohesion instruments. It reflects significant efforts to ensure coherence between the National Strategic Reference Framework for the investment of Structural Funds and the NRP, and could serve as inspiration for others. However, information is lacking on the implementation of the general administrative capacity programme, which is important in dealing with the forthcoming injection of Structural Funds. Cohesion Policy funding will amount to 3.3% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. Maintaining sound public finances and the conditions for low inflation and price stability are the core objectives for macro-economic policies. Raising the employment rate is seen as key for sustaining the economy's strong growth performance in the future and for raising living standards. The Commission supported this analysis in the APR.
8. The Implementation Report confirms a prudent fiscal policy as the key element of macroeconomic stability in the framework of a currency board monetary regime pegging the kroon to the euro. Good progress has been made on almost all the targets formulated in last year's NRP. Public finances continue to be sound, at a surplus of 2.3% of GDP in 2005. Inflation has increased somewhat to above 4% year-on-year in

2005 and in 2006 to date, and is projected to remain above 4% in 2007-2008. External imbalances in the form of large trade and current account deficits remain persistent, and appear even to be rebounding in 2006 after a decline in 2005. However, these developments should be seen in the context of very strong growth and a rapid catching-up process with the EU as a whole.

9. With the GDP growth rate at 10.5% in 2005 and projected to be even higher in 2006, a prudent fiscal policy stance is needed to avoid adding further to demand pressures, which would heighten the risk of the economy overheating. Consequently and appropriately, the fiscal policy targets as outlined in the programme shift from balanced budgets in last year's NRP to budget surpluses for 2006. With regard to the sustainability of public finances, the current surplus contributes as a first step towards limiting the projected budgetary impact of an ageing population. Estonia's strategy of putting sustainability concerns at the heart of fiscal policy, including the implementation of a comprehensive pension reform which involves the accumulation of assets as well as a gradual increase in the pension age, influences positively the long-term outlook for the public finances. Further reform measures are in preparation.
10. Overall, the focus of macro-economic policies and measures proposed in the NRP on long-term fiscal sustainability and creating favourable conditions for further employment growth are appropriate. These policies have proved successful during the past year. On the whole, the ambition with regard to fiscal surpluses has become more pronounced in the Implementation Report, which should contribute to maintaining macro-economic stability and improving long-term fiscal sustainability.

Micro-economic policies

11. Estonia identified R&D and innovation as a key challenge for sustaining strong economic growth and enhancing competitiveness. Last year's Commission APR suggested focusing more strongly on increasing private R&D investment, and on the role of foreign direct investment in that context. In addition, the NRP proposed measures to improve the business environment and the functioning of markets and infrastructure.
12. Estonia is making good progress in relation to the R&D and Innovation key challenge. The government has increased state budgetary allocations for R&D in 2006 by 50.6%. Business R&D expenditure is also on the increase. Moreover, Estonia has upgraded targets that have already been achieved, such as the numbers of innovative enterprises and of R&D personnel. However, human resources may prove to be a bottleneck, both in the public and private sector. It also has to be ensured that R&D results are translated into new innovative products and services. A clear focus on priority research sectors and improved inter-ministerial cooperation will be crucial. Particular attention will be needed to strengthen the cooperation between universities and enterprises, to increase the number of scientists and engineers and to create more attractive conditions for R&D-intensive foreign direct investment. The government has recently approved a new strategy on R&D and Innovation, which will address these issues.
13. The Implementation Report includes measures to improve the business environment, including the regulatory environment. In terms of better regulation, a system of

regulatory impact assessment and an action plan to reduce the administrative burden for entrepreneurs is to be introduced, but the concrete shape and implementation of these measures remains unclear. State fees are to be generally reduced, including those for starting a business. The legal framework for one-stop-shops to assist in the establishment of new companies has been prepared and notaries have been empowered to implement all procedures necessary for setting up a business. A new target has been set for setting up a company (7 instead of 25 days by 2008). In order to improve businesses' access to finance, the parliament has approved legislation establishing the Estonian Development Fund to support innovative start-ups, which should start to function in the beginning of 2007. In addition, the start-up scheme managed by Enterprise Estonia is being reorganised to better suit SMEs' needs and should apply from 2007. No progress appears to have been made regarding the envisaged network of local business angels.

14. A proactive competition policy is envisaged for 2007, but it is not clear how much progress has been made on strengthening the national competition authority and on improving its cooperation with sectoral regulators, in order to increase competition in regulated sectors such as network industries. The implementation of competition rules through the criminal enforcement system remains a challenge.
15. Considerable investments for the development of the public transport infrastructure of rail and road systems and the establishment of nation-wide broadband access are planned for 2007 and 2008. Measures to improve e-services in the public sector and strengthen ICT education at university level are continuing. The Estlink undersea cable between Estonia and Finland, aiming at increased security of supply and a more efficient electricity market, should be finalised by the end of 2006.
16. Progress is being made on a broad range of environmental issues, notably energy, waste, water and nature protection. The implementation of an ecological tax reform has started by increasing pollution charges and implementation of the Energy Conservation Programme is enhancing energy efficiency and the production of energy from renewable sources.
17. Overall, there is good progress on the R&D and innovation challenge, and appropriate measures are also being taken in all other key micro-economic areas, although these are at differing stages of implementation.

Employment policies

18. The NRP identified employment as a key challenge, including increasing the employment rate, reducing structural unemployment, and improving skills through lifelong learning. The Commission highlighted in last year's APR the need to develop further active labour market policies and to improve skills in order to further increase labour supply and achieve the ambitious employment target. 19. A large number of measures have been taken to increase the employment rate. Many labour market indicators, including the long term unemployment rate, have improved. The favourable labour market situation has allowed more ambitious employment related targets and deadlines to be set. However, reducing structural unemployment and getting inactive people into the labour market remains important in order to raise labour supply. Labour shortages exist in certain sectors partly due to emigration. Estonia recently revised downwards its target for increasing support for the

unemployed through active labour market policies. At the same time, the number of unemployed currently participating in such schemes is very low. Therefore a higher level and efficiency of active labour market support is needed for a range of disadvantaged groups. An important new law on labour market services and benefits establishes a system of case management and should help ensure that benefits are more closely linked to participation by unemployed recipients in activation measures. The government is discussing its future approach to targeted work-based immigration.

20. The government has announced it will propose an update of the labour law for 2007 to improve the flexibility of the labour market. Considering that only 16.5% of the employees in Estonia were in non-standard employment or self-employed in 2005 (EU25 39.6%), the promotion of flexible forms of work should be further pursued in order to generate further labour supply. Principles to regulate temporary agency workers are due to be put forward by the end of 2006. A reinforced social dialogue would be helpful for achieving progress.
21. Estonia spends a high share of its GDP on education. The overall educational level is good, but education and training systems are not sufficiently geared to market demand. Skill shortages are evident in various sectors. The majority of action taken has dealt with vocational education and training. For general education, curricula reform and a new financial model are anticipated. A “Youth Work Strategy” for 2006-2013 has been adopted, which is important given that educational attainment levels of young people have declined recently. A lifelong learning strategy was approved in 2005, but the strategy does not cover all systems and levels of education and training. A major concern is the low rate of adult participation in lifelong learning, which has recently decreased and is just over half the EU average. A new financing system for lifelong learning is being established.
22. Overall, there has been progress on increasing employment supported by strong economic growth, although further policy reinforcements are necessary in several areas. To increase the supply of labour and increase labour productivity, it would be necessary to raise the skills level of the labour force by reinforcing the reform effort in education, lifelong learning and active labour market policies. It would also require progressing further with the renewal of the labour laws to create a more flexible labour market.

PART III: CONCLUSIONS

21. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
22. Estonia is making very good progress with the implementation of measures responding to the country's key challenges of R&D and innovation and employment and to the four priority actions formulated by the 2006 Spring European Council. It also makes impressive efforts to ensure coherence between the National Reform Programme and cohesion policy and the Implementation Report can be considered a model in this regard.

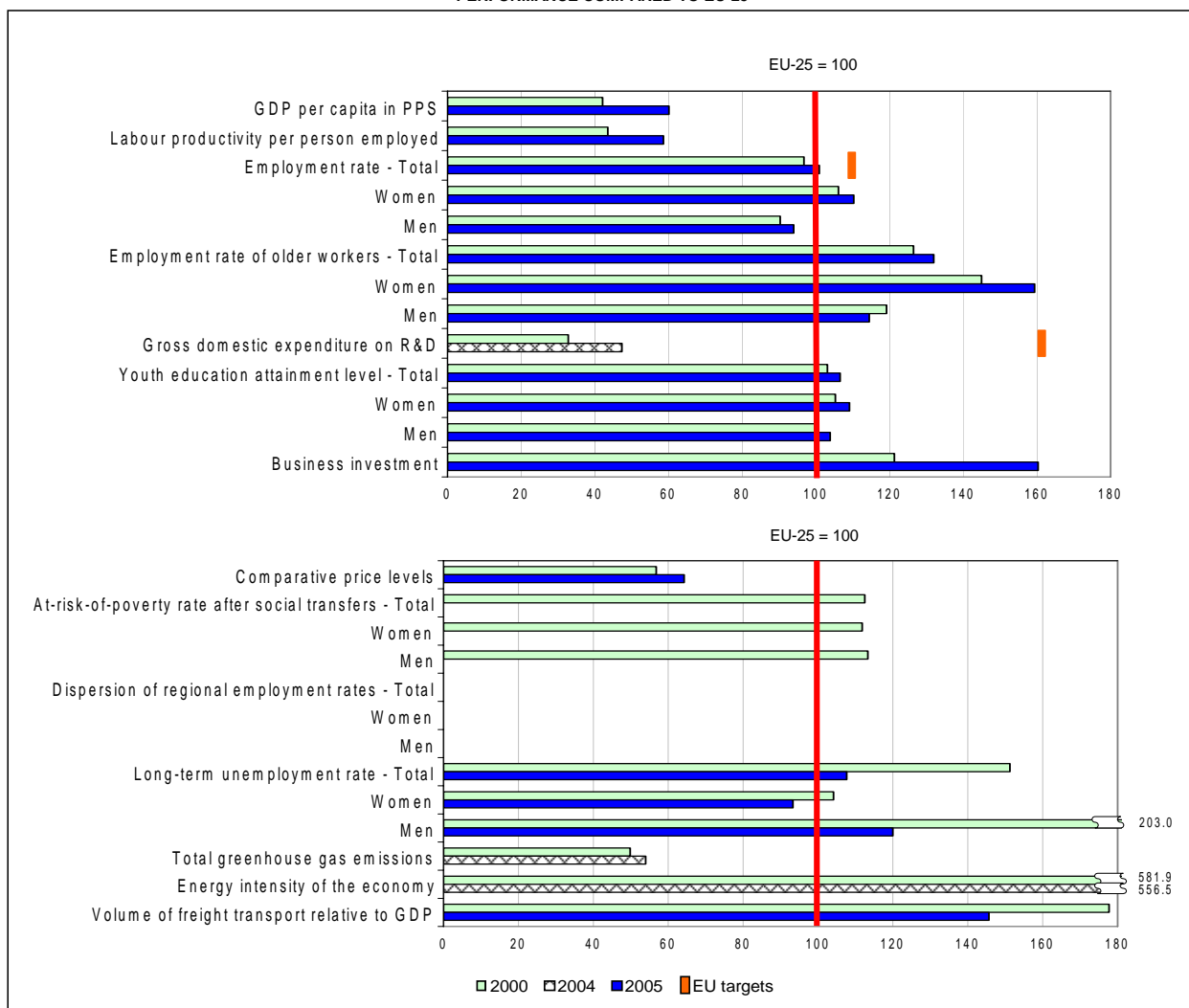
23. Among the strengths of the Estonian National Reform Programme and its implementation are: the upgrading of several policy targets, which shows an appropriately ambitious approach; the establishment of the new Strategy Office to strengthen implementation, which is a good example for others; the successful macro-economic policies proposed in the National Reform Programme on fiscal sustainability and on creating favourable conditions for employment growth; the considerable effort made to increase both public and private R&D expenditure and to improve the framework conditions for business R&D; measures to facilitate start-ups and financing of innovative SMEs; and progress on a broad range of environmental issues, notably ecological tax reform.
24. It will be important for Estonia over the period of the National Reform Programme to focus on , clearer prioritisation and improved inter-ministerial cooperation for the effective use of R&D and innovation expenditure; reinforcing efforts to ensure that R&D results are translated into innovative services or products; encouraging closer cooperation between universities and enterprises; vigorously implementing the planned proactive competition policy; improving labour market flexibility through further progress in the renewal of labour laws; reinforcing active labour market policies and raising the skills level of the labour force further by reinforcing the reforms in education and lifelong learning

PART IV: STATISTICAL GRAPHS AND DATA

ESTONIA

	EE							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	42.1	43.7	46.8	50.3	53.0	60.1		100.0	100.0	100.0	
Labour productivity per person employed	43.5	45.0	47.4	50.0	52.8	58.6		100.0	100.0	100.0	
Employment rate							70.0				70.0
Total	60.4	61.0	62.0	62.9	63.0	64.4		62.4	63.3	63.8	
Women	56.9	57.4	57.9	59.0	60.0	62.1		53.6	55.7	56.3	
Men	64.3	65.0	66.5	67.2	66.4	67.0		71.2	70.9	71.3	
Employment rate of older workers											
Total	46.3	48.5	51.6	52.3	52.4	56.1		36.6	41.0	42.5	
Women	39.0	42.1	46.5	47.3	49.4	53.7		26.9	31.7	33.7	
Men	55.9	56.7	58.4	58.9	56.4	59.3		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.61	0.71	0.72	0.79	0.88	0.94p	1.9	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	79.0	79.8	81.4	81.5	80.3	82.6		76.6	77.1	77.5	
Women	83.7	85.2	85.8	85.1	87.5	87.6		79.5	80.1	80.3	
Men	74.2	74.7	77.1	77.9	73.2	77.6		73.7	74.2	74.7	
Comparative price levels	56.8	59.7	62.1	63.2	62.9p	64.2p		100.0	100.0p	100.0p	
Business investment	22.2	22.5	24.9	25.1	28.4	27.9		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	18.0	18.0	18.0	18.0	:	:		16.0e	16.0e	:	
Women	19.0	19.0	19.0	20.0	:	:		17.0e	17.0e	:	
Men	17.0	17.0	17.0	17.0	:	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	-	-	-	-	-	-	-	13.4	12.2	11.9	
Women	-	-	-	-	-	-	-	20.5	17.3	16.9	
Men	-	-	-	-	-	-	-	9.9	10.2	9.7	
Long-term unemployment rate											
Total	5.9	6.0	5.4	4.6	5.0	4.2		3.9	4.1	3.9	
Women	5.0	5.4	4.4	4.4	4.4	4.2		4.8	4.7	4.5	
Men	6.7	6.6	6.3	4.8	5.6	4.2		3.3	3.6	3.5	
Total greenhouse gas emissions	45.2	45.2	45.4	49.7	50.0	:		90.7	92.7	:	
Energy intensity of the economy	1214.8	1273.0	1153.2	1179.1	1140.2	:		208.8	204.9	:	
Volume of freight transport relative to GDP	177.9	159.0	164.7	150.8	159.5	152.5		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Greece

Assessment of National Reform Programme

1. Greece has experienced strong economic growth, averaging 4.4% since 1999, with labour productivity growth clearly above the EU average. GDP per capita is estimated at 83% of the EU average for 2006. The employment rate foreseen for 2006 (60.7%) remains far below the EU-wide target, particularly for women and older workers, and unemployment (9.3%) is still high. After many years of high public deficit, Greece is expected to reduce the deficit significantly in 2006 (2.6% of GDP), while public debt ratio remains one of the highest in the EU (at 104.8% of GDP).
2. Greece experienced recently strong growth of GDP and employment, falling unemployment and some recovery of competitiveness. The government deficit has been above 3% of GDP for a number of years, accompanied by high debt. Economic policy is confronted with the task of creating a virtuous circle between macro-economic stability, micro-economic reforms aimed at boosting competition and enhancing the efficiency and ability to innovate of the Greek productive system, and measures aimed at raising labour market participation and employment as well as securing social cohesion. Consolidation of public finances to achieve long-term sustainability would help reduce economic uncertainty, create more favourable conditions for private investment and make room for enhanced expenditure on human capital and infrastructure.

PART I: GENERAL ASSESSMENT

3. The Greek 2005-2008 National Reform Programme (NRP) identified key challenges in the field of public finances, employment, education and lifelong learning, as well as in a broad range of micro-economic and environmental policy areas. The Commission broadly shared this analysis and in the 2006 Annual Progress Report (APR) invited Greece to pay further attention to fiscal consolidation; R&D and innovation; modernising public administration; active labour market policies and the reforms of education and training. The Commission also expressed concerns over the lack of targets, timetables and budgetary implications in the NRP.
4. The 2006 Implementation Report addresses the challenges set out in last year's NRP. Greece is moving ahead relatively strongly in the macro-economic area, whereas progress in implementation of the micro-economic and employment reforms is limited.
5. There is good progress on consolidation of public finances. There are promising signs of progress in improving the business environment; R&D and innovation; improving public administration; and education and training, although actions in these areas need to be strengthened and vigorously implemented. Progress is limited on: reforming the pensions system; environmental management and infrastructure; public procurement; reducing undeclared work; the level and efficiency of active labour market policies; and on increasing adult participation in lifelong learning.

6. Greece is partly responding to the commitments made by the 2006 Spring European Council. Progress has been made to reinforce entrepreneurial incentives, to improve the business regulatory environment, to strengthen competition and to improve the functioning of network industries and of public sector enterprises. However, the time and cost of starting up a business remains high, while nothing is reported on the number of procedures necessary for recruitment of the first employee. Moreover, more emphasis on youth employment is needed.
7. Communication on the Growth and Jobs Strategy with a wider range of stakeholders and citizens has improved. Coordination remains at political level. A constructive cooperation between the government and the social partners has been established and the Lisbon Observatory set up by the Greek Economic and Social Committee is assessing implementation. More work is needed to step up cooperation between central, regional and local level. The Implementation Report partially addresses the concerns expressed by the Commission over the lack of targets, timetables and budgetary implications. The National Strategic Reference Framework for the investment of Structural Funds includes a 60% earmarking for Growth and Jobs. However, there is a need to better integrate the two processes and to improve the absorption of the Structural and Cohesion Funds. Cohesion Policy funding will amount to 1.3% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macroeconomic policies

8. The government deficit is expected to fall in 2006 and 2007 to below 3% of GDP with fiscal consolidation being more based on permanent measures and less on one-off measures. On the expenditure side, government consumption in nominal terms was reduced by 1.7% in 2006. A further reduction is budgeted in 2007, achieved through efficiency improvements. However, the lack of control of current expenditure, such as public consumption, pensions and health care has left primary current expenditure almost unaltered and this remains one of the main causes of fiscal slippage. The deficit of the public sector lies behind the sizeable slippage, which is expected to reach 8.5% of GDP in 2006. On the revenue side measures are announced to fight tax evasion and broaden the tax base as well as a series of measures to improve resource allocation and public enterprise performance and efficiency.
9. The Implementation Report assumes that the ambitious expected increase in employment levels will make an important contribution to sustainable public finances. It also puts forward a number of reforms in the health care sector, although there is no information on the quantitative and financial impact of these measures on government expenditure. The Implementation Report does not present a strategy for reforming the pension system. Nevertheless, a public consultation was launched in spring 2006 and an Advisers Committee established to study the social security system and the problems faced by the pension system. The government has announced that the reform of the pension system will be initiated after the next elections.

10. The government has invested much effort into restoring fiscal balance in the short-term, but has now to ensure the long-term sustainability of public finances. The substantial budgetary impact of ageing is of particular concern and needs to be considered a major priority.

Microeconomic policies

11. The NRP considers the following as key challenges: structural reform in product markets to strengthen the business environment, competition and export promotion; developing the knowledge society; improving capital markets; environment and sustainable development; and modernisation of public administration. In the 2006 APR, the Commission subscribed to this broad range of micro-economic policies.
12. Over the last two years Greece has adopted a number of measures to reinforce entrepreneurial incentives, for example reductions in corporate taxation. It has taken steps to improve the business regulatory environment, such as reforms to shop opening hours, simplification of licensing, and the establishment of a legal framework for one-stop-shops for setting up a business. There have also been measures adopted to strengthen competition and to improve the functioning of network industries (energy and telecommunications) and of public sector enterprises. However, the time and cost of starting up a business remains high, while nothing is reported on the number of procedures necessary for recruitment of the first employee. The NRP included a large number of actions focused on SMEs, manufacturing, tourism, land use, the environment and modernising public administration. The Implementation Report describes the plans to introduce better regulation practices, in the context of the modernisation of public administration. A comprehensive digital strategy aimed at spreading ICT use, an area where Greece lags behind, was launched at the end of 2005.
13. The most visible progress in terms of product market reform can be seen in the energy sector, where the European legislative framework has been transposed into national law to open up and organise the markets for electricity, natural gas and bio-fuels. Ensuring the independence of the energy regulator is important given the strong market position of the incumbent. Energy infrastructure projects are progressing, notably for cross-border connections. The transposition of the regulatory framework for electronic communications has been completed, but requires secondary legislation.
14. There has been some progress regarding the implementation of internal market legislation. However, Greek performance in this area remains among the weakest in the EU. In spite of legislative changes, public procurement continues to be problematic, with a large number of complaints lodged with the Commission. While the powers of the Competition Authority have been reinforced through the introduction of a programme for immunity from and reduction of fines (leniency) for firms revealing cartels, more action is needed to strengthen competition in the highly regulated professional services sector.
15. A consultation document for the development of Research, Technology and Innovation for the programming period 2007-2013 was published in 2006. It includes proposals to create innovation poles, clusters and business incubators, and measures to assist SMEs to become more innovative. The ambitious target to

increase the level of R&D expenditure to 1.5% of GDP by 2010 (from 0.6% of GDP in 2004) is reaffirmed. The proposals for a new legislative framework that would improve R&D governance, and make possible a more systemic approach to R&D and innovation possible are a positive development. The effectiveness of these measures needs to be confirmed, given their early stage and the limited capacity of the economy to transform further R&D funding into market-led innovation.

16. Some progress is reported in setting up the regulatory framework on the environment and the sustainable use of resources. However, Greece still has major problems to resolve regarding environmental infrastructure, in particular, the closure of illegal landfills and/or contaminated sites, and the functioning of waste water treatment plants. Significant investment will be needed to implement the Integrated Pollution Prevention and Control Directive. Concerning the use of renewable energy sources, administrative and technical problems and barriers such as complex licensing procedures have led to slow take up, although some positive initiatives have been taken.
17. Implementation has progressed in most micro-economic areas, but most of the measures are at an early stage or need additional measures to have impact. The development of adequate economic and environmental infrastructures and cost-effective public services remains most important for raising competitiveness. Progress in setting up and completing the environmental regulatory framework will need adequate infrastructure and strong enforcement to bear fruit. It is necessary to increase investment in research, and rapidly establish a comprehensive research and innovation strategy. The reinforcement of the regulatory and enforcement capability of the public administration, in particular the reform of public procurement, spatial planning, tax services, environmental management and the management of Structural Funds and state-aid, is essential for the successful implementation of reforms.

Employment policies

18. The NRP highlighted the need to raise the low employment rates, particularly for women, to tackle high unemployment, and to develop education and lifelong learning as the central employment priorities. It stressed the need to improve the functioning of the labour market and the adaptability of workers and enterprises, and to tackle undeclared work. The Commission subscribed to this analysis but underlined the need to reinforce active labour market policies, reform education and training, and reinforce regional and social cohesion.
19. The gender employment gap remains high with structural unemployment persistently high and concentrated amongst women. Several measures have been developed to facilitate reconciliation of family and work life. Unemployment among young people remains particularly high. Measures to address youth unemployment have been launched, and implementation will be completed by the end of 2007. Expenditure on active labour market policies is low and declining. There is no report on any review of the impact of the tax and benefit system and its interaction with the active measures. A clear active ageing strategy for retaining older people in employment is also lacking. In order to better match labour supply and demand, the development of an employment services network including private operators is foreseen.

20. Some measures have been introduced to improve the adaptability of workers and enterprises, support mobility and control undeclared work. However, non-wage labour costs remain high and have not been sufficiently addressed. There is also a need to further diversify working time arrangements and encourage part-time work in the public sector. Better design of employment protection legislation and renewed efforts to offer credible support to workers in their labour market transitions could improve "flexicurity" and contribute to reducing the sizeable informal sector.
21. The important commitments made in the NRP to improve investment in human capital through improvements in the quality of education and a significant increase in participation in lifelong learning (currently at 1.8% of the working population) now need urgent implementation. Particularly importantly, action is needed to increase public expenditure on education towards reaching the national target of 5% of GDP and to ensure efficient and effective use of these additional financial resources; to implement the framework laws on lifelong learning; to implement measures to reduce the number of pupils dropping out of school and to combat adult illiteracy; and to develop measures to improve skills in the public administration. Further attention should be paid to improving the transition from school to work and the relevance of education and training to labour market needs. There is no information on how to ensure better access to training for school leavers, low-skilled workers, older workers and workers in SMEs.
22. The Implementation Report covers a number of areas where important policies are introduced to tackle Greece's employment challenges. This requires a sustained commitment and better monitoring in close cooperation with social partners. More flexibility in the formal labour market will facilitate the transformation of undeclared work into regular employment and, coupled with stricter controls, should improve employment security for workers currently in the informal sector. Effective delivery of active labour market policies as a part of the modernisation of employment services, and the successful implementation of education and training reforms are equally crucial. Continued attention for youth employment is needed.

PART III: CONCLUSIONS

23. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
24. Greece is making limited progress in the implementation of its National Reform Programme. Greece is moving ahead relatively strongly in the macro-economic area, whereas progress with micro-economic and employment reforms is still insufficient. There is a limited policy response to commitments made by the 2006 Spring European Council. Regarding governance, better coordination and stronger ownership among administrative levels is needed.
25. Among the strengths of the Greek National Reform Programme and its implementation is the good progress made on the consolidation of public finances. There are promising signs of progress on: improving public resource allocation; improving the business environment; R&D and innovation; ICT; and education and training.

26. The policy areas in the Greek National Reform Programme where weaknesses need to be tackled with the highest priority are: improving the long-term sustainability of public finances by reforming the pension system; modernisation of the public administration; stronger measures to increase employment rates, tackle unemployment and undeclared work, modernise employment protection and promote labour mobility; and enhancing the quality and labour market relevance of education and training. Against this background, it is recommended that Greece:

ensure the continuation of fiscal consolidation and debt reduction and fix a timetable for the implementation of pension reform with a view to improving long-term fiscal sustainability;

modernise its public administration by building up effective regulatory, control and enforcement capacities, including through upgrading skills, in order to ensure effective use of Structural Funds;

modernise employment protection including legislation, reduce the tax wedge on labour, and strengthen active labour policies to foster flexibility and security in the labour market and transform undeclared work into formal employment;

increase investment in compulsory and higher education, implement the reform of lifelong learning and improve quality and responsiveness to labour market needs, reduce early school leaving, and increase adult participation.

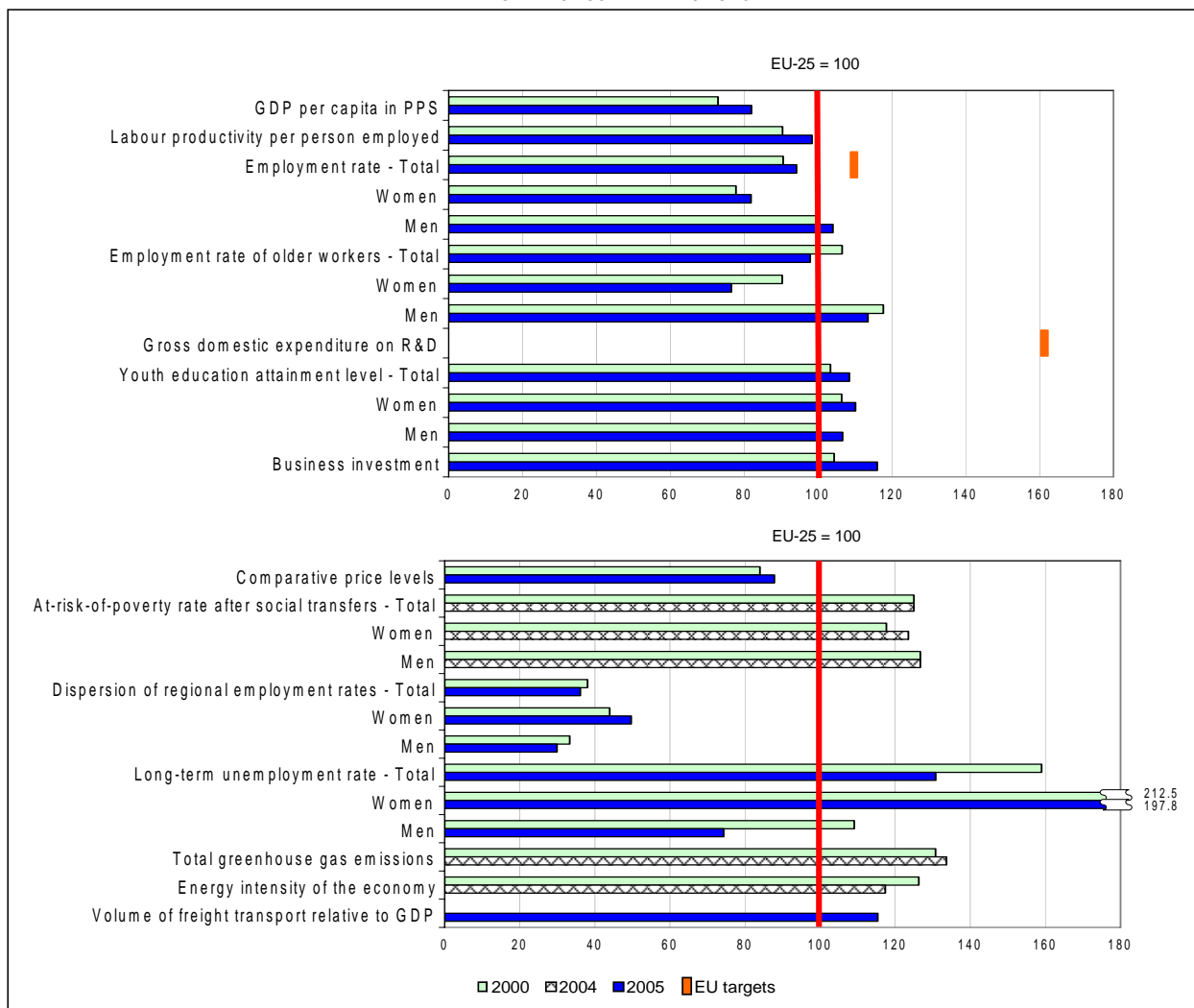
27. In addition, it will be important for Greece over the period of the National Reform Programme to focus on: accelerating efforts to set up a research and innovation strategy and to increase investment in R&D; improving the transposition of internal market directives; ensuring that Structural Funds are used effectively to help underpin Greece's reform policies, including on environmental protection; speeding up progress towards meeting the SME policy targets set by the 2006 Spring European Council; implementing policies to encourage women's participation in employment; and putting in place a consistent active ageing strategy.

PART IV: STATISTICAL GRAPHS AND DATA

GREECE

	GR							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	72.9	73.2	77.2	80.9	81.8	82.0		100.0	100.0	100.0	
Labour productivity per person employed	90.4e	91.8e	96.9e	100.4e	98.6e	98.4e		100.0	100.0	100.0	
Employment rate							64.1				70.0
Total	56.5	56.3	57.5	58.7	59.4	60.1		62.4	63.3	63.8	
Women	41.7	41.5	42.9	44.3	45.2	46.1		53.6	55.7	56.3	
Men	71.5	71.4	72.2	73.4	73.7	74.2		71.2	70.9	71.3	
Employment rate of older workers											
Total	39.0	38.2	39.2	41.3	39.4	41.6		36.6	41.0	42.5	
Women	24.3	22.9	24.0	25.5	24.0	25.8		26.9	31.7	33.7	
Men	55.2	55.3	55.9	58.7	56.4	58.8		46.9	50.7	51.8	
Gross domestic expenditure on R&D		0.64		0.63			1.5	1.86e	1.86e		3.0
Youth education attainment level											
Total	79.2	80.2	81.1	81.7	83.0	84.1		76.6	77.1	77.5	
Women	84.6	84.8	86.0	86.8	86.8	88.5		79.5	80.1	80.3	
Men	73.6	75.3	76.1	76.6	79.2	79.7		73.7	74.2	74.7	
Comparative price levels	84.0	84.5	82.2	84.5	85.1p	87.8p		100.0	100.0p	100.0p	
Business investment	19.1	19.6	19.9	21.2	21.0	20.2		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	20.0	20.0		21.0b	20.0			16.0e	16.0e		
Women	20.0	22.0		22.0b	21.0			17.0e	17.0e		
Men	19.0	19.0		20.0b	19.0			15.0e	15.0e		
Dispersion of regional employment rates											
Total	5.1	4.3	3.8	3.2	4.1	4.3		13.4	12.2	11.9	
Women	9.0	8.6	8.2	6.5	8.3	8.4		20.5	17.3	16.9	
Men	3.3	2.6	2.0	2.1	2.5	2.9		9.9	10.2	9.7	
Long-term unemployment rate											
Total	6.2	5.5	5.3	5.3	5.6	5.1		3.9	4.1	3.9	
Women	10.2	9.1	8.6	8.9	9.4	8.9		4.8	4.7	4.5	
Men	3.6	3.3	3.1	3.0	3.0	2.6		3.3	3.6	3.5	
Total greenhouse gas emissions	118.6	120.0	119.8	123.6	123.9			90.7	92.7		
Energy intensity of the economy	263.6	260.6	258.0	247.8	240.4			208.8	204.9		
Volume of freight transport relative to GDP				108.0		120.8		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Spain

Assessment of National Reform Programme

1. Over the last decade Spain has experienced annual average real GDP growth at around 3.7% and a sustained pace of catching up to GDP per capita, which could reach 99% of the EU average in 2006. Inflation is expected to remain around one percentage point above the euro area average. As a result of strong job creation, the employment rate has increased significantly and is projected to attain 66% at the end of the current year, still below but approaching the 70% target set for the EU as a whole under the Growth and Jobs Strategy. Unemployment has considerably decreased and at a rate below 8.5% is close today to the EU average.
2. Having nearly completed the catching-up with EU levels of per capita GDP, Spain is facing the task of simultaneously maintaining strong and balanced growth while reducing external imbalances and job creation, and enhancing productivity. Moreover, strong job creation remains coupled with a persistent strong segmentation of the labour market. Structural determinants, such as insufficient competition in certain sectors, especially utilities and some services, explain some of the persistent inflation differential. For productivity to grow sufficiently to maintain competitiveness, physical, human and knowledge capital will need to increase in quantity and quality.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified seven key policy areas: budgetary stability; R&D strategy; a better environment for business; promoting competition; infrastructure development; a better functioning of the labour market; and better education and human capital. The Commission shared this analysis but considered in the 2006 Annual Progress Report (APR) that further attention was needed to: boost competition in the retail and electricity sectors; to tackle the segmentation in the labour market (where a large number of workers have fixed-term contracts and few are able to move to permanent contracts); and to increase female employment.
4. Overall progress in implementation of the NRP is good and measures have been adopted in all key policy areas. Reinforcement of macro-economic and budgetary stability continues and the objective of full GDP per capita convergence with the EU25 is close to being met. While a pension reform is proposed, it will not fully counterbalance the significant projected increase in age-related spending. Many positive micro-economic measures are being taken and should help address low productivity. Emphasis should now be put on implementation, in particular of policies to boost research and innovation and improve the business environment. There is some progress on generating competition in the retail and the energy sectors, but further measures are needed to help ease inflationary pressure. A new agreement with social partners aims to help address a number of the labour market challenges but overall there is only partial progress in the employment field, where particular attention should be paid to the implementation of the new education law in order to

fight early school leaving and raise the general level of skills. Reinforced measures are needed to address the segmented labour market. Although progress on increasing the availability of child care is in line with the NRP objective, more progress is needed.

5. Spain is responding adequately to the commitments agreed at the 2006 Spring European Council. For example, an ambitious yet realistic target has been set for R&D expenditure, one-stop shops for business start-ups are being extended across the country and Spain has declared the aim of ensuring all unemployed people receive a job or training within six months.
6. Governance of the Strategy for Growth and Jobs has improved. However, reinforcement of the weak involvement of regional governments is limited to R&D and regional R&D targets need to be aligned with the overall R&D investment target set in the NRP. Involvement of stakeholders continues to be limited outside the employment field, where the agreement for better growth and employment reflects good cooperation with social partners and a good basis on which to progress further. Tools to monitor implementation are appropriate and include an extensive set of indicators. Additional work is needed to develop an assessment system to evaluate the impact of measures on growth and jobs objectives. Details on timetables and budgetary implications continue to be limited, making it difficult to assess the practicability of measures and their impact on budgetary stability. A clear link between the NRP objectives and the National Strategic Reference Framework priorities for the investment of Structural Funds has been established and aligned with the cohesion policy strategic guidelines for 2007-2013. This is also reflected in the earmarking of this funding to priorities under the Growth and Jobs Strategy, meeting the commitment agreed by the Council in this respect.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The NRP set the key challenge of reinforcing macro-economic and budgetary stability in order to support real GDP convergence (to reach the EU-25 average by 2010). Continuing efforts to achieve greater budgetary stability were also recommended in the 2006 APR. Sustained real convergence should be supported by enhanced productivity growth. An important quantified target has been set on public finances to reduce government debt to 34% of GDP by 2010 (38% of GDP in 2008).
8. The stabilizing role of fiscal policy has been reinforced at central and regional level. Specifically, a reform of the general law for budgetary stability was adopted, requiring budgetary targets to be set out in cyclically-adjusted terms. The reform also aims at increasing the transparency of public accounts and improving co-ordination with regional and local administrations. In addition, a reform of the pensions system has been announced aiming mainly at a better alignment between contributions and benefits. However, the reform might not be ambitious enough, and more information on budgetary impact is needed to better assess its adequacy and the consequence for long term sustainability.

9. Overall, there is satisfactory progress in the macro-economic area. Growth remains strong and Spain should continue to approach full convergence with the EU-25. An estimated government budget surplus of around 1.5% of GDP in 2006 will mean that gross debt is being reduced faster than targeted. These achievements are built on good recent performance, notably in terms of fiscal consolidation. However, growth is still mainly based on job creation, while productivity growth shows no signs of the recovery necessary to prevent further deterioration in competitiveness caused by persistently higher inflation than in the euro area as a whole. Such inflation differentials, which are of a cyclical and structural nature, contribute to the widening of current account deficits. Improving budgetary discipline and improving insufficient competition in certain utilities and services sectors (see below) will partly address this persistence. Significant increases in housing prices and household indebtedness may have an effect on medium-term growth prospects, if not adequately addressed.

Micro-economic policies

10. The NRP identified four key policy areas for action in the micro-economic area: R&D and innovation; business environment; competition, efficiency of public administration and better regulation; and infrastructure. Improving competition was identified by the 2006 APR as requiring further attention, in particular in the retail distribution and electricity sectors.
11. The comprehensive R&D and innovation plan was a strength of the NRP. Spain is making good progress with its implementation, with efforts to increase public-private collaboration, to improve research excellence and to expand the information society. There is a good record so far in terms of the substantial increase and better focus of resources as well as in the improved framework, but the mobilisation of private funds remains the key challenge. Achieving the research investment target (2% of GDP by 2010) hinges on whether the significant public funding effort will stimulate business spending. Coordination between central and regional governments is vital and most regions have concluded agreements for the implementation of programmes. Given the projected increase in funds, the level of coordination, quality and effectiveness needs careful monitoring to ensure funding can be used fully and effectively in less-developed regions and to improve the conditions under which research centres and firms collaborate. Initiatives to increase the use of ICT have stimulated a significant increase in investment. Progress is taking place in public e-services.
12. Reforms to improve the business environment are on course. The attention given to SMEs is welcome. The range of financing tools approved should help boost the number of start-ups and access to finance. The enlarged geographical coverage of one-stop-shops and the extension of the possibility of fast registration to all private limited companies are welcome steps towards simplification, although adequate implementation of such measures is still needed. A new state evaluation agency will start working on better regulation on 1st January 2007, but there is little information available on its specific function or whether it will systematically perform impact assessment of new regulations. The development of entrepreneurship education is progressing well at all educational levels.
13. Although some measures have been taken to increase competition in the retail distribution sector, more far reaching measures are needed. Competition in the

electricity market shows modest progress. The current regulated electricity tariff system is creating negative effects on the market structure by favouring incumbents. A progressive phase out is proposed (with liberalisation by 2011), but considerably later than required by the relevant EU directive. Gas price liberalisation is advancing faster, to be completed by 2008. There are concerns with respect to the new competences of the electricity market regulator. Spain has undertaken several measures to increase security of supply. In addition, there is a strong commitment to implement interconnection projects, since they are crucial to achieve further competition and to ensure security of supply in the Spanish market. Agreements at the recent Spanish-French summit may be helpful in this respect. On the positive side, a regional market with Portugal has started and new norms for auctioning interconnection capacity seem promising. The adoption of new competition legislation is a positive development and the steps taken to introduce a leniency programme are welcomed. Finally measures may be taken to promote competition in professional services following a forthcoming study by the “Tribunal de Defensa de la Competencia”. Spain should be encouraged to make further efforts to reorient state aid as the amount of sectoral aid programmed remains a source of concern.

14. Implementation of the infrastructure plan is progressing well. Measures on the environment are promising, but require full implementation since Spain is one of the EU countries furthest from its Kyoto target. The Spanish Action Plan on energy efficiency could contribute to reducing energy consumption and CO₂ emissions. The plan on renewable energy is promising in terms of CO₂ emission reductions and should help Spain achieve its renewable energy objectives for 2010. However, despite these promising steps, additional measures and the use of the Kyoto Clean Development Mechanism (buying allowances from abroad) will be necessary to reduce the gap.
15. Overall, Spain is making good progress in responding to its microeconomic key challenges. There is a strong implementation effort in the area of R&D and infrastructure and, to a lesser extent, on the business environment. Only modest progress is reported in the area of competition, where more far reaching measures will be needed to halt the deterioration in price competitiveness.

Employment policies

16. The NRP identified two key employment challenges: a better functioning of the labour market and better education and human capital. It also set quantitative targets for 2010: 66% overall employment rate, 57% female employment rate and reducing early school leaving to 15%. The Commission shared this analysis considering that a stronger response was needed to tackle segmentation in the labour market. It is also necessary to further increase female employment, despite recent progress.
17. Improved flexibility of permanent contracts would contribute to a smooth restructuring of the labour market. The major measure reported by the Implementation Report is the Agreement for Improved Growth and Employment, signed in 2006 by the Government and the social partners. This agreement introduces measures to promote permanent contracts through a new subsidy scheme, and the possibility, until the end of 2007, to transform fixed-term contracts into permanent ones, with a lower severance cost than for regular permanent contracts. Whilst a step in the right direction, this does not include the public sector, where the use of fixed-

term contracts is increasing. It fails to address part-time work, sets time limits on the application of certain measures and only introduces short-term changes in employment protection legislation. It will have a positive short term effect but mid-term perspectives seem uncertain. The Agreement for Improved Growth and Employment foresees that the government will assure that all unemployed people will receive training or a job offer within the first six months, but the Implementation Report does not present any concrete measure in this respect. The Agreement includes an action plan for modernising the public employment services, which appears particularly timely, as the share of contracts they manage appears to be diminishing. Despite efforts to legalise undeclared work among immigrants through an amnesty and special regularisation process, it appears that new challenges are arising concerning the regulation of current migration flows and the integration of migrants.

18. The planned law on gender equality is a positive step. It aims to reduce the gender employment gap and increase the presence of women in high ranking positions. However, efforts must be intensified in the provision of childcare, where very modest progress is reported. A new law is expected to be proposed in January 2007 to raise the quality of life of persons in need of assistance. It aims to create up to 300,000 new jobs within 10 years, and will facilitate the access of women to the labour market.
19. Spain has a segmented labour market with permanent contracts offering a high degree of job protection coexisting with temporary contracts with almost no restriction on hiring and firing. In 2005, temporary contracts accounted for one-third of total employment (more than double the EU average). Although these contracts are a way to increase flexibility, resorting to them does not address the fundamentals of inflexible permanent contracts (which do not provide for a more flexible organisation of working time, internal mobility, or a higher use of part-time work). The high use of fixed-term contracts, coupled with a high turnover rate of temporary jobs, gives little incentive either for employers or workers to invest in human capital. A comprehensive long-term approach to rebalancing flexibility and security in order to tackle the structural segmentation of the labour market might require further measures.
20. Investment in human capital is a key issue. However, there is little progress in reducing the rate of early school leavers (30.8% in 2005, double the EU average) and increasing the share of the population aged 20-24 having completed secondary studies. A new education law provides an additional budget aiming to raise quality and increase equality in education. It contains measures to reduce early school leaving and improve the integration of immigrant pupils at school, and foresees free pre-school education for children between three and six years old. The effective implementation of education reforms, notably at regional level, is crucial, as is the proposed integration of the occupational and vocational training systems, which will allow a better response to labour market needs.
21. A series of important employment measures going in the right direction have been adopted or planned. However, difficulties remain, with labour productivity growth and overall skill levels still considerably below the EU average. Further progress towards a "flexicurity" approach balancing flexibility and security for workers requires additional measures to address labour market segmentation. More efforts are

needed to promote women's employment and ensure a better work-life balance. Further efforts may also be needed to integrate recent immigrants into formal employment. More intense reform is needed to reduce early school leaving, and the implementation of the recent law on education should be monitored closely, notably at regional level.

PART III: CONCLUSIONS

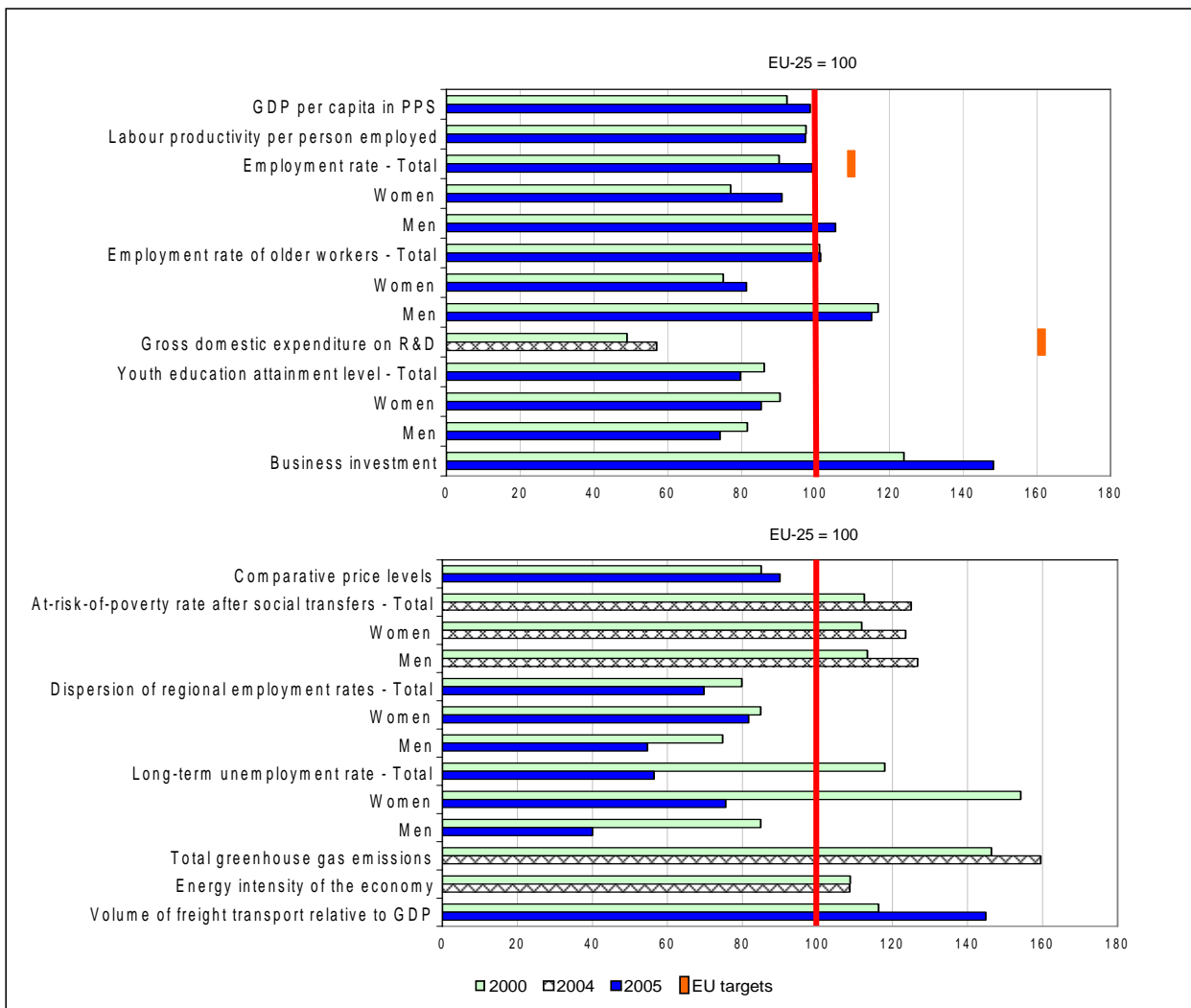
22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
23. Spain is making good progress in the implementation of its National Reform Programme and the commitments agreed at the 2006 Spring European Council. Further implementation of new laws and measures across the seven key policy areas are now essential in order to increase employment and productivity and progress towards full GDP per capita convergence with EU-25.
24. Important strong points in the implementation and reinforcement of the Spanish National Reform Programme include: a quicker than targeted reduction of government debt; good progress on implementation of the R&D and innovation plan; the inclusion of entrepreneurship in national curricula at all education levels; and satisfactory progress towards the quantified objectives, in particular for female employment.
25. The policy areas in the Spanish National Reform Programme where weaknesses need to be tackled with the highest priority are: improving competition in electricity markets and reducing segmentation in the labour market; and further improvements to education and training. Against this background, it is recommended that Spain:
 - take further measures to increase competition in the energy sector, notably by improving cross-border interconnection capacity to ensure security of supply;
 - modernise employment protection, including legislation in order to foster flexibility and security in the labour market; to counter segmentation; and to increase the attractiveness of part-time work.
 - ensure the effective implementation of education reforms, also at regional level, to reduce early school leaving, and to integrate training systems to provide a better response to labour market needs.
26. In addition, it will be important for Spain, over the period of the National Reform Programme, to focus on: the need to contain inflation in the medium-term; raising competition in professional services and retail markets; improving the regulatory framework; implementing environmental measures, in particular to reduce CO₂ emissions; raising skill levels and productivity and integrating immigrants into the labour market; and increasing access to childcare. Significant developments in the housing market may have an effect on medium-term growth prospects.

PART IV: STATISTICAL GRAPHS AND DATA

SPAIN

	ES							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	92.3	93.2	95.2	97.4	97.7	98.6		100.0	100.0	100.0	
Labour productivity per person employed	97.5	97.5	98.7	99.6	98.1	97.3		100.0	100.0	100.0	
Employment rate							66.0				70.0
Total	56.3	57.8	58.5	59.8	61.1	63.3b		62.4	63.3	63.8	
Women	41.3	43.1	44.4	46.3	48.3	51.2b		53.6	55.7	56.3	
Men	71.2	72.5	72.6	73.2	73.8	75.2b		71.2	70.9	71.3	
Employment rate of older workers											
Total	37.0	39.2	39.6	40.7	41.3	43.1b		36.6	41.0	42.5	
Women	20.2	21.7	21.9	23.3	24.6	27.4b		26.9	31.7	33.7	
Men	54.9	57.7	58.4	59.2	58.9	59.7b		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.91	0.91	0.99	1.05	1.06	1.12ep	2.0	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	66.0	65.0	63.7	62.2	61.2	61.8		76.6	77.1	77.5	
Women	71.9	71.4	70.3	69.2	68.4	68.5		79.5	80.1	80.3	
Men	60.1	58.8	57.4	55.5	54.4	55.4		73.7	74.2	74.7	
Comparative price levels	85.0	85.1	85.0	86.6	87.4p	90.0p		100.0	100.0p	100.0p	
Business investment	22.7	22.7	22.7	23.6	24.7	25.8		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	18.0	19.0	19.0b	19.0	20.0b	:		16.0e	16.0e	:	
Women	19.0	20.0	21.0b	20.0	21.0b	:		17.0e	17.0e	:	
Men	17.0	17.0	18.0b	18.0	19.0b	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	10.7	10.0	9.3	9.0	8.7	8.3		13.4	12.2	11.9	
Women	17.4	16.3	15.1	14.5	14.8	13.8		20.5	17.3	16.9	
Men	7.4	6.9	6.4	6.1	5.5	5.3		9.9	10.2	9.7	
Long-term unemployment rate											
Total	4.6	3.7	3.7	3.7	3.4	2.2b		3.9	4.1	3.9	
Women	7.4	6.0	5.9	5.7	5.1	3.4b		4.8	4.7	4.5	
Men	2.8	2.3	2.3	2.4	2.2	1.4b		3.3	3.6	3.5	
Total greenhouse gas emissions	132.8	132.9	138.9	141.0	147.9	:		90.7	92.7	:	
Energy intensity of the economy	227.0	225.4	226.3	219.7	222.5	:		208.8	204.9	:	
Volume of freight transport relative to GDP	116.4	121.0	133.8	135.3	149.2b	151.7		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



France

Assessment of National Reform Programme

1. After a period of weak growth, economic activity has picked up appreciably, settling in 2006 at a rate slightly below its potential. Per capita labour productivity growth is just below the European average for the last ten years, whereas hourly productivity is growing faster than the European average. GDP per capita is 108% of the EU average in 2006. The employment rate (63.5% in 2006) has improved only slightly since 2002. Though well down on June 2005, the unemployment rate remains high (9.3 % in 2006).
2. Budgetary consolidation should be accompanied by a shift in government spending priorities towards key economic development factors. The persistence of high unemployment through several economic cycles shows that the employment problems are essentially structural. Stronger competition in the services markets would have a positive impact on growth and employment.

PART I – GENERAL ASSESSMENT

3. The Implementation Report reproduces the three priorities of the "social growth" plan contained in the 2005-2008 National Reform Programme (NRP), namely, creating the conditions for strong economic growth, reducing unemployment and raising employment levels, and building a knowledge-based economy. In its 2006 Annual Progress Report, the Commission stressed that further care was needed to permanently correct the public deficit, promote better regulation and more open markets and strengthen employment measures.
4. The Implementation Report shows some good progress on the implementation of the NRP. The consolidation of public finances continues, as witnessed by the reduction in the structural deficit. This consolidation goes hand in hand with measures to increase the potential for growth. The initiatives in relation to research, innovation, energy and the development of SMEs should form a solid basis on which to strengthen industrial policy. Measures aimed at liberalising services and further opening up competition have been undertaken, but on the other hand they are still limited. Against a background of weak growth in the active population, the relaunching of integration schemes has contributed to a marked reduction in the unemployment rate. However, the level and rates of employment have increased only slightly, owing in part to the continuing segmentation of the labour market.
5. The Implementation Report takes account of the commitments made at the 2006 Spring European Council in the areas of research and innovation, energy and support for business. An ambitious yet realistic target (3% of GDP) has been set for 2010 for public and private investment in research.
6. The NRP is the subject of interministerial monitoring, under the authority of the Prime Minister's office (Secretariat-General for European Affairs). The Implementation Report has been approved by the Interministerial Committee on

Europe, chaired by the Prime Minister. France has taken a number of significant steps to improve the ownership, visibility and programmatic role of the NRP. The French authorities have set up machinery for consulting the social partners on drafting the Implementation Report and have plans for jointly evaluating its implementation and for taking steps to enhance ownership of the Lisbon Strategy at national level. The visibility of the Lisbon Strategy has been enhanced by appointing a coordinator at ministerial level, the Minister for Finance, and by establishing a regular dialogue at that level with the social partners. Civil society has participated throughout, through the Economic and Social Council, in the follow-up and implementation of the NRP. The French authorities have also taken the initiative to set out the links with the NRP during budget debates in Parliament and to consult local authorities. Lastly, the general public has been consulted about the Lisbon Strategy via the Internet. The National Reference Strategic Framework for the Structural Funds has synergies with the NRP and France is setting targets (of 60% for the convergence objective and 75% for the regional competitiveness and employment objective) for expenditure towards meeting the Lisbon priorities.

PART II – ASSESSMENT BY POLICY AREA

Macro-economic policies

7. Faced with an ageing population, the Implementation Report confirms that consolidation of public finances is a prerequisite for lasting growth. The medium-term projections of the 2007 draft Finance Act envisage an equilibrium situation or even a surplus in 2010 depending on the growth scenario used. Debt is forecast to fall by 3% of GDP by 2008, to 63.6%, which is, however, still above the 60% reference standard of the Stability and Growth Pact. The debt reduction target, which has become a national commitment, will, it is predicted, be met by using income from asset sales to pay off debt and by improving management of the debt of the whole state apparatus.
8. The budget deficit reduction drive outlined in the NRP has been confirmed by the introduction of new measures. In making its autumn 2006 forecasts, the Commission proceeded on the basis of a gradual reduction in the general government deficit and the virtual disappearance of exceptional factors, reflecting the lasting nature of French budgetary consolidation.
9. Though admittedly linked to the general economic recovery, this consolidation is also due to tighter control of public spending. The 2007 budget thus confirms the introduction of an expenditure standard more restrictive for central government, whose expenditure growth rate should be less than inflation. The 2003 pensions reform significantly reduced the expected outgoings, while leaving a financing deficit linked to the ageing of the population estimated at around 3% of GDP by 2050. A new meeting between the social partners is scheduled for 2008 to redefine the parameters of the pensions system after 2012. The upcoming sickness insurance reform and the reduction in unemployment insurance expenditure ought also to help the public finances recover despite an increase in local government spending. These reforms are a step in the right direction, even if they are probably insufficient on their own to ensure sustainable public finances in the long term.

10. The regulatory framework has been profoundly reworked by applying the organic laws for public finances to the 2006 and 2007 budgets and by setting up a national conference on public finances and a Public Finance Guidance Council. However, the application of expenditure standards to the various public administration subsectors seems to be behind schedule in so far as the expenditure trend targets remain non-binding.
11. Overall, the budgetary consolidation and public deficit reduction drive embarked on in recent years is continuing, even if the deficit still remains relatively high. These improvements remain dependent on the trend in local government and social security spending, control over which remains weak. Moreover, at its current level, the structural deficit is still far removed from the French authorities' medium-term objective of a balanced budget by 2010.

Micro-economic policies

12. The Implementation Report describes the measures taken to enhance competitiveness and spread the knowledge-based economy. These measures are numerous and detailed in the areas of research, industrial innovation and SME development. They are more limited in the areas of simpler and better regulation, services liberalisation and opening up competition. The Implementation Report also dwells at length on environmental and energy issues.
13. Notable progress has been made in the field of research, with the aim of devoting 3% of GDP to it in 2010 (broken down into 1% public and 2% private funding). A trio of pilot and coordination structures has been set up: the National Research Agency, the Research Evaluation Agency and the High Council for Science and Technology. Steps have been taken to promote project-based research, public/private partnership between research players, international cooperation and the attractiveness of scientific careers. These measures seem capable of forming a solid basis for the future, even if the functioning of the existing public research structures and their cooperation with the new structures still give cause for concern.
14. As regards industrial policy and innovation, the opening-up for business of the Industrial Innovation Agency and of the 66 competitiveness poles and the new support measures for innovating enterprises seem promising. Significant progress has also been made in the field of telecommunications (very rapid spread of high-speed services) and in that of e-commerce and administration. However, more still needs to be done to promote innovation, e.g. through better use of public tendering procedures and more effective intellectual property rules.
15. The measures announced in support of SMEs are a step in the right direction, as witness the increase in the number of start-ups. Since the formalities for setting up a business have already been greatly simplified, the key initiatives relate to improving the legal and tax framework, developing "growth SMEs" and supporting exports. However, more could be done to improve access by SMEs to public contracts. Initiatives must also be taken to support young businesses and to foster the entrepreneurial spirit among the public and within universities.
16. Progress has been made towards simpler regulation, in keeping with the aim of improving law-making, as witness the changes to the public financing regulatory

framework, the expansion of e-administration and the ongoing work on assessing the administrative burden of legislation. However, greater use could be made of impact studies and yet more can be done to simplify administrative legislation and procedures. The French authorities have not set themselves an overall quantified target for reducing the administrative burden on business.

17. Measures are also presented in the field of the environment and energy saving. These include steps to prevent climate change, the reduction of greenhouse gas emissions by industry, a new law aimed at achieving a "good ecological state" of fresh water by 2015, a national health/environment plan covering, among other things, atmospheric pollutants, environmental research and eco-innovation drives, and a new framework law on energy. This law provides for a reduction in energy intensity and greenhouse gases between now and 2050 by developing such renewable energy sources as wind power and biomass and through continued reliance on nuclear energy.
18. The Implementation Report mentions the continued liberalisation of the distributive trades and network industries and the drive to modernise the financial sector, but it is silent on the issue of state aid. In the sectors of gas and electricity and of rail freight, obstacles to competition remain, despite the transposition of the Directives and the improved contestability of markets, in the form of the incomplete decoupling of production, transmission and distribution, and the degree of concentration in the gas and electricity markets. Despite certain positive measures, numerous restrictions continue to exist in France in the areas of the regulated professions and financial services.
19. Overall, the micro-economic measures described in the report in relation to R&D, innovation and SME development are capable of creating a firm basis for strengthening the French economy. Additional measures to help attain the better regulation objective and a more ambitious approach to competition might, however, prove both useful and necessary.

Employment policies

20. With a view to attracting more people into work and keeping them there, a number of measures have been taken to strengthen the financial incentives to employment, to improve support and empowerment for job-seekers, and to develop employment in personal services. The reduction of social charges on low wages (1.1% of GDP in 2006) has helped to stabilise the proportion of total employment accounted for by unqualified employment, although the rate of unemployment in these categories has increased in recent years. In order to improve the effectiveness of the employment premium, the amounts allocated have been revised upwards and the measure has been refocused. The measure aimed at temporarily maintaining payment of minimum incomes to persons returning to employment has been reformed to increase its incentive value. The employment service has been reorganised and job search monitoring has been enhanced.
21. In order to deal with the worrying situation facing young people, a number of measures have been enhanced or introduced, namely, the extension of assisted contracts, work-linked training, "youth in enterprise" contracts and the creation of a junior apprenticeship contract, voluntary civilian service, an entry route into employment and new training schemes. A special effort is now being made to help

the older workforce in the form of the 2006-2010 Concerted Action Plan for the Employment of Older Workers, the aim of which is to achieve an employment rate of 50% among 55-64 year-olds by 2010. A raft of measures is planned, namely, the creation of an "older worker" contract, the phasing-out of automatic retirement of workers before the age of 65 and of the older workers' redundancy contribution, a widening of the scope for combining work with retirement and an information campaign to change mentalities. The plan is a necessary complement to the 2003 pensions reform and a first stage in the development of a global strategy of active ageing.

22. Reconciling the adaptation of workers and the adaptability of businesses remains a major challenge for France in view of the segmentation of its labour market between types of contract. Although the vast majority of existing contracts are permanent, in 2005 78% of recruitments were made on the basis of temporary contracts. The NRP stressed the introduction of the "new recruitment contract" (*contrat nouvelles embauches - CNE*) in very small enterprises, with simplified redundancy arrangements for the first two years. The CNE is set to be evaluated in late-2008. According to the French authorities, the impact on the job market should be between 50 000 and 150 000. In order to maximise job creation and return-to-work outcomes, the balance between permanent contracts and atypical contracts ought to be reassessed. One aim should be to make it easier to switch from one type of contract to another.
23. The NRP touched only indirectly on the need to invest more in human capital. The Implementation Report is more explicit on the French strategy as regards both basic training and further training. Despite the availability of substantial budget resources (1.4% of GDP in 2005 for further training alone), the vocational training take-up rate is below the European average (7.6% of workers in 2005). It would also be a good thing if vocational training were more sharply focused on the less well integrated categories.
24. All in all, recent measures have placed the emphasis on the return to employment of the most disadvantaged groups, and in particular of those on minimum incomes, the less qualified, handicapped people, young people and older people.

PART III: CONCLUSIONS

25. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
26. France is making some good progress on the implementation of its National Reform Programme and the actions agreed by the 2006 Spring European Council. Against the background of a buoyant economy, France is continuing with its budgetary consolidation drive while at the same time seeking to increase its growth potential, notably through fresh commitments towards research and innovation. Its performance in relation to employment is by and large mixed.
27. Among the strong points of the reforms undertaken, the establishment of competitiveness poles and of new structures for research and innovation appears

particularly promising, as does the target for total expenditure on R&D of 3% of GDP by 2010. The recent reform of the public finance regulatory framework ought to contribute decisively to better public spending management. The decline in unemployment, for the first time since 2001, is a positive development and the recent measures to help young job-seekers seem to be a step in the right direction.

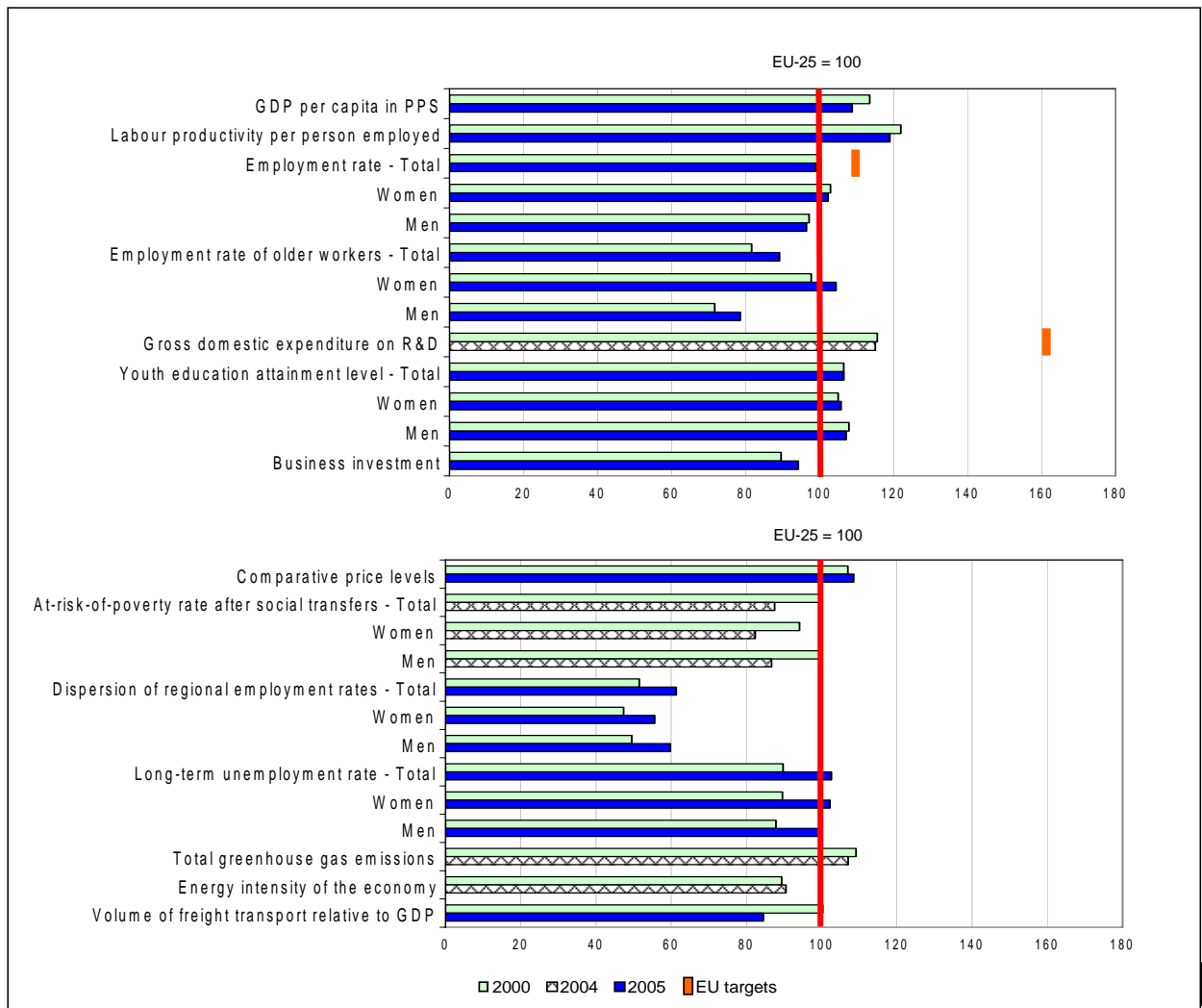
28. The policy areas in the French National Reform Programme where weaknesses need to be tackled with the highest priority are: sustaining the improvements in the public finance situation by ensuring that central government commitments are respected and monitoring developments in local funding and social security spending; improving shortcomings in competition in some network industries and some transport sectors; and implementation of an overall strategy to ensure a more fluid labour market and continued employment of older workers, notably by improving access to lifelong learning. Against this background it is recommended that France:
- ensure the sustainability of its public finances through further budgetary consolidation and debt reduction. The meeting on pension systems scheduled for 2008 will have to hang on to the gains made following the introduction of the 2003 reform;
 - take steps to improve competition in the gas, electricity and rail freight sectors;
 - modernise employment protection and enhance lifelong learning to foster flexibility and security in the employment market and combat segmentation among contract types by making it easier to switch between temporary contracts and permanent contracts.
29. In addition, it will be important for France over the period of the National Reform Programme to focus on: reducing the high level of debt, which threatens the sustainability of the public finances when the ageing of the population is factored in, which in the absence of increased budgetary consolidation may necessitate further reforms; strengthening competition in the regulated professions; and enhancing the policies of improving regulation and encouraging entrepreneurship, notably as regards support for the young businesses and promotion of the entrepreneurial spirit in society.

PART IV: STATISTICAL GRAPHS AND DATA

FRANCE

	FR							EU25					
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target		
GDP per capita in PPS	113.6	113.9	112.0	111.6	109.5	108.8	3.0	100.0	100.0	100.0	70.0		
Labour productivity per person employed	122.0	122.2	120.3	120.4	119.0	119.0		100.0	100.0	100.0			
Employment rate								:	62.4	63.3		63.8	
Total	62.1	62.8	63.0	63.3	63.1	63.1		62.4	63.3	63.8			
Women	55.2	56.0	56.7	57.3	57.4	57.6		53.6	55.7	56.3			
Men	69.2	69.7	69.5	69.4	69.0	68.8		71.2	70.9	71.3			
Employment rate of older workers								:	36.6	41.0		42.5	
Total	29.9	31.9	34.7	36.8	37.3	37.9		36.6	41.0	42.5			
Women	26.3	27.8	30.8	32.9	33.8	35.2		26.9	31.7	33.7			
Men	33.6	36.2	38.7	40.9	41.0	40.7		46.9	50.7	51.8			
Gross domestic expenditure on R&D	2.15	2.20	2.23	2.17	2.14	2.13p		1.86e	1.86e	:		3.0	
Youth education attainment level								:	76.6	77.1		77.5	
Total	81.6	81.8	81.7	80.4b	80.7	82.6		76.6	77.1	77.5			
Women	83.5	83.2	82.8	82.1b	82.4	85.0		79.5	80.1	80.3			
Men	79.6	80.3	80.5	78.6b	78.9	80.1	73.7	74.2	74.7				
Comparative price levels	107.0	105.5	106.1	105.8	108.0p	108.5p	100.0	100.0p	100.0p				
Business investment	16.4	16.5	15.8	15.8	16.1	16.4	18.3	17.1	17.4				
At-risk-of-poverty rate after social transfers								:	16.0e	16.0e	:		
Total	16.0	13.0b	12.0	12.0	14.0b	:	16.0e	16.0e	:				
Women	16.0	13.0b	13.0	13.0	14.0b	:	17.0e	17.0e	:				
Men	15.0	12.0b	12.0	12.0	13.0b	:	15.0e	15.0e	:				
Dispersion of regional employment rates								:	13.4	12.2	11.9		
Total	6.9	8.3	8.0	7.2	7.1	7.3	13.4	12.2	11.9				
Women	9.7	10.8	10.6	8.9	8.7	9.4	20.5	17.3	16.9				
Men	4.9	6.6	6.1	6.2	5.9	5.8	9.9	10.2	9.7				
Long-term unemployment rate								:	3.9	4.1	3.9		
Total	3.5	3.0	3.1	3.7	3.9	4.0	3.9	4.1	3.9				
Women	4.3	3.6	3.5	4.1	4.3	4.6	4.8	4.7	4.5				
Men	2.9	2.4	2.6	3.4	3.5	3.5	3.3	3.6	3.5				
Total greenhouse gas emissions	99.0	99.0	98.1	98.9	99.2	:	90.7	92.7	:				
Energy intensity of the economy	186.6	188.3	186.1	188.5	185.5	:	208.8	204.9	:				
Volume of freight transport relative to GDP	100.4	97.5	95.4	92.9	93.3	88.5	100.1e	104.6be	104.7e				

PERFORMANCE COMPARED TO EU-25



Ireland

Assessment of National Reform Programme

1. Over the last few decades, Ireland has experienced a rapid increase in real GDP per capita to, in 2006, 138% of the EU average, one of the highest in the EU. Employment levels have also grown rapidly, and labour productivity growth has been well above the EU average. Recent employment growth has been driven by increased participation and immigration from the new Member States, resulting in 2006 in an employment rate expected to reach 68.5% and an unemployment rate of 4.3%.
2. Ireland combines an already strong economic performance in terms of growth and employment with robust plans for further reform emphasising catching-up needs in areas such as infrastructure provision, human capital (education and skills), R&D and innovation, domestic competition conditions and pension provision, while striving for a continuing increase in labour force participation. The Irish economy faces risks, notably a disproportionately-sized residential construction sector and evidence of declining external competitiveness. A careful prioritisation of expenditure should reduce those risks and promote reforms that strengthen the prospects for further sustainable, higher-productivity growth, by expanding physical and human capital and reducing inflationary pressures.

PART I: GENERAL ASSESSMENT

3. Ireland's 2005-2008 National Reform Programme (NRP) identified as the overall key challenge to sustain and improve its recent good economic performance, based on taking advantage of the opportunities presented by globalisation and the internal market. Within that, it identified 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. In its 2006 Annual Progress Report (APR), the Commission noted Ireland's generally strong policy framework and very good economic performance. Nevertheless, it invited Ireland to pay further attention to: ensuring policies on R&D and science and innovation investment were robust enough to reach the ambitious targets set; and to improving pension coverage. The Commission also noted that competition in services was not identified by the Irish authorities as a key challenge.
4. Its 2006 Implementation Report shows that Ireland is generally making very good progress with the implementation of its NRP. The report includes new strategies and policy proposals which have the potential to address many of the Commission's concerns. There has been significant progress in implementing Ireland's NRP measures on: energy liberalisation and increasing the use of renewable energy sources; further enhancing the business environment, especially for SMEs; and tackling early school leaving. Encouraging initial progress has been made to: upgrade Ireland's infrastructure; reverse shortfalls in R&D investment; boost

innovation; reinforce pensions policy; increase competition (including in professional services); improve the transposition of EU Directives into national law; introduce comprehensive impact assessment for planned legislation; integrate disadvantaged groups into the labour market; develop skills; and increase access to childcare. This progress needs maintaining and some measures should be strengthened.

5. There is some progress towards meeting the commitments made at the 2006 Spring European Council, but insufficient information is provided to assess this fully. No target for R&D investment in 2010 is given in the report, despite the adoption of a major new strategy for Science, Technology and Innovation. The report states that Ireland already meets the target on establishing a business within a week via a one-stop shop. Steps have been taken to expand entrepreneurship education but this is not yet part of the curricula for all pupils. While the commitment to ensure that unemployed young people get a job or training within six months of becoming unemployed is not explicitly addressed, the early implementation of plans to extend support to unemployed 16-24 year olds should enable progress to be made.
6. Effective efforts to reinforce Ireland's already robust social partnership have been made, with a ten-year framework for the partnership established ("Towards 2016"), after a process including debates in parliament, in 2006. Stakeholders were extensively consulted on the forthcoming National Development Plan for 2007-13, which will underpin implementation of large parts of the NRP. However, the Implementation Report, unlike the NRP itself, was not discussed as such by Parliament before being finalised. There appears to be adequate coherence between the NRP and National Strategic Reference Framework for the investment of Structural Funds. In implementing its NRP, Ireland (along with the UK) continues to emphasise cross-border co-operation within the island of Ireland. This constitutes a significant added value.

PART II: ASSESSMENT BY POLICY AREA

Macroeconomic policies

7. The Commission concurs with the Implementation Report's assessment that overall macroeconomic performance has been impressive and that medium-term prospects remain good. The very large and ongoing net immigration should help moderate labour cost pressures and increase the economy's supply potential. However, the Commission also shares the concerns expressed in the Implementation Report regarding accumulating imbalances. Output and employment growth increasingly rely on an unsustainably high level of residential construction which aggravates inflationary pressures and carries risks of a sharp downward adjustment in the wider economy. Significant increases in housing prices and household indebtedness may have an effect on medium-term growth prospects. The recent deterioration of external competitiveness is also unwelcome. Prudent macroeconomic management should guide the economy towards better balance and respond to the possible materialisation of such risks.
8. Prioritising public investment in infrastructure and other growth-promoting expenditure is recognised as a key challenge. Recent developments noted in the

Implementation Report include the "Transport 21" transport infrastructure programme and the latest multi-annual capital investment framework (to 2010). The forthcoming 2007-2013 National Development Plan will set out strategy for infrastructure, human capital and R&D investment. The manageability of the very large overall capital programme being undertaken by Ireland is challenging as shown by recent implementation shortfalls. Important recent initiatives to improve the appraisal, management and accountability of major capital projects should be instrumental in tackling this challenge. Concerns exist that the construction-related elements of the current NDP have contributed to inflationary pressures by bidding up the price of scarce resources and in consequence have risked reducing the potential returns from such capital investment, making judicious prioritisation all the more important in the future.

9. On economic and budgetary sustainability, the Commission previously noted that pension arrangements merited further attention, including the adequacy of their coverage (still significantly below government targets). The Implementation Report mentions incentives announced in the 2006 Budget to encourage additional pension saving by those on low-incomes from maturing Special Savings Investment Accounts and by individuals having hitherto underfunded their pensions. Policy developments include the National Pensions Review presented by the Pensions Board to the government in October 2005, the Board's August 2006 follow-up report analysing options for a mandatory or quasi-mandatory pension system and the government's commitment in "Towards 2016" to the presentation in 2007 of a Green Paper on pensions policy. Though the pension reform process is still at an early stage, the Green Paper will be important in furthering agreement on a way forward.
10. Overall, prioritising growth-promoting expenditure and continuing to focus on economic and budgetary sustainability should underpin further growth and job creation and facilitate implementation of the structural reforms envisaged.

Microeconomic policies

11. In the area of micro-economic policy the NRP presented the key priorities of improving competitiveness, infrastructure, regulation and social inclusion; increasing R&D investment and efficiency; encouraging greater innovation and entrepreneurship; and sustainable development.
12. Ireland shows good progress in R&D and innovation. Gross expenditure on R&D increased from 1.35% of GNP in 2002 to 1.43% in 2004. Business expenditure increased in absolute terms but remained stable in relative terms (0.93% of GDP) due to the high rate of economic growth. The R&D target (2.5% of GNP by 2013) seems feasible but the lack of intermediate targets, notably for 2010, is an obstacle in assessing progress. The recently adopted Science, Technology and Innovation Strategy provides an adequate framework to build up a world-class research base, concentrating on higher education, links between research institutions and business and increasing R&D efforts by indigenous companies, including SMEs: in this respect there are plans to introduce a knowledge acquisition grants scheme and an innovation vouchers scheme. Further action should be taken to support enterprises in transforming R&D input into innovation output and to promote and reward innovation performance. The proposal for a commercialisation fund to support academics in taking basic research forward to market can contribute to this, as can

the proposed intellectual property fund to assist research institutions and firms with obtaining and managing patents. The government has established a list of indicators to monitor implementation of the strategy, but insufficient information is at this stage provided on budget allocations and timelines on possible effects in terms of leverage of private sector investment, and on progress so far.

13. The Implementation Report presents a broad range of measures with the objective of improving competitiveness, some impacting significantly on SMEs. However, despite some signs of progress, limited information is provided on measures on specific SME policy and on entrepreneurship education. The key issue of business start-ups is not covered in detail, although Ireland operates a scheme to allow companies to be incorporated in five working days. The Implementation Report merely mentions that one-stop-shops for start-ups are in place and that a company may be established within a week. An Enterprise Advisory Group consisting of senior executives has been set up, a welcome new institutional arrangement. Several better regulation initiatives are now in place, including impact assessments on new legislation. A simplification exercise is underway, although the Implementation Report does not cover in detail the reduction of the administrative burden for enterprises. On ICTs, there is good progress in broadband rollout, e-inclusion and e-business but specific measures to promote the competitiveness of ICT industries are missing. The government plans to announce a Knowledge Society Action Plan by end 2006. A new Competition Act was introduced in March. The Competition Authority has undertaken three major studies covering insurance, banking and the professions sector. On industrial policy, the Implementation Report seems consistent with the NRP and implementation is progressing.
14. Ireland's transposition of EU internal market legislation into national law has improved and the deficit is now under the 1.5% interim target. Only part of the public procurement package has been transposed and the rest should be transposed urgently.
15. Concerning deregulation in the electricity market, independent suppliers now supply 42% of total demand. Other progress in this area includes the newly introduced independent electricity grid and the ongoing electricity market integration with Northern Ireland. Progress in implementing measures to stimulate renewable electricity and biofuels is reported. The upward revision of the 2010 target to 15% is welcome. Revision of the Irish strategy for tackling climate change will be of key importance as Ireland will have to identify further emissions reduction policies and measures in order to meet its targets. No progress is reported regarding road pricing or congestion charging, despite these issues being mentioned in the NRP.
16. Overall, Ireland has made good progress implementing measures responding to its key micro-economic challenges.

Employment policies

17. The key labour market challenges identified in the 2006 APR were increasing labour supply and development of a highly skilled and adaptable workforce.
18. New labour supply measures include enhancements to measures to prevent unemployment, their extension to cover 55-64 year olds, and a commitment to

extend this type of active engagement to lone parents, people with disabilities and unemployed 16-24 year olds. A new national childcare investment programme (2006-2010) has been launched to support the creation of 50,000 childcare places and an early childcare supplement of €1,000 per annum has been introduced. Consultation has been launched on proposed reforms affecting welfare support for lone parents, designed to increase employment participation.

19. The thrust of labour supply measures is positive and much attention is given to the successful transition from inactivity into sustainable employment of inactive and marginalised groups such as lone parents, people with disabilities and travellers. However, that transition will require that the necessary services, such as a comprehensive childcare infrastructure and market-driven training, are provided in ways appropriate to the needs of the groups concerned. Such effective provision of services is also essential to ensure greater gender equality in the Irish labour market, notwithstanding recent welcome reductions in the gender pay gap. Implementation of the National Disability Strategy, and related Government Department Sectoral Plans (including proposals for a comprehensive Employment Strategy for people with disabilities), is a positive step. The increasingly important role of migrants (currently some 10% of the labour force) in the Irish economy demands that more attention be given to their effective labour market and social integration.
20. Research is underway to underpin a new national skills strategy to be published in 2007 and more resources have been committed to existing programmes aimed at improving the skill level of the workforce. The scale of the issue is demonstrated by the fact that some 38% of 25-64 year olds have less than upper second-level education (2003 data) while participation levels in lifelong learning, at 8%, are well below the EU average (11%). The new Strategy should further facilitate the development of a coherent approach to matching education and training provision with market needs. While there is a clear commitment to focusing on the needs of the low-skilled, including older workers, there may be a need for greater innovation in ensuring that such groups are enabled to access further training and education or given more incentives to do so.
21. Progress continues to be made in addressing early school leaving (12.3% in 2005) and 86.1% of 20-24 year olds have at least upper secondary level education. Roll-out of the action plan for educational inclusion should reinforce progress.
22. Overall, the steps undertaken show good evidence of commitment to tackling the key issues of labour supply and skills.

PART III: CONCLUSIONS

23. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
24. Ireland is making very good progress in the implementation of its National Reform Programme and of the commitments made by the 2006 Spring European Council. Furthermore, governance of the Growth and Jobs Strategy has gained political

visibility, notably due to the recently concluded social partnership agreement, “Towards 2016”.

25. Among the strengths of the Irish National Reform Programme and its implementation are: the recently adopted Science, Technology and Innovation Strategy 2007-2013 and the substantial increase of public investment in R&D; recognition of the need to prioritise public investment in infrastructure and other growth-promoting expenditure; measures to address early school leaving and enhance skills, such as the welcome commitment to develop by 2007 a long-term national skills strategy.
26. It will be important for Ireland over the period of the National Reform Programme to focus on: speeding up progress in formulating concrete measures to reform pension arrangements; further emission reduction measures; accelerating progress in increasing labour market participation, including by establishing a comprehensive childcare infrastructure, further developing a cohesive policy towards inward migration and placing a particular emphasis on support to older and low-skilled workers. An intermediate target for R&D investment should be set for 2010 and developments in the housing market, which may affect medium-term growth prospects, should be carefully monitored.

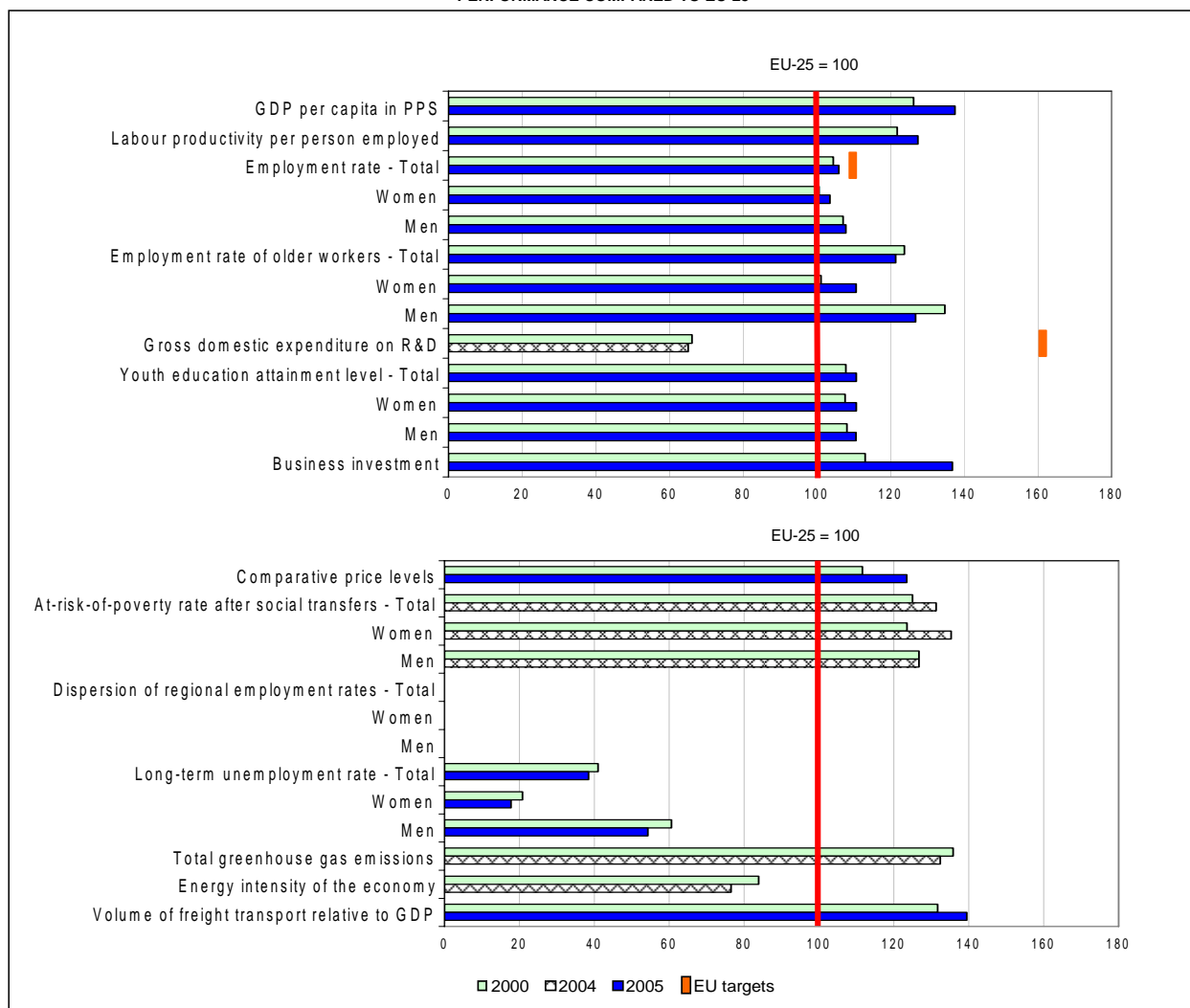
PART IV: STATISTICAL GRAPHS AND DATA

IRELAND

	IE							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	126.3	128.5	132.3	133.7	135.8	137.5		100.0	100.0	100.0	
Labour productivity per person employed	121.8	123.3	127.1	127.9	128.3	127.4		100.0	100.0	100.0	
Employment rate							:				70.0
Total	65.2	65.8	65.5	65.5	66.3	67.6		62.4	63.3	63.8	
Women	53.9	54.9	55.4	55.7	56.5	58.3		53.6	55.7	56.3	
Men	76.3	76.6	75.4	75.2	75.9	76.9		71.2	70.9	71.3	
Employment rate of older workers											
Total	45.3	46.8	48.0	49.0	49.5	51.6		36.6	41.0	42.5	
Women	27.2	28.7	30.8	33.1	33.7	37.3		26.9	31.7	33.7	
Men	63.2	64.6	65.0	64.6	65.0	65.7		46.9	50.7	51.8	
Gross domestic expenditure on R&D	1.23e	1.10e	1.10e	1.16e	1.21ep	1.25ep	*	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	82.6	83.9	84.0	85.1p	85.3p	85.8p		76.6	77.1	77.5	
Women	85.6	87.4	87.3	88.5p	88.4p	88.9p		79.5	80.1	80.3	
Men	79.7	80.4	80.7	81.6p	82.3p	82.6p		73.7	74.2	74.7	
Comparative price levels	111.6	116.0	122.4	126.6	123.1p	123.4p		100.0	100.0p	100.0p	
Business investment	20.7	18.8	18.1	19.2	20.9	23.8		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	20.0	21.0	:	21.0b	21.0	:		16.0e	16.0e	:	
Women	21.0	23.0	:	22.0b	23.0	:		17.0e	17.0e	:	
Men	19.0	20.0	:	20.0b	19.0	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	-	-	-	-	-	-	-	13.4	12.2	11.9	
Women	-	-	-	-	-	-	-	20.5	17.3	16.9	
Men	-	-	-	-	-	-	-	9.9	10.2	9.7	
Long-term unemployment rate											
Total	1.6	1.3	1.4	1.6	1.6	1.5		3.9	4.1	3.9	
Women	1.0	0.8	0.8	1.0	1.0	0.8		4.8	4.7	4.5	
Men	2.0	1.7	1.8	1.9	2.0	1.9		3.3	3.6	3.5	
Total greenhouse gas emissions	123.2	126.5	123.7	122.6	122.7	:		90.7	92.7	:	
Energy intensity of the economy	175.1	172.5	166.1	155.2	156.9	:		208.8	204.9	:	
Volume of freight transport relative to GDP	131.8	125.3	135.3	141.6	148.4	146.0		100.1e	104.6be	104.7e	

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

PERFORMANCE COMPARED TO EU-25



Italy

Assessment of National Reform Programme

1. Economic growth in Italy has been consistently lower than the EU average since the early 1990s. As a result, Italy's GDP per capita is estimated to have fallen to below 102% of the EU average in 2006, down from over 116% in 1995. Prospects for 2006 point to an improvement of the economic situation, but real GDP growth is still expected to be below the EU average. The general government deficit has been above 3% of GDP since 2003 and the debt remains very high and started increasing again in 2005. On the positive side, Italy has enjoyed robust employment growth over the past decade and its unemployment rate in the first half of 2006 fell to 7% of the labour force, below the EU average. Nevertheless, the employment rate, projected at 58.6% in 2006, remains well below the EU average and is much lower in the South.
2. Structural weaknesses feeding into low productivity growth and deteriorating competitiveness are at the root of Italy's poor growth performance in recent years. Reversing this requires an economic policy strategy that creates a virtuous circle between: macro-economic stability; micro-economic reforms aimed at boosting competition and enhancing the organisational efficiency and ability to innovate of the Italian productive system; and measures aimed at raising labour market participation and employment, including by tackling regional disparities. Consolidation of public finances to achieve their long-term sustainability is a necessary pre-condition for this strategy, as it would help reduce economic uncertainty, create more favourable conditions for investment and make room for enhanced expenditure on human capital and infrastructure.

PART I: GENERAL ASSESSMENT

3. The six priorities that were highlighted in the 2005-2008 National Reform Programme (NRP) have been largely confirmed this year. These are: ensuring long-term fiscal sustainability; extending the area of free choice for citizens and companies; granting incentives for scientific research and technological innovation; strengthening education and training; upgrading infrastructure; protecting the environment. In its 2006 Annual Progress Report (APR), the Commission pointed out that stronger measures were needed: on fiscal sustainability; to boost competition, especially in network industries and services; and to increase labour supply and raise employment rates, including by tackling regional disparities.
4. The 2006 Implementation Report, presented by the new government, attempts to remedy the weaknesses identified by the Commission, in particular by integrating macro-economic and employment issues, which in 2005 were largely covered in documents separate from the NRP, and by providing more detail on concrete and timetabled measures, particularly in the micro-economic area. There has been significant reinforcement of the NRP since last year and it is now crucial to follow ambition with effective action to implement the measures set out, in order to start

closing the competitiveness gap between the Italian economy and other euro area countries.

5. Progress in implementing the reinforced NRP has been good on enhancing competition and simplifying regulation of professional services and on expanding the use of ICT. There has been some encouraging progress or a clear commitment to move forward on: fiscal consolidation; putting in place targets and measures to boost investment in R&D; transposing EU Directives into national law on time; liberalisation of energy markets; better regulation, including the creation of a central unit attached to the Prime Minister; establishing a coherent strategy for infrastructure investment; improving environmental protection; "flexicurity"; integrating disadvantaged people into the labour market; and reducing the tax wedge on labour. In all these areas, it is crucial that planned measures are fully and promptly followed through. Further progress is needed on: implementing pension reforms and containing health care expenditure; improving employment services throughout the country; boosting access to childcare; reducing early school leaving; university reform; and developing a comprehensive lifelong learning strategy.
6. Progress has been mixed on meeting the specific commitments agreed at the 2006 Spring European Council. A target has been set for R&D investment and steps have been taken to enhance the effectiveness of one-stop shops for starting up businesses. However, the Implementation Report does not mention entrepreneurship education, measures to ensure unemployed young people get a job or relevant training within six months, or steps to allow businesses to recruit their first employee through a single contact point.
7. Consultation and efforts to develop ownership of the NRP at the level of central and local governments and the social partners have been reinforced. The new Italian government has continued its predecessor's practice of appointing a national co-ordinator at senior ministerial level. The establishment of a technical inter-ministerial committee to drive implementation of the NRP is also positive in terms of co-ordination. Some positive steps have been taken to improve monitoring and to improve public awareness of the reform process. The Implementation Report highlights the necessary links between the Growth and Jobs Strategy and the 2007-2013 National Strategic Reference Framework for the investment of EU Structural Funds.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The Implementation Report confirms and emphasises the consolidation and long-term sustainability of public finances as central to a comprehensive strategy to remedy the weaknesses of the Italian economy and raise its growth potential.
9. The current high public debt and the weak budgetary position are a risk to the long-term sustainability of public finances, exacerbated by the pressure on public spending created by an ageing population. The fiscal consolidation strategy confirms the commitment to reduce the general government deficit to below 3% of GDP by 2007. The corrective measures for 2007 in the draft Budget Law, due to be adopted

by Parliament by the end of the year, appear appropriate to achieve this. Thus, the approval of the 2007 Budget Law in line with the stated targets and its subsequent rigorous implementation will represent an important step towards long-term fiscal sustainability. The draft Budget Law also envisages measures worth 1.3% of GDP to finance growth-enhancing and redistributive measures, including reducing the fiscal costs of employment. After 2007, the government intends to pursue fiscal consolidation so as to reduce the debt to below 100% of GDP by 2011. Achieving this will require credible strategies in the budgets for the relevant years and their rigorous implementation.

10. The Implementation Report recognises that the full implementation of the pension reforms now in progress is crucial to limiting increases on age-related public expenditure in the long term. In this light, the repeated postponement of the revision of the actuarial coefficients in line with life expectancy is a cause for concern. The report indicates that the government and the social partners will soon start negotiations aimed at further refining the pension system: it is important that its long-term sustainability is preserved. The success of the pension reforms, both in terms of financial sustainability and social adequacy, will also depend on further progress in increasing employment rates, particularly among women and older workers. Promoting the financial sustainability of health care systems while preserving accessible and high-quality care remains a major challenge. Measures to improve sustainability have been adopted but some regions continue to exceed expenditure ceilings.
11. Italy shows clear commitment to long-term fiscal sustainability, but the risks remain significant and the full implementation of the proposed 2007 budget followed by an even more rigorous approach to consolidation over the next few years will be crucial. The implementation of pension reforms and the reinforcement of proposed measures on pensions and healthcare are also essential.

Micro-economic policies

12. The Implementation Report highlights four micro-economic priorities: R&D, “free choice for citizens and companies”, infrastructure and environment. The report attaches great priority to strengthening competition and deepening the internal market.
13. Through new initiatives and reinforcing existing instruments, the report indicates the aim of reaching the ambitious target of investing 2.5% of GDP in R&D by 2010. Specific measures are set out to foster private-public partnerships, including a new tax credit system to encourage business cooperation with research institutions, to streamline and simplify public support for innovation and to improve the numbers of researchers in universities and research institutions. The measures go in the right direction but are not set within a comprehensive strategic framework, making it difficult to assess to what extent they can change current stable trends in R&D expenditure. In order to increase the efficiency of public spending on R&D, the report envisages the creation of an independent evaluation agency for universities and research, which should help increase the efficiency of public spending on R&D. However, it does not propose detailed measures aimed for example at increasing researchers' mobility or at the reform and internationalisation of universities

14. Measures to improve and expand the use of ICT have been rationalised and progress is taking place. The report describes innovative uses of ICT in relation to the preservation of cultural heritage, the digitalisation of justice and police services and the strengthening of e-governance for SMEs. Electronic communication issues (digital television, broadband), largely absent from the original NRP, are covered in the report, including specific measures to enhance broadband coverage in rural areas.
15. The Implementation Report attaches great importance to increasing competition and implementing internal market legislation. An inter-ministerial committee has been established to monitor, speed up and improve the implementation of EU legislation. Internal rules will be modified to enable Italy to transpose directives into national law more quickly. Currently, and despite recent progress, the percentage of directives not implemented on time is well above the 1.5% target. The government recently adopted far-reaching reforms to address regulation restricting competition in professional services and other service sectors, including banking and insurance, taxi services and retail shops. Draft laws concerning the liberalisation of energy markets and of local public services have been presented to Parliament. It is important that this process continues and is properly implemented. The steps taken to introduce a programme for immunity from and reduction of fines (leniency) for firms revealing cartels are welcome.
16. There is a clear commitment to improving the business environment. A better regulation task force has been established. Several initiatives are already ongoing such as the best practices study on simplification, the pilot project on the measurement of administrative costs (which also concerns SMEs) and the decree to repeal all pre-1970 redundant laws. A new bankruptcy law has been introduced. The programme also envisages new measures, including the introduction of class action in the legal system, the extension and reinforcement of one-stop shops and the simplification of procedures to start up an enterprise. These initiatives are likely to contribute to reducing the burden on businesses. The NRP mentions impact assessment, but little information is given on future steps.
17. The Implementation Report sets out a strategic framework and priority projects for upgrading road, sea and rail infrastructure and improving the use of IT for traffic monitoring and control. These infrastructure improvements are urgently needed. The Implementation Report does not discuss the possibilities of public-private partnership and infrastructure charging for accelerating implementation and ensuring efficiency and sustainability.
18. The Implementation Report puts some emphasis on environmental protection. However, budgetary implications and broader environmental and economic impacts are not fully evaluated. The need to revise current policies to tackle climate change is acknowledged but limited detail is given on how this will be achieved whilst a review of the national plan for reduction of CO₂ is ongoing.
19. The micro-economic measures set out in the Implementation Report have the potential, if implemented promptly and effectively in synergy with macro-economic stability and labour market reform, to reduce Italy's dependence on traditional sectors, help SMEs to grow and new businesses to emerge and thus to help to improve Italy's competitiveness. However, implementation is still in the early stages and major challenges remain.

Employment policies

20. The Implementation Report confirms education and training as a priority and integrates the challenge of increasing labour supply and raising employment rates into the core of the reform programme, hence providing a more coherent and comprehensive policy framework.
21. The implementation of the NRP measures varies: though employment services have improved on average, they still lag significantly behind in Southern regions and the nationwide computerised labour market data system is not yet completed. Some measures to promote labour mobility within Italy are advancing, though the revised apprenticeship system is still to be fully implemented. The report announces new initiatives to tackle North/South employment disparities and for reconciling work and family life, but further improvement of childcare provision is necessary. Funding to assist disadvantaged people to obtain employment will increase, and the link with the national strategy for social protection and social inclusion is underlined.
22. The cut in taxes on labour for those on permanent contracts, as well as for some specific categories (such as R&D personnel and apprentices), aims to foster stable employment and competitiveness. The proposed cut is higher for permanent workers in Southern regions, and even larger for disadvantaged women in the same regions, thus helping to address regional disparities and low female participation in the South.
23. There are moves to combine labour market flexibility with increased social protection via increased social rights for temporary workers and the increase of their social security contributions, leading to improved pension rights. Further developments are needed, and the report announces the intention to create a new unemployment insurance system. New measures, the detail of which is not yet provided, are foreseen for health and safety at work and to tackle undeclared work.
24. Implementation of measures to boost human capital is progressing, although slowly in some areas, for example guidance and counselling systems, transparency of training opportunities and validation of prior learning. Little information is provided on recent education and training reforms, including in the university system, which are reported to have been stopped. The report would benefit from further detail on much needed measures on early school leaving and quality of education across the country. Despite some progress, the situation in terms of training for workers requires further significant efforts in the context of developing a comprehensive lifelong learning strategy.
25. Overall, some progress is indicated in a number of employment policy areas. But the description of the different measures, especially in terms of content, timetables and results, is not always sufficiently detailed to allow evaluation of their adequacy.

PART III: CONCLUSIONS

26. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:

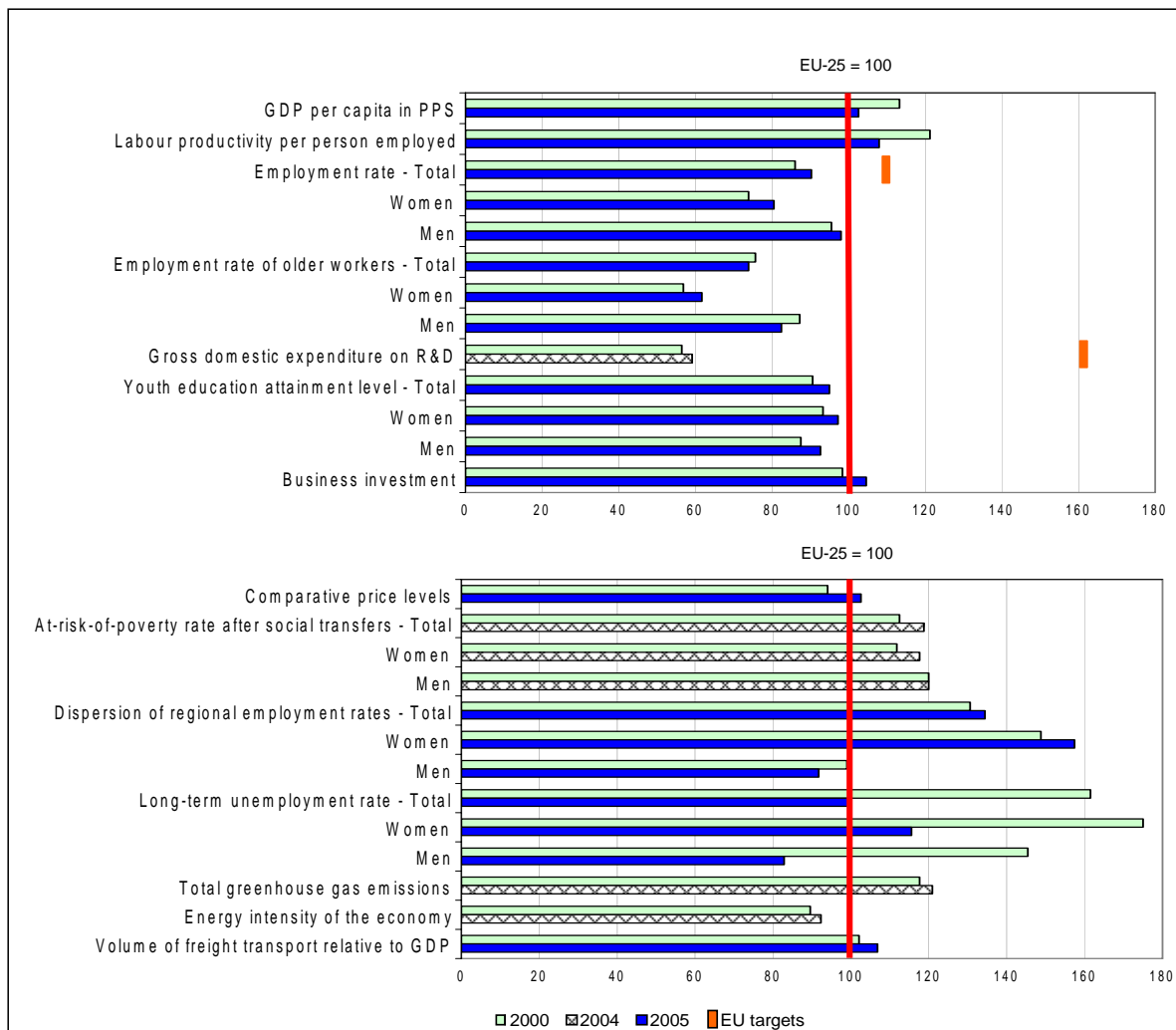
27. Compared to last year's National Reform Programme, the Italian Implementation report presents a clearer strategy, covering all policy areas and the synergies between them and is thus more ambitious. Progress is most extensive in the micro-economic field. Strategies and measures proposed in the macro area are generally appropriate but implementation is crucial. Employment policy needs to be reinforced in certain key areas. Progress has been mixed on meeting the commitments agreed at the 2006 Spring European Council.
28. Among the strengths shown by the Italian Implementation Report are: measures to enhance competition in professional and other services; initiatives to expand the use of ICT; and measures to step up the co-ordination of action to improve the business environment.
29. The policy areas in the Italian National Reform Programme where weaknesses need to be tackled with the highest priority are: fiscal sustainability, where commitment needs to be translated into effective action; competition in product and services markets, where the vigorous implementation of proposed reforms should be an initial basis for progress; increasing formal employment; and improving education and lifelong learning. Against this background it is recommended that Italy:
- rigorously pursue fiscal consolidation so as to put the debt-to-GDP ratio on a declining path and fully implement the pension reforms with a view to improving the long-term sustainability of public finances;
 - pursue the implementation of recently announced reforms aiming at increasing competition in products and service markets;
 - reduce regional disparities in employment by tackling undeclared work, increasing childcare provision and ensuring the efficient operation of the employment services throughout the country;
 - develop a comprehensive lifelong learning strategy and improve quality and labour market relevance of education.
30. In addition, it will be important for Italy over the period of the National Reform Programme to focus on: R&D, where despite welcome policy developments in specific areas, the overall strategy is still incomplete; effective measures to improve the sustainability of healthcare provision, while preserving quality and accessibility; sustainable use of resources, where implementation and subsequent further reinforcement of measures are essential; implementing plans to improve infrastructure; and establishing a comprehensive system of impact assessment for proposed regulation.

PART IV: STATISTICAL GRAPHS AND DATA

ITALY

	IT							EU25					
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target		
GDP per capita in PPS	113.3	112.0	110.0	107.6	105.5	102.6	:	100.0	100.0	100.0	70.0		
Labour productivity per person employed	121.2	118.6	115.0	111.6	110.3	108.0		100.0	100.0	100.0			
Employment rate	53.7	54.8	55.5	56.1	57.6b	57.6		62.4	63.3	63.8			
Women	39.6	41.1	42.0	42.7	45.2b	45.3		53.6	55.7	56.3			
Men	68.0	68.5	69.1	69.6	70.1b	69.9		71.2	70.9	71.3			
Employment rate of older workers	27.7	28.0	28.9	30.3	30.5b	31.4		36.6	41.0	42.5			
Women	15.3	16.2	17.3	18.5	19.6b	20.8		26.9	31.7	33.7			
Men	40.9	40.4	41.3	42.8	42.2b	42.7		46.9	50.7	51.8			
Gross domestic expenditure on R&D	1.05	1.09	1.13	1.11	1.10	:		2.5	1.86e	1.86e		:	3.0
Youth education attainment level	69.4	67.9	69.6	71.0	73.4	73.6			76.6	77.1		77.5	
Women	74.2	73.0	74.3	75.1	78.6	78.1			79.5	80.1		80.3	
Men	64.5	62.7	64.8	66.8	68.2	69.2			73.7	74.2		74.7	
Comparative price levels	94.0	95.5	97.9	102.3	102.7p	102.6p		100.0	100.0p	100.0p			
Business investment	18.0	18.0	19.2	17.9	18.2	18.2		18.3	17.1	17.4			
At-risk-of-poverty rate after social transfers	18.0	19.0	:	:	19.0b	:		16.0e	16.0e	:			
Women	19.0	20.0	:	:	20.0b	:		17.0e	17.0e	:			
Men	18.0	19.0	:	:	18.0b	:		15.0e	15.0e	:			
Dispersion of regional employment rates	17.5	17.1	16.7	17.0	15.6	16.0		13.4	12.2	11.9			
Women	30.5	29.6	29.1	29.7	25.7	26.6		20.5	17.3	16.9			
Men	9.8	9.4	8.9	9.1	8.7	8.9		9.9	10.2	9.7			
Long-term unemployment rate	6.3	5.7	5.1	4.9	4.0	3.9		3.9	4.1	3.9			
Women	8.4	7.6	6.9	6.6	5.5	5.2		4.8	4.7	4.5			
Men	4.8	4.4	4.0	3.8	2.9	2.9		3.3	3.6	3.5			
Total greenhouse gas emissions	106.7	108.0	108.1	111.1	112.1	:		90.7	92.7	:			
Energy intensity of the economy	186.9	184.0	184.1	189.2	189.1	:		208.8	204.9	:			
Volume of freight transport relative to GDP	102.2	100.9e	102.7e	93.7e	104.9be	111.9e		100.1e	104.6be	104.7e			

PERFORMANCE COMPARED TO EU-25



Cyprus

Assessment of National Reform Programme

1. In 2006, Cyprus's GDP per capita is projected at 84% of the EU average. Over the last decade, Cyprus sustained robust economic growth with an average real GDP increase of 3½% per year, outstripping by more than 1% the EU25 average of 2¼%. 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. The total employment rate foreseen at 68% is close to the EU-wide target, while the unemployment rate, despite a moderate rise, is projected to remain low at 5.4% (in 2006). Labour productivity per person employed is expected to remain below the EU average.
2. Cyprus enjoys buoyant economic growth and high employment rates, but the long-term fiscal challenge resulting from an ageing population is large. An improvement of the quality of public finances through a shift of expenditure towards human resources, modern infrastructure and R&D and innovation would support healthy levels of growth and contribute to diversifying the economy. Reforming health care and the pension system, while sustaining the progress in reducing government debt, would help in addressing the sustainability of public finances. Ensuring that wages reflect developments in productivity would contribute to gaining further flexibility and stem emerging risks to competitiveness.

PART I: GENERAL ASSESSMENT

3. The Cypriot 2005-2008 National Reform Programme (NRP) emphasised the objective of increasing the growth potential of the economy and living standards for citizens. It identified 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. In its 2006 Annual Progress Report (APR), the Commission drew attention to the need for stronger action to address the long-term sustainability of the public finances, including through reforms of social security, and for measures to reduce the rate of early school leaving.
4. Its 2006 Implementation Report shows that Cyprus is generally making good progress with the implementation of its NRP. The NRP provided a clear and comprehensive overview of numerous specific measures and linked them well to final objectives. There has been progress towards the vast majority of the R&D and employment targets presented in the NRP. In addition, progress has been generally good on fiscal consolidation; increasing the quality of, and access to, ICTs; improving the business environment; and upgrading basic infrastructure. Although further steps are required, satisfactory initial progress has been made in the following areas: improving the transposition of EU legislation into national law; improving environmental sustainability; energy liberalisation, energy efficiency and security of supply; reinforcing public employment services. There has been limited progress on: reforming health care and social security systems; better regulation; tackling anti-

competitive regulation in professional services; and reforms of the vocational education and training systems.

5. Progress in responding to the commitments made by the 2006 Spring European Council has overall been fairly good, for example on speeding up start-up procedures and establishing a single administrative contact point for business founders.
6. The efforts to develop ownership of the Growth and Jobs Strategy have been strengthened significantly. It has been repeatedly announced publicly that the Growth and Jobs Strategy and the Convergence Programme constitute the pillars of economic policy. The implementation mechanism and the consultation process are quite extensive and they encompass the participation of all stakeholders; including the Council of Ministers, a Parliamentary Committee, the creation of a National Advisory Committee (involving all stakeholders as well as social partners) and other committees. In order to increase public awareness, the government organised a number of seminars and public events, together with other activities covered extensively in the media. The efficient and effective use of Structural and Cohesion funding is a key factor to boost investments in several sectors, and it is therefore important that the increase in funding is matched by a similar increase in the absorption capacity.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The macro-economic focus in the NRP is on fiscal consolidation and debt reduction, through expenditure restraint and increased revenues. The NRP also targets the improvement of fiscal management via gradual implementation, starting from 2007, of three-year medium-term budgetary frameworks; expected to enhance expenditure control while linking medium-term targets with the annual budgetary procedure. Furthermore, it aims to restructure government expenditure towards capital outlays, while enhancing transparency. The NRP also includes measures to address the long-term sustainability of public finances, including labour supply and reforms in health care and social insurance, notably the pension system. Labour flexibility and wage moderation measures are also addressed.
8. Good progress has been recorded on fiscal consolidation. In 2005, the general government deficit declined to 2.3% of GDP from 4.1% of GDP the previous year, while the gross government debt-to-GDP ratio subsided to 69¼% of GDP from 70¼% of GDP in 2004. Moreover, economic projections hinted at a further reduction in 2006. Regarding the health care system, practical measures on the long delayed reform are expected to be implemented in 2007. The Health Insurance Organisation, which is responsible for the implementation of the national health insurance scheme, is finalising an action plan for the implementation of the reform. On social security reform, government proposals are presented, though the precise adjustments are yet to be agreed with the social partners, while their budgetary impact is left open. The target date for implementation of the first measures is 2007.
9. Overall, the progress made on the macro-economic reform measures outlined in the NRP is good. There is a particularly pressing need for concrete action to secure the

long term sustainability of public finances, and progress in reducing government debt in preparation for future costs of ageing should be sustained. Links and compatibility between the NRP objectives and the priorities set out in Cyprus's National Strategic Reference Framework for the investment of Structural Funds are identified in the Implementation Report, particularly for transport and environmental infrastructure projects, including strategic investments facilitating international trade (i.e. ports, access to ports) and interventions in support of ICT priorities. It is therefore important that the substantial increase in the available Structural Funding as from 2007 is matched by an equivalent increase in the absorption capacity. To this end, additional strengthening of the relevant public administration may be necessary.

Micro-economic policies

10. There are four micro-economic 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. The Implementation Report contains a comprehensive, detailed and precise list of initiatives addressing these challenges, as well as national priorities in other microeconomic policy areas.
11. The Implementation Report sets out many measures dealing with research policy and research capacities which confirm their importance in the Cypriot authorities' agenda. The strategy in this area is almost to build a new system from scratch, including developing and enhancing the institutions and infrastructure to carry out the research, as opposed to filling gaps or addressing specific weaknesses. Consequently, it is too early at this stage to assess whether the efforts are sufficient. Concerning the new R&D spending target of 1% of GDP by 2010 (0.4% of GDP in 2005), the public third of the target is comfortably achievable but the private sector input will need to be boosted. To this end, the government will increase funds to support private-public research links and is contemplating the use of tax incentives. However, no action is envisaged to establish venture capital funds.
12. Cyprus devotes particular attention to ICTs. It concentrates on e-Government, digital literacy and the use of ICT by business. Measures put forward in the NRP have been implemented carefully and on time. Several interesting new projects have been put forward – actions raising awareness of network security, a helpdesk system for public services, and cost-saving projects in health care. However, broadband take up is still low, in spite of widespread availability and more affordable prices. The market review process under the European regulatory framework has started with some delay but is now proceeding steadily.
13. The actions to enhance 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, although one exception is professional services, where restrictions like pricing regulation and advertising bans are common place. Implementation of the various actions listed seems to be proceeding according to plan. On better regulation, there are still only some very preliminary and incomplete measures. Some interesting measures announced in the NRP (introducing comprehensive evaluations of state aid, establishment of a loan guarantee facility and e-Procurement) are due for implementation later. Cyprus has managed to further reduce its deficit in transposing EU legislation into national law, now well below the 1.5% mark, but should remain vigilant on the quality of transposition.

14. The importance of environmental sustainability for growth and jobs was well recognised in the NRP, in particular with regard to the impact of environmental degradation on tourism. Implementation of the infrastructure projects listed in the NRP is ongoing. Cyprus will potentially have to prioritise large investments to meet EU environmental standards within the deadlines foreseen in the Accession Protocol, in particular on solid waste and wastewater treatment.
15. Efforts to upgrade basic infrastructure are being pursued actively with a range of ongoing or planned projects, mainly on roads, harbours and airports, aiming at addressing road congestion and improving accessibility from abroad. Many projects will be financed through public-private partnerships. Implementation of the projects listed in the NRP seems on track.
16. In order to reach its targets relating to renewable energy sources and conservation of energy, Cyprus reinforced in 2006 its support schemes, including by setting up a one-stop-shop for large renewable energy investments. Plans for a new energy centre that will contribute to security of supplies are at the engineering study phase. It will include a liquefied gas terminal and strategic oil storage facilities. Energy market liberalisation started in Cyprus with the 2004 accession to the EU. A number of licenses for the generation of electricity have already been granted and others are under consideration. New private suppliers are expected to enter the market by 2008.
18. Overall, the implementation of the vast majority of measures seems to be proceeding as planned. The Implementation Report also includes a number of new measures. However, the effectiveness of the policies can only be assessed in the longer term. The Report does not deal with encouraging venture capital investments and tackling anti-competitive regulation in the area of professional services.

Employment Policies

19. The NRP focused on achieving full employment, improving quality and productivity at work and strengthening social and territorial cohesion. The 2006 Implementation Report confirms as the main priorities in the employment area: 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 also pointed out in the APR the importance of lifelong learning and skills.
20. Ambitious but realistic employment targets have been set and a wide range of well-targeted active labour market policies put in place. An overhaul of the public employment services, including a candidate placement system, to help match labour supply and demand through personalised services, is also advancing. Nevertheless, there is limited clarity on the effectiveness of policies, particularly for the young. Female employment is high and a wide range of support measures are advancing. Important gender imbalances remain by occupation, and professional qualifications, as well as in labour market participation, employment and unemployment. The only initiative that is proposed to tackle this is a study in 2007, to suggest policy measures to reduce the very high pay gap. While the total employment rate of older workers is above the EU target for 2010, further measures are in progress, including

the gradual increase of the retirement age to 63 years by 2008. The establishment and implementation of an economic migration strategy and enactment of an adjusted immigration law are delayed.

21. Regarding the adaptability of workers and enterprises, part-time and fixed-term employment, though slightly increased in 2005, remain low despite an appropriate legal framework being in place. The report focuses on active labour market policies and the modernisation of public employment services as means to increase flexibility of the labour market. A small pilot project, aimed at encouraging more women to take up work, is running. However, there is limited clarity on policy initiatives in support of the security aspect, particularly as regards the envisaged reforms of the social protection system.
22. Cyprus has a lifelong learning strategy which aims to: promote access to lifelong learning for all; strengthen infrastructures and systems; promote lifelong learning supporting research and development; and promote effective governance. There is limited clarity as to the content and timeframes for its implementation, and indicators and benchmarks in the field are not provided. Progress is slow in implementing the reforms of the vocational education and training systems, including the outdated apprenticeship scheme, to make them more credible and better attuned to labour market needs. Budgetary resources earmarked to this end are limited. Policy measures to reduce further the number of early school leavers are in progress. The development of a training providers' certification system is expected in 2007. The vocational qualifications system has already provided five occupational standards, and implementation is to be completed gradually during the 2007-2013 period.
23. Overall, Cyprus is performing quite well on employment. The Implementation Report provides a thorough account of policy measures under implementation that go in the right direction. They include measures to provide employment opportunities for young people, and overcome difficulties and impediments in the transition from education to work. While education is strong on many fronts, there is room for substantial improvement, especially in developing adaptability and skills. Full implementation of a comprehensive lifelong learning strategy with stronger links between technical/vocational and continuing training will improve participation in training, notably for young, low-skilled and older workers, and will also encourage the progress of social dialogue on flexicurity.

PART III: CONCLUSIONS

24. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
25. Cyprus is making good progress in the implementation of its National Reform Programme, and of the four areas for priority action formulated by the 2006 Spring European Council. Overall, the implementation of the majority of measures seems to be proceeding as planned.
26. The strengths of the National Reform Programme and its implementation in 2006 include: progress in the field of fiscal consolidation; a new policy to develop a

comprehensive research and innovation system; and the maintenance of a good overall employment performance supported by a broad range of active labour market measures.

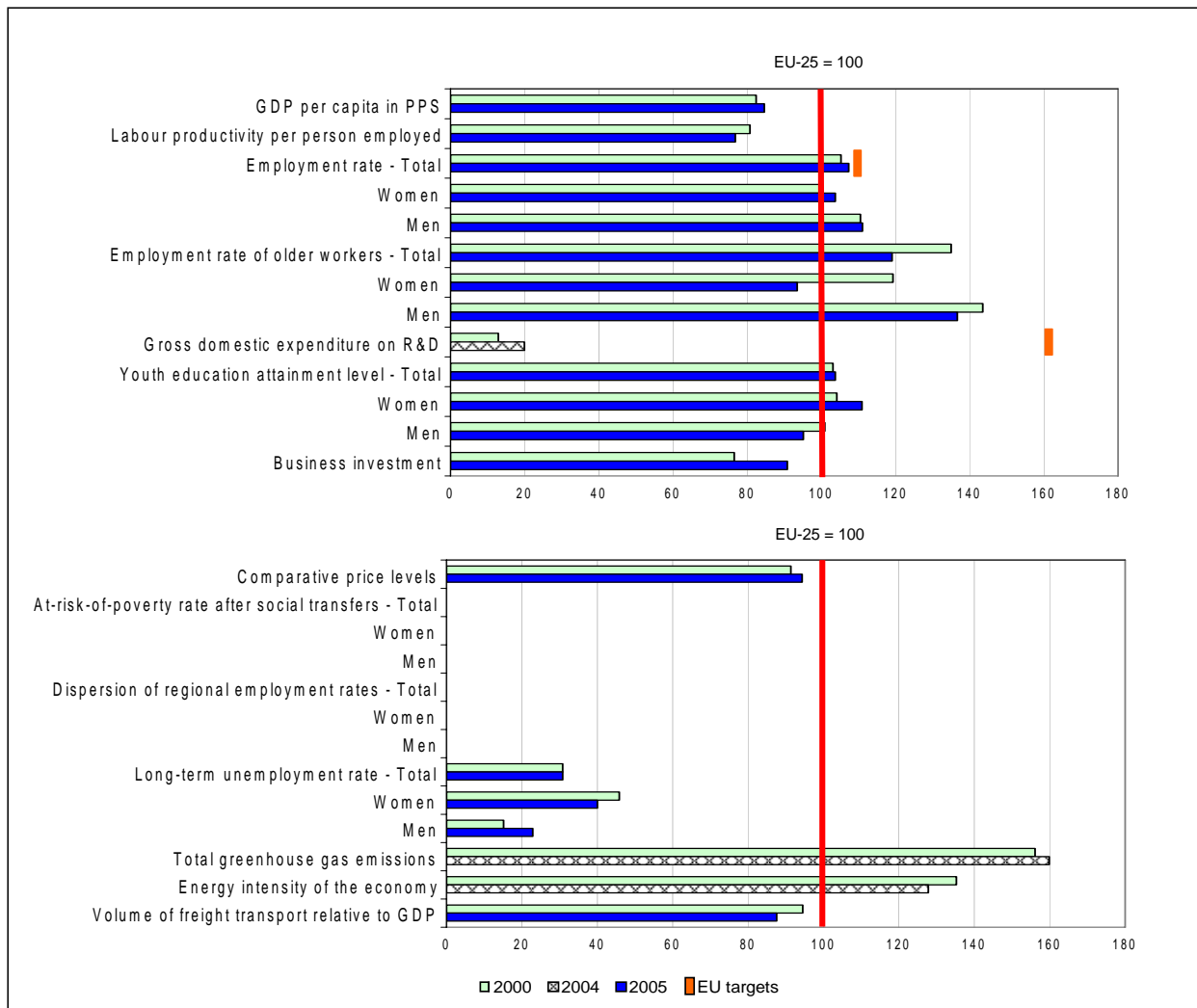
27. The policy areas in the Cypriot National Reform Programme where weaknesses need to be tackled with the highest priority are: addressing ageing-related expenditure, where measures are not progressing; and increasing labour market opportunities for young people. Against this background, it is recommended that Cyprus:
- take steps to implement reforms of the pension and health care systems and sets a timetable for their implementation with a view to improving long-term sustainability;
 - enhance life long learning, and increase employment and training opportunities for young people by accelerating the reforms of the vocational, education, training and apprenticeship system.
28. In addition, it will be important for Cyprus over the period of the National Reform Programme to focus on: measures to encourage venture capital investments and to improve competition in the area of professional services.

PART IV: STATISTICAL GRAPHS AND DATA

CYPRUS

	CY							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	82.4	84.4	82.6	80.4	84.1	84.6		100.0	100.0	100.0	
Labour productivity per person employed	80.7	80.1	77.8	74.2	76.7	76.8		100.0	100.0	100.0	
Employment rate							71.0				70.0
Total	65.7	67.8	68.6	69.2	68.9	68.5		62.4	63.3	63.8	
Women	53.5	57.2	59.1	60.4	58.7	58.4		53.6	55.7	56.3	
Men	78.7	79.3	78.9	78.8	79.8	79.2		71.2	70.9	71.3	
Employment rate of older workers											
Total	49.4	49.1	49.4	50.4	49.9	50.6		36.6	41.0	42.5	
Women	32.1	32.2	32.2	32.7	30.0	31.5		26.9	31.7	33.7	
Men	67.3	66.9	67.3	68.9	70.8	70.8		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.24	0.25	0.30	0.35	0.37	0.40p	1.0	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	79.0	80.5	83.5	79.5	77.6	80.4		76.6	77.1	77.5	
Women	82.8	84.9	89.5	87.0	83.8	89.1		79.5	80.1	80.3	
Men	74.4	75.4	76.7	71.3	70.7	71.1		73.7	74.2	74.7	
Comparative price levels	91.3	91.9	90.9	96.5	93.3p	94.3p		100.0	100.0p	100.0p	
Business investment	14.0	13.8	15.1	14.3	14.7	15.8		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	:	:	:	15.0	:	:		16.0e	16.0e	:	
Women	:	:	:	17.0	:	:		17.0e	17.0e	:	
Men	:	:	:	14.0	:	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	-	-	-	-	-	-	-	13.4	12.2	11.9	
Women	-	-	-	-	-	-	-	20.5	17.3	16.9	
Men	-	-	-	-	-	-	-	9.9	10.2	9.7	
Long-term unemployment rate											
Total	1.2	0.8	0.8	1.0	1.2	1.2		3.9	4.1	3.9	
Women	2.2	1.1	1.0	1.3	1.6	1.8		4.8	4.7	4.5	
Men	0.5	0.6	0.5	0.7	0.9	0.8		3.3	3.6	3.5	
Total greenhouse gas emissions	141.6	140.7	145.1	152.8	148.2	:		90.7	92.7	:	
Energy intensity of the economy	282.3	274.4	269.9	287.9	261.8	:		208.8	204.9	:	
Volume of freight transport relative to GDP	94.6e	93.9e	95.7	99.5	76.5	91.7		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Latvia

Assessment of National Reform Programme

1. Supported by one of the highest productivity growth rates in the EU, real GDP in Latvia has grown at an annual average rate of about 8% since 2000. GDP per capita is estimated at 51.3% of the EU average in 2006, still one of the lowest in the EU. After years of sluggish development, the total employment rate in 2006 is over 65% and moving fast towards the national 2010 target of 67%. Labour market supply constraints (triggered by outward migration and a decrease in working age population) result in upward wage pressure and difficulties in keeping a balance between growth in nominal wages and productivity. Other imbalances, as evidenced by high inflation and a wide external account deficit, persist.
2. The main policy challenge for Latvia in terms of growth and employment performance is to preserve macro-economic stability in the face of persistent inflationary pressures, a very wide current account deficit and strong credit growth as well as to transform the economy away from low-technology, labour-intensive goods. To this end economic policy is confronted with the task of stepping up fiscal consolidation in order to contain demand pressures, increasing labour force participation and improving productivity growth.

PART I: GENERAL ASSESSMENT

3. The Latvian 2005-2008 National Reform Programme (NRP) identified five main economic policy priorities: 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. In the 2006 Annual Progress Report (APR) the Commission shared this analysis and drew Latvia's attention to the need for: 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; and stronger measures to adapt education and training to labour market needs and to develop and implement a coherent lifelong learning strategy.
4. Its 2006 Implementation Report shows that Latvia is generally making some progress with the implementation of its NRP. Progress during 2006 in implementing Latvia's reform strategy in the macro-economic area has been mixed, with greater efforts required to reduce risks to stability. Implementation in the micro-economic and employment area is not yet at full speed. In the area of research and innovation, and especially regarding effective partnerships between research and education institutions and businesses, first measures have been initiated, but implementation will mainly be as of 2007. Progress can also be noted in railway infrastructure investment, public procurement and renewable energy. The Implementation Report indicates some progress on health and safety measures at work and highlights the need to tackle rural-urban disparities. Some initiatives have been taken on better regulation, including work on the modernisation of the insolvency law. Progress is limited on lifelong learning and the administrative capacity of the education system.

5. With regard to the 2006 Spring European Council conclusions, work is progressing modestly. The start-up procedure has been streamlined, but one-stop-shops for starting an enterprise are not yet fully operational and the issue of providing single administrative contact points to hire the first employee is not addressed in the Implementation Report. Further measures to promote entrepreneurship education would be welcome, in particular to introduce it fully in the national curriculum in secondary education.
6. Consultation and efforts to develop ownership of the Strategy for Growth and Jobs have continued over the past year. Discussions have been held with Parliament and social partners on relevant topics. Two new supervisory structures have been put in place to monitor the implementation of the NRP: one within the government and another involving local governments and social partners. The Minister for Economics has been appointed as national coordinator for the implementation of the Growth and Jobs Strategy. The Latvian authorities have ensured coherence between the implementation of the NRP and the investment of Structural Funds in areas such as transport and social infrastructure, R&D and innovation, information society and the development of human capital. Cohesion Policy funding will amount to 3.36% of GDP in the 2007-2013 period. Information is lacking on the implementation of the general administrative capacity programme, particularly important in view of the forthcoming injection of structural funds.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. Economic growth has been high and medium-term prospects remain strong. However, booming domestic demand, high inflation, labour market shortages, rapid credit growth and further deterioration of the current account deficit are causing concern over macro-economic stability and may affect medium-term growth prospects. Prudent macro-economic management should guide the economy towards better balance and seek to prevent the materialisation of risks to stability. Against this background, it is of concern that the fiscal policy target for 2006 shifts from the small surplus achieved in 2005 to a clear deficit. Furthermore, according to the Implementation Report, the pro-cyclical stance is likely to remain in the near future.
8. The Implementation Report indicates that some progress has been achieved in improving budgetary planning procedures, in particular through the introduction of medium-term budgetary planning from 2007.
9. Maintaining economic and budgetary sustainability by a more restrictive fiscal stance that does not add to demand pressures and a careful prioritisation of growth-promoting expenditure is a key contribution to preventing overheating of the economy. Such a macro-economic policy would also help underpin further growth and job creation and facilitate implementation of the structural reforms envisaged.

Micro-economic policies

10. The Latvian NRP presented two micro-economic priorities: stimulating knowledge and innovation and developing a favourable and attractive environment for investment and work. The Commission's analysis was in line with this.
11. Progress in implementation of measures aiming at an improved performance in R&D and innovation is limited. Latvia has set an ambitious target for expenditure on R&D of 1.5% of GDP by 2010. The attainment of this ambitious R&D target depends on the rigorous implementation of the measures announced for 2007 and of the Law on Scientific Activity (public investments are increasing by 0.15% of GDP in every year). Particular attention will have to be paid to improving cooperation between industry and research institutions, including by the fast and effective implementation of the planned technology transfer contact points and the technology incubators. It will be important to ensure that private sector R&D and innovation funding is not crowded out by public funds. The established Technology Agency is a positive step in that direction, in that it should enable better administration and prioritisation of research programmes. Measures which target an increase in the number of scientists, researchers and engineers are welcome, but a stronger response will be needed to overcome bottlenecks. The implementation of the lifelong learning strategy and Structural Funds support to technological and engineering studies should help address the issue. The now to established intellectual property council will improve the framework conditions for innovation. The setting-up of an integrated e-government infrastructure is also an improvement, but more efforts will be required to improve the supply of online public services.
12. Progress in implementing measures to develop a favourable and attractive environment for investment and work is mixed. A new law on public procurement will allow for the use of "green procurement" criteria for public purchases and will strengthen competition. Progress is reported on preserving nature, which is key for the tourism sector. Noteworthy also are the increased investment in road and railway infrastructure and new measures to promote renewable energy and environmental technologies. In the field of better regulation, some measures have been taken. For example, work on a new insolvency law seems promising but its coming into force is only envisaged for July 2007. New guarantees and venture capital funds were set up in 2006, while new measures to improve SMEs' access to finance are foreseen in the next financial planning period. 13. The inquiries into markets which might suffer from insufficient competition are welcomed. Such assessments and action could be extended to regulated professions such as pharmacy and legal services.
14. The implementation of measures in the field of research and innovation was rather limited in 2006 and mainly scheduled for 2007. Fast and effective progress will therefore be needed in order to meet the high ambitions of the NRP in that field. The measures implemented in 2006 to improve the business environment constitute progress in addressing this key challenge, although considerable further measures will be required, including in the field of better regulation.

Employment policies

15. The key employment challenges identified in the 2005 APR were fostering employment and improving education and skills. These issues are reflected in the Implementation Report. Latvia concentrates on an inclusive labour market (taking a lifecycle approach); economic activities in regions; tackling undeclared work; access

to education and lifelong learning; co-operation between public administration, education establishments and employers; and on technological and natural science knowledge. Some measures tackle gender equality and reconciling work and family though an overall gender-mainstreaming approach is lacking.

16. Latvia is taking measures to increase labour supply, though these need to be reinforced in face of current trends in outward labour migration. The Implementation Report indicates that the number of participants in active labour market programmes has increased, which may help to increase labour supply, foster labour market participation and bring down long-term unemployment. Therefore the plans to reduce the financing of active labour market policies by half during the next Structural Funds planning period go in the wrong direction. Increased efforts should be made to improve access to childcare. Initiatives to improve health and safety at work and general health care standards and to tackle undeclared work are furthering progress. Measures to improve financial incentives to work include a general increase in the tax-free income threshold and an increase in the minimum wage by more than 30% in 2007. While the tax changes may have a positive effect, it is not clear that higher minimum wages would help slowing emigration and improving employment. Furthermore, existing wage pressure in the economy could intensify. Internal mobility and support for commuting should also be strengthened.
17. Further measures to upgrade the skills of the workforce are necessary to improve labour productivity. Despite some positive trends in education problems remain. There is a general fragmentation of the education system: the vocational education system appears under-developed and the quality of higher education programmes needs to be improved. The delays in approving and implementing a lifelong learning strategy could lead to insufficient funding during 2007-2013, while 2005 has seen a decrease in already quite low adult participation in education and training. Established policies are continuing, aimed at improving education infrastructure, but some new areas for action have been identified in the Implementation Report, such as boosting efficiency in the education system, raising the quality of engineering and natural science studies and improvements in career development. The Implementation Report does not address the administrative capacity of education systems, although the issue has entered the national debate. Efforts are being undertaken to improve the administrative capacity of public administration at all levels, but they could need more substantial Structural Funds support if significant progress is to be made.
18. Overall, the steps undertaken in 2006 continue the established approach to tackling key employment challenges. To increase labour supply and the level of education and skills it is very important that the lifelong learning strategy and active labour market policies are strengthened. Productivity should be underpinned by a lifelong learning strategy as well as by education and training systems more responsive to labour market needs.

PART III: CONCLUSIONS

19. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:

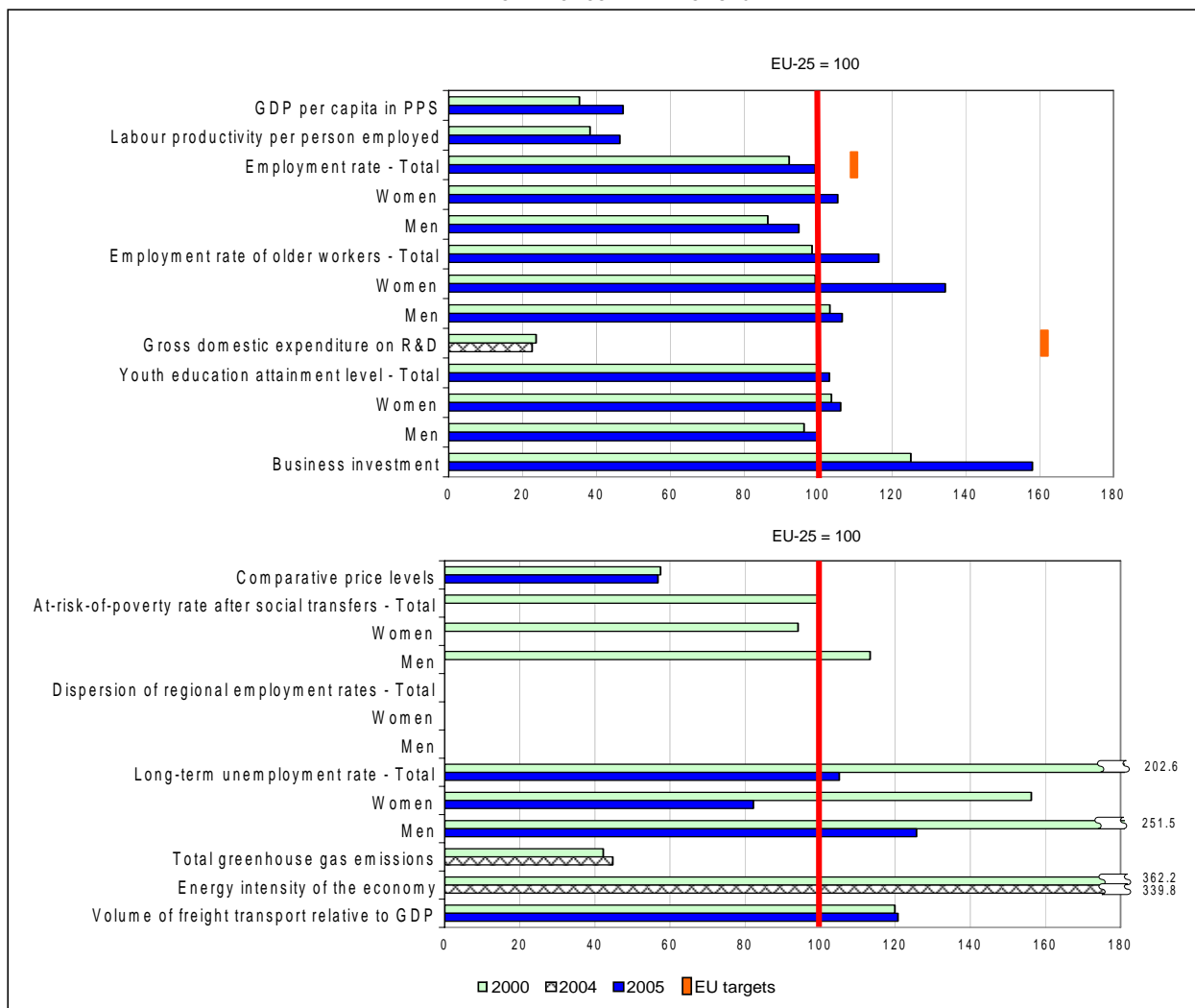
20. Latvia is making progress in the implementation of its National Reform Programme, in particular in the micro-economic and employment areas. However, policy responses to address the macro-economic key challenge and the 2006 Spring European Council conclusions are less comprehensive. Regarding the governance of the Growth and Jobs Strategy, the process has gained political visibility since the adoption of the National Reform Programme and stakeholder involvement has improved.
21. Among the strengths of the Latvian National Reform Programme and its implementation are several measures taken to facilitate the start-up and financing of innovative SMEs, including the establishment of new guarantee and venture capital funds and developments in promoting a one-stop-shop to establish companies. Latvia has also implemented a set of measures that have successfully supported labour market performance.
22. The policy areas in the Latvian National Reform Programme where weaknesses need to be tackled with the highest priority are: more concrete measures to secure macro-economic stability and prevent the overheating of the economy; further development of the R&D strategy to improve prioritisation and increase private sector involvement; and stronger measures to increase labour supply and strengthen the skills of the labour force. Against this background, it is recommended that Latvia:
 - maintain economic and budgetary sustainability by pursuing a more restrictive fiscal policy, so as to contribute to the prevention of overheating and a careful prioritisation of expenditure;
 - make faster progress in the implementation of the research and innovation policy reforms, in order to meet effectively the ambitious targets set out in its National Reform Programme. This concerns especially policies to stimulate partnerships between research and education institutions and businesses;
 - intensify efforts to increase labour supply and productivity by improving regional mobility, enhancing the responsiveness of education and training systems to labour market needs and putting in place a lifelong learning system.
23. In addition, it will be important for Latvia over the period of the National Reform Programme to focus on: faster progress on establishing a single contact point for the administrative formalities involved in hiring the first employee; promoting entrepreneurship education; pursuing active labour market policies; and improving access to childcare.

PART IV: STATISTICAL GRAPHS AND DATA

LATVIA

	LV							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	35.4	37.1	38.7	40.8	42.8	47.2		100.0	100.0	100.0	
Labour productivity per person employed	38.3	39.4	40.2	41.3	42.7	46.3		100.0	100.0	100.0	
Employment rate							67.0				70.0
Total	57.5	58.6	60.4	61.8	62.3	63.3		62.4	63.3	63.8	
Women	53.8	55.7	56.8	57.9	58.5	59.3		53.6	55.7	56.3	
Men	61.5	61.9	64.3	66.1	66.4	67.6		71.2	70.9	71.3	
Employment rate of older workers											
Total	36.0	36.9	41.7	44.1	47.9	49.5		36.6	41.0	42.5	
Women	26.7	30.0	35.2	38.8	41.9	45.3		26.9	31.7	33.7	
Men	48.4	46.2	50.5	51.3	55.8	55.2		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.44	0.41	0.42	0.38	0.42	0.57	1.5	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	76.5	71.7	77.1b	75.4	79.5	79.9		76.6	77.1	77.5	
Women	82.4	77.5	84.3b	80.9	85.1	85.2		79.5	80.1	80.3	
Men	70.9	66.2	70.0b	70.1	74.2	74.7		73.7	74.2	74.7	
Comparative price levels	57.5	58.2	57.6	55.4	56.4p	56.8p		100.0	100.0p	100.0p	
Business investment	22.9	23.8	22.5	22.9	25.6	27.5		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	16.0	:	16.0	16.0	:	:		16.0e	16.0e	:	
Women	16.0	:	16.0	17.0	:	:		17.0e	17.0e	:	
Men	17.0	:	16.0	16.0	:	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	-	-	-	-	-	-	-	13.4	12.2	11.9	
Women	-	-	-	-	-	-	-	20.5	17.3	16.9	
Men	-	-	-	-	-	-	-	9.9	10.2	9.7	
Long-term unemployment rate											
Total	7.9	7.2	5.5	4.4	4.6	4.1		3.9	4.1	3.9	
Women	7.5	6.3	4.6	4.4	4.3	3.7		4.8	4.7	4.5	
Men	8.3	8.1	6.4	4.3	4.8	4.4		3.3	3.6	3.5	
Total greenhouse gas emissions	38.3	41.2	40.9	41.3	41.5	:		90.7	92.7	:	
Energy intensity of the economy	756.0	816.5	750.3	725.1	696.3	:		208.8	204.9	:	
Volume of freight transport relative to GDP	120.0	119.9	122.3	133.1	128.6	126.4		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Lithuania

Assessment of National Reform Programme

1. Lithuania has been experiencing one of the fastest real GDP growth rates in the EU, averaging nearly 8% over the period 2001-2005 and its economy is forecast to grow at a similar level (7.8%) in 2006. However, GDP per capita is expected to reach only 55% of the EU average in 2006. Domestic demand has accelerated rapidly in the last years, has been the driver of economic growth, and has led to higher external accounts deficits. Inflation is expected to rise to almost 4% in 2006 from 2.7% in 2005. As a result of the strong economic growth and increased labour shortages the labour market has tightened rapidly. Unemployment fell sharply from 11.4% in 2004 to 8.3% in 2005 and is expected to decrease further to around 6% in 2006. The employment rate is estimated to increase from 62.6% in 2005 to 64.5% in 2006.
2. The main economic policy challenge for Lithuania in terms of growth and employment performance is to address inflationary pressures, strong credit growth and a widening current account deficit. While ongoing pension and health care reforms contribute to the sustainability of public finances, fiscal consolidation can play an important role in sustaining macroeconomic stability. Skills gaps and significant wage pressures against the background of strong economic growth and increased labour shortages, partly due to emigration, would be alleviated by higher internal labour mobility and continued high productivity growth, to which increasing R&D activity and its effectiveness could contribute.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 Lithuanian National Reform Programme (NRP) set three key national priorities: to sustain fast economic growth and a stable macroeconomic environment; to promote the competitiveness of Lithuanian companies; to promote employment and investment in human capital. The Commission's January 2006 Annual Progress Report (APR) identified as points requiring further attention: strengthening of the science and technology base; additional efforts to strengthen innovation systems; further reinforcements of active labour market policy; and promotion of labour mobility.
4. Its 2006 Implementation Report shows that Lithuania is generally making good progress with the implementation of its NRP. The majority of the NRP measures are being implemented. Overall progress is good on: pension, healthcare and tax reforms; upgrading transport infrastructure; establishing a national energy strategy; and modernising initial education and training. There is initial progress on: boosting R&D and innovation; developing ICT use; better regulation; increasing competition in professional services; and reinforcing active labour market policies to increase the employability of vulnerable groups, though in all these areas implementation remains in the early stages. There has been limited progress on promoting labour mobility and on increasing adult participation in lifelong learning. Lithuania is faced with mounting inflationary pressures and developing a comprehensive strategy to contain these is not given a sufficiently high priority in the Implementation Report.

Seemingly promising initiatives to further reinforce Lithuania's attractiveness for foreign direct investment have been taken or are in the pipeline, but a sufficiently coherent strategy is not yet fully in place.

5. Progress has been moderate on fulfilling the specific policy commitments agreed at the Spring European Council. Lithuania is programming measures to reinforce entrepreneurship education and is developing a comprehensive energy policy. However, the report does not directly address the issues of one stop-shops for rapid business start-ups, or of adjusting existing less ambitious national targets in line with the European Council conclusion committing Member States to ensuring young people leaving education get a job or further training within six months.
6. Lithuania has built further on substantial consultation and efforts to develop ownership of the NRP before publication. An inter-ministerial commission ensures coordination and ownership of the NRP within the government. Lithuania has established a special framework for stakeholder involvement in monitoring the implementation of the NRP, which might serve as a useful example for other Member States. Four focus groups (macro issues, R&D and innovation, enterprise policy and employment), chaired by social and economic partners and also involving researchers and representatives of state institutions analyse the implementation of the NRP in respective areas and propose changes and new measures if necessary. The Lithuanian authorities have gone a good way towards ensuring coherence between the implementation of the NRP and the investment of Structural Funds. The Structural Funds contribute significantly to NRP areas such as transport and social infrastructure, R&D and innovation, information society, the business sector and the development of human capital. Cohesion Policy funding will amount to 3.4% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The Implementation Report confirms the key macroeconomic priorities and objectives identified in the 2005 NRP. The pension reform aiming at the introduction and consolidation of a funded private pension pillar is on track. Increasing the retirement age to 65 years - already mentioned as an aim in last year's NRP - will be considered in the light of a study to be conducted in 2008. This would contribute to the future adequacy and sustainability of pensions, as well as providing a necessary boost to labour supply (see "Employment Policies" below). The first stage of the health care reform covering the period 2003-2005 has been finalised and the second stage of the restructuring of health care institutions covering 2006-2008 has started. An e-health project is also being implemented. The first step of the tax reform has been carried out, with the personal income tax reduced from 33% to 27% as of 1 July 2006. A temporary "social tax" (a de facto increase in the corporate income tax) as a compensatory measure is to be collected in 2006 and 2007. Overall, the pension, health care and tax reforms broadly progress as planned.
8. Some efforts have been made to attract further foreign direct investments. Several measures have been taken, such as the establishment of industrial parks, the implementation of clusters and the provision of tax and administrative incentives for

business activity in the free economic zones. An investment promotion programme with a wide range of measures to attract foreign direct investment is being prepared and negotiated with stakeholders, with the aim of final government approval in early 2007. It will be vital, in order to improve Lithuania's competitiveness, to ensure that the final programme is based on a coherent strategy and is vigorously and rapidly implemented.

9. Another area which needs further consideration is ensuring that wage growth adjusts according to productivity gains. This would contribute to a stable macroeconomic environment by increasing economic flexibility and moderating increases in unit labour costs, thus preserving Lithuania's competitiveness.
10. The NRP aimed at Lithuania meeting the conditions for participation in the euro area by a sustainable fiscal policy. The government deficit has up to now been largely successfully contained. The Implementation Report states that the fiscal deficit should not exceed 1.2% of GDP in 2006 and confirms the targets of 1.3% for 2007 and 1% in 2008, despite a recently more expansionary fiscal stance underpinned by higher than expected government revenues. However, the picture on inflation is less positive, with pressure on wages and prices from rising energy costs and labour market shortages. The Implementation Report forecasts average annual inflation to accelerate to 3.9% in 2006 – compared to the original NRP projection of 2.1% - and 4.7% in 2007. Despite this trend, no new plans or reinforced measures to contain inflation are announced in the report. The government's plan to further cut the personal income tax to 20% could exacerbate inflation if followed through in the short-term, but is currently on hold (a reduction to 24% as of January 2008 is already approved). Strong domestic demand partly fuelled by the ongoing rapid credit growth has resulted in a widening of the current account deficit. In this context, fiscal policy should play an increased role in supporting price stability and limiting risks of overheating, while continuing to improve incentives to work.
11. Lithuania has made good progress in the implementation of the measures aiming at the sustainability of public finances and continued economic growth, but a stronger commitment to achieving macro-economic stability is needed.

Micro-economic policies

12. In the area of micro-economic policy the NRP presented the promotion of competitiveness as the key priority. The Commission shared that view but also stressed the importance of infrastructure development and R&D and innovation policies.
13. As regards R&D and innovation, Lithuania is moving in the right direction. However, many measures are still at the conceptual stage. Lithuania will need to increase substantially public sector spending on research in order to reach the target of 1% of GDP by 2010 (from 0.6% in 2004) and the envisaged reform to allocate more R&D financing on a competitive basis will be crucial to improve the efficiency of this public funding. Substantial efforts to leverage private sector spending will also be needed to achieve the ambitious overall 2% target for research investment. Crucial areas are the improvement of research skills to match the needs of enterprises, effective public-private cooperation and the effective implementation of plans in preparation to concentrate R&D programmes on key sectors. The

implementation of the Higher Education Development Plan for 2006–2010 is starting. A comprehensive policy for human resources in the R&D area needs to be pursued. This is particularly urgent as the results of reforms of the R&D and education system will only appear in the medium term. Several measures concerning innovation are still mere proposals, whose eventual outcome is uncertain. There is scope for further effort to create better links between the R&D and innovation system and the country's enterprises, which should facilitate the application of research results to improve the competitiveness of traditional industries and enhance the conditions for creating spin-offs from research institutions. There are successful initiatives to promote clusters and set up national technology platforms.

14. A national energy strategy has been drafted which includes: the liberalisation of electricity and gas sectors; privatisation of oil refineries and state transportation companies; measures to minimise pollution and ensure the safe decommissioning of Unit 2 of Ignalina Nuclear Power Station; the integration over the coming years of Lithuania's energy systems with the energy systems of the EU; and further regional cooperation with a view to creating a single electricity market for the Baltic States. An energy efficiency programme for 2006-2010 will promote energy savings and the use of energy from renewable sources as well as contribute to the reduction of greenhouse gas emissions. The transport infrastructure projects "Rail Baltica" and "Via Baltica", aiming at better connecting the Baltic States with European transport networks, are considered as a priority. The report presents promising measures for broadband development, e-government and ICT use, though in some cases more concrete plans will need to be developed. It includes a set of promising environmental protection measures, such as green public procurement, which should be pursued.
15. To further enhance competitiveness, Lithuania presents some promising measures, such as a National Plan for Better Regulation including a methodology on defining and reducing administrative burdens. The Implementation Report pays attention to the needs of SMEs but does not address all relevant issues in detail. Setting up a one-stop-shop for business start-ups and reducing the time to set up a business are still pending issues. New measures should help foster entrepreneurship education once they are implemented. Given that significant restrictions exist in the area of professional services (fixed and recommended prices, etc.) efforts should be made to build on the work undertaken by the national competition authority to remove unjustified restrictive regulation.
16. Overall, Lithuania demonstrates willingness to engage in the structural reforms needed in the relevant micro-economic areas and this is feeding through into important reforms in areas such as better regulation and infrastructure. Further reinforcement of R&D policies is needed.

Employment Policies

17. The Implementation Report, while announcing no new measures, confirms the NRP's commitments to increase employment and invest in human capital with a view to achieving an overall employment rate of 68.8% by 2010. It states that the key employment targets might be achieved earlier than foreseen. Already, the 2005 employment rate for older workers (49.2%) and women's employment rate (59.4%) were higher than those projected in the NRP. However, shortages of labour in certain

sectors are a threat to the sustainability of growth. Pronounced regional differences in employment also need to be more actively addressed.

18. The NRP set out a range of measures to improve labour supply. Implementing plans, not yet confirmed, to increase the pension age to 65 (see (7) above) would contribute to this. New active labour market measures, such as job rotation (temporary substitution of an employee with a job seeker, for up to 12 months, for example in periods of leave, training, etc.), have been introduced and their coverage expanded to include more vulnerable groups as well as the inactive population. These measures, together with those in the National Social Inclusion Strategy, should help to increase the employability of vulnerable groups, especially if steps are taken to make employment more attractive for such groups. Given the increasing expenditure on active labour market policies, it is important to ensure effective monitoring and quality control. Steady progress can be observed on improving health care, social partnership and labour market institutions, but progress on measures to better prepare young people for employment is slow. In particular, the adoption of the Youth Entrepreneurship Programme and the new law on vocational training should be speeded up. The report describes measures to tackle the tendency for women's employment to be concentrated in certain sectors (segregation) and to encourage female entrepreneurs, but the gender pay gap and equal pay for equal work are not mentioned. Similarly, efforts to ensure a better work-life balance should be stepped up. To reach the ambitious NRP targets, effective action will need to be taken to increase the availability of high quality childcare in all regions.
19. Measures to improve the adaptability of workers and enterprises are in progress. The Labour Code has been amended to allow part-time work, overtime and seasonal work to be regulated in collective agreements. Legislation for new forms of work organisation is in preparation. The impact of tax reform (see also "Macro-economic policies") started in July 2006 on the situation of the low-paid remains to be seen. To address the shrinking supply of labour partly resulting from emigration, a draft strategy for the management of inward and outward economic migration has been prepared. Given regional differences and labour shortages, cooperation with social partners is necessary to draw up effective measures to increase labour mobility, on which there has been little progress so far. Though the NRP did not cover occupational health and safety, the negative trends in this area call for a review of the existing measures.
20. A number of initiatives approved prior to the NRP to improve human capital now need to be complemented with reinforcements in certain areas. On-going measures include a programme for special education services and the creation of a National Qualifications System. A programme to restructure teacher training was approved in May 2006. Preparations for introducing a technological module in secondary schools are in progress. To increase the quality of education, the development of the education monitoring and management system and the setting up of a school evaluation agency are under way. This focus on quality should be reproduced throughout the education system, including higher education, which at the moment seems to be more quantity oriented. Projects aimed at raising the level of adult participation in education and training aim to reach the NRP target of 10% by 2010. Despite the existence of a lifelong learning strategy, this 10% target appears ambitious, especially since adult participation has dropped slightly (from 6.5% in

2004 to 6.3% in 2005). Targeted action is also needed to ensure that the proportion of older workers participating in training rises faster than that of the overall workforce.

21. Overall, the most NRP employment measures are progressing steadily and certain policies have been reinforced, in particular active labour market policies. Further action is needed to increase youth employability, the availability of childcare and, especially, labour mobility.

PART III: CONCLUSIONS

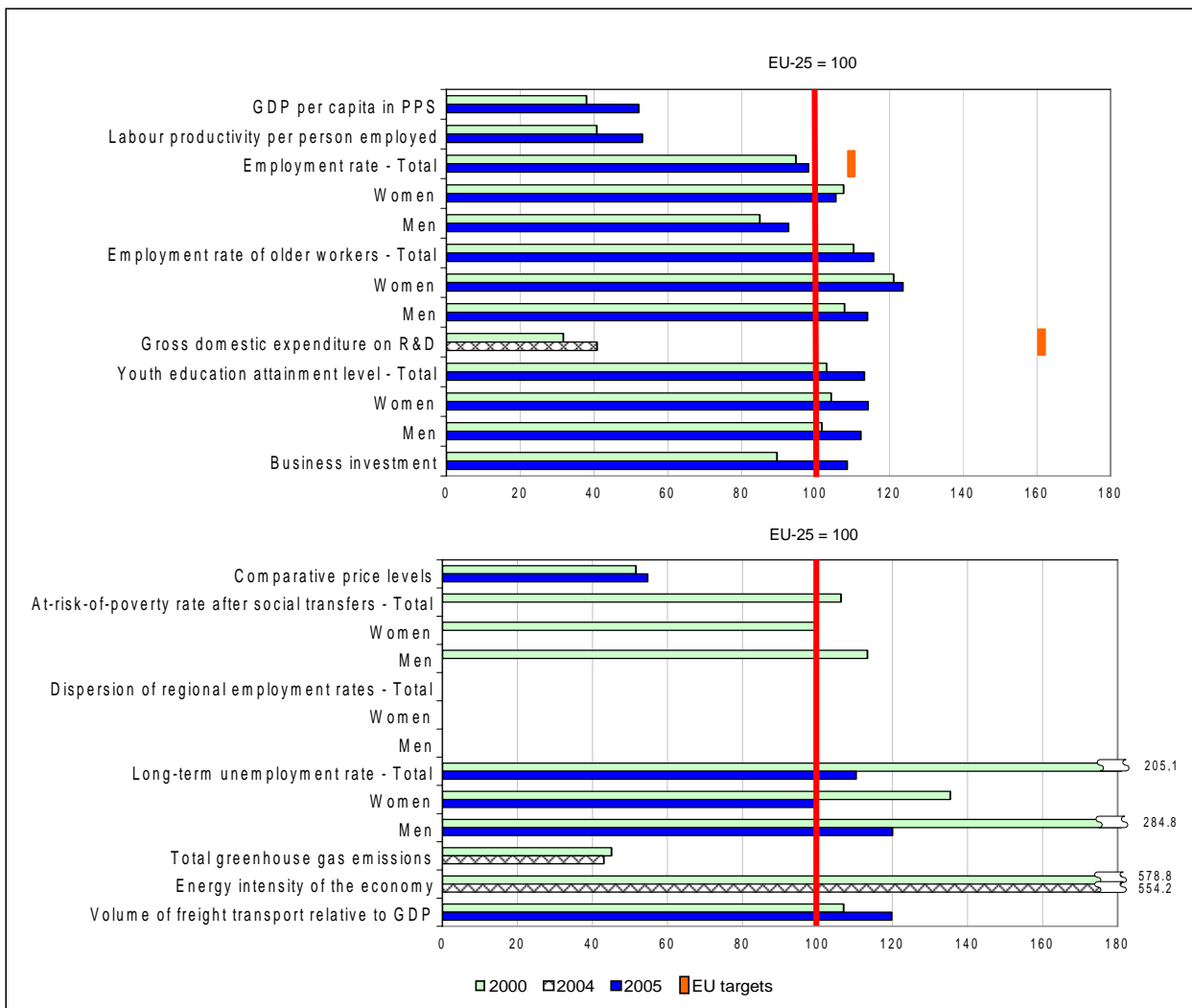
22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
23. Lithuania is making good progress in the implementation of the National Reform Programme, in most of the main policy areas across the macro, micro and employment sectors. However, with many important measures at the conceptual stage, there remains much to do in terms of implementation. Progress has been moderate on fulfilling the commitments agreed at the 2006 Spring European Council.
24. Among the strengths of the Lithuanian National Reform Programme and its implementation are: the pension, health and tax reforms; measures to upgrade road and rail infrastructure; the establishment of a national energy strategy; the reinforcement of active labour market policy, notably the new job rotation measures; and steps to modernise initial education and training.
25. The policy areas in the Lithuanian National Reform Programme where weaknesses need to be tackled with the highest priority are: reinforcing measures aimed at increasing investment in R&D, which do not so far appear sufficient to reach the ambitious target set; placing a stronger emphasis on measures to promote labour mobility; and taking additional steps to increase participation in lifelong learning, especially by older workers. Against this background, it is recommended that Lithuania:
 - continue its efforts to strengthen its R&D system and to reach its ambitious target for overall investment in R&D, notably by raising public expenditure on this area;
 - intensify efforts to increase the supply of skilled labour by improving regional mobility of labour and by promoting lifelong learning, with a special focus on the participation of older workers.
26. In addition, it will be important for Lithuania over the period of the National Reform Programme to focus on: achieving macro-economic stability and containing inflation; increasing foreign direct investment; facilitating business start-ups; environmental protection; improving youth employability; expanding entrepreneurship education; increasing the availability of childcare; and strengthening occupational health and safety

PART IV: STATISTICAL GRAPHS AND DATA

LITHUANIA

	LT							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	38.0	40.2	41.9	45.2	47.8	52.1		100.0	100.0	100.0	
Labour productivity per person employed	40.8	44.8	44.8	47.1	49.6	53.1		100.0	100.0	100.0	
Employment rate							68.8				70.0
Total	59.1	57.5	59.9	61.1	61.2	62.6		62.4	63.3	63.8	
Women	57.7	56.2	57.2	58.4	57.8	59.4		53.6	55.7	56.3	
Men	60.5	58.9	62.7	64.0	64.7	66.1		71.2	70.9	71.3	
Employment rate of older workers											
Total	40.4	38.9	41.6	44.7	47.1	49.2		36.6	41.0	42.5	
Women	32.6	31.1	34.1	36.7	39.3	41.7		26.9	31.7	33.7	
Men	50.6	49.2	51.5	55.3	57.6	59.1		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.59	0.67	0.66	0.67	0.76	0.76	2.0	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	78.9	80.5	81.3b	84.2	85.0	87.8		76.6	77.1	77.5	
Women	82.9	83.8	83.2b	87.9	88.5	91.8		79.5	80.1	80.3	
Men	75.0	77.1	79.4b	80.6	81.5	83.9		73.7	74.2	74.7	
Comparative price levels	51.6	53.0	54.6	54.9	54.6p	54.7p		100.0	100.0p	100.0p	
Business investment	16.4	17.9	17.4	18.2	18.9	18.9		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	17.0	17.0	17.0	15.0	:	:		16.0e	16.0e	:	
Women	17.0	17.0	17.0	15.0	:	:		17.0e	17.0e	:	
Men	17.0	18.0	16.0	14.0	:	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	-	-	-	-	-	-	-	13.4	12.2	11.9	
Women	-	-	-	-	-	-	-	20.5	17.3	16.9	
Men	-	-	-	-	-	-	-	9.9	10.2	9.7	
Long-term unemployment rate											
Total	8.0	9.3	7.2	6.0	5.8	4.3		3.9	4.1	3.9	
Women	6.5	7.7	6.8	6.0	6.2	4.5		4.8	4.7	4.5	
Men	9.4	10.8	7.6	6.0	5.5	4.2		3.3	3.6	3.5	
Total greenhouse gas emissions	40.9	40.0	38.5	33.8	39.9	:		90.7	92.7	:	
Energy intensity of the economy	1208.4	1256.8	1272.7	1194.8	1135.6	:		208.8	204.9	:	
Volume of freight transport relative to GDP	107.1	96.4	115.3	116.9	113.7	125.4		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Luxembourg

Assessment of National Reform Programme

1. GDP growth gathered momentum (5.5% in 2006 compared with 4.0% in 2005). GDP per capita is expected to be at 237.9% of the EU-25 average. The employment rate (65.1% in 2006) is slightly below the EU average (63.8%). Unemployment reached a historic peak in 2004 (5.1%, which was three points higher than in 2001) but fell in 2006 to around 4.6%. Inflation has risen since 2002; after touching 3.8% in 2005, it should fall back to 3.2% in 2006.
2. Though Luxembourg's economy remains very healthy at present, there are a number of problems: the potential for longer-term growth could increasingly be affected by declining competitiveness owing to relatively fast growth in payroll costs. R&D policy also remains relatively underdeveloped. Lastly, the employment rate of the resident population remains below the EU average, and it is particularly low among older workers.

PART I: GENERAL ASSESSMENT

3. Luxembourg's 2005-2008 National Reform Programme (NRP) identified the following key objectives: a high-quality education and training system, an economy integrated into Europe and the wider world, an attractive economic environment, a stable macro-economic framework and compliance with the principles of sustainable development. While endorsing these priorities, the Commission nevertheless took the view, in its 2006 Annual Progress Report (APR), that more should be done to achieve the ambitious objectives in research and innovation and, in the field of employment, to address the situation of older and disabled workers.
4. The 2006 Implementation Report shows that Luxembourg has taken or is taking appropriate measures to balance its budget and curb inflation, to modernise government, to develop research, to guarantee compliance with the principles of sustainable development, to do more to prevent unemployment, to step up activation measures, to reshape inclusion policy for the disabled and to improve ways of reconciling private and working life. The continuing problems of students repeating years, teaching and organisation, above all in secondary education, demand that efforts to reform the education and training systems be maintained. Despite the lack of improvement (a very low employment rate and an average exit age from the labour market that is falling), there have been no new measures specifically aimed at further increasing employment among older workers. The Implementation Report implicitly covers the challenge of integrating the economy into the European and international economy from both the macro-economic standpoint (external competitiveness) and the micro-economic standpoint (strengthening competitiveness and developing European infrastructure).
5. The Implementation Report is in tune with most of the priorities for action identified by the 2006 Spring European Council. It responds appropriately to the European Council's calls to increase support for research. It partly responds to the European

Council's calls in respect of increasing employment rates among women, recognising qualifications and providing support for SMEs. Additional measures are needed to facilitate the recruitment of the first employee and speed up the establishment of new businesses.

6. The NRP was the product of a wide-ranging consultation exercise among the social partners. The social partners also helped draft the Implementation Report. The Implementation Report was then discussed in the Luxembourg Parliament, which organised a public hearing to include civil society in the debate. Measures have been taken to raise awareness (conference, website). Reforms are being monitored by means of a competitiveness scoreboard. Generally speaking, the Implementation Report does not, however, provide precise benchmarks for the measures presented; the monitoring of year-on-year progress could usefully be improved.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. Some of the fiscal consolidation measures taken address spending, for instance modulating the indexation of wages and welfare benefits until 2009, when the budget is expected to be back in balance, and optimising the government's capital spending. Other measures decided in the spring concern revenue: certain contributions and taxes have risen. These measures may help balance the budget, even if the recent deterioration is attributable primarily to a sharp increase in spending. Taken together, these measures will undoubtedly have a limited – though real – adverse impact on activity.
8. Modulating indexation, flanked by other measures cited in the Implementation Report (but the impact of which is difficult to quantify), can also help achieve the objective of controlling inflation. It can also help curb rising payroll costs, which have risen faster in Luxembourg than in neighbouring countries, even though the country's competitiveness has been declining for a number of years.
9. Generally speaking, the implementation of the macro-economic policies set out in Luxembourg's Implementation Report is progressing to plan and should contribute significantly in the medium term to the achievement of the objectives set. Reforms will, however, be needed to ensure the long-term viability of the pensions system as the marked growth in employment in the past will be matched in the future by a comparable increase in the number of pensioners. The ratio of contributors to pensioners is therefore set to worsen even if employment continues to rise at the present rate. However, very little has yet been done to reform the pensions system.

Micro-economic policies

10. Luxembourg has designed and started implementing a body of measures aimed at improving the economic environment, and in particular at developing transport infrastructure, increasing the speed and security of electronic communications and introducing e-government projects. Enterprise training programmes are available, and an online one-stop-shop has been set up for businesses. The deficit in transposing EU directives into national law, after affecting 4.4% of directives in

November 2005, affected only 3.4% in September 2006. Import rules and practices will be assessed with a view to improving competitiveness. The Implementation Report is, however, relatively short on detail concerning certain measures: examples include the methodology adopted for simplifying administration and for reducing the administrative burden, and the specific measures to be implemented in order to reduce the transposition backlog significantly by mid-2007. Reforms of the laws on bankruptcy and improving access to financing for SMEs were announced in 2005, but the report provides no information on their progress. Furthermore, additional measures are needed for SMEs, especially to facilitate the recruitment of their first employee and the procedures for starting up a business. In order to promote competitiveness in certain sectors, professional services need to be reformed, and the national competition authorities should be allocated sufficient resources to perform their duties.

11. Luxembourg has managed to increase public funding for R&D and attract new private R&D investment. It has been made easier for foreign researchers to work in the country. The funding of government research centres has been reformed, and new public-private partnerships are planned. Clear budget priorities for research and innovation should be maintained in order to bring R&D investment up to 3% of GDP by 2010. The planned public-private partnerships should be fleshed out and speeded up. Subsequent stages in the reforms should focus on improving governance, coordinating public research and fostering links with private research.
12. On the issue of sustainable development, the report presents a comprehensive and promising package of measures under way, including efforts to establish protected areas, assistance for sustainable consumption and eco-efficiency, new legislation laying down building standards, a voluntary agreement with industry on energy efficiency, and direct aid and tax incentives for renewable energy sources. The 2008 review of the integrated energy strategy, which will address eco-efficiency, competitiveness and security of supply, will be crucial. Mention is also made of projects involving eco-technologies.
13. The micro-economic measures set out in the Implementation Report are steps in the right direction. The onus should now be on monitoring implementation and analysing annual progress. A number of measures aimed at improving the economic environment need to be described in greater detail, and further measures should be adopted for SMEs and to promote competition.

Employment policies

14. The Implementation Report does not address the issue of older workers. It focuses on raising employment rates, improving education and training systems, integration into the labour market, support for female employment and the development of career-transition mechanisms. The signing of a tripartite agreement with the social partners, followed by the tabling of legislative proposals, is expected to bring substantial and rapid progress in these areas.
15. Support for the employment of women is continuing with the development of "maison-relais" (before- and after-school centres for children), the numbers of which are expected to increase considerably, and other comparable services. The government is also continuing to support gender-equality schemes. However,

relatively little is being done to address gender gaps on the labour market (employment, unemployment, inactivity, pay). Assistance for the integration into the labour market of young people, among whom unemployment, though declining, nevertheless remains fairly high (13.8% in 2005), should be increased by creating a training allowance, reforming employment measures and supporting informal learning. The government also wants to give young people a greater incentive to look for work by abolishing the unemployment benefits paid to them after a waiting period.

16. To permit flexible retirement arrangements for older workers, whose employment rate has hardly changed (31.7% in 2005), and to raise the relatively low age at which people leave the labour market (58.2 years of age in 2003, 57.7 years in 2004), only tripartite negotiations are planned for the autumn of 2006. People remote from the labour market will benefit from reforms in the areas of training and activation; they are also targeted by the reorganisation of "social initiatives benefiting employment" (semi-sheltered employment). Active measures for households on the guaranteed minimum income have now been made more effective. Lastly, the employment service will be reformed in 2007 on the basis of an OECD audit.
17. A legislative proposal recently tabled reorganises vocational training in several areas, including continuing vocational training and vocational retraining. An individual right to training should be created before the end of 2006. More specialised forms of training (in entrepreneurship or for women in business) seem, however, to have been much less developed. A scheme will be adopted before the end of 2006 to help keep redundant workers in the labour market by means of redeployment, outplacement or training. Another "flexicurity" measure, viz. a plan to reform labour law by abolishing the distinction between workers and employees, figures in the tripartite agreement of April 2006.
18. Quality assurance is developing in the primary and secondary education sectors (pilot school in 2005, quality agency planned for 2007), and the gap in performance between children from indigenous and minority communities has been significantly reduced. A new definition of core skills and new curricula were launched in the primary sector in September 2006; they will be extended to the secondary sector in 2007. The number of students repeating years, which remains high overall, and a continuing shortage of secondary teachers (to the disadvantage of the most vulnerable students) call for further reforms, as do the excessive fragmentation and inadequate take-up (one secondary student in two) of education affording general access to university studies. The objective of the reforms is a highly skilled labour force. Action to stop early school leaving is covered by a legislative proposal tabled in October 2006.
19. There are encouraging new developments as regards supporting the employment of women and stepping up the activation of young people, but the results cannot yet be seen. Education reforms also have some way to go. There is currently no substantial strategy to raise the employment rate among older workers.

PART III: CONCLUSIONS

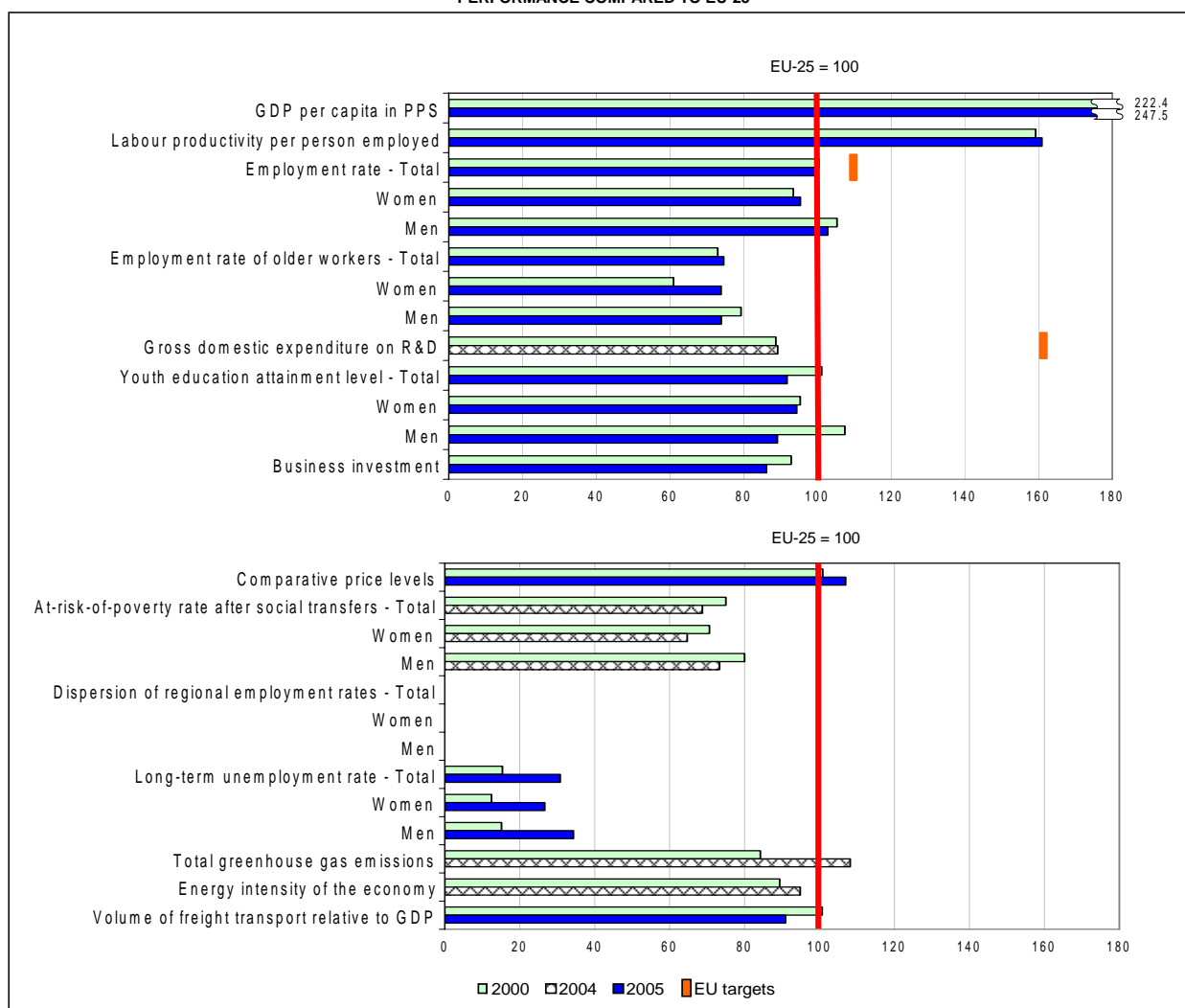
20. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II – and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
21. Luxembourg is making very good progress on implementation of its National Reform Programme and of the actions agreed by the 2006 Spring European Council, but there is still room for improvement regarding the weaknesses identified in 2005. The macro-economic measures adopted hold out the prospect of fiscal consolidation and lower inflation. A promising set of measures are now being implemented at the micro-economic level. Greater efforts are required, however, to implement a system to monitor and assess annual progress, and a number of measures need to be introduced, for instance to assist business start-ups and SMEs. Despite encouraging reforms on the employment front, no new initiative has been announced to raise the level of employment among older workers, and major reforms to improve the education system have yet to materialise.
22. Among the strengths of the drafting, implementation and reinforcement of the National Reform Programme is the agreement between the government and the social partners on a system designed to curb the inflationary trends observed since 2002 by temporarily suspending the indexation of wages and benefits. The same tripartite agreement organises a system of assistance for businesses that promotes ways of keeping workers in employment where there is a danger of redundancy. Luxembourg can also pride itself on the major expansion in childcare facilities. The priority accorded to R&D is also to be applauded. Last but not least, a comprehensive set of measures have been taken to guarantee sustainable development, and the energy strategy is a step in the right direction.
23. It will also be important for Luxembourg over the period of the National Reform Programme to focus on: a strategy for further increasing the employment rate among older workers; a detailed strategy aimed in particular at further reforming the current early-retirement systems; further efforts are also needed to reduce drop-out rates, especially in secondary education, and to remove the artificial barriers between different types of education; the impact on youth unemployment of the measures recently adopted for young people needs to be monitored very closely; and in order to render the economic environment more attractive, greater support is needed for competitive markets, for the transposition of EU directives and for SMEs.

PART IV: STATISTICAL GRAPHS AND DATA

LUXEMBOURG

	LU						2010 National target	EU25			2010 EU target
	2000	2001	2002	2003	2004	2005		2000	2004	2005	
GDP per capita in PPS	222.4	214.6	220.7	232.7	237.5	247.5		100.0	100.0	100.0	
Labour productivity per person employed	159.2	148.0	149.5	156.0	157.0	160.9		100.0	100.0	100.0	
Employment rate							:	62.4	63.3	63.8	70.0
Total	62.7	63.1	63.4	62.2	62.5	63.6					
Women	50.1	50.9	51.6	50.9	51.9	53.7		53.6	55.7	56.3	
Men	75.0	75.0	75.1	73.3	72.8	73.3		71.2	70.9	71.3	
Employment rate of older workers								36.6	41.0	42.5	
Total	26.7	25.6	28.1	30.3	30.4	31.7					
Women	16.4	15.2	18.4	20.6	22.2	24.9		26.9	31.7	33.7	
Men	37.2	35.9	37.7	39.7	38.3	38.3		46.9	50.7	51.8	
Gross domestic expenditure on R&D	1.65	:	:	1.66	1.66	1.56p	3.0	1.86e	1.86e	:	3.0
Youth education attainment level								76.6	77.1	77.5	
Total	77.5	68.0	69.8	72.7b	72.5	71.1					
Women	75.8	69.0	65.5	75.6b	73.4	75.8		79.5	80.1	80.3	
Men	79.2	67.0	74.0	69.7b	71.6	66.6		73.7	74.2	74.7	
Comparative price levels	100.9	102.9	102.5	105.3	106.1p	107.0p		100.0	100.0p	100.0p	
Business investment	17.0	18.3	17.3	16.9	16.2	15.0		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers								16.0e	16.0e	:	
Total	12.0	12.0	:	10.0b	11.0	:					
Women	12.0	13.0	:	11.0b	11.0	:		17.0e	17.0e	:	
Men	12.0	12.0	:	9.0b	11.0	:		15.0e	15.0e	:	
Dispersion of regional employment rates								13.4	12.2	11.9	
Total	-	-	-	-	-	-					
Women	-	-	-	-	-	-		20.5	17.3	16.9	
Men	-	-	-	-	-	-		9.9	10.2	9.7	
Long-term unemployment rate								3.9	4.1	3.9	
Total	0.6	0.6	0.7	0.9	1.1	1.2					
Women	0.6	0.6	0.9	0.9	1.4	1.2		4.8	4.7	4.5	
Men	0.5	0.5	0.6	1.0	0.8	1.2		3.3	3.6	3.5	
Total greenhouse gas emissions	76.4	78.5	86.4	90.1	100.3	:		90.7	92.7	:	
Energy intensity of the economy	186.6	190.7	196.7	181.8	194.3	:		208.8	204.9	:	
Volume of freight transport relative to GDP	100.8	110.0	109.5	113.0	109.5	95.2		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Hungary

Assessment of National Reform Programme

1. Since the mid-1990s, Hungarian GDP has grown at an average annual rate of 4.2% and is expected to expand by 4% in 2006. The employment rate has recently been stagnating close to 57%, far below the EU wide target. At the same time, the unemployment rate, which was around 6% until 2004, has increased and is expected to reach close to 7.5% in 2006. The participation rate, 61.6% in the first half of 2006, is the second lowest among the Member States. Over the past six years, the lack of fiscal discipline has been weighing increasingly on the economy. The budget deficit has increased from around 3% of GDP in 2000 to 7.8% of GDP in 2005 and about 10% of GDP in 2006 (including the burden of second pillar pension funds).
2. In order to lay the basis for sustainable growth and job creation, the overriding priorities for Hungary are fiscal consolidation followed by ensuring the long-term sustainability of public finances. Given the expected significant long-term rise in age-related expenditure, fiscal consolidation based on enhanced expenditure control and underpinned by urgent sound reforms of the public administration, health care, pension and education systems would be conducive to fiscal sustainability. At the same time, other measures to stimulate potential growth and employment, including by improving the functioning of labour markets and without jeopardising fiscal consolidation, are important. Various institutional and regulatory measures would also significantly improve the micro-economic environment.

PART I: GENERAL ASSESSMENT

3. Hungary's 2006 Implementation Report takes the form of a revised National Reform Programme (NRP). In line with the government's new strategy, it outlines plans to establish a sustainable budgetary position in the short term, which is conducive to growth and job creation over the medium term. The report maintains the nine key challenges identified in the 2005 NRP and complements them by a new priority for energy and the environment and a new emphasis on active labour market policies. In its 2006 Annual Progress Report (APR), the Commission identified as areas requiring further attention: ensuring sustainable public finances; enhancing competition in network industries; improving the business environment; and increasing the responsiveness of education and training to labour market needs.
4. Progress in implementation is limited overall. The Implementation Report sets out a new, better integrated and more concrete reform strategy, but only partly addresses the concerns identified by the Commission in its APR. Some important reform steps have been taken and the revised NRP announces a number of additional, forward-looking measures and strengthens previous commitments. The process of liberalisation of network industries is on course. Progress has been good on reforms to the unemployment benefit system. There have been initial signs of progress on: making finance more easily available to SMEs; energy efficiency and increasing the use of renewable energy sources; reintegrating disabled people and other disadvantaged groups into employment; reducing undeclared work; education and

training reform and putting in place a lifelong learning strategy. Progress has been disappointing on: fiscal consolidation (where the budget deficit has deteriorated very substantially); improving the business environment; reducing and redirecting state aids; and on increasing labour mobility. The previously encouraging pace of reforms in research and innovation has slowed down.

5. Limited progress has been made towards meeting the commitments made at the 2006 Spring European Council. For example, ambitious targets to speed up company start-ups are so far not accompanied by concrete steps sufficient to achieve them.
6. In the Implementation Report, the objectives and measures presented are more clearly linked to the overall reform strategy and government "ownership" seems stronger than before. The coordination of the Strategy for Growth and Jobs remains at a ministerial level. Since 1 July 2006, national reform plans for growth and jobs are managed by the National Development Agency, which is also responsible for investments financed by Structural Funds. This new institutional set-up is expected to improve co-ordination between Structural Fund investment and the priorities of the NRP. Cohesion Policy funding will amount to 3.2% of GDP in the 2007-2013 period. As with the NRP, consultations with social partners took place before the presentation of the Implementation Report.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The macro-economic key challenge of reducing the fiscal deficit has become the central issue for the Hungarian economy. Hungary also faces a very significant rise in age-related expenditure over the long term, which puts it in the high risk category regarding the sustainability of public finances.
8. The implementation of the original deficit-reduction strategy of the 2005 NRP was inadequate in the period until summer 2006. After major slippages in the budget deficit in the first half of 2006, especially on the expenditure side, the government started to implement initial fiscal consolidation measures. These included increasing VAT, personal income tax, corporate profit tax and employees' social contributions, introducing tax on income from interest, solidarity tax, some cuts in price subsidies, the nominal freeze of most expenditure items until 2008 and improving the efficiency of the public administration by exploiting economies of scale. Further reforms planned include laying-off 10% of public administration employees; introducing means-testing for subsidies; increasing the retirement age; decreasing early retirement by improving incentive schemes to stay in work and by revamping the disability pension system; putting health care services on a strict insurance basis and introducing patient contributions; and restructuring pharmaceutical subsidies. Further structural reform plans remain to be spelled out.
9. However, the government deficit is still expected to reach 10.1% of GDP instead of the targeted 6.2% of GDP in 2006. The large deficit has also led to a significant increase in government debt to above 60% of GDP and contributed to a high external deficit and consequently to a depreciation of the currency of around 8% in the first

half of the year. The government now intends to reduce the budget deficit to around 3% of GDP by 2009.

10. Against the background of a serious deterioration in public finances in 2006, the expenditure containing and structural reform measures envisaged, if fully specified and implemented, would lead to a substantial reduction of the government deficit and should contribute to addressing Hungary's macro-economic key challenge. The government's structural reform plans for public finances and the new emphasis put on the sustainable equilibrium of the state budget also point in this direction. However substantial risks remain, as also reflected in the more cautious deficit projections contained in the Commission's Autumn forecast. Hence, the planned strategy needs to be both further specified and persistently pursued in order to achieve its purpose.

Micro-economic policies

11. In 2005, the NRP identified R&D and innovation, the business environment, competition, and the development of infrastructure as micro-economic key challenges. These remain priorities and are complemented with energy policy and environment development.
12. Concerning R&D and innovation, after the important and positive reforms carried out between 2003 and 2005, progress has slowed down. Although research and innovation remains one of the main priorities identified in the NRP, no major new measures to address this area have been implemented. The finalization and adoption of the new Science, Technology and Innovation Strategy is delayed. Overall, a comprehensive and coordinated strategy is needed, focusing on more intense cooperation between academia and industry and on innovation support mechanisms for Hungarian firms, as well as incentives encouraging foreign-owned firms to invest in research and innovation and to bring them closer to the local entrepreneurial environment. A key planned step is the reform of the Hungarian Academy of Science. This reform should notably lead to the concentration of resources on carefully selected subjects and on the best performing research teams, as well as the development of incentives to cooperate with the private sector and full integration into the European Research Area.
13. ICTs feature significantly in the micro-economic reforms in Hungary. Initiatives concentrate on e-Government, broadband and ICT use by business and households. The direction is the right one, but the Implementation Report does not sufficiently describe concrete measures.
14. Obstacles still hinder entrepreneurial activities and the revised NRP acknowledges the importance of improving the business environment. Preparatory work for introducing impact assessments has been carried out but adequate implementing structures need to be devised. The setting-up time for business is long and start-up costs are high in Hungary compared to the EU average. New procedures to allow companies to be incorporated and to register via an on-line one-stop-shop are positive. Nevertheless, more needs to be done to reach the one-week target indicated for setting up a company in 2007. Furthermore, limited progress has been achieved towards promoting entrepreneurship education and on the establishment of a single contact point for recruiting the first employee. Measures to improve access to finance

for enterprises have been adopted and should contribute to facilitating SME financing. Special care needs to be taken when facilitating access to venture capital for SMEs, so that measures in this direction achieve their objectives and respect state aid rules.

15. As regards environmental and energy issues, the developments in "greening" public procurement and the establishment of a new strategy for the use of renewable energy sources and of energy efficiency action plans are welcomed. However, no adaptation measures are set up although the revised NRP mentions that Hungary is weak in preparing for potential consequences of climate change.
16. The process of liberalisation of network industries is on course, although ownership of the electricity transmission networks, including the system operation, reverted to the incumbent after only two years of unbundling. Rail freight market opening is not yet fully accomplished or has not yet led to significant market entry, but the government intends to launch additional action, which would be welcome. The Commission is concerned about the absence of concrete objectives for state aid policy both in the 2005 NRP and in the 2006 revised NRP, particularly in view of decisive and concrete steps required to achieve a reduction of the overall level of state aid and a redirection from sectoral to horizontal objectives, in particular R&D. While the implementation of internal market legislation is progressing, Hungary needs to pay attention to the quality of its transposition of EU directives into national law, as the number of infringement cases is relatively high.
17. Overall, though there has been encouraging progress in certain areas of micro-economic reform, Hungary will need to increase the pace and scope of change if it is to improve competitiveness sufficiently to stimulate the level of growth and job creation necessary to underpin a rapid improvement in its overall economic position.

Employment policies

18. Raising the employment and activity rate, improving the labour market situation of the disadvantaged, reducing regional labour market disparities and enhancing human capital have been identified as the key employment challenges. The Commission pointed in the 2006 APR to the need for increasing the responsiveness of education and training systems to labour market needs and for upgrading skill levels, particularly for the low-skilled. The government is trying to minimise the effect of budgetary austerity measures in terms of decreasing employment and activity rates and to limit the effects on the most vulnerable groups. Against this background, the revised NRP sets the following priorities: strengthening the role of active labour market policies; targeted support for the employment of disadvantaged people; promoting lifelong learning; and improving the quality, effectiveness and efficiency of education.
19. Measures to increase the employment rate of young people, women and older workers are being implemented, and further measures have been announced. The employment of those at the start of their career is aided by the temporary reduction of the employers' contribution payment, which will be extended to the long-term unemployed and women returning from maternity leave. The abolition of employment restrictions for people receiving childcare allowance and the extension

of childcare provision are expected to increase activity rates for women. In addition to the targeted programmes of the public employment service and the facilitation of part-time work, there are intentions to support active ageing by reducing early retirement and revising the system of disability benefits. However, more needs to be done to make work pay and encourage people to participate in the labour market. The integration of employment and social services systems has begun. A number of adequate measures have been taken to reform the social benefit system. These are due to be complemented by the revision of disability benefits with a stronger focus on rehabilitation. The revision of the support and accreditation system for organizations employing people with disabilities, and the decision to launch comprehensive development programmes in disadvantaged micro-regions with dominantly Roma population are welcome. However, more remains to be done to improve the situation of these groups and to reduce regional disparities.

20. Besides completing the reform of the unemployment benefit system, measures to increase "flexicurity" are limited to the modification of the Labour Code. Since taxes and social contributions levied on employment have increased, additional efforts will be required to transform undeclared work into regular employment through strong and coherent incentives and sanctions. In this respect, establishing the planned link between health service entitlements and contribution payments would be an important step. The scope of measures presented to increase geographical mobility is narrow.
21. The implementation of measures investing in human capital has started and a number of further measures are announced. The modular revision of the qualification register has been completed and the integration of vocational schools has begun. Training programmes combined with income support for people lacking basic education are in progress. However, the recently announced education reform does not pay adequate attention to qualitative aspects. Efforts to tackle segregation and to provide pupils with skills responding to labour market needs, including by increasing the number of science and technology graduates, are still missing. A lifelong learning strategy has been put in place. Implementation of this strategy has yet to begin.
22. Overall, while there have been important steps taken in some aspects of employment policy, stronger action is required to: improve the labour market situation of the disadvantaged; in particular the Roma; tackle regional disparities; transform undeclared work into formal employment; strengthen incentives to work; and to upgrade the skills of the current and future workforce.

PART III CONCLUSIONS

23. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
24. Hungary has made limited progress in the implementation of its National Reform Programme. However, it should be noted that in October 2006 Hungary submitted a revised National Reform Programme. After major budgetary slippages, the government has had to significantly review its fiscal adjustment path. Some reforms have been implemented in both the employment and micro-economic policy areas.

But much more remains to be done in those fields as well as in improving macro-economic stability. Limited progress has been made towards meeting the commitments made at the 2006 Spring European Council.

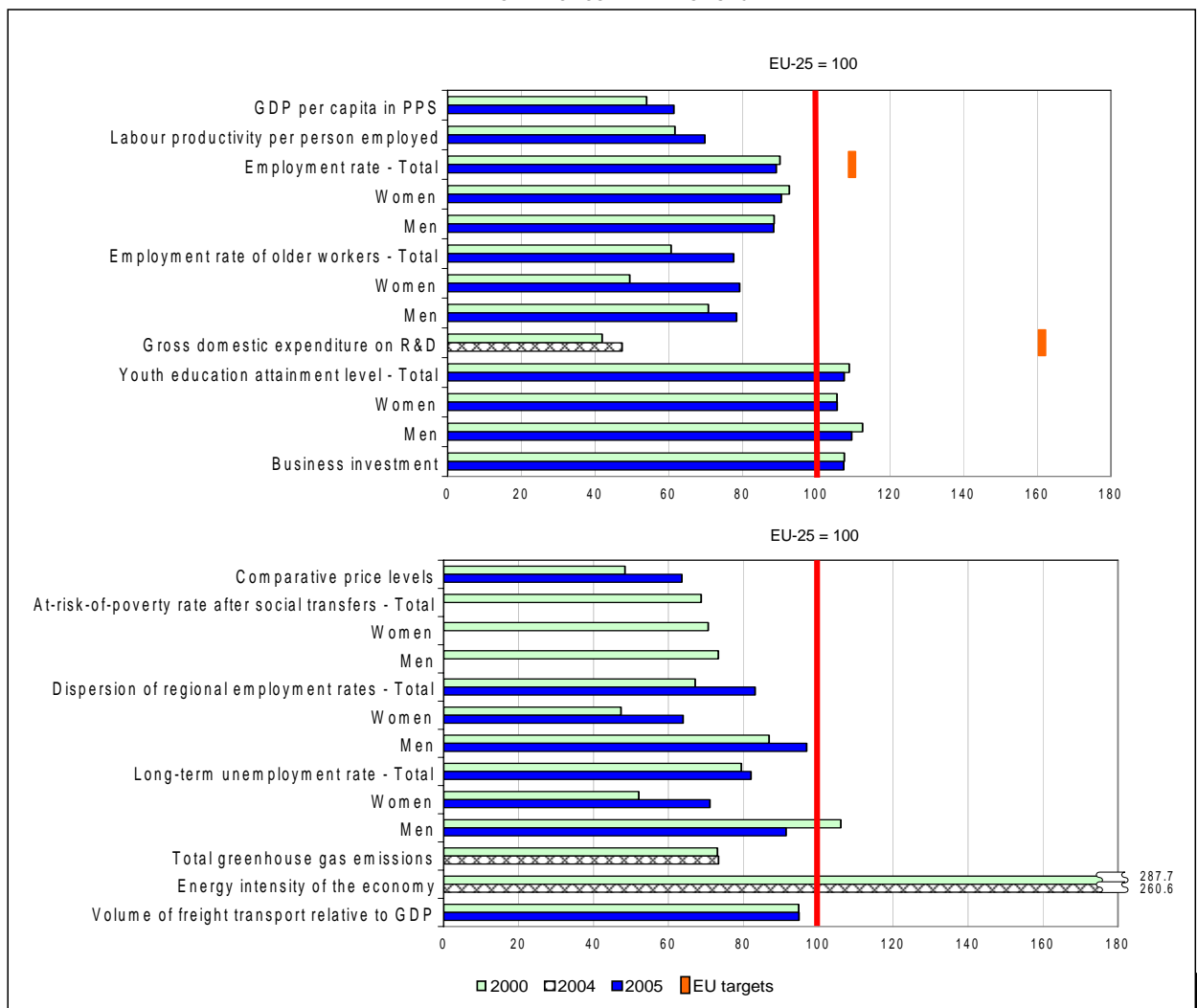
25. Among the strengths of the National Reform Programme and its implementation are: recently adopted corrective measures, including both revenue increases and expenditure cuts, aiming to reduce the deficit; the reform of the unemployment benefit system; initial steps towards the integration of the employment and social services systems; and the lifting of restrictions to market entry in certain areas, in particular the retail pharmaceutical sector.
26. The policy areas in the Hungarian National Reform Programme where weaknesses need to be tackled with the highest priority are: implementing the planned budgetary consolidation strategy and laying the foundations for the long-term sustainability of public finances, currently at high-risk; reinforcing active labour market policies; increasing incentives to work; improving the quality of education and training and making it more responsive to labour market needs. Against this background, it is recommended that Hungary:
 - continue to implement the necessary measures to ensure a credible reduction of the government deficit and of gross debt ratios, with increased reliance on the expenditure side, including through the establishment of more thorough and comprehensive expenditure rules;
 - reform the public administration, health care, pension and education systems with a view to ensuring long-term fiscal sustainability and improve economic efficiency. This should include steps to further limit early retirement, reduce the number of new recipients of disability pensions and further restructure health care;
 - reinforce active labour market policies, introduce further incentives to work and to remain on the labour market and complete the establishment of an integrated employment and social services system;
 - increase access to and responsiveness of education and training systems to labour market needs, including through the provision of a sufficient number of technology and science graduates.
27. In addition, it will be important for Hungary over the period of the National Reform Programme to focus on: reform of the public research system; reducing and redirecting state aids; developing a more coherent strategy for R&D, innovation and ICT; further reductions of the administrative burden on enterprises; improving the labour market situation of the disadvantaged; transforming undeclared work into formal employment; reducing persistent regional disparities in employment; and developing a lifelong learning strategy.

PART IV: STATISTICAL GRAPHS AND DATA

HUNGARY

	HU							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	54.0	56.9	59.1	60.1	60.9	61.4		100.0	100.0	100.0	
Labour productivity per person employed	61.7	65.4	67.7	67.8	69.0	69.8		100.0	100.0	100.0	
Employment rate							58.7				70.0
Total	56.3	56.2	56.2	57.0	56.8	56.9		62.4	63.3	63.8	
Women	49.7	49.8	49.8	50.9	50.7	51.0		53.6	55.7	56.3	
Men	63.1	62.9	62.9	63.5	63.1	63.1		71.2	70.9	71.3	
Employment rate of older workers											
Total	22.2	23.5	25.6	28.9	31.1	33.0		36.6	41.0	42.5	
Women	13.3	14.9	17.6	21.8	25.0	26.7		26.9	31.7	33.7	
Men	33.2	34.1	35.5	37.8	38.4	40.6		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.78	0.92	1.00	0.93	0.88	0.94	1.8	1.86e	1.86e		3.0
Youth education attainment level											
Total	83.5	84.7	85.9	84.7b	83.5	83.4		76.6	77.1	77.5	
Women	84.0	85.0	86.3	86.1b	84.9	84.9		79.5	80.1	80.3	
Men	83.0	84.5	85.5	83.4b	82.0	81.9		73.7	74.2	74.7	
Comparative price levels	48.4	52.0	56.9	59.0	61.9p	63.6p		100.0	100.0p	100.0p	
Business investment	19.7	19.2	18.0	18.5	18.8	18.7		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	11.0	11.0	10.0	12.0	:	:		16.0e	16.0e	:	
Women	12.0	12.0	10.0	12.0	:	:		17.0e	17.0e	:	
Men	11.0	11.0	9.0	12.0	:	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	9.0	8.8	9.4	8.5	9.4	9.9		13.4	12.2	11.9	
Women	9.7	9.2	9.8	9.2	10.6	10.8		20.5	17.3	16.9	
Men	8.6	8.7	9.1	8.1	8.6	9.4		9.9	10.2	9.7	
Long-term unemployment rate											
Total	3.1	2.6	2.5	2.4	2.7	3.2		3.9	4.1	3.9	
Women	2.5	2.1	2.2	2.3	2.6	3.2		4.8	4.7	4.5	
Men	3.5	3.0	2.8	2.5	2.8	3.2		3.3	3.6	3.5	
Total greenhouse gas emissions	66.3	68.5	66.1	68.1	68.0	:		90.7	92.7	:	
Energy intensity of the economy	600.5	588.6	579.6	566.6	534.1	:		208.8	204.9	:	
Volume of freight transport relative to GDP	94.9	89.2	85.0	82.9	89.1	99.3		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Malta

Assessment of National Reform Programme

1. Following strong real economic growth averaging 4.5% during the second half of the 1990's, the Maltese economy almost stalled during 2001-2005, reflecting intensive industrial restructuring, unfavourable cyclical developments and deteriorating international competitiveness. For 2006, GDP is expected to grow by 2.3%. Labour productivity growth has been well below the EU average during the past five years but this gap is projected to close in 2006. Since 2001, GDP per capita has declined in comparison to the rest of the EU and is expected to amount to 68.7% of the EU average in 2006. Malta's employment rate is estimated at around 53.8% in 2006.
2. The structural nature of Malta's recent weak economic performance necessitates appropriate reforms to unleash its long-term growth potential. Implementing structural expenditure reforms would contribute to sound public finances in the medium-term and help release more public funds for growth-enhancing spending such as R&D, human capital and innovation. Combining efforts to reform health care and pension reform with a comprehensive review of the tax-benefit system could simultaneously facilitate moves into regular employment and improve the long-term sustainability of public finances. Growth and employment would benefit from stepping up action to improve the business environment, reducing and redirecting state aid towards horizontal objectives and strengthening competition in sectors such as professional services.

PART I: GENERAL ASSESSMENT

3. As key challenges, the Maltese 2005-2008 National Reform Programme (NRP) identified the sustainability of public finances, competitiveness, the environment, employment and education and training. Fiscal sustainability is to be achieved by reducing public sector expenditure and fostering economic growth. Priorities to address this challenge include ensuring the sustainability of pension and health care systems and reviewing the tax framework. Competitiveness and environment challenges cover the business environment, better regulation, R&D, innovation and ICT, tourism and infrastructure and competition. Increasing the employment rate, particularly for women and older workers, is the employment challenge, while improving on the current situation is the challenge in education and training. In its 2006 Annual Progress Report (APR), the Commission agreed with this assessment but considered that further attention should be paid to competition, the quality of the regulatory system, and making work more attractive by comprehensively reviewing the tax and benefit system and reducing the tax burden on labour.
4. Malta is making good progress overall in implementing its NRP in most key areas. It is on the right track concerning the sustainability of public finances and implementing significant measures in the environmental and education and training areas. More modest progress has been made in the business environment and on R&D and innovation. However, in policy areas requiring further attention according to the Commission's 2006 APR - competition issues and measures to make work

more attractive – progress has been limited. Plans to further liberalise key sectors should be considered, as should the reduction of state aids and their redirection towards horizontal objectives with an emphasis on R&D. Employment rates are far below the EU average, especially for women and older workers; measures taken so far are insufficient to attract people to the labour market. Importantly, in October 2006 the government announced a tax reform aimed at reducing the tax-burden on labour.

5. Malta is partly responding to the commitments made by the 2006 Spring European Council; for example, good progress has been made on entrepreneurship education. However, more concrete steps are needed to fully meet commitments in the area of improving the business environment.
6. Malta's NRP involved extensive consultation with stakeholders. This practice continues. All relevant ministries are involved. The Implementation Report makes appropriate reference to the use of Structural Funds. Consistency of the National Strategic Reference Framework 2007-2013 with reforms under the Lisbon Growth and Jobs Strategy seems guaranteed. The share of spending earmarked for Growth and jobs objectives is likely to increase substantially. Cohesion Policy funding will amount to 2.4% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The challenge of sustainable public finances identified in the NRP and endorsed by the APR is broadly addressed by Malta in its Implementation Report. Implementation of all twelve measures falling directly under the macro-economic area has been fairly satisfactory, though progress varies between measures. In the more significant examples, such as reform of the pension system, draft legislation has been submitted to Parliament for discussion. However, implementation of measures on health care reform spelled out in the NRP is delayed and seems insufficient to reverse past spending trends. Yet long-term sustainability depends on reversing those trends. Finally, the Implementation Report underlines a number of strategic options for tax reform, subsequently developed in the 2007 budget document, aimed at fostering economic growth. In the one case where the budgetary cost is quantified (reducing public sector employment), the information given refers only to 2005 and 2006.
8. According to the most recent information, the Maltese authorities' budgetary objectives - reduction of the general government deficit below 3% of GDP by 2006 and a satisfactory reduction of the gross debt ratio are being achieved. Provided that the measures announced by the Maltese authorities are rigorously implemented, Malta appears on track to meet its budgetary targets. The pursuit of further fiscal consolidation together with the implementation of reforms strengthening the economy's export capabilities would reduce the current account imbalance to more sustainable levels.

9. Apart from helping ensure a sound budgetary position, redirecting public expenditure towards growth-enhancing spending – such as R&D, human capital and innovation - could also help unleash Malta's growth potential.

Micro-economic policies

10. Competitiveness and environment were identified as key micro-economic challenges in the Maltese NRP. The competitiveness challenge includes business environment and better regulation; R&D, innovation and ICT; tourism; and infrastructure and competition.
11. The business environment is improving. The emphasis on SMEs is welcome, but measures put in place focus primarily on financial aspects. Malta also needs to do more to reduce the administrative burden for SMEs. More concrete steps concerning one-stop shops are needed. The creation of the Better Regulation Unit in 2005 to control unnecessary administrative burdens is very welcome, but there is as yet no practice of systematic impact assessment and progress towards simplification remains slow.
12. There has been some progress with R&D and innovation and ICT. The revised "National Strategic Plan for Research & Innovation, 2007-2010" reflects growing recognition of the importance of R&D and innovation for shaping the economy, although the process is still young. The plan sets Malta's overall national R&D intensity target (0.75% of GDP in 2010), although there seem to be problems in data collection and measuring progress - in a recent data revision, the R&D intensity rose from 0.016% of GDP to 0.64% of GDP in 2004, but it is unclear whether expenditure data relate only to R&D or to innovation as well. The strategy gives the government a stronger role in facilitating the necessary changes, launches a fund to identify and support platforms of strategic importance and initiates some university reforms. However, an innovation strategy which aims to integrate existing innovation measures and create the conditions for a broader based innovation performance across the entrepreneurial system is still in the design phase. Specific measures proposed in the NRP are limited to the enhancement of existing tax incentives for R&D investment and to a loan guarantee scheme to support innovative start-ups. The government is making progress with setting up of a National ICT Framework aiming to provide a favourable environment for ICT companies. The Framework promotes ICT skills positively, but lacks details on online public services.
13. Progress in improving Malta's infrastructure is reported; plans for expanding port infrastructure are to be completed by end of 2006. Although Malta is considering connection to Europe's energy networks, further efforts are needed in this regard. This would increase competition, an issue highlighted for further attention in the Commission's APR. Competition is being improved – for example, yacht marinas will start to be privatised at the end of 2008, and the liberalisation of imported oil products is being initiated. In sectors such as distribution, transport and construction, on the other hand, where liberalisation of entry was announced in the NRP, the Implementation Report provides no information on specific measures. And despite the fact that professional services are heavily regulated, there is no indication of reform. Given existing competition issues in some sectors, Malta should strengthen its competition authority. It is to be hoped that a programme for immunity from and reduction of fines (leniency) for firms revealing cartels will soon be adopted and

made operational. Accelerating the reduction of overall and sectoral state aids is necessary, as is the redirection of state aids towards horizontal objectives in particular R&D.

14. The environment is high on Malta's reform agenda, accounting for 65% of expenditure envisaged by the NRP. Good progress is reported on "greening" public procurement and implementing measures for sewage treatment. New plans and strategies are under development, including an Environmental Technologies Action Plan, a Biodiversity Strategy in 2008 and a package of environmental economic instruments. Progress will depend on proper implementation. The Maltese government has recently launched its first renewable energy policy and has also introduced one-off grants for the purchase of energy efficiency products for domestic use; however, further efforts are needed. The environment plays an important role in the competitiveness of the tourism sector, a priority sector for the NRP. A new Strategic Plan (completed in 2006) is a welcome measure to ensure the effectiveness of intervention. Adequate progress will depend on its proper implementation.
15. Overall, Malta has made good progress implementing measures to tackle its micro-economic key challenges. However, more could be done to enhance the regulatory framework and stimulate competition – including by liberalising professional services and further reducing state aid and redirecting it towards horizontal objectives – so as to boost growth and employment.

Employment policies

16. Employment and education were considered as key priorities by the Maltese NRP. Malta has made limited progress increasing its low overall employment rate and more measures are needed, in particular regarding the employment rate for women and older workers. Recently, reform measures have been taken and the employment rate for women went up in 2005, although it is still very low at 34%. The adoption of fiscal measures aimed at helping women return to work, encouraging part-time work, recognising married female workers within small family businesses and encouraging the use of childcare services, should help to improve the situation. However, without further reform the target for a female activity rate of 40% by 2010 looks very unlikely to be reached. Promising initial results are visible in reducing long-term unemployment, but too little attention is paid to disadvantaged categories such as immigrants and people with disabilities. Some training activities have been launched to foster access to the labour market for the young, older people and the low skilled. The employment rate of older people remains very low (around 30%) compared to the EU average and decreased in 2005. To tackle this issue, specific training schemes targeted at older workers are being introduced; however there is a strong need to intensify these.
17. Efforts to adapt the tax and benefit system to make work more attractive and curb undeclared work should be intensified with a view to increasing labour supply. The tax reform announced includes the revision of tax bands, which should alleviate the tax burden, as well as changes in the calculation system for social security contributions for part-time workers. However, not enough is being done on the benefit side. Tackling the widespread phenomenon of undeclared work would help improve the sustainability of public finances and impact positively on employment

rates, especially female employment. The government has paid some attention to this problem and taken some initiatives to reduce social benefit fraud.

18. The government has started restructuring and downsizing the public administration to shift people from the public to the private sector. Although recent data suggest that the private labour market is absorbing the newly unemployed from the public sector, there is no tangible impact in terms of employment growth.
19. Education remains a top priority, considering that the overall level of education of the Maltese population is still low relative to many other EU Member States. Government priorities include establishing a new regulatory framework for education, creating a Higher Education Directorate, establishing technology learning centres, improving guidance services, and reinforcing educational certification systems. The government has also set out a strategy to develop entrepreneurial skills. Other specific measures target early school leaving, preventing social exclusion and lifelong learning. Notable success has been achieved, with more young people choosing to continue their education beyond the compulsory age and attending IT-related courses. Nevertheless, the rate of early school leavers is still too high and the number of students attending higher or further education needs increasing.
20. Further reform of education and training systems is necessary to further raise the population's low average level of qualifications, to reduce early school leaving and to increase staying-on rates for further and higher education. The government has taken important and appropriate measures to tackle these issues, but results are still insufficient. More incisive fiscal policy aimed at making work more attractive is important, accompanied by pension reform. Further efforts to increase labour market participation, especially by women, are needed. Considering the size of the problem and its impact on the economy, undeclared work should be tackled more seriously.

PART III CONCLUSIONS

21. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
22. Malta is making good progress in the implementation of its National Reform Programme. It also addresses most of the commitments made by the 2006 Spring European Council. Implementation is advancing strongly in the area of fiscal sustainability, considered by the authorities to be a crucial element for achieving more growth and jobs and adopting the euro. The implementation efforts in the micro-economic and employment area are more moderate.
23. Among the strengths of the Maltese National Reform Programme and its implementation are: the ongoing development of essential R&D and innovation strategies; a new scheme to foster entrepreneurial skills; and a promising set of comprehensive initiatives in the field of training.
24. The policy areas in the National Reform Programme where weaknesses need to be tackled with the highest priority are: improving competition in several sectors, including professional services; reduction and redirection of state aids; and boosting

investment in R&D; and improve labour supply. Against this background, it is recommended that Malta:

- take further measures, including reinforcing the competition authority, to strengthen competition, notably in professional services; reduce state aids and redirect them towards horizontal objectives, especially R&D;
- step up efforts to attract more people into the labour market, particularly women, intensify efforts to tackle undeclared work and implement changes to the tax and benefit system to make working more attractive.

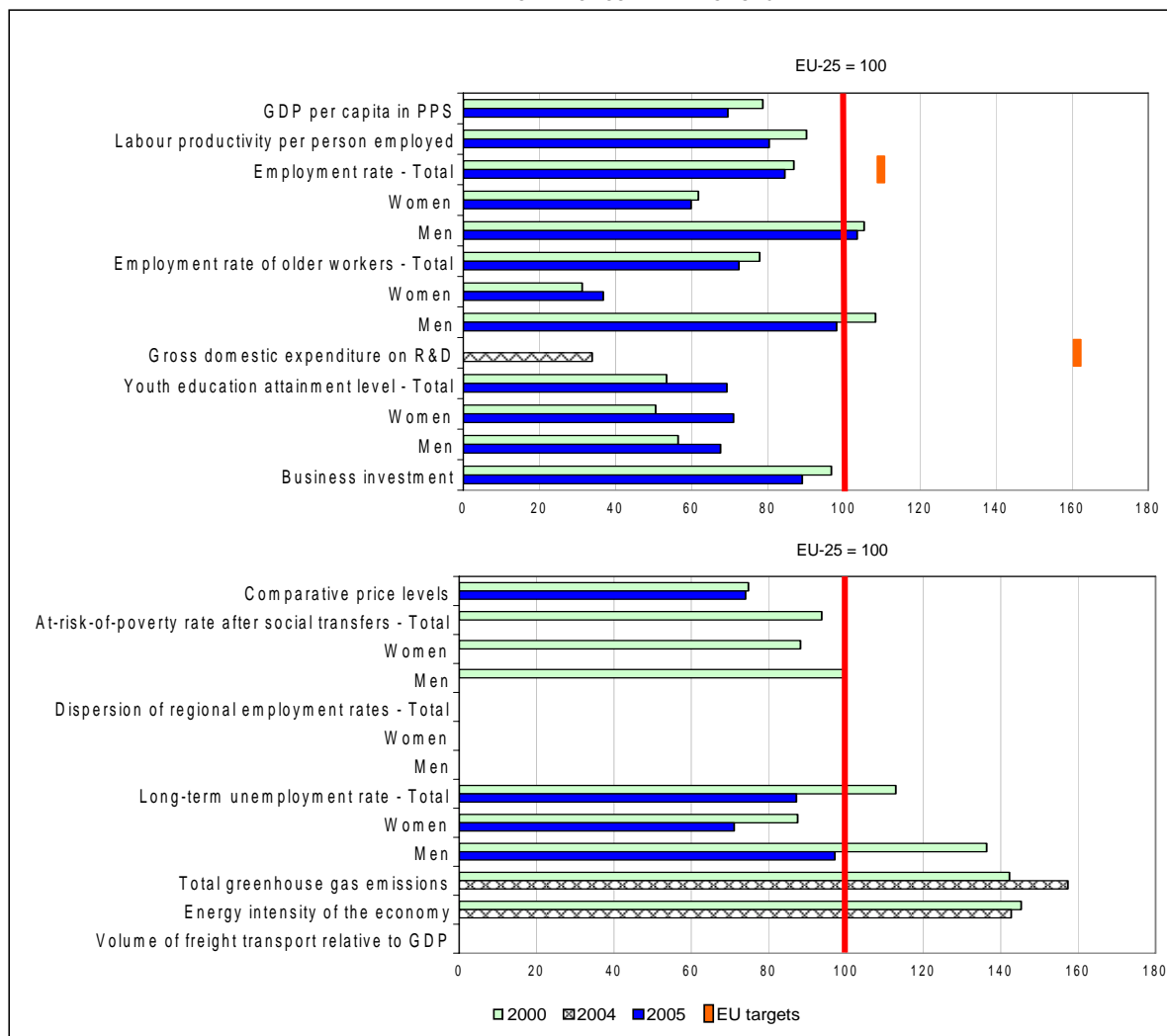
25. In addition, it will be important for Malta over the period of the National Reform Programme to focus on: implementing and reinforcing delayed measures on health care reform; introducing systematic impact assessment and speeding up progress towards simplification of regulations; measuring R&D expenditure more accurately; connecting Malta to Europe's energy networks; building on results achieved in raising educational attainment and reducing early school leaving; and increasing the employment rate of older workers, in which using early retirement schemes to downsize the public sector should be avoided.

PART IV: STATISTICAL GRAPHS AND DATA

MALTA

	MT							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	78.7	74.6	75.6	73.7	70.2	69.5		100.0	100.0	100.0	
Labour productivity per person employed	90.2	85.5	86.9	84.4	81.7	80.4		100.0	100.0	100.0	
Employment rate							57.0				70.0
Total	54.2	54.3	54.4	54.2	54.0	53.9		62.4	63.3	63.8	
Women	33.1	32.1	33.9	33.6	32.7	33.7		53.6	55.7	56.3	
Men	75.0	76.2	74.7	74.5	75.1	73.8		71.2	70.9	71.3	
Employment rate of older workers											
Total	28.5	29.4	30.1	32.5	31.5	30.8		36.6	41.0	42.5	
Women	8.4	10.2	10.9	13.0	11.5	12.4		26.9	31.7	33.7	
Men	50.8	50.4	50.8	53.8	53.4	50.8		46.9	50.7	51.8	
Gross domestic expenditure on R&D	:	:	0.26	0.26	0.63b	:	0.75	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	40.9	40.1	39.0	45.1b	51.0	53.7		76.6	77.1	77.5	
Women	40.2	38.7	42.2	48.8b	52.4	57.0		79.5	80.1	80.3	
Men	41.6	41.4	36.1	41.3b	49.8	50.5		73.7	74.2	74.7	
Comparative price levels	74.8	75.5	73.7	74.4	74.9p	74.0p		100.0	100.0p	100.0p	
Business investment	17.7	15.4	11.0	14.6	17.9	15.5		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	15.0	:	:	:	:	:		16.0e	16.0e	:	
Women	15.0	:	:	:	:	:		17.0e	17.0e	:	
Men	15.0	:	:	:	:	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	-	-	-	-	-	-	-	13.4	12.2	11.9	
Women	-	-	-	-	-	-	-	20.5	17.3	16.9	
Men	-	-	-	-	-	-	-	9.9	10.2	9.7	
Long-term unemployment rate											
Total	4.4	3.7	3.3	3.2	3.4	3.4		3.9	4.1	3.9	
Women	4.2	2.7	2.4	2.4	3.0	3.2		4.8	4.7	4.5	
Men	4.5	3.9	3.5	3.4	3.7	3.4		3.3	3.6	3.5	
Total greenhouse gas emissions	129.0	118.4	139.8	140.1	145.9	:		90.7	92.7	:	
Energy intensity of the economy	303.2	266.6	263.9	284.2	292.4	:		208.8	204.9	:	
Volume of freight transport relative to GDP	:	:	:	:	:	:		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



The Netherlands

Assessment of National Reform Programme

1. After a booming period in 1996-2000 when real annual GDP growth averaged 4%, GDP growth in the Netherlands came to a near standstill in 2002. The subsequent recovery started slowly and was somewhat uneven until early 2005, but has gathered pace since then. GDP per capita stands at 125% of the EU average in 2006. Labour productivity growth has exceeded the euro area average by around half a percentage point over the past decade. Unemployment is expected to be around 4% in 2006. The overall employment rate is projected to improve to 74.4% in 2006 and continue to exceed the overall target for the EU (70%). The share of part-time employment in the overall employment rate is high in comparison to other Member States.
2. The key challenge facing the Dutch economy is to further reduce the underutilisation of available labour resources, by increasing the low average number of hours worked and increasing the participation of older workers and minorities. The current strong labour demand against the background of already relatively low unemployment underscores the need to further increase labour participation in order to ensure sustainable economic growth in the medium-term. Increased labour utilisation would also contribute to the sustainability of public finances in the light of population ageing. Increased investment in R&D could also raise the potential growth of the Dutch economy and thus also have a positive effect on financial sustainability.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified the following key challenges: 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. The Commission shared the analysis of the main priorities, but considered its 2006 Annual Progress Report (APR) that further attention should be given to increasing the number of hours worked by part-time workers and the integration of minorities into employment.
4. The 2006 Dutch Implementation Report includes additional policy initiatives aimed at addressing these two issues. These will need to be vigorously implemented and supplemented if they are to fully achieve their aims. The Netherlands is making good progress in implementing measures on: reforming pensions, health insurance and disability schemes; further reducing the administrative burden for businesses, where the Netherlands is already an example of good practice; stimulating innovation; increasing the use of ICT by business and public administration; strengthening the position of consumers; increasing competition; reforming public procurement; improving environmental protection; energy liberalisation; increasing the employment rate of older workers; tackling youth unemployment; and further reinforcing education, training and lifelong learning. Meanwhile the budget deficit has now been successfully curbed. Initial progress has been made on implementing measures to: widen access to entrepreneurship education; increase the extent and effectiveness of active labour market policies; increase the number of hours worked

by part-time workers, including by improving access to and the affordability of childcare; and raise the employment rate of minorities. Progress towards the ambitious R&D target of 3% of GDP by 2010 has been rather limited.

6. The Netherlands is reinforcing its NRP to respond to the commitments made by the 2006 Spring European Council, for example by taking measures to reduce costs for national patents, provide one-stop shops for business start-ups and to increase energy efficiency. However, further steps will be needed to fully meet some of those commitments, such as creating a single public administration point for the recruitment of the first employee.
7. In order to strengthen the governance of the Lisbon Strategy for Growth and Jobs the government involved regional and local authorities in drafting the Implementation Report. Social partners and stakeholders in the environmental area were consulted. The views of a large number of stakeholders are taken into account in the preparation and implementation of the NRP. Moreover, stakeholders are offered the opportunity to submit to the European Commission, alongside the NRP and the Implementation Report, separate, independent contributions. The Implementation Report was discussed in the Parliament. The Dutch National Strategic Reference Framework for the investment of EU Structural Funds was established in line with the NRP objectives. The Implementation Report is also closely linked to the National Strategy Report on Social Protection and Social Inclusion.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The Implementation Report reiterates the challenges set in the NRP in four broad macro-economic policy areas: promoting macro-economic stability; maintaining a sustainable budgetary position; improving coherence between macroeconomic, structural, and employment policies; and ensuring employment-friendly wage developments.
9. The Implementation Report does not set out new macro-economic measures. The budget deficit was curbed from 3.1% GDP in 2003 to 0.3% GDP in 2005. The implementation of the new surveillance scheme to help ensure the appropriate conduct of pension funds is planned to come into effect as of 1 January 2007. New health insurance and disability schemes have been implemented and a law to lower corporate taxes has been adopted. The substantial costs associated with population ageing are correctly identified in the Implementation Report. The relatively high structural primary surplus contributes to easing the projected long-term budgetary impact of this ageing process, but is not sufficient to fully cover these costs. The Implementation Report does not set out specific measures to further improve the sustainability of public finances. The Implementation Report points towards continued wage restraint. However there is a risk of significantly stronger than anticipated wage growth in the coming years given strong economic growth prospects, the rapidly tightening labour market and the fact that no agreements with social partners are currently foreseen. Further increases in household indebtedness may have an effect on medium-term growth prospects.

10. Generally, the policies outlined in the Implementation Report appear sufficient to further improve the macro-economic situation and are progressing as planned. However, as strong growth and a tightening labour market are likely to put pressure on wages, the Dutch competitive position risks deteriorating. In addition, there remains a risk to the sustainability of public finances.

Micro-economic policies

11. Improving labour productivity growth by boosting innovation and R&D is one of the key challenges addressed in the Implementation Report. In addition, there is a range of measures to improve the business climate and to strengthen competition.
12. The government has committed itself to the R&D expenditure target of 3% of GDP in 2010. The public R&D budget for the forthcoming years is, while increased relative to the current position, not yet at the level required to fully meet the public expenditure part of this target (1% of GDP). However, the greater challenge is to stimulate more private investment in R&D, which would need to rise from 1.03% of GDP to 2% of GDP by 2010 to meet its share of the target. Increases in and better targeting of public support, combined with incentives and more efficient markets, will have a positive effect on private R&D expenditure but efforts will need to be intensified over the next few years if the target is indeed to be met. The Implementation Report announces measures to augment the numbers of researchers. These measures include attracting more foreign researchers and encouraging young researchers to participate in creative PhD programmes and to acquire work experience in research institutions.
13. There is good progress on implementing measures to stimulate innovation. The scheme for innovation vouchers, innovation performance contracts (IPC), and the "Small Business Innovation Research" programme, encourage companies (especially SMEs) to innovate by using external knowledge. The Implementation Report provides detailed budgetary information for sector-specific policies and incentives for the development of clusters, noting as well the importance of international cooperation in this field. These measures are effective in fostering innovation. Measures to increase the use of national patents, especially by SMEs, are under consideration. The Implementation Report also announces an action plan to strengthen the role of the government as "launching customer". Other initiatives concentrate on the take-up of ICT, especially by SMEs and the public administration.
14. There are new initiatives to improve the business climate, complementing ambitious policies in place. Initiatives to promote balanced regulation and the empowerment of consumers, such as the proposal to create a Consumer Authority, aim at creating a level-playing field between business and consumers. The revised Competition Act will allow the Dutch Competition Authority to impose fines on managers and structural measures (splitting of companies, selling departments) on enterprises. The Commission supports measures such as this that increase the detection and deterrence of cartels. Public procurement legislation has been simplified and the Dutch and EU requirements harmonized. There has been good progress with the reduction of the deficit in transposing EU legislation into national law. New energy legislation sets the conditions for further ownership unbundling of energy companies, in other words separating the distribution activities from other commercial activities

to ensure fair competition. This unbundling will come into force in circumstances where public independent network management is at risk.

15. The functionality of the one-stop-shop (*Bedrijvenloket*) website for businesses should be widened to allow interaction and transaction between the entrepreneur and public administration. The Implementation Report does not provide information on progress with regard to the creation of a single public administration point for the recruitment of the first employee. The Dutch pilot projects on entrepreneurship education are welcome. The Netherlands would benefit, however, from including entrepreneurship education permanently in the curricula of secondary and higher education. The Netherlands is a front-runner in the area of Better Regulation. The Dutch "Standard Cost Model" has inspired several other Member States to develop policies along similar lines. The Netherlands seems to be on track to reach its target set for the reduction of administrative costs (25% by 2007). The impact assessment system ("business effects test") has been improved by a new methodology producing more quantitative data on compliance costs. Measures were adopted to simplify permit procedures and reduce the number of permits by 42% and the number of licensing systems by 22%. A new measure concerns the planned reduction of costs linked to supervision by 25%. The Netherlands does not yet have a formal obligation to consult stakeholders on proposed regulation but this will be considered in early 2007.
16. The 2006 'Future Environment Agenda' proposes among other things the setting up of agreements with industry for the stimulation of eco-innovations. A 500 million euro package of measures, half of it financed from private sources, has been developed for the period 2006-2012, to stimulate cleaner and more sustainable energy production. The 'Task Force on Energy Transition' has presented its action plan, which describes 26 pathways towards a more sustainable energy system in 2050. Each pathway consists of projects and supporting activities in the areas of energy conservation and renewable energy, which the Commission would welcome. Implementation of the Environmental Technology Action Plan (ETAP) has already begun. A new sustainable procurement programme has started in order to meet the targets of 100% sustainable procurement by the national government and 50% by other tiers of government by 2010.

Employment

17. The Implementation Report highlights developments in improving labour supply, which is the principal employment challenge, and on enhancing productivity growth through investment in human capital. Moderate wage development also remains a priority. The significant measures to increase financial incentives to work for social and disability benefit recipients have led to a further decline in their number. An increasing number of municipalities focus their attention on all benefit recipients. A demand driven and tailor-made reintegration policy, combined with effective and full use of the available active labour market policies budget, should further increase outflow, including for the most difficult to help. There is an ongoing exercise to reassess disability benefit recipients who are unemployed, with the aim of helping them to return to the labour market. So far, 20% have found a job eight months after their assessment, but the final results will not be available until early 2008. As from 2007, a "gatekeeper" to check the job seeking activities of those entering the unemployment benefit scheme will be introduced. Successful delivery of these

policies requires monitoring mechanisms and improved cooperation between the municipalities and the agencies which implement active labour market policies

18. The government is implementing policies to lower parents' childcare costs by considerably increasing the government contribution and a new compulsory employers' contribution. This aims to increase the total number of hours worked by women and part-time workers. The national employment target (65% working at least 12 hours weekly by 2010) is far from being reached (54.1%). The new obligation for schools to organise care before and after school also aims to help raise female participation in the labour market. However, despite recent reductions, the marginal tax burden on the second income remains high and might therefore remain a barrier to increasing the number of hours worked.
19. The national interim target for older workers (40% working at least 12 hours weekly by 2007) is likely to be achieved in 2006 (39.7% in 2005). A new target has been set at 45% for 2010. To this end, social partners are committed to increase the participation of older and low-skilled workers in lifelong learning. A job, apprenticeship, or other support is offered within six months to 84% of unemployed youth. New jobs for young people are created via the Task Force on Youth Unemployment which is making good progress in reaching its target (40,000 jobs by 2007). "Operation Youth" (Operatie Jong) aims at an integrated approach for disadvantaged youth. To respond to the call for further efforts to facilitate the integration of minorities into employment, the government and the social partners have agreed various measures aimed at tackling discrimination, offering sufficient training places, and reducing early school leaving, which is particularly high among minority youth. The national employment rate target for minorities has not been renewed.
19. To increase the adaptability of enterprises, the government underlines the importance of continued moderate wage development. References to "flexicurity" in the Implementation Report are limited to underlining the activating role of the social security system. Further changes in employment protection legislation are not expected before the national Social Economic Council's opinion, expected by the end of 2006. The Implementation Report expands and intensifies measures for 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. Substantial measures are being taken to reduce early school leaving, particularly high among minorities, all of which should contribute to reaching the ambitious national target. Significant additional measures on early and pre-school education are envisaged later. To achieve the national target for participation in lifelong learning (20% by 2010) and to tackle the slight decline over recent years (16.6% in 2005 compared to 17.4% in 2003), employers will benefit from tax reductions if their (young) employees obtain a formal qualification.
20. In order to increase labour supply and human capital, the successful implementation of employment policies in the NRP continues to be dependent on strong cooperation, driven by demand from local employers, between government, implementing agencies, municipalities and social partners, and on effective monitoring. Despite positive measures to increase the number of hours worked by part-time workers, additional efforts will be required. The government favours general policies with a high degree of tailoring to individual circumstances, rather than those aiming at

specific groups. The integration of minorities into employment can only be successful if these policies effectively reach out to this group and are combined with appropriate monitoring.

PART III: CONCLUSIONS

21. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
22. The Netherlands is making good progress with the implementation of its National Reform Programme. While there are certain risks in the macro area, notably with regard to potential wage inflation, household indebtedness, and the tightening of the labour market, overall the policy framework is appropriate. Despite only moderate progress on R&D, the Netherlands is generally moving ahead significantly in the micro-economic field. Notwithstanding high headline employment rates for most groups, the picture in the employment field is more mixed. The Netherlands is reinforcing its National Reform Programme to respond to the commitments made by the 2006 Spring European Council but further steps will be needed.
23. Among the strengths of the Dutch National Reform Programme and its implementation are: the measures to boost competition; the application of the Standard Cost Model for measuring administrative burdens and the scheme for innovation vouchers, both of which being widely taken up by other Member States; measures on reforming pensions, health insurance and disability schemes; and reforms aimed at raising educational attainment, expanding lifelong learning and creating better links between education and the labour market.
24. The policy area in the Dutch National Reform Programme where weaknesses need to be tackled with the highest priority is in improving labour supply. Against this background, it is recommended that the Netherlands:

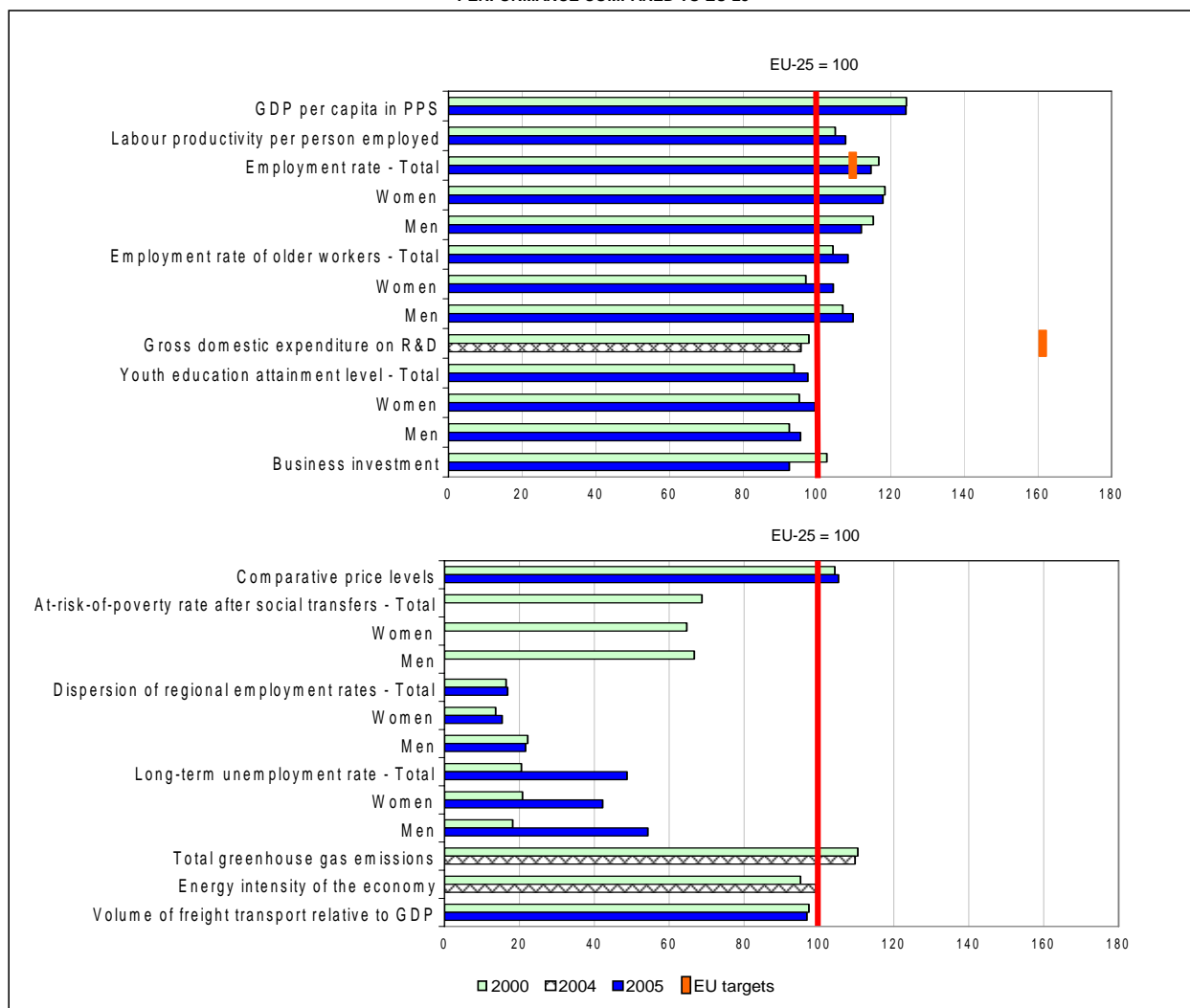
take further measures to improve labour supply, notably of older workers, women and disadvantaged groups.
25. In addition, it will be important for the Netherlands over the period of the National Reform Programme to focus on: measures to increase private sector R&D expenditure; further action to fully meet the commitments agreed by the 2006 Spring European Council. In addition, if existing measures do not over time succeed in significantly raising overall hours worked in the economy, further incentives will need to be considered.

PART IV: STATISTICAL GRAPHS AND DATA

NETHERLANDS

	NL							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	124.3	127.0	125.3	124.7	124.4	124.2		100.0	100.0	100.0	
Labour productivity per person employed	105.0	107.0	105.7	106.2	107.4	107.8		100.0	100.0	100.0	
Employment rate							:				70.0
Total	72.9	74.1	74.4	73.6	73.1	73.2		62.4	63.3	63.8	
Women	63.5	65.2	66.2	66.0	65.8	66.4		53.6	55.7	56.3	
Men	82.1	82.8	82.4	81.1	80.2	79.9		71.2	70.9	71.3	
Employment rate of older workers											
Total	38.2	39.6	42.3	44.3	45.2	46.1		36.6	41.0	42.5	
Women	26.1	28.0	29.9	31.8	33.4	35.2		26.9	31.7	33.7	
Men	50.2	51.1	54.6	56.7	56.9	56.9		46.9	50.7	51.8	
Gross domestic expenditure on R&D	1.82	1.80	1.72	1.76	1.78p		:	1.86e	1.86e		3.0
Youth education attainment level							3.0				3.0
Total	71.9	72.7	73.1	75.0	75.0	75.6		76.6	77.1	77.5	
Women	75.7	76.8	77.4	78.0	78.9	79.9		79.5	80.1	80.3	
Men	68.2	68.7	68.8	72.0	71.2	71.4		73.7	74.2	74.7	
Comparative price levels	104.2	104.0	105.3	106.6	105.2p	105.2p		100.0	100.0p	100.0p	
Business investment	18.8	17.9	16.4	15.9	15.9	16.1		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers							:				:
Total	11.0p	11.0p	11.0p	12.0p				16.0e	16.0e		
Women	11.0p	12.0p	12.0p	12.0p				17.0e	17.0e		
Men	10.0p	11.0p	11.0p	12.0p				15.0e	15.0e		
Dispersion of regional employment rates											
Total	2.2	2.3	2.2	2.3	2.3	2.0		13.4	12.2	11.9	
Women	2.8	3.1	3.0	3.2	2.8	2.6		20.5	17.3	16.9	
Men	2.2	2.2	1.8	2.0	2.1	2.1		9.9	10.2	9.7	
Long-term unemployment rate											
Total	0.8	0.6	0.7	1.0	1.6	1.9		3.9	4.1	3.9	
Women	1.0	0.7	0.9	1.1	1.6	1.9		4.8	4.7	4.5	
Men	0.6	0.5	0.6	1.0	1.5	1.9		3.3	3.6	3.5	
Total greenhouse gas emissions	100.1	100.9	100.3	100.5	101.6			90.7	92.7		
Energy intensity of the economy	198.5	200.7	201.1	202.2	203.2			208.8	204.9		
Volume of freight transport relative to GDP	97.4	94.9	93.1	93.7	102.7	101.3		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Austria

Assessment of National Reform Programme

1. The Austrian economy is forecast to grow by 3.1% in 2006, half a percentage point above the euro area average. Labour productivity growth has also been just above the euro area average. GDP per capita is projected at 122.5% of the EU average in 2006. The employment rate is expected to increase from 68.6% in 2005 to 69.0% in 2006, well above the EU average. The employment rate for older workers increased to 31.8% in 2005 from 28.8% in 2004, but remains one of the lowest in the EU. An end to the upward trend in unemployment is projected, with stabilisation at a rate of 5.1% in 2006. While unemployment is still well below the EU average, it affects in particular young people (10.3%).
2. Austria enjoys a strong economic performance, but its growth potential could be improved by addressing the low employment rate of older workers and promoting competition and productivity particularly in the services sector. Recent reforms to the pension system are helping to consolidate public finances, which together with further reforms of public administration and health care could help free up resources for activities supporting economic growth and labour supply.

PART I: GENERAL ASSESSMENT

3. The Austrian 2005-2008 National Reform Programme (NRP) identified seven strategic priority areas: public finance sustainability, R&D and innovation, infrastructure, international competitiveness, the environment, labour market, and education and training. The Commission agreed with these priority areas but, in its 2006 Annual Progress Report (APR), also considered that further attention should be given to competition in services, the low employment rate of older workers and vocational training of adults.
4. The Implementation Report shows that Austria is making good progress with implementing its NRP. The report addresses most of the concerns identified by the Commission in its APR. Overall, commitments concerning macro and micro-economic and employment policies have largely been met. Progress has been good on: improving international competitiveness and the business environment; increasing public investment in R&D and providing tax incentives for private investment; reinforcing active labour market measures; and making the transition from school to work smoother by modernising the apprenticeship system. There has been initial progress on the promotion of active ageing, though despite an upward trend, the employment rate of older workers remains low. Austria has improved the sustainability of public finances, though further measures will be necessary to meet agreed targets. Competition in services is an area where progress has been rather limited. Vocational training for adults has not been significantly reinforced.
5. Austria's response to the conclusions of the Spring European Council 2006 is adequate overall. A positive development is the creation of a one-stop-shop system to register new businesses. Some initiatives have been launched with respect to creating

a more entrepreneurial culture, but more remains to be done. In the field of knowledge and innovation some progress towards the declared targets has been made. SMEs have been the focus of a number of past policy initiatives, some of which have now been further expanded. Increasing employment opportunities for priority target groups has been given substantial attention. Austria remains committed to increasing the use of renewable energy and has increased its targets for the use of certain energy sources.

6. Governance remains strong. The political visibility of the Strategy for Growth and Jobs has been upgraded by assigning responsibility at ministerial level. Consultation and efforts to develop ownership of the report have been substantial. A wide range of stakeholders was consulted, including the parliament, social partners, regions, municipalities and economic research institutes. The report highlights the contribution of Structural Funds to the NRP and confirms that in the next programming period 2007-2013 around 78% of Structural Funds under the Competitiveness and Employment objective and 60% of Structural Funds under the Convergence objective will be allocated to competitiveness and employment enhancing measures.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The Austrian NRP 2005 identified the sustainability of public finances as the key macro-economic challenge, an analysis shared by the Commission. Thanks to a recent comprehensive reform of the pension system, the long-term sustainability of Austria's public finances is at low risk and if the numbers of older people in employment continues to rise, this will further improve the situation. However, a certain degree of risk remains. The Austrian NRP announced some expenditure cuts but in very general terms.
8. In the Stability Programme that followed the NRP, the authorities presented a plan to reform the law governing adoption of the federal government's budget so as to make public finances more sustainable. The first part of the reform package was to come into force on 1 January 2007. It is important that the new government continues the implementation of the reform measures. The Stability Programme also estimated that the administrative reform mentioned in the NRP would produce savings of about €1.9 billion in the period 2005-2010. This represents about 0.8% of GDP overall, so it is clear that more measures are needed to achieve the government's declared goal of a balanced budget in 2008 and, more generally, over the economic cycle. According to the Implementation Report, the administrative reform is running according to plan, yet the only new measure to be introduced in order to enhance long-term sustainability is the campaign against tax fraud, illegal work and smuggling, to take effect from 1 January 2007. As its impact is not quantified, it is difficult to judge whether it will enhance long-term sustainability.
9. Overall, the macro-economic situation is good but more should be done by the Austrian authorities to present a clear medium-term scenario to move from the 1.2% of GDP budget deficit officially foreseen for 2006 to the declared goal of a balanced budget in 2008.

Micro-economic policies

10. In this area, the NRP identified as key challenges: improvement of the business environment, particularly for SMEs; environmental sustainability; and investment in research and innovation, including in energy efficiency.
11. Important improvements have been made to the business environment and international competitiveness has been enhanced. Reform of the trade code will considerably facilitate start-up procedures, e.g. by creating a one-stop-shop system to register new businesses. The number of regulated trades needing a special qualification has been reduced and bankruptcy procedures have been improved. However, recruiting the first employee is still not easy, and concrete measures are not visible. The general goal of reducing administrative costs to businesses by 25% shows clear commitment to a better regulatory environment. The SME promotion act 2006 (*KMU Förderungsgesetz 2006*) is a potential source of inspiration for other Member States. It includes several measures that reduce SMEs' costs by a total of €1.5 billion (0.6% of GDP). The SME package adopted in 2006 (*Förderpaket für Kleinst- und Kleinbetriebe*) includes measures to facilitate SME access to microcredit, equity and working capital finance. Initiatives have been launched with respect to creating a more entrepreneurial culture, but results are not yet apparent. Various initiatives exist to promote entrepreneurship education. However, given that school leavers' attitudes tend to be less entrepreneurial than is average across the EU, a more systematic follow-up is needed, including regular monitoring of results.
12. The Implementation Report states that the Services Directive is likely to have a positive effect on services in Austria. However, implementation of the Services Directive on its own will not solve all issues regarding the lack of competition in professional services in Austria. A number of national measures have already been introduced which will improve the quality of service and efficiency in some regulated professions, but not necessarily improve competition. Austria still has high levels of regulation of professions and there is no evidence that a substantial reform process is in progress. Austria has improved its performance on the transposition of internal market legislation into national law and is now better than average.
13. Austria remains committed to spending 3% of GDP on R&D in 2010 and has reached in 2006 an estimated level of 2.43% of GDP (compared to the 2.5% set as an intermediate objective). The pace of growth in R&D intensity is slowing down, mainly because business R&D spending remains moderate. Several government initiatives, mainly using tax incentives, have attempted to encourage private R&D (the 'FuE Mittelstandsoffensive' is the latest). Austria attracts significant R&D investment from abroad, although the foreign share in overall finance is declining gradually. The 'Headquarter Strategy' is intended to attract foreign R&D centres and keep them in Austria. In addition, Austria is prioritising the development of international centres of excellence and also aims to build a new university centre of excellence, the Institute of Science and Technology Austria. In innovation policy, a programme to develop lead markets is in preparation and initiatives to use public procurement to promote innovation are envisaged. Austria is also making good progress on a number of other key indicators of innovation, as well as on R&D expenditure, and is now high in the EU innovation rankings.

14. In line with one of its NRP key challenges, over the last year Austria has taken some measures to increase the proportion of renewable energy sources so as to reach the goals set in the Green Electricity Act (Ökostromgesetz). Austria has prioritised energy efficiency improvements but will have to identify further emission reduction policies and measures in order to meet its burden sharing target. Austria reports a substantial investment effort in transport infrastructure, well-balanced among different modes.
15. Austria has continued efforts to deploy e-government services at all levels of government and become the leading member country in this field. Public funding to rollout broadband in rural areas and a comprehensive e-health infrastructure are being put into place.
16. Austria has introduced or expanded a wide range of micro-economic policy measures relating particularly to R&D, improvements in the business environment for SMEs and better regulation. Careful monitoring and evaluation of these measures is needed in order to ensure that they meet their objectives.

Employment policies

17. The NRP focused on attracting people into employment, adaptability issues, promoting active ageing and on "flexicurity", as well as on qualifications and education reforms. The Commission's 2006 APR identified the low employment rate of older workers and vocational training of adults as challenges requiring further attention.
18. To attract and retain more workers in employment, priority has been given to active labour market policy; expenditure on qualification and the creation of new jobs has substantially increased, especially for older people, women and young people. However, measures are not always well targeted to individual needs. To tackle the low employment rate of older workers, the Austrian government has implemented, alongside recent pension reforms, measures to raise awareness and an early intervention strategy. In the context of rising youth unemployment, a number of measures have been carried out, notably the provision to unemployed people under 25 of training or re-integration measures unless they are offered a job within three months, improvements to the apprenticeship system and more apprenticeship places. Nevertheless, an important gap persists, especially for immigrants. To reconcile family and work better, the report announces steps to create additional childcare facilities, but the target set (18,000 additional childcare places, Vienna not included, and the adjustment of opening hours to parents' needs) does not seem ambitious enough, nor is it supported by any concrete implementation plan. A subsidised wage scheme introduced in 2006 aims to stimulate employment in low-wage sectors, targeting younger and older long-term unemployed. However, few employers have made use of the scheme and many of the newly created jobs are part-time.
19. Initiatives related to increasing the adaptability of workers and enterprises include the introduction of a service cheque in 2006 to increase and promote legal employment in household-related services. While the public employment service and some government initiatives are trying to reduce the gender pay gap and break down gender segregation, a stronger commitment from employers is required. "Flexicurity" has been enhanced, among other things by continued use of labour foundations.

Safeguarding adequate levels of security for the rapidly increasing number of employees in atypical forms of employment and preventing segmentation of the labour market into two tiers, with on one hand workers on permanent contracts and on the other those without such a contract and with little prospect of moving into one, will be a challenge.

20. Some measures have been implemented to increase human capital, including early language teaching for immigrant children. However, the linked issues of reducing the high percentage of early school leavers among young immigrants and improving their qualifications need to be further addressed. The low participation in vocational training of less qualified and older workers remains a challenge. Overall, the dispersion of responsibilities for lifelong learning in the governmental structure results in the lack of a coherent and effective approach.
21. Implementation of employment policies is generally progressing well. Substantially increased spending on active labour market measures has had a positive impact, although the effectiveness of some measures could be enhanced even further. Despite some progress, the low employment rate of older workers remains a major challenge requiring further efforts, especially to step up lifelong learning and to reform the tax and benefit system. Some response to rising youth unemployment has been given, but more support for young immigrants is necessary. Finally, further steps are needed to fight gender segregation in the labour market.

PART III CONCLUSIONS

22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
23. Austria is making good progress in the implementation of its National Reform Programme, especially in the micro-economic area, where a substantial range of measures has been implemented across the board except on competition in services. Macro-economic stability is strong, though additional impetus will be necessary to continue addressing risks to the long-term sustainability of public finances. Progress has also been generally good on employment policy, although more needs to be done in some areas. Austria's response to the conclusions of the 2006 Spring European Council is adequate overall.
24. Among the most promising areas of reform undertaken by Austria and which could inspire others are its good record in using renewable energy sources. Another area is Austria's efforts to reduce SMEs' administrative costs.
25. The policy areas in the Austrian National Reform Programme where weaknesses need to be tackled with the highest priority are increasing labour supply from older workers and improving the skills of disadvantaged young people. Against this background Austria is recommended to:
 - improve incentives for older workers to continue working, notably by implementing a comprehensive lifelong learning strategy with a particular focus

on job-related training and reforming tax benefits systems; and enhance the skills and qualifications of vulnerable youth.

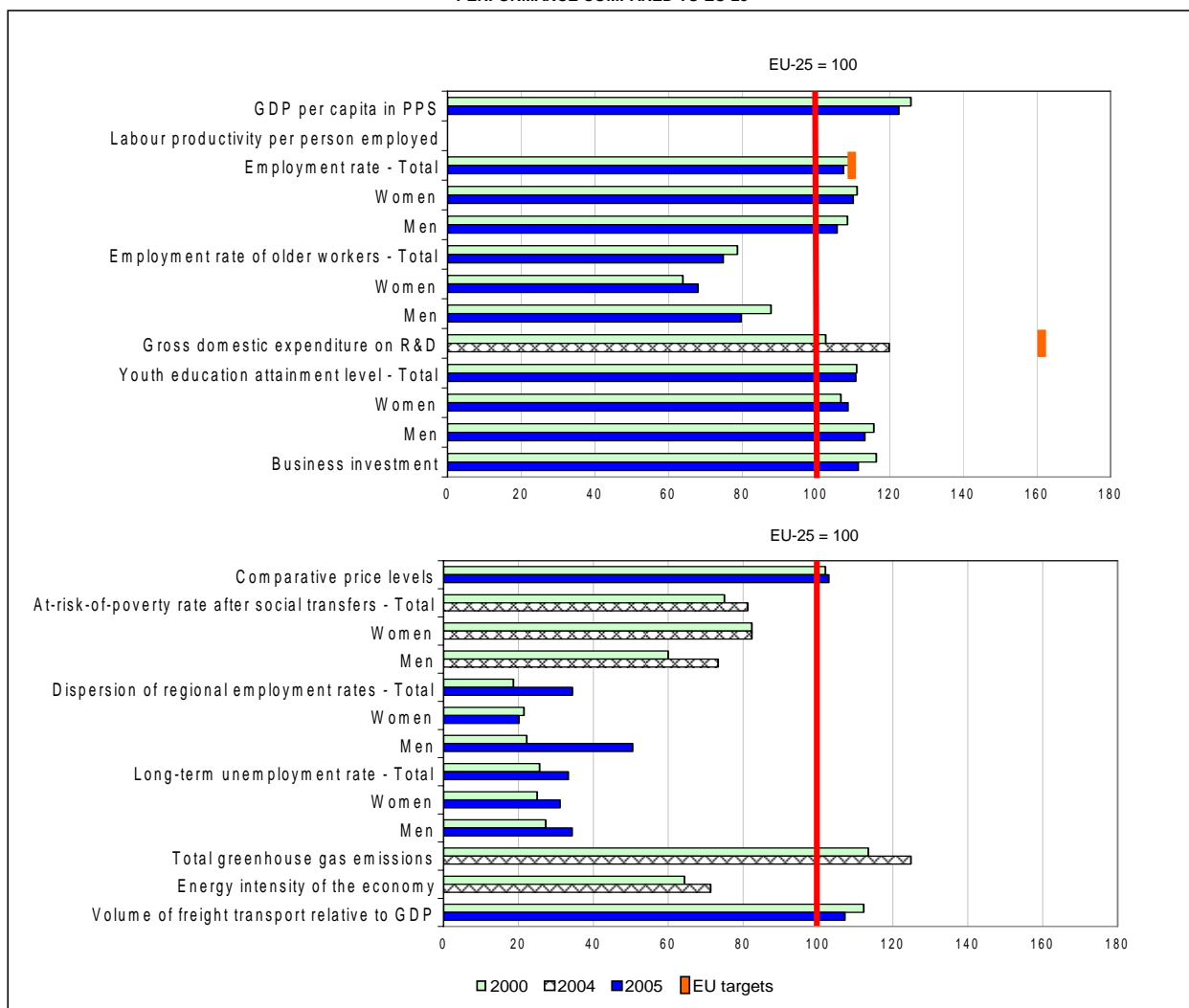
26. In addition, it will be important for Austria over the period of the National Reform Programme to focus on: achieving the target of a balanced budget in 2008; increasing competition in services; strengthening the entrepreneurial culture; identifying further emission reduction policies and measures; and tackling the gender segregation of the labour market, including by improving the availability of childcare.

PART IV: STATISTICAL GRAPHS AND DATA

AUSTRIA

	AT							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	125.8	122.1	120.0	120.3	121.7	122.5		100.0	100.0	100.0	
Labour productivity per person employed	:	:	:	:	:	:		100.0	100.0	100.0	
Employment rate											
Total	68.5	68.5	68.7	68.9	67.8b	68.6	:	62.4	63.3	63.8	70.0
Women	59.6	60.7	61.3	61.6	60.7b	62.0		53.6	55.7	56.3	
Men	77.3	76.4	76.4	76.4	74.9b	75.4		71.2	70.9	71.3	
Employment rate of older workers											
Total	28.8	28.9	29.1	30.3	28.8b	31.8		36.6	41.0	42.5	
Women	17.2	18.4	19.3	20.8	19.3b	22.9		26.9	31.7	33.7	
Men	41.2	40.1	39.6	40.4	38.9b	41.3		46.9	50.7	51.8	
Gross domestic expenditure on R&D	1.91e	2.04e	2.12	2.21e	2.23	2.36e	3.0	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	85.1	85.1	85.3	84.2	85.8b	85.9		76.6	77.1	77.5	
Women	84.9	85.3	84.6	83.4	86.5b	87.3		79.5	80.1	80.3	
Men	85.3	84.9	86.1	85.1	85.1b	84.6		73.7	74.2	74.7	
Comparative price levels	102.0	102.6	105.2	105.7	103.6p	102.9p		100.0	100.0p	100.0p	
Business investment	21.3	20.9	19.2	20.1	19.8	19.4		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	12.0	12.0	:	13.0b	13.0	:		16.0e	16.0e	:	
Women	14.0	14.0	:	14.0b	14.0	:		17.0e	17.0e	:	
Men	9.0	9.0	:	12.0b	11.0	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	2.5	2.6	2.5	2.9	3.5	4.1		13.4	12.2	11.9	
Women	4.4	4.3	3.3	3.8	3.2	3.4		20.5	17.3	16.9	
Men	2.2	2.5	3.7	3.6	3.9	4.9		9.9	10.2	9.7	
Long-term unemployment rate											
Total	1.0	0.9	1.1	1.1	1.3b	1.3		3.9	4.1	3.9	
Women	1.2	1.1	1.2	1.1	1.4b	1.4		4.8	4.7	4.5	
Men	0.9	0.7	1.0	1.1	1.3b	1.2		3.3	3.6	3.5	
Total greenhouse gas emissions	102.9	107.8	110.0	117.2	115.7	:		90.7	92.7	:	
Energy intensity of the economy	134.4	142.8	139.9	149.0	146.1	:		208.8	204.9	:	
Volume of freight transport relative to GDP	112.3	117.1	119.1	118.3	117.5b	112.2		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Poland

Assessment of National Reform Programme

1. In 2006, GDP per capita is expected to reach 51% of the EU average. Between 2001 and 2006, Poland had an annual growth rate of 3.3%. Labour productivity has grown at rates well above the EU average over the last decade and labour market conditions have been improving lately. Despite the recent fall in the unemployment rate, it remains the highest in the EU (projected at almost 15% in 2006, down from 17.7% in 2005) and the employment rate (estimated at more than 54% in 2006) remains the lowest. The government deficit (pension reform costs not included) amounted to 2.5% of GDP in 2005 and is expected to reach 2.2% of GDP in 2006.
2. Poland's growth and jobs performance is constrained by a number of interconnected structural problems, including the low level of labour utilisation, slow progress in economic restructuring, underinvestment and the imbalances in government finances. Economic policy is confronted with a complex challenge of addressing these growth constraints. Removing disincentives to work and reforming the social security system could simultaneously contribute to a stronger performance of the labour market, and improve the sustainability of public finances, which are burdened by high mandatory social expenses.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified the following key challenges: consolidation and better management of public finances; developing entrepreneurship and innovation; infrastructure development; ensuring a competitive environment in network sectors; creating and sustaining jobs and reducing unemployment; and improving the adaptability of workers and enterprises by investing in human capital. In its 2006 Annual Progress Report (APR), the Commission invited Poland to pay further attention to: increasing competition; raising public sector R&D and innovation; developing a comprehensive strategy for investment in infrastructure and environmental protection; a more complete approach to raising employment and addressing regional disparities. Concerns were also expressed over the lack of targets, timetables, budgetary implications and information on monitoring and evaluation in the NRP.
4. The 2006 Implementation Report partially addresses these concerns. A timetable for implementation with expected impacts of the measures proposed together with qualitative and quantitative indicators are now presented. There is more information on the financial resources devoted to these reforms.
5. Poland has made limited progress with the implementation of its NRP. There is progress in implementing measures on redirecting state aid away from a given industry and towards horizontal support; better regulation; measures to improve the business environment (especially for SMEs), and encouraging entrepreneurship. There are encouraging signs of progress on health care reform; removing barriers in professional services; efforts to boost R&D and innovation; and environmental

protection. These measures need to be strengthened and implemented. Progress with fiscal consolidation relies predominantly on positive cyclical developments, while the implementation of expenditure reforms is lagging. Progress has been disappointing on: better budgetary planning and on restraining public expenditure; improving transport infrastructure; energy liberalisation; attracting and retaining more people in employment; improving the adaptability of workers and enterprises; and reforms of education and training.

6. Progress has been limited towards meeting the commitments made at the 2006 Spring European Council, for example on facilitating business start-ups and offering young people leaving education guarantees of employment or training opportunities within six months. Neither has a clear target for R&D investment for 2010 so far been set.
7. Ownership of the reform process has improved but more remains to be done. The Implementation Report was not discussed by Parliament before being finalised. The establishment of an inter-ministerial implementation group is encouraging, as is the decision to strengthen cooperation with social partners, via this group. Cooperation between central, regional and local governments now needs to improve. The Commission welcomes Poland's commitment to devote at least 60% of Structural Funds expenditure towards growth and jobs objectives. Although there is progress, governance of Structural Funds investment needs to be better integrated with that of implementation of the NRP. The new law on public finance will have an important impact on how well Poland is able to absorb the structural and cohesion funding available for 2007-2013. Cohesion Policy funding will amount to 3.4% of GDP in the 2007-2013 period. To enhance communication on Growth and Jobs issues, the government has set up a committee of government, members of the national and European Parliaments, regional and local authorities, business and media. Cooperation between government and the Polish Lisbon Strategy Forum to communicate with a wide range of stakeholders and citizens is encouraging.

PART II: ASSESSMENT BY POLICY AREA

Macroeconomic policies

8. The NRP identified one key challenge in the area of macroeconomic policy: the consolidation and better management of public finances. The Commission supported this choice and recommended preparing a more detailed assessment of the macroeconomic and budgetary impact of reforms.
9. The Implementation Report presents budgetary costs and target indicators. It refers to tax changes endorsed by the government in June 2006, although many of these have not been implemented. Moreover the report presents projections from the January 2006 convergence programme, yet these have been superseded by projections in the draft 2007 budget. Expenditure reforms, especially on social spending, are identified as key for public finances and employment. However, the implementation of these reforms is delayed. Implementation of the key reform linking farmers' contributions to the social security fund (KRUS) with their income is scheduled now for 2008, later than originally planned. Furthermore, it appears that the reform is limited and

will have to be continued after 2008. The projected increase in contributions is only 10%, whereas they cover less than 10% of KRUS expenditure.

10. There is no information provided on progress since September 2005 in the harmonisation of temporary early pensions (“bridge pensions”) for people working in difficult conditions. Implementation is planned for 2007. The government will decide in 2007 on the final shape of reforms in the disability benefit system (linking the level of benefit to the level of pensions in the reformed pension system), with implementation scheduled for 2008. The intention to achieve savings from reforming administration is no longer mentioned. The plan to introduce a basket of guaranteed medical services financed by the state health care fund seems promising, as it is likely to result in better targeting of public spending on health care, but implementation is not expected until after 2007.
11. The four-year nominal state budget deficit anchor of PLN 30 billion, around €7.84 billion, (no more than 3% of GDP in 2005) is not formally adopted by law and may be undermined by plans to increase social expenditure during the current favourable economic cycle. Given optimistic revenue projections, should the business cycle become less favourable, the anchor may not be met (as no sanction would be applied). According to the draft 2007 budget, implementation of multi-annual task-oriented budgetary planning for the whole state budget is scheduled only for 2011, rather than 2009.
12. The approach towards making public finances more sustainable is broad and covers the appropriate areas. Implementation however, remains incomplete. The fiscal regime in Poland has been ‘expenditure-led’ which has entailed adjusting tax revenues to the planned levels of government expenditure. As a result, the general government expenditure to GDP ratio is significantly higher than in other Member States at a comparable level of economic development. The existing national fiscal rules do not appear sufficient to contain the excessive expenditure growth in Poland. Stronger commitment to public finance reform, especially concerning expenditure, and faster implementation is needed.

Microeconomic policies

13. The 2005-2008 NRP identified as key microeconomic challenges: developing entrepreneurship; increased innovation by companies; infrastructure development and upgrading; and ensuring a competitive environment in network sectors. The Commission broadly shared this view, although recommended more emphasis on competition, on reinforcing public sector R&D and innovation, and on developing comprehensive strategies for infrastructure investment and environmental protection.
14. A range of initiatives is being implemented to improve the business environment and develop entrepreneurship. A system to measure administrative costs, and simplification of the tax system, are useful steps. However, the start of a “one-stop-shop” system for the registering of new businesses has been repeatedly postponed. There are no measures mentioned to reduce the time and costs of registration and to facilitate the recruitment of the first employee. A comprehensive ICT strategy and speeding up of governmental ICT projects would help in this area.

15. The adoption of the regulatory reform programme is a major step forward but will require considerable implementation efforts. Since access to finance is a chronic problem for SMEs, steps to improve it are valuable, especially those focused on technology-based start-ups and using the Structural Funds. Poland has made significant efforts to reduce its backlog in transposing EU legislation into national law, but needs to ensure the quality of transposition. The reform of commercial jurisdiction is promising. Promising work to reform the legal profession is underway and similar reforms should be made with respect to other professions. Efforts to reduce the overall level of state aid, and to increase the share of horizontal state-aid are welcome, but further efforts are required to redirect it, in particular towards R&D.
16. Poland has proposed measures to increase R&D and innovation. Law amendments and tax exemptions will help address a lack of business innovation. However, a more comprehensive strategy for attracting foreign direct investment, notably in medium and high-tech industries, is needed. The reform of public procurement rules could now stimulate innovative products and services. Pilot projects on clusters and technology start-ups are valuable and there are plans to introduce them on a much larger scale. The reform of public sector R&D with its extra focus on a limited number of large projects and on the best performing institutions is welcome, but the legislative changes still need to be adopted and implemented. A document on increasing innovation over the 2007-13 period has been drawn up: it will be important to ensure that this leads to a coherent strategic approach and prioritisation of measures, as well as the use of benchmarking and the continuous evaluation of measures. Poland should set a firm and realistic target for overall investment in R&D, given that the target originally set in the NRP is now recognised by the Polish authorities as unattainable.
17. Measures to improve transport infrastructure need to be stepped up and should be coordinated with regulatory measures. The simplification of the administrative processes for investment and a review of spatial planning are still awaited. Improving infrastructure, along with enhancing the broad business environment, should help in attracting much needed foreign direct investments. Market opening in the energy sector and in railways is not progressing sufficiently. Poland should remove obstacles to new competitors in these sectors. However, in telecommunications, recent regulatory decisions in line with EU laws are to be welcomed. The recent regulatory, institutional and other developments related to regulatory supervision in the network and financial sectors raises concerns over the functioning of such regulators and their ability to guarantee competition, and in particular, access to these markets.
18. In the energy markets, emphasis has been put on securing supply and on environmental sustainability. Less attention is devoted to the role of competition in delivering these objectives. In particular, the energy plans assume the creation of four vertically integrated groups incorporating generation, retail and distribution services prior to the unbundling of distribution services. While the commitment to unbundling is welcome, this sequencing could delay it until after the 1 July 2007 deadline and make the process more difficult. There is progress on encouraging environmental reform but this now needs an integrated environmental strategy.

19. The micro-economic measures, implemented or planned, could boost the business environment, innovation, entrepreneurship and infrastructure. The postponement of the implementation of some measures raises concerns that not all the necessary reforms will be completed.

Employment policies

20. Creating and sustaining jobs and reducing unemployment, and improving the adaptability of workers and enterprises by investing in human capital, were among the main employment priorities of the NRP 2005-2008. The Commission subscribed to this choice, but pointed to the need for: an appropriate policy mix to favour employment growth; further reform of the tax and social benefit systems; stronger measures to reduce regional imbalances; and a more effective approach to transform undeclared work into formal employment.
21. The implementation of measures to attract and retain more people in employment is slowly progressing. For the first time since 2001, employment growth has resumed. The government has set targets for 2010 for the employment rate (57%-58%) and the unemployment rate (12%-13%). The 2006 National Action Plan for Employment specifies in more detail reforms announced in the NRP, including timetables and budgetary implications. Expenditure on active labour market policies has increased, but with little focus on skills development (in 2005, only 5.2% of unemployed people received training). Modernisation of the public employment services is underway, but so far with few tangible effects. The low staff-client ratio remains a concern. The government plans to integrate more young people in the labour market through activation programmes, but a clear commitment to deliver specific services is missing. A law aimed at increasing the employability of people with disabilities has been presented to Parliament.
22. Progress on the implementation of measures to improve the adaptability of workers and enterprises is slow. Although Poland has the lowest employment rate of older workers in the EU, and one of the lowest average exit ages from the labour force, early retirement entitlements (initially to be phased out by the end of 2006) have been extended till 31 December 2007. Policies to promote a "flexicurity" approach focus only on one component (promoting flexible forms of employment), underplaying the role of active labour market policies, lifelong learning and social security systems. Increasing flexibility in the retirement age and equalising the retirement age of women and men has been postponed to after 2008. Although the tax-wedge in Poland is one of the EU's highest, plans to reduce charges on the wages of low-wage workers have been discontinued. A study is in progress on undeclared work, but results will be available only by the end of 2007. The government is preparing a draft programme covering access to childcare and women's participation in employment, but no information on its planned implementation is presented. The need to reduce regional disparities, in particular through more occupational and geographical mobility is addressed only partially.
23. To improve and increase investment in its people, Poland is developing a lifelong learning strategy but implementation is scheduled only for 2007-2008. Although the Commission in the 2006 APR expressed concern about the lack of a fully-fledged strategy for vocational training, no concrete steps are presented to address this. Increasing participation in education and training, in particular for low-skilled

workers, remains a challenge. The mismatch between the education system and the needs of the economy has contributed to a very high rate of youth unemployment.

24. Labour market reforms envisaged in the NRP, and then specified in the National Action Plan for Employment, are in general appropriate and respond to Poland's challenges. However, they may not prove sufficient and implementation of some of the reforms, for example lowering the tax burden on labour, is delayed or abandoned,. Determined action and strong commitment are needed to implement reforms urgently through an appropriate policy mix encompassing making work pay, activation, prevention of unemployment, and improving skills.

PART III: CONCLUSIONS

25. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
26. Poland is making limited progress in the implementation of its National Reform Programme. There are signs that Poland is beginning to move ahead strongly in the micro-economic area, even though implementation of many measures is still in the early stages. Implementation of the macro-economic and employment reforms is so far insufficient. There is a limited policy response to the commitments made by the 2006 Spring European Council.
27. Among the most promising reforms being undertaken by Poland are simplifications to the tax system, the introduction of systematic impact assessments for legislation and steps to increase SME's access to finance.
28. The policy areas in the Polish National Reform Programme where weaknesses need to be tackled with the highest priority are: fiscal consolidation; improving competition in network industries and financial sectors; increasing the quantity and quality of R&D; making active labour market policies more extensive and more effective; and improving human capital and incentives to work. Against this background Poland is recommended to:
 - pursue its action to step up fiscal consolidation and supplement the nominal state budget deficit "anchor" (deficit ceiling) with an expenditure rule, in order to contain overall expenditure growth;
 - improve competition in network industries and in the financial sectors, including through a review of the role of regulators;
 - in order to boost R&D and innovation, pursue the reform of the public research sector and introduce policies to better attract and maximise the benefits of medium and high-tech foreign direct investment;
 - complete the reform of public employment services in order to increase the level and efficiency of active labour market policy to cover a larger share of unemployed, especially older persons and youth;

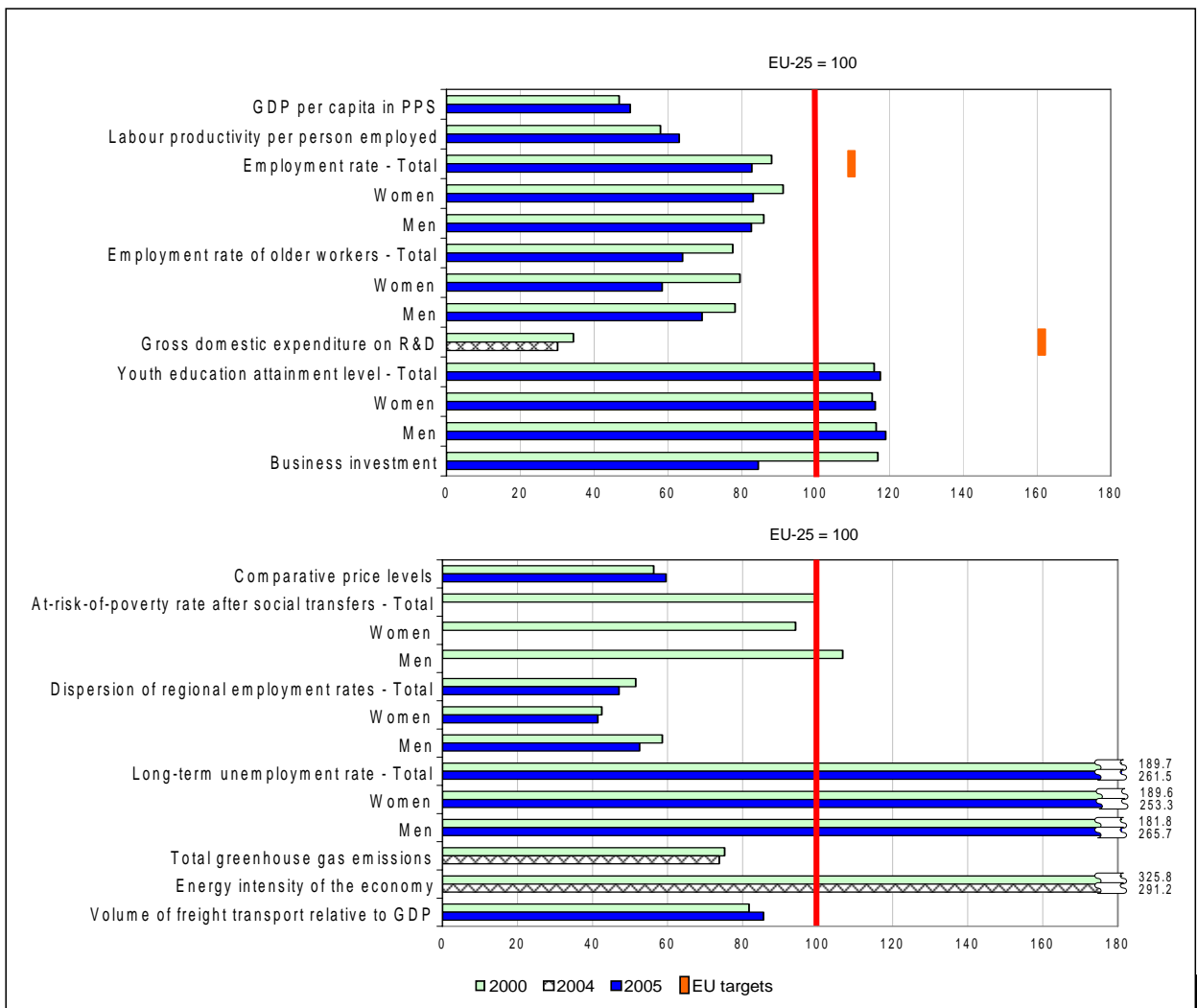
- lower the tax burden on labour and review benefit systems in order to improve work incentives, while developing policies to increase adult participation in lifelong learning and to modernise education and training systems in view of labour market needs.
29. In addition, it will be important for Poland over the period of the National Reform Programme to focus on: upgrading transport infrastructure; improving environmental protection; further reducing and redirecting state aids; the full liberalization of energy markets; speeding-up the business registration process; and ensuring that cohesion policy instruments underpin the structural measures highlighted in the Implementation Report with a view to contributing to boosting growth, competitiveness, employment and social cohesion. A firm and realistic target for overall investment in R&D by 2010 should be set.

PART IV: STATISTICAL GRAPHS AND DATA

POLAND

	PL							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	46.8	46.1	46.3	46.9	48.8	49.8	:	100.0	100.0	100.0	70.0
Labour productivity per person employed	58.0e	50.3	51.5	59.5	62.1	63.1		100.0	100.0	100.0	
Employment rate							1.65 (2008)				3.0
Total	55.0	53.4	51.5	51.2	51.7	52.8		62.4	63.3	63.8	
Women	48.9	47.7	46.2	46.0	46.2	46.8		53.6	55.7	56.3	
Men	61.2	59.2	56.9	56.5	57.2	58.9		71.2	70.9	71.3	
Employment rate of older workers											
Total	28.4	27.4	26.1	26.9	26.2	27.2		36.6	41.0	42.5	
Women	21.4	20.4	18.9	19.8	19.4	19.7	26.9	31.7	33.7		
Men	36.7	35.6	34.5	35.2	34.1	35.9	46.9	50.7	51.8		
Gross domestic expenditure on R&D	0.64	0.62	0.56	0.54	0.56	0.57	1.65 (2008)	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	88.8	89.7	89.2	90.3	90.9	91.1	76.6	77.1	77.5		
Women	91.7	91.8	91.9	92.8	93.1	93.3	79.5	80.1	80.3		
Men	85.8	87.7	86.5	87.9	88.7	88.9	73.7	74.2	74.7		
Comparative price levels	56.3	62.9	59.5	53.4	52.4p	59.6p	100.0	100.0p	100.0p		
Business investment	21.4	17.3	15.3	14.9	14.6	14.7	18.3	17.1	17.4		
At-risk-of-poverty rate after social transfers											
Total	16.0	16.0	17.0	17.0	:	:	16.0e	16.0e	:		
Women	16.0	15.0	16.0	16.0	:	:	17.0e	17.0e	:		
Men	16.0	16.0	17.0	17.0	:	:	15.0e	15.0e	:		
Dispersion of regional employment rates											
Total	6.9	7.2	7.3	7.2	6.4	5.6	13.4	12.2	11.9		
Women	8.7	8.9	9.2	8.7	7.6	7.0	20.5	17.3	16.9		
Men	5.8	5.9	6.3	6.4	6.0	5.1	9.9	10.2	9.7		
Long-term unemployment rate											
Total	7.4	9.2	10.9	11.0	10.3	10.2	3.9	4.1	3.9		
Women	9.1	10.8	12.3	11.7	11.0	11.4	4.8	4.7	4.5		
Men	6.0	7.8	9.7	10.3	9.6	9.3	3.3	3.6	3.5		
Total greenhouse gas emissions	68.2	67.7	65.5	67.7	68.4	:	90.7	92.7	:		
Energy intensity of the economy	680.2	673.5	654.2	623.1	596.6	:	208.8	204.9	:		
Volume of freight transport relative to GDP	81.8	79.9	80.5	81.9	88.7b	89.6	100.1e	104.6be	104.7e		

PERFORMANCE COMPARED TO EU-25



Portugal

Assessment of National Reform Programme

1. The Portuguese economy is gradually recovering from the slow growth of the last few years, but has not yet reached its potential. The sharp deceleration of trend growth since the late 1990s reflects the unwinding of imbalances in government finances, external account and private sector indebtedness, which had accumulated over the boom period. Although going down as a result context of the fiscal consolidation process, the general government deficit still stands at an estimated 4.6% of GDP in 2006, while the current external deficit is foreseen at 9% of GDP. Both GDP per capita and labour productivity remain below EU average . Sluggish activity in the last few years has led to a decline in the employment rate (expected to be some 67.5% in 2006). The unemployment rate is projected at some 7.6% in 2006, with a significant concentration on youth and long-term unemployment.
2. Portuguese economic performance is held back by lags in price competitiveness and innovative capacity vis-à-vis other Member States. Stronger progress in upgrading the supply structure and raising productivity, notably through reinforced investment in human capital as well as in research and development, would significantly contribute to speeding up economic growth in a lasting way. The major challenge for policy is to reconcile the promotion of stronger growth and the improvement of the external balance with the restoration of sound public finances, itself a key condition for stronger economic performance in the longer run. This can be achieved by redesigning public spending in favour of uses more supportive to potential growth.

PART I: GENERAL ASSESSMENT

3. The Portuguese 2005-2008 National Reform Programme (NRP) is built on four strategic priorities: strengthening budgetary consolidation; reform of public administration; fostering scientific and technological development; and increasing the qualification levels of the population. The Commission's 2006 Annual Progress Report (APR) shared this analysis, but considered that further attention should be given to; long-term sustainability of the public finances; effective competition in network industries, in particular telecommunications and energy; the modernisation of work organisation to improve the adaptability of enterprises; and further measures to ensure a less segmented labour market and to improve social cohesion.
4. Portugal has made good progress implementing the measures in the NRP. The Portuguese reform strategy has been strengthened by the Technological Plan. This ambitious programme aims to increase the knowledge intensity of the economy and to bring Portugal close to the EU average in the area of technology, R&D and innovation. Furthermore, there is significant progress in implementing measures on retirement rules and pensions for civil servants and on pension reform for the private sector. Initial steps have been set out and are being taken with regard to better regulation, access to finance for businesses, the reform of public administration, the efficient operation of energy markets and generation of electricity from renewable sources. Most employment policy measures are also still in the initial stage of

implementation, but significant and adequate initiatives have been programmed in several areas. Further measures are necessary to rebalance flexibility and security in the labour market. Progress towards the transposition of EU-legislation into national law and the reduction of state aid has been rather limited. The budgetary impact of measures (including also expected expenditure savings) for the next two years still needs to be further detailed, taking into account both the Stability Programme and the programming of Structural Funds for 2007-2013. Cohesion Policy funding will amount to 1.8% of GDP in the 2007-2013 period.

5. The Implementation Report indicates that progress with respect to the 2006 Spring European Council conclusions is generally good. For example, on and off line one-stop shops allow very rapid business start-ups. Steps have been taken to improve the business environment for SMEs and there are plans to expand entrepreneurship education.
6. There has been good progress on improving governance of the Lisbon Strategy for Growth and Jobs. The responsibilities of the national coordinator have been extended to the implementation of the Technological Plan, for which an on-line monitoring system has been put in place. The strategic priorities in both the NRP and the National Strategic Reference Framework are coherent. As highlighted in the Portuguese Implementation Report, attention should be paid to ensuring an adequate level of financial support from Structural Funds to the implementation of the NRP.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The NRP considered Portugal's commitment to fiscal consolidation as a key driver of macro-economic policies and identified as a key target achieving a general government deficit below 3% of GDP by 2008 – down from 6% of GDP in 2005 and from the estimated 4.6% for 2006. NRP measures in this area, reflecting the strategy aimed at reducing primary expenditure in a sustained way, concentrate on public administration reform, governance, and reforming old-age pension systems and health care schemes. This choice of priorities is relevant for Portugal. The Commission identified in the 2006 APR the sustainability of public finances as a point requiring further action, since the restoration of sound public finances is crucial to return to stronger economic growth over the medium-term.
8. Reform of the public administration is going in the right direction. Central government structures have been streamlined to decrease expenditure and raise efficiency. Crucially linked with this reform will be the new rules for government staff, namely on mobility, contractual arrangements and careers. The reform includes some promising measures, but will have impact only as of 2007. Controllers have been appointed in various ministries to oversee budgetary execution, and tight reporting obligations on budgetary execution have been established. However, the announced measures to halt the growing share of wages in government spending have not yet been fully taken.
9. Concrete policy initiatives have been taken to address challenges arising from Portugal's ageing population. Changes in civil servants' retirement rules and pension

arrangements were implemented in January 2006, promoting convergence towards the general private sector pension scheme. The reform of the latter, designed to strengthen the link between contributions and benefit levels, is taking shape. To deal with rising health expenditure, various schemes covering different categories of civil servants have been adjusted, resulting in lower benefits on average. The health services network has been re-shaped. Lower co-payments for medicines have also been introduced, while the process of transforming government hospitals into more independent entities with more management freedom has continued, with gains in efficiency expected to yield some expenditure savings.

10. Portugal has generally made significant progress implementing macro-economic measures which can both improve the sustainability of public finances and help create conditions for sustainable economic growth, thereby facilitating a correction of the sizeable external deficit. More information is needed to assess the sufficiency of the measures targeting a reduction of the government deficit over the medium-term and aiming at long-term fiscal sustainability. The administrative reform will be key to containing public spending. Full implementation of the measures regarding contractual arrangements and careers would further reduce the share of wages in government spending on a structural basis. In all, continued firm control over public expenditure and timely implementation of the on-going reforms will be required if the macro-economic aims set out in the NRP and Implementation Report are to be achieved.

Micro-economic policies

11. The micro-economic part of the NRP covers competitiveness and entrepreneurship; R&D and innovation; territorial cohesion and environmental sustainability; and market efficiency. In its APR the Commission agreed that these are priority areas, but also identified other points requiring further attention, including the need for stronger measures for effective competition in network industries, especially telecommunications and energy.
12. Portugal has made significant progress to facilitate the start-up of new business. A new scheme is now in place, with the possibility to set up a new company within one hour. One-stop shops have been opened across the country, complemented by a fully-fledged on-line service. Moreover, a number of promising initiatives to improve access to finance are in the pipeline. Further efforts are needed with regard to the introduction of entrepreneurship in secondary schools. 13. Portugal has made some progress with other efforts to improve the business environment. An extensive programme to improve regulation was adopted in May 2006, but implementation on the ground so far is limited. In the field of electronic communications, the regulator still needs to notify some markets but substantial progress has been made in opening the local access network through the implementation of the Regulation on unbundled access to the local loop, resulting in significantly lower wholesale prices. New technologies are increasingly being used to improve the efficiency of administrative processes. However, there is room for improvement with regard to the take-up of ICT by businesses, the transposition of EU legislation into national law, improved competition in financial markets and the reduction and redirection towards horizontal objectives of state aid.

14. Portugal has strengthened its R&D and innovation strategy. The Implementation Report deals with science and technology measures largely on the basis of the government's "Technological Plan". Steps have been taken to accelerate ICT take up and development of an information society, within the "Connecting Portugal" action plan. A substantial increase in the public budget for science and technology is foreseen and there is an implicit national target to spend 1% of GDP in public funding for R&D by 2009. The knowledge and science base is to be strengthened and human resources reinforced. Research institutions will be given more support to improve organisation, infrastructure, internationalisation and evaluation, as well as to help them obtain economic returns from research. A joint venture with Spain for the creation of a nanotechnology laboratory of world relevance in the form of a new international organisation is developing well. Consortia between state laboratories, other research institutes, universities and enterprises have been introduced to stimulate linkages and increase scale within an overall reform of the state laboratories system. These are welcome steps, which will improve Portugal's capacity to use additional funding effectively to undertake R&D and transform it into successful innovation. Vigorous implementation, together with further steps to stimulate linkages between research and industry and to foster private R&D, are now necessary to allow demand to respond to the supply push offered by some of the measures.
15. A strategic approach is being developed to improve security of energy supply, environmental sustainability and competitiveness and innovation. This includes the setting of an ambitious target for generation of electricity from renewable sources (39% by 2010). Further emission reduction measures will be needed to meet the burden sharing target. Portugal is taking measures to improve competition in energy markets. First steps have been taken towards separating production and distribution activities in energy markets. Competition is being enhanced by the increased interconnection capacity with Spain, but the existence of controls on the prices distributors can charge end consumers may weaken competition by favouring incumbents. Measures to open the gas market have been initiated.
16. Portugal is implementing the micro-economic measures announced in last year's NRP and has strengthened its strategy for R&D and innovation, where effective implementation, improved science-industry linkages and better governance will be crucial. The business climate is improving. Additional steps are needed to further improve efficiency in energy markets.

Employment policies

17. Last year's NRP set as key priorities in the employment area: enhancing education and qualifications; promoting job creation; anticipating and managing restructuring; promoting flexibility and security; and modernising social protection. The Commission's 2006 APR shared this analysis, but considered that further attention should be given to the adaptability of workers, notably the low-skilled. It also called for the modernisation of work organisation to improve the adaptability of enterprises and for further measures to ensure a less segmented labour market and to improve social cohesion.
18. Although labour market performance has improved modestly, significant investments have been announced to increase the availability of childcare and care for the elderly,

thus facilitating the reconciliation of work and family life. Recent changes to the social security system will contribute to active ageing, but are insufficient without a comprehensive strategy to promote longer, healthy working lives, with adequate training and quality jobs. The unemployment benefit scheme has been improved by strengthening activation mechanisms to help people return to the labour market. Further efforts are necessary to increase labour market opportunities for the long-term unemployed, women, youth and older workers. The gender pay gap in the private sector has hardly changed, and gender segregation in particular occupations and sectors, remains very high. No specific measures are set out aimed at addressing these challenges.

19. Collective bargaining has given insufficient attention to modernising work organisation and the labour market continues to be highly segmented. Currently, almost 40% of those employed are on fixed-term contracts or self-employed, and labour market adjustments are often made at the expense of those without permanent contracts, irrespective of their qualification levels or potential to maximise productivity. A Green Paper on labour relations was published in 2006, with the intention of opening a debate that may lead to changes to the Labour Code. These changes, coupled with the on-going measures to reform social security, improve skills and modernise the public employment service, go in the right direction. However, very little has been done to review employment protection legislation, changes to which should be pursued within a global approach to balancing flexibility and security in the labour market ("flexicurity").
20. Portugal has launched an ambitious programme to reduce the number of early school leavers, to increase the level of educational attainment, and increase participation in lifelong learning. This ambitious programme aims at strongly expanding upper secondary-level education and training and qualifying one million adults by 2010. Many isolated education and training measures have been launched and improved over the years. However, Portugal still lacks a National Qualifications Framework to support a comprehensive lifelong learning strategy that is sensitive to labour market needs and supports a life cycle approach to work.
21. The Implementation Report describes progress on the extensive reforms to improve labour market performance and address the structural "qualification" weaknesses. It indicates that significant and largely adequate reforms have been launched in most of the necessary areas, except that of flexicurity, where a coherent overall approach is needed. Most of the employment measures concerned are still in the initial stage of implementation. Ensuring their quality and effectiveness will require strong commitment from all stakeholders and a strengthened focus on monitoring, control and evaluation. Social cohesion, poverty levels and inequality of income distribution, continue to be serious problems in Portugal. Better coordination of the economic, protection and social dimensions of employment policies remains necessary.

PART III: CONCLUSIONS

22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:

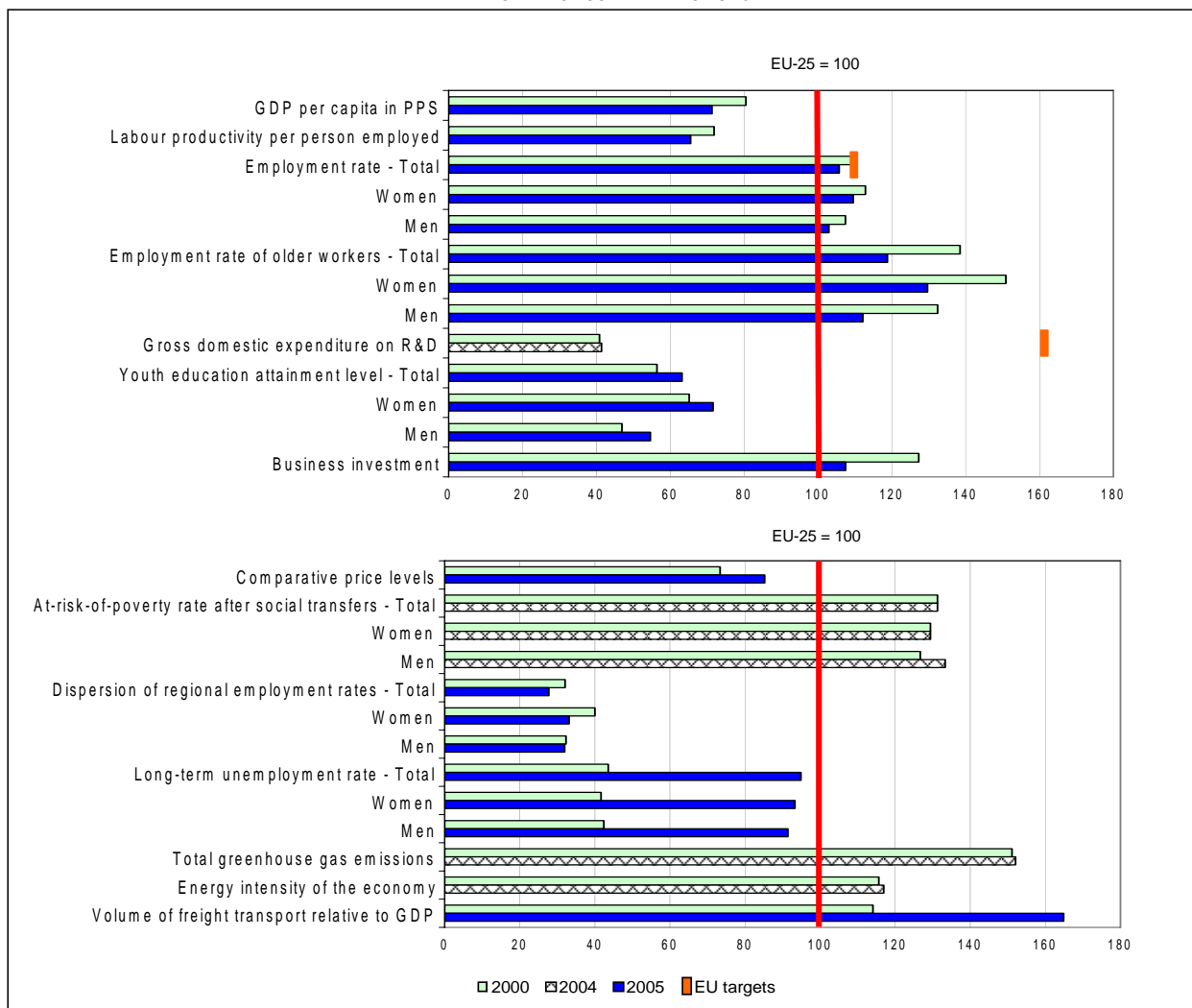
23. Portugal is making good progress on implementing the measures in the National Reform Programme, especially in the macro and micro-economic areas. On employment related policies, there has also been progress, especially on reforming education and training, but the important area of the adaptability of the labour market and flexicurity is not yet being fully addressed. Progress towards meeting the commitments made at the 2006 Spring European is generally good. Considerable further efforts across all policy areas will be necessary to fully achieve the objectives of the programme, given their welcome ambition and Portugal's point of departure.
24. Important strong points of the reform process in Portugal include the extensive reforms launched to the public administration, the measures to facilitate business start-ups within an hour, the adjustment of old-age pension schemes and comprehensive consolidation measures in health care. Efforts to reinforce R&D have been strengthened and dovetailed into a coherent strategy through the ambitious Technological Plan. Extensive reforms are also being implemented in the education sector in particular with measures to increase literacy levels of the young and rationalise the national school network.
25. The policy areas in the Portuguese National Reform Programme where weaknesses need to be tackled with the highest priority are: improving educational attainment and lifelong learning; improving the adaptability of the labour market and addressing segmentation. These issues must be addressed in the context of further progress with the administrative reform and keeping rising spending on social transfers under control. Against this background Portugal is recommended to:
- in the context of the on-going correction of fiscal imbalances and public administration reform, redirect public spending towards uses more supportive to potential growth, while maintaining firm control over public expenditure overall;
 - implement measures to strongly improve the education attainment levels of the young, and develop a vocational training system that is relevant to labour market needs and based on a "National Qualifications Framework";
 - modernise employment protection, including legislation to foster flexibility and security to reduce the high levels of labour market segmentation.
26. In addition, it will be important for Portugal over the period of the National Reform Programme to focus on: ensuring that the promising Technological Plan is fully implemented, the linkages between research and industry consolidated and the involvement of the private sector strengthened; ensuring effective competition in energy and financial services markets; reducing emissions; reducing the deficit in transposing EU legislation into national law; and addressing the factors undermining social cohesion.

PART IV: STATISTICAL GRAPHS AND DATA

PORTUGAL

	PT							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	80.5	79.9	79.4	72.7	72.3	71.3		100.0	100.0	100.0	
Labour productivity per person employed	71.9	71.4	71.3	65.9f	65.9f	65.5f		100.0	100.0	100.0	
Employment rate							70.0				70.0
Total	68.4	69.0	68.8	68.1	67.8	67.5		62.4	63.3	63.8	
Women	60.5	61.3	61.4	61.4	61.7	61.7		53.6	55.7	56.3	
Men	76.5	77.0	76.5	75.0	74.2	73.4		71.2	70.9	71.3	
Employment rate of older workers											
Total	50.7	50.2	51.4	51.6	50.3	50.5		36.6	41.0	42.5	
Women	40.6	40.3	42.2	42.4	42.5	43.7		26.9	31.7	33.7	
Men	62.1	61.6	61.9	62.1	59.1	58.1		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.76e	0.80	0.76e	0.74	0.77ep	0.81p	1.8	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	43.2	44.4	44.4	47.9	49.6	49.0		76.6	77.1	77.5	
Women	51.8	53.0	52.9	55.5	58.7	57.5		79.5	80.1	80.3	
Men	34.6	35.9	36.1	40.4	40.8	40.8		73.7	74.2	74.7	
Comparative price levels	73.4	74.6	76.2	87.3b	85.7p	85.2p		100.0	100.0p	100.0p	
Business investment	23.3	22.6	21.4	19.4	19.2	18.7		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	21.0	20.0	20.0p	19.0p	21.0b	:		16.0e	16.0e	:	
Women	22.0	20.0	:	:	22.0b	:		17.0e	17.0e	:	
Men	19.0	20.0	:	:	20.0b	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	4.3	3.5	3.8	3.9	3.5	3.3		13.4	12.2	11.9	
Women	8.2	6.8	5.9	6.3	5.9	5.6		20.5	17.3	16.9	
Men	3.2	2.7	3.5	3.2	3.2	3.1		9.9	10.2	9.7	
Long-term unemployment rate											
Total	1.7	1.5	1.7	2.2	3.0	3.7		3.9	4.1	3.9	
Women	2.0	1.9	2.1	2.7	3.4	4.2		4.8	4.7	4.5	
Men	1.4	1.2	1.4	1.8	2.6	3.2		3.3	3.6	3.5	
Total greenhouse gas emissions	137.1	139.6	147.1	139.6	141.0	:		90.7	92.7	:	
Energy intensity of the economy	241.5	243.9	254.7	234.7	239.6	:		208.8	204.9	:	
Volume of freight transport relative to GDP	114.2	123.8	122.2	114.2	164.9b	172.6		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Slovenia

Assessment of National Reform Programme

1. The Slovene economy has grown steadily at an average rate of almost 4% per annum over the past decade. In 2006, GDP per capita is estimated to be 82% of the EU average. Although labour productivity growth has been strong, Slovenia's productivity is still below the EU average. Since 2000, inflation has been markedly reduced and appears to have now settled at 2.5%. The employment rate is expected to stay above the EU average, while the unemployment rate at just over 6% is one of the lowest in the EU. However, structural problems on the labour market persist, as shown by low employment of older workers and high youth unemployment.
2. Despite a generally strong economic performance, shortcomings remain that result in subdued potential growth. Structural rigidities in the labour and product markets, in particular, impede faster catching-up with EU productivity levels. Job opportunities and increased labour market participation depend on promoting entrepreneurship, innovation and competition. Sustained growth will also depend crucially on continuously containing inflationary pressures and continued fiscal consolidation. In the light of high projected costs of population ageing, adjustments in the pension and health care system together with labour market measures would contribute to ensuring the long-term sustainability of public finances.

PART I: GENERAL ASSESSMENT

3. The Implementation Report gives a detailed account of the progress made with addressing the five priority challenges, as identified in the last year's National Reform Programme (NRP) based on the "Slovenia's Development Strategy": a competitive economy and faster growth; a knowledge-based society; an efficient state; a modern social state and higher employment; and sustainable development. The Commission agreed with the challenges identified and called in its 2006 Annual Progress Report (APR) for stronger measures to ensure the sustainability and adequacy of the pension system and to promote active ageing, as well as for a more coherent strategy for R&D and innovation.
4. Slovenia is making good progress in implementing the overall reform agenda. On the macro-economic area, policy action has focused on further adjustments of the tax system, including incentives for private R&D investment. Greater reform effort, however, would be desirable as regards enhancing the long-term sustainability of public finances, which continues to be under threat, notwithstanding a few initiatives related to reducing general government expenditure. Positive steps have been taken in some key micro-economic areas, such as entrepreneurship and better regulation. On the other hand, progress on further strengthening the framework for competition and on establishing stronger links between public R&D institutions and businesses has been less concrete. Slovenia has launched the major employment reforms announced in the NRP. However, the efficiency of the employment services remains a challenge, especially in the context of aiming for increased flexibility on the labour market. While certain measures to encourage active ageing have been taken, a

stronger response to address the weaknesses identified by the Commission in the 2006 APR is needed.

5. Progress in implementing the commitments taken at the 2006 Spring European Council is rather limited. Little progress has been made in redirecting increased public funding for R&D towards priority technological sectors. The extension of the one-stop-shop system for all forms of company start-ups is scheduled to be completed in 2007 and should establish a single administrative contact point for recruiting the first employee. A stronger response is also needed to the European Council commitments in the area of employment, in particular to ensure the effectiveness of existing active labour market policies.
6. Since January 2006, a government office has been co-ordinating the implementation of the reforms, while the monitoring procedures are currently being developed by the relevant ministries. To build broad political support for reforms, the involvement of stakeholders has been strengthened, mainly through the "Partnership for Development" agreement – a political commitment to implement socio-economic reforms, signed by most parliamentary parties in April 2006. The reform strategy has continued to be widely debated in public, involving the tripartite Economic and Social Council, local authorities and the media. Specific objectives such as the promotion of entrepreneurship and quality of human resources, R&D, innovation and technological development, are linked to specific measures indicated in the draft National Strategic Reference Framework (NSRF), establishing the financing priorities for the Structural and Cohesion Funds for 2007-2013. The NSRF earmarking exercise should allow for a clearer view on how the Cohesion and Structural Funds will contribute to promoting competitiveness and creating jobs. Cohesion Policy funding will amount to 1.7% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. On 1 January 2007, when Slovenia introduces the euro, the main short-term macro-economic objective of the NRP will be accomplished. The sustainable fulfilment of the Stability and Growth Pact criteria and real convergence become the immediate challenges.
8. Since the presentation of the NRP, significant progress has been made on most of the areas underlying the fiscal consolidation strategy. In particular, a thorough overhaul of the tax system has been undertaken in order to enhance the efficiency of general government revenue while, at the same time, reducing tax burdens on both capital and labour. Among various policy options to cover for the revenue loss due to this tax reduction, an increase in reduced and standard VAT rates, by 0.5 and 1 percentage points respectively, is under consideration. The government has launched a scrutiny of general government expenditure and put forward a list of cost-saving measures. They are estimated to cut public spending by 1.6 percentage points compared with 2006, according to the proposed 2007-2008 budget. Wage pressures are expected to remain contained, based on the new pay agreement in the public sector for 2007-2009, which – together with the pay agreement in the private sector for 2006-2007 – fosters wage moderation. It nevertheless remains to be seen

whether, and for how long, the announced measures will be sufficient to avoid budgetary slippage.

9. Against the backdrop of a very high share of fixed spending commitments, the long-term sustainability of public finances will start eroding as age-related expenditure rises fast due to rapid population ageing. In this context, Slovenia needs stronger measures ensuring the adequacy of the pension system. Given the very gradual increase in the pension age (61 for women in 2013 and 63 for men in 2008) and weak financial incentives to work longer, a strengthening of the pension reform should be considered.
10. While the policy measures on the revenue side appear largely appropriate, stronger expenditure measures will be needed to ensure effective fiscal consolidation. The relatively favourable macroeconomic growth conditions in 2006 and 2007, with the economy growing slightly above potential, should offer the opportunity to proceed with reforms that enhance the sustainability of public finances in the long term.

Micro-economic policies

11. As regards the private sector contribution to R&D, the 2006 Implementation Report contains an extensive set of new measures including additional tax incentives for R&D expenditure and a €5.6 million, three-year programme co-financing business research. Additional measures to enhance intellectual property rights protection and foster private public co-operation in R&D and innovation are welcome and should be further developed. However, the report pays no specific attention to the governance measures needed to ensure the development of a coherent and successful national research and innovation system. In particular there are no measures aiming at improving the coordination role of the new Office for Growth or at clarifying the status of the Slovene Technology Agency.
12. The competition challenge is addressed through a wide range of measures such as those towards opening up energy markets to competition. On the other hand, the opening of the rail freight market is not yet fully accomplished. The ongoing efforts to strengthen, streamline and improve the coherence of competition regulations are useful but further measures are needed to ensure that the Slovenian Competition Protection Office is sufficiently equipped to investigate and sanction anti-competitive behaviour. This includes strengthening the resources of the authority and removing any legal obstacles that may prevent the authority from exercising its powers effectively. Significant restrictions still exist in the regulation of professional services including among other things fixed pricing, recommended prices, and advertisement bans. Encouraging first steps have been taken to increase the competitiveness of this sector and this now needs to be translated into regulatory reform which enhances competition. In electronic communications, so far incomplete measures, have been taken to privatise the incumbent operator and stimulate competition.
13. The business environment has been enhanced by progress towards administrative cost reduction and simplification. However, there has been little progress towards reducing the time and costs for start-ups. Slovenia should further ensure that the extension of the one-stop-shop system for registering all forms of companies is completed in 2007 and that a single contact point for recruiting the first employee is established. The various measures to provide a more stable and transparent tax

environment for enterprises are welcome and should support the competitiveness of the Slovenian economy. Progress has been made in improving SME access to equity finance, notably through plans to establish a first venture capital fund with public-private-partnership, and in promoting entrepreneurial skills. However, further effort could be made to stimulate ICT take-up by businesses. Meanwhile there is progress in ICT use by the public administration.

14. Relatively slow progress on the sustainable use of natural resources is reported. While the NRP mentioned measures continuing the environmental tax reform, including taxes on energy and CO₂ emissions, limited attention is paid to this in the Implementation Report. As Slovenian energy intensity is higher than the EU-average, the progress reported on promoting efficient energy use and the use of renewable energy sources is welcome. No concrete measures or targets are pointed out for implementing the EU Environmental Technologies Action Plan and there is a risk that the growth and employment opportunities which can be provided by sustainable industry technologies may be missed.
15. Although the penetration of foreign direct investment into the Slovene economy has been low, partly due to delays in the privatisation process, progress has been made with measures to improve the supply of industrial sites, to remove administrative barriers and to reduce initial costs, as well as to promote Slovenia as a destination for foreign direct investment. Further privatisation should attract a significant proportion of foreign capital. The importance given to supporting the internationalisation of SMEs is also positive.
16. As regards the challenge of better regulation, progress has been made following the adoption of a programme aiming at introducing better drafting of regulations and decisions.
17. Overall, Slovenia is making progress in some key micro-economic areas, such as entrepreneurship and better regulation. However, progress on developing a coherent national strategy for R&D and innovation and further strengthening the framework for competition has been less clear.

Employment policies

18. While the employment rate of older people increased from 29% in 2004 to 30.7% in 2005, achieving the NRP target of 35% by 2008 remains a challenge. Some specific measures to promote employment of older workers have been taken. Nevertheless, it is important that the announced active ageing strategy, due by the end of 2006, strengthens the approach to retaining older people in the labour market, especially older women (18.5% in 2005). A number of measures taken in 2006, such as income tax and education reforms, should help tackle the difficulties educated young people encounter in entering the labour market. However, there is no direct follow-up to the commitment in the Slovene NRP to ensure access to a job for graduates within six months of completing their studies. Social and unemployment benefits have been reformed to increase conditionality. However, measures ensuring that the most disadvantaged are not further marginalised have not received due attention. In particular, there are no signs of improved performances by employment services in terms of prevention of unemployment and activation measures helping people into

employment. The recent introduction of a quota system has improved employment opportunities for people with disabilities.

19. As regards the adaptability of workers and enterprises, the 2005 reform of payroll tax is gradually reducing the high tax burden on labour and creating higher incentives to work. Intensive negotiations with the social partners are delaying the revision of the Labour Relations Act, intended to promote "flexicurity" in the labour market. The fight against undeclared work is given a higher profile than in the 2005-2008 NRP and new measures have been proposed by the government. Some measures have been taken to facilitate the reconciliation of work and private life, for example through access to part-time work for parents, but a wider introduction of employee-friendly working time has not yet materialized, though it was announced in the NRP.
20. The establishment of several new independent higher education institutions is aimed at raising the quality of higher education, improving links to the labour market, and implementing a new approach to financing higher education. In view of the difficulties of the integration of young graduates into the labour market, it will be important to closely monitor the success of this reform. To further address the skills gap, it is important to complement the recent measures focusing on the quality of secondary vocational education, with measures to increase its attractiveness, especially for occupations in demand, and to develop integrated career counselling and guidance. Low-skilled older workers, particularly those threatened by industrial restructuring, require further attention, notably in the context of the lifelong learning strategy, due at the end of 2006. The initiatives announced to encourage private investment in human capital should be complemented by measures targeting a wider population.
21. In the past year Slovenia has launched most of the major employment reforms set out in the NRP. Activation policies helping people into employment and policies to prevent long-term unemployment need to be enhanced to accompany the increasing contractual flexibility of benefits, stronger conditions attached to the receipt of benefits and the gradual increase in the pension age. Rapid implementation of an effective active ageing strategy is crucial to retain older workers in the labour market. The barriers to the employment of young people should be removed by improving incentives to work, along with quality of education and its responsiveness to labour market needs.

PART III: CONCLUSIONS

22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
23. Slovenia is making good progress in the implementation of its National Reform Programme. Slovenia is taking appropriate measures in some key areas such as entrepreneurship and better regulation. It has launched most of the major reforms of employment policies, benefiting from relatively favourable macroeconomic growth conditions. Progress with public expenditure reform is less evident. The same is true in the microeconomic field of progress in enhancing the innovation and competition framework. With respect to the labour market, progress on the implementation of the

active ageing strategy and on the removal of barriers to youth employment has not so far been rapid enough. Progress in implementing the commitments made at the 2006 Spring European Council is rather limited.

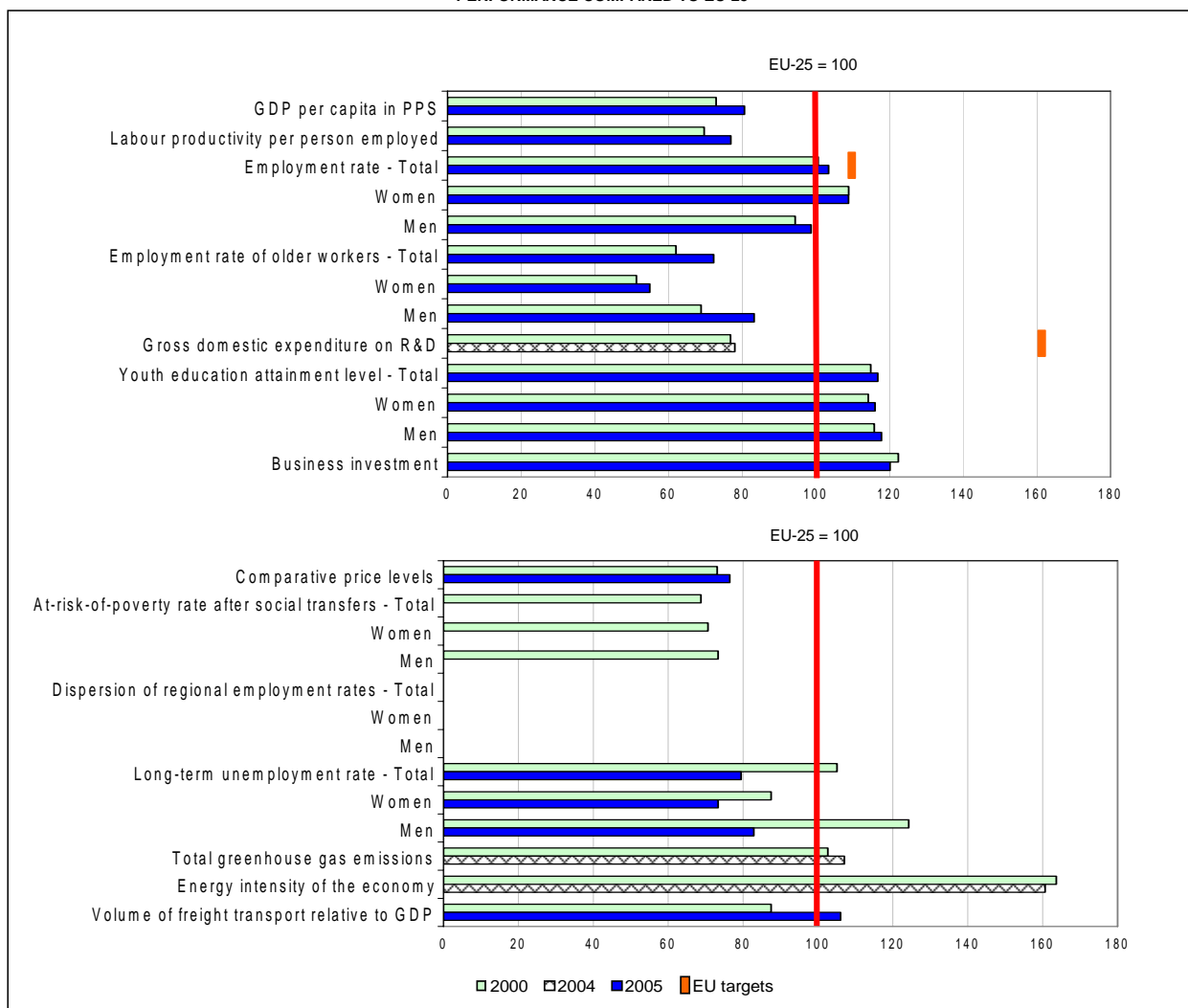
24. The strengths of the National Reform Programme and its implementation include: the fiscal reform efforts; the various measures to promote entrepreneurship; the ongoing restructuring of state funds into portfolio investors; the decreasing share of state aid in GDP; and the progress towards the full liberalisation of energy markets and the creation of a second player in the market.
25. The policy areas in the Slovenian National Reform Programme where weaknesses need to be tackled with the highest priority are: improving long term fiscal sustainability and increasing the employment rate of older workers; and strengthening the activation and prevention aspects of employment policy, currently slow in responding to the fast changing conditions on the labour market. Against this background, it is recommended that Slovenia
 - take further steps to strengthen the reform of the pension system and promote active ageing, with a view to increasing the employment rate of older workers and improving long-term sustainability.
 - enhance employment services to support the move towards more flexible contractual arrangements and increased conditionality of benefits, giving high priority to offering services at an earlier stage of unemployment.
26. In addition, it will be important for Slovenia over the period of the National Reform Programme to focus on: setting concrete and realistic targets for investment in R&D; improving the effectiveness of the new Office for Growth and of the Slovenian Technology Agency; strengthening the legal framework for protecting intellectual property rights; improving competition, notably in professional services, and enhancing the effectiveness of the Competition Protection Office; better promotion of environmental technologies and energy efficiency; shortening start-up times for businesses and reducing related costs; integrating young people in the labour market; strengthening the link between the education system and the labour market; and reducing the segmentation of the labour market.

PART IV: STATISTICAL GRAPHS AND DATA

SLOVENIA

	SI							EU25				
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target	
GDP per capita in PPS	72.9	73.9	74.5	75.9	79.2	80.6		100.0	100.0	100.0		
Labour productivity per person employed	69.7	71.2	70.9	72.5	75.4	76.9		100.0	100.0	100.0		
Employment rate							67.0 (2008)				70.0	
Total	62.8	63.8	63.4	62.6	65.3	66.0		62.4	63.3	63.8		
Women	58.4	58.8	58.6	57.6	60.5	61.3		53.6	55.7	56.3		
Men	67.2	68.6	68.2	67.4	70.0	70.4		71.2	70.9	71.3		
Employment rate of older workers												
Total	22.7	25.5	24.5	23.5	29.0	30.7		36.6	41.0	42.5		
Women	13.8	15.8	14.2	14.6	17.8	18.5	26.9	31.7	33.7			
Men	32.3	35.9	35.4	33.2	40.9	43.1	46.9	50.7	51.8			
Gross domestic expenditure on R&D	1.43	1.55	1.52	1.32	1.45		3.0	1.86e	1.86e		3.0	
Youth education attainment level												
Total	88.0	88.2	90.7	90.8	90.5	90.5		76.6	77.1	77.5		
Women	90.8	90.3	93.3	94.0	94.1	93.2		79.5	80.1	80.3		
Men	85.4	86.3	88.3	87.7	87.1	88.0		73.7	74.2	74.7		
Comparative price levels	73.1	73.2	75.5	77.9	75.8p	76.4p		100.0	100.0p	100.0p		
Business investment	22.4	21.0	19.6	20.0	21.0	20.9		18.3	17.1	17.4		
At-risk-of-poverty rate after social transfers												
Total	11.0	11.0	10.0	10.0				16.0e	16.0e			
Women	12.0	12.0	11.0	11.0				17.0e	17.0e			
Men	11.0	10.0	9.0	9.0				15.0e	15.0e			
Dispersion of regional employment rates												
Total	-	-	-	-	-	-	-	13.4	12.2	11.9		
Women	-	-	-	-	-	-	-	20.5	17.3	16.9		
Men	-	-	-	-	-	-	-	9.9	10.2	9.7		
Long-term unemployment rate												
Total	4.1	3.7	3.5	3.5	3.2	3.1		3.9	4.1	3.9		
Women	4.2	4.0	3.6	3.6	3.4	3.3		4.8	4.7	4.5		
Men	4.1	3.5	3.4	3.4	3.1	2.9		3.3	3.6	3.5		
Total greenhouse gas emissions	93.1	97.7	98.6	97.3	99.2			90.7	92.7			
Energy intensity of the economy	341.7	349.6	344.6	341.1	329.2			208.8	204.9			
Volume of freight transport relative to GDP	87.6e	88.5	84.0	87.2	100.9	111.0		100.1e	104.6be	104.7e		

PERFORMANCE COMPARED TO EU-25



Slovakia

Assessment of National Reform Programme

1. GDP per capita is estimated to reach 57.1% of the EU average in 2006. Annual GDP growth averaged over 4% for the period 1995-2005, and is expected to accelerate to around 6.7% in 2006. Since the mid-1990s, labour productivity growth has been above the EU average. Strong economic growth is also being reflected in a better labour market performance, with employment anticipated to increase by some 2.6% in 2006. The employment rate is projected to increase to around 58.9% in 2006 which is still far below the EU-wide target (70%). The unemployment rate is estimated to decrease by some two percentage points to around 14.3% in 2006. It is likely to remain one of the highest in the EU, particularly affecting young people (30.1% in 2005). The employment rate for older people, although rising, remains very low (30.3% in 2005).
2. Although enjoying strong GDP growth, Slovakia faces high structural unemployment and wide regional disparities. Large-scale reforms of social, labour market and health care policies have contributed to fiscal consolidation and strong employment growth. The challenge for economic policy is to ensure that strong growth is sustained in the coming years and that it improves the labour market situation and diminishes regional disparities. Measures enhancing the innovation and business environment, in combination with reforms of the education system, would strengthen growth potential, although it would be necessary to ensure that the implementation of such measures did not have a negative effect on the fiscal consolidation process

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Program (NRP) was drafted by the government which left office in June 2006. The 2006 Implementation Report was prepared and adopted by the newly elected government, with regard to action taken by the previous one. The report refers to some future intentions. However, a thorough revision of the NRP is expected only later this year. The key challenges defined in the NRP remain: developing the information society; increasing R&D and innovation; improving the business environment; improving education and raising employment. The Commission's analysis in its Annual Progress Report (APR) was that further attention was needed in the areas of: stimulating R&D and innovation; tackling regional disparities and structural unemployment; and the integration of vulnerable groups.
4. Slovakia has made some progress in the implementation of the NRP. Whilst reconfirming the aims of stable public finances and entry into the euro area by 2009, the focus of the Implementation Report is on the main microeconomic and employment challenges. The targets set in the NRP for deficit reduction and employment growth remain valid. There has been progress in improving the business environment and introducing e-government. Employment growth has been strengthened by a set of measures and incentives in the areas of taxation and active labour market policy. There has been progress in reforming tertiary education. The

2007 national budget includes the macro-economic target of a reduced budget deficit of 2.9% of GDP. There is a need for a more rapid implementation of the R&D and innovation strategy, supported by an increased financial allocation. Structural unemployment has not been well addressed, with long-term unemployment remaining the highest in the EU, and the employment rate of some disadvantaged groups very low. Reform of primary and secondary education and the preparation of a lifelong learning strategy should be taken forward quickly.

5. Progress has been mixed in meeting the commitments made at the 2006 Spring European Council. For example, while action has been taken to facilitate business start-ups, no commitment has been made on offering young people leaving education guarantees of employment or training opportunities within six months.
6. The Implementation Report was prepared under the political direction of the Office of the Government and the Ministry of Finance, with monitoring and assessment undertaken by relevant ministries in cooperation with the social partners. After the government approved the report it was adopted by the Parliamentary Committee for EU Affairs. Local and regional authorities were not involved in the development of the report. The priorities for future Structural Fund interventions, in coherence with the key challenges identified in the NRP, will require an appropriate budgetary allocation. Cohesion Policy funding will amount to 3.3% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. In the Implementation Report the new government committed itself to the macro-economic goals of the NRP: attaining high and sustainable economic growth and achieving long-term sustainability of public finances by 2010. The fiscal policy challenge for 2007 is now to reduce the budget deficit to below 3% of GDP, including the cost of the pension reform.
8. In October 2006 the government approved the 2007 budget, targeting a general government deficit of 2.9% of GDP. With this aim in mind, the government decided on wide-ranging current and capital expenditure restraint, including in the areas of education and R&D. This seems inconsistent with the commitments made in the NRP to support a knowledge-based society. Some elements of the health care reform introduced since mid-2003, such as hard-budget constraints and increased cost-sharing, were abolished in 2006. As a result, public debt in the health care system might accelerate again, having a negative impact on public finances. The 2004 tax reform will be modified through a lower VAT rate (10%) on medical products and lower tax-free income for higher income groups. These changes are expected to slightly increase the deficit. Various adjustments to the pension reform launched in 2005, in particular a decrease in the size of the second funded pension pillar, are being considered but no changes have yet been adopted.
9. The government-approved 2007 budget respects the aim of fiscal consolidation. However, given the high current account deficit and favourable growth expectations for 2007, the deficit target does not seem ambitious.

Micro-economic policies

10. The NRP identified three key microeconomic challenges: a better business environment, higher R&D and innovation, and developing the information society. In the 2006 APR the Commission agreed on these challenges and underlined the importance of stimulating R&D and innovation. Measures to improve the business environment and the priority given to ICT development, including in education, were highlighted as the strong points of the Slovak NRP.
11. Some progress has been made in improving the business environment. Different methodologies for assessing regulatory impacts have been developed, but their specific implications and next steps are unclear. The government has approved the creation of one-stop shops for setting up businesses, to be run by bodies responsible for issuing business permits. This should now be followed up by establishing a single entry-point for recruiting the first employee through the same institutions. Law enforcement has been strengthened by the reform of the judiciary, but continuous efforts to enhance the judicial system and economic governance are necessary. New state aid legislation has been adopted, and the regional aid rules are under preparation. Sectoral state aid should be redirected towards horizontal priorities.
12. Slovakia has been very successful in reducing its deficit in transposing EU internal market legislation into national law.
13. There is no overall strategy to support SMEs and their access to finance needs improving. Significant improvements in the better regulation system are required, in particular in order to strengthen the institutional structures for better regulation, and to reinforce efforts in the areas of impact assessment, consultation of stakeholders, simplification and measurement and reduction of administrative costs. Initial preparatory work is on-going regarding two energy policy initiatives foreseen in the NRP: the identification of barriers obstructing the opening of the power supply market and of barriers to the use of renewable energy.
14. The manifesto of the new Slovak government from August 2006 sets an R&D investment target of 0.8% of GDP in 2010, whereas at the 2006 Spring European Council Slovakia had set a target of 1.8% of GDP in 2010. It is therefore disappointing that the Implementation Report does not indicate figures on R&D spending in 2005, or make reference to planned future public R&D spending. Given the proposal to allocate large-scale funding for R&D and innovation from the Structural Funds in 2007–2013, it is crucial that a comprehensive R&D and innovation strategy be put in place. An Innovation Strategy for 2007-2013 and related legislation have been drafted, but not yet approved. This delays the establishment of long-term priority areas for R&D investment and the allocation of appropriate support from public R&D programmes. The public R&D support agency has been reformed and has started to implement programmes. However, the reform of research undertaken by the higher education system has been delayed.
15. In the area of Information Society, the progress achieved in implementing e-government measures needs to be backed up by the implementation of the “Roadmap for the introduction of public administration electronic services” and of related legislation. Digital literacy is consistently supported. More should be done to increase broadband deployment and the take-up of ICT.

16. Overall progress in the micro-economic area has been mixed. A number of policy reviews and studies announced in the NRP have been completed, but little information is provided on subsequent planned policy initiatives. Specific strategies, measures and time lines are missing. The main micro-economic challenges and priority areas are rightly identified, but a stronger commitment to advance with implementation is needed.

Employment policies

17. Four key priorities are identified by Slovakia in the field of employment: achieving a high employment rate; a modern educational policy; coping with demographic changes; and promoting social inclusion. Last year's APR identified three areas requiring further attention: tackling regional disparities; structural unemployment; and integration of vulnerable groups such as disabled people and the Roma minority.
18. In order to attract and retain more people in employment, several legislative amendments and measures have been put into practice. This has helped lead to an increase in the employment rate (57.7% in 2005) and a decrease in unemployment (from 18.2% in 2000 to 16.4% in 2005). Changes in the tax system have slightly reduced the overall tax burden and increased support for working parents. However, social contributions remain high and combined with the increased minimum wage may discourage job creation and promote undeclared work. New employment legislation aims to improve employment conditions, encourage self-employment, and strengthen the focus of active labour market policies on certain disadvantaged groups. Employment support for disabled people has been made more efficient and increased in scale.
19. A new strategy has been formulated for the reconciliation of work and family life, aiming at increasing female employment. However, the high gender pay gap remains unaddressed. To support mobility and decrease regional employment disparities, a new allowance has been introduced for commuters, replacing the previous mobility benefit, which had proved inefficient. A better synergy between housing, employment and regional development policies still needs to be created. Labour market policy needs to take account of the different needs of regions, depending on their level of economic development. In spite of the positive labour market developments for youth and older people specific active labour market measures for young people and a comprehensive active ageing strategy are required. Another disadvantaged group in a critical employment situation is the Roma minority, forming a substantial part of the long-term unemployed. The high long-term unemployment rate has remained almost unchanged since 2000 (11.8%) and requires more attention.
20. The long-term objective to reduce the tax and social security burden has been addressed by increasing the tax exempted part of income. The government has announced changes to the Labour Code to increase the level of employment protection legislation to create incentives to encourage flexible forms of work organisation and to encourage the employment of disadvantaged groups. However, the overall impact on employment growth remains to be seen. There is little progress in raising one of the lowest participation rates of adults in training in the EU. Preparation of the lifelong learning strategy has been ongoing for several years and is now postponed until 2007.

21. With the aim of increasing investment in human capital, the government's commitment to support a knowledge-based society implies more funding. The planned reform of the university education system has been launched and the adoption of first legislative changes implemented during 2006. The essential reform of primary and secondary education has been postponed until 2007-2008 and the revision of the curricula does not seem to be progressing sufficiently. Nonetheless, Slovakia meets the EU-wide education and training targets of 10% early school leavers rate (5.8% in 2005), and 85% for the population of 22 year olds having completed upper secondary education (91.5%).
22. Since the presentation of the NRP, good progress can be seen in the support of employment growth through tax incentives and reformed employment services for certain target groups. Despite the positive trends in the overall employment situation in Slovakia, there are still groups of unemployed people requiring more attention. Employment growth amongst young people and older workers has not been sufficiently backed up by targeted active labour market policies. The employment situation of the Roma population is not sufficiently addressed. The reform of the educational system and preparation of the lifelong learning strategy has not advanced sufficiently to ensure the adaptation of acquired skills to emerging and changing labour market needs.

PART III: CONCLUSIONS

23. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
24. Slovakia is making progress in the implementation of its National Reform Programme. However, important challenges and the need for further measures remain, particularly in the microeconomic and employment fields. Progress has been mixed in meeting the commitments made at the 2006 Spring European Council.
25. Among the strengths of the National Reform Programme and its implementation are: policies to improve the business environment and create an information society are now beginning to pay off; employment growth has been strengthened by new tax incentives, mobility measures and some improvement in the service offered to certain disadvantaged groups; and progress in the reform of tertiary education alongside new measures to support ICT use and the integration of disadvantaged children into education system.
26. The policy areas in the Slovak National Reform Programme where weaknesses need to be tackled with the highest priority are: within the context of fiscal consolidation, redirecting more resources to R&D, innovation and education and developing clear strategies and priorities in these areas; reinforcing action on improving skills and lifelong learning; and additional efforts to reduce long-term unemployment, especially among vulnerable groups including the Roma minority. Against this background, it is recommended that Slovakia:

- reallocate expenditure towards R&D and education and complete the development of a coherent national R&D and innovation strategy, with strong interconnections between research institutions and business;
- adopt a lifelong learning strategy that addresses the needs of the labour market and improves qualification levels and skills, and complement the reform of tertiary education with reform of primary and secondary education;
- develop a comprehensive approach to tackling long-term unemployment, notably by developing targeted active labour market policies for the most vulnerable groups.

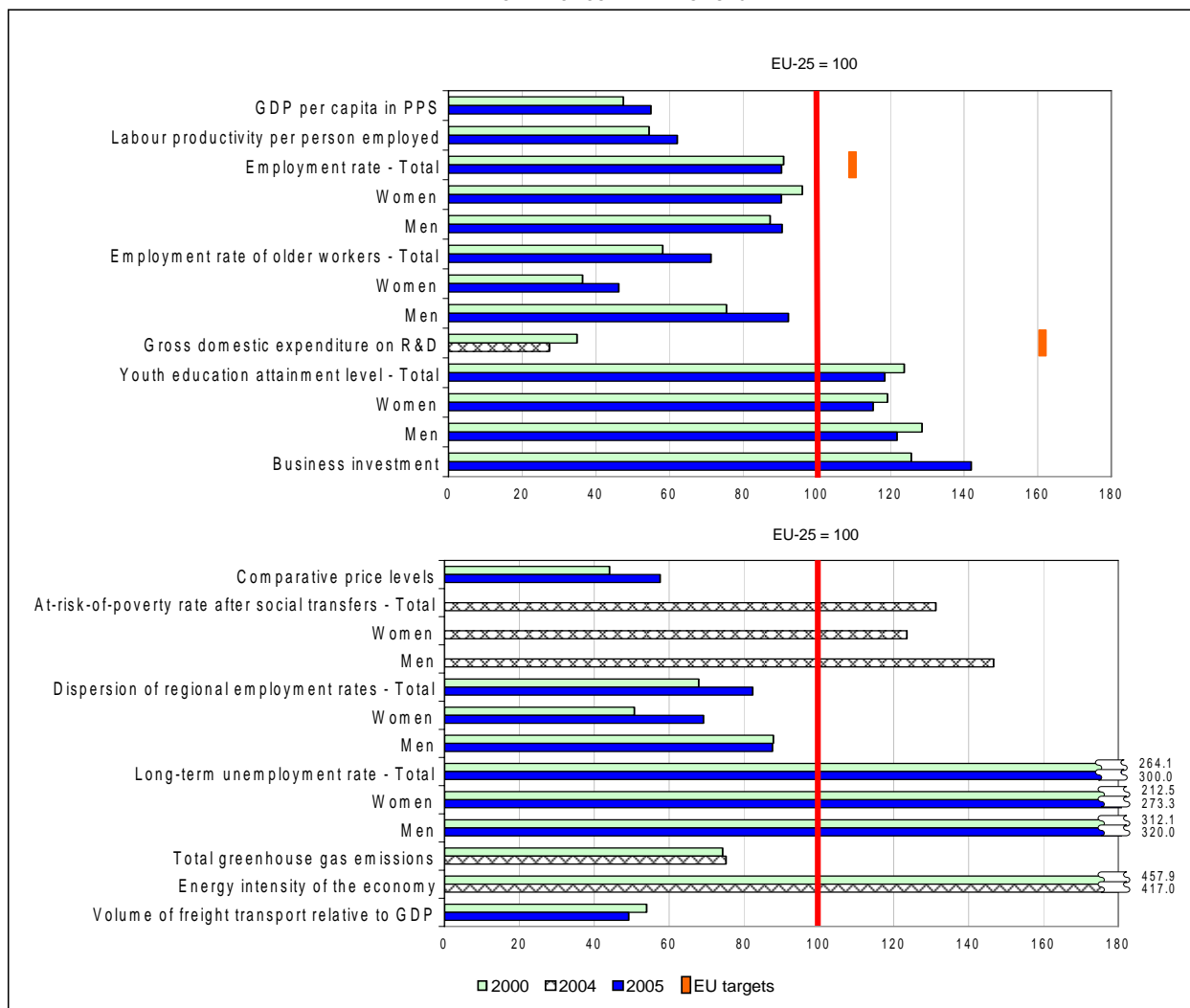
27. In addition, it will be important for Slovakia over the period of the National Reform Programme to focus on: continued efforts on ICT policies, especially on broadband infrastructure; improvements in the better regulation system; addressing the gender pay gap; and developing an active ageing strategy to increase employment of older workers.

PART IV: STATISTICAL GRAPHS AND DATA

SLOVAKIA

	SK							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	47.5	48.5	51.0	51.9	52.9	55.0		100.0	100.0	100.0	
Labour productivity per person employed	54.5	55.9	58.9	58.8	60.3	62.1		100.0	100.0	100.0	
Employment rate							:				70.0
Total	56.8	56.8	56.8	57.7	57.0	57.7		62.4	63.3	63.8	
Women	51.5	51.8	51.4	52.2	50.9	50.9		53.6	55.7	56.3	
Men	62.2	62.0	62.4	63.3	63.2	64.6		71.2	70.9	71.3	
Employment rate of older workers											
Total	21.3	22.4	22.8	24.6	26.8	30.3		36.6	41.0	42.5	
Women	9.8	9.8	9.5	11.2	12.6	15.6		26.9	31.7	33.7	
Men	35.4	37.7	39.1	41.0	43.8	47.8		46.9	50.7	51.8	
Gross domestic expenditure on R&D	0.65	0.63	0.57	0.58	0.51	0.51	0.8	1.86e	1.86e	:	3.0
Youth education attainment level											
Total	94.8	94.4	94.5	94.1	91.7	91.8		76.6	77.1	77.5	
Women	94.8	95.1	95.4	94.5	92.0	92.6		79.5	80.1	80.3	
Men	94.8	93.8	93.5	93.7	91.3	91.0		73.7	74.2	74.7	
Comparative price levels	44.1	44.6	44.6	50.5	54.9p	57.6p		100.0	100.0p	100.0p	
Business investment	23.0	25.4	24.1	22.4	21.7	24.7		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	:	:	:	21.0	21.0p	:		16.0e	16.0e	:	
Women	:	:	:	21.0	21.0p	:		17.0e	17.0e	:	
Men	:	:	:	21.0	22.0p	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	9.1	8.3	7.3	7.6	9.0	9.8		13.4	12.2	11.9	
Women	10.4	9.8	8.8	9.0	10.5	11.7		20.5	17.3	16.9	
Men	8.7	7.3	6.1	6.7	8.1	8.5		9.9	10.2	9.7	
Long-term unemployment rate											
Total	10.3	11.3	12.2	11.4	11.8	11.7		3.9	4.1	3.9	
Women	10.2	11.3	12.5	11.7	12.4	12.3		4.8	4.7	4.5	
Men	10.3	11.3	11.9	11.3	11.3	11.2		3.3	3.6	3.5	
Total greenhouse gas emissions	67.4	71.7	69.0	69.8	69.7	:		90.7	92.7	:	
Energy intensity of the economy	955.9	1015.8	976.0	929.6	854.3	:		208.8	204.9	:	
Volume of freight transport relative to GDP	54.1	50.0	47.3	48.3	48.1	51.5		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25



Finland

Assessment of National Reform Programme

1. Finnish GDP growth has expanded at an annual rate of 3.5% during 1995-2005 and is expected to peak at 4.9% in 2006, which is well above the EU average. Although labour productivity per person employed has been above the EU average over the last decade, there are marked differences between sectors. GDP per capita is estimated to attain 116% of the EU average in 2006. The employment rate is expected to reach 69.5% in 2006. During recent years, it has increased in all age groups, especially among older people. For women, the employment rate is high, at 66.5% in 2005. The unemployment rate is estimated to decline to 7.7% in 2006, which is only slightly below the expected EU average (8.0%).
2. While Finland's growth performance has been very good, some structural challenges remain in the operation of labour, goods and services markets, as indicated by persistently high unemployment and high relative price levels. Higher public sector productivity and pension reform would both have important positive effects on increasing the growth potential of the economy. Improvements in the functioning of the labour market may lead to counterbalancing the decline in the working age population and help maintain the sustainability of public finances. Strengthened competition in goods and services markets would have a positive impact on consumer choice, productivity and job creation.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) presented three medium-term challenges: the sustainability of public finances, improving competitiveness and productivity; and improving the functioning of the labour market. These challenges are defined in a very broad sense and linked to eleven macro, micro and employment key priorities. The Commission broadly shared this analysis of the main priorities, but considered in its 2006 Annual Progress Report (APR) that a stronger response was needed regarding competition in services and employment of certain categories of workers.
4. Though detailed information is not always provided, the 2006 Implementation Report shows that Finland is generally making very good progress with the implementation of its 2005-2008 NRP, especially on policies to improve the sustainability of public finances, the further strengthening of the knowledge economy and employment of elderly workers. Some progress has been made in ensuring the availability of skilled labour in order to prevent bottlenecks on the labour market and in introducing further activation measures to increase employment among certain groups, such as young people at high-risk of unemployment, the unemployed themselves and the low-skilled. Limited progress has been achieved on increasing competition in the service sector, especially in retail trade.
5. Finland is generally responding well to the commitments made by the 2006 Spring European Council. An ambitious target for R&D expenditure has been set for 2010.

Progress has been made on the business environment for SMEs. Steps have been taken towards ensuring young unemployed people get early access to a job or to training. However, no measures have been taken to allow recruitment of the first employee through a single contact point.

6. Extensive attention is paid to ownership, and the governance of the Growth and Jobs Strategy in Finland has gained visibility through a broad-based consultation of government officials and a wide range of stakeholders and representatives of NGOs. The Finnish objective for 2007-2013 is to allocate at least 75% of Structural Funds financing to know-how, innovation activity, R&D, entrepreneurship and employment. This would make the National Strategic Reference Framework (NSRF) for the investment of Structural Funds consistent with the objectives of the Lisbon agenda. It is essential to ensure coherence between NSRF and NRP processes at the planning, implementation and reporting levels.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The overarching policy goal identified in the NRP is to ensure the sustainability of public finances in the face of demographic change. Whilst Finland's overall macro-economic performance is quite strong, new challenges will be faced in the medium and long term. Within the main key challenge of promoting sustainability of public finances, key priorities are controlling public expenditure, ensuring the capacity to fund welfare services and improving public sector productivity.
8. The measures designed for boosting public sector efficiency and the quality of services are progressing beyond their initial stages of implementation. Timely progress has been made in implementing the public sector productivity programme for the central government, a programme assessing income and expenditure for local governments and a project to reform municipal and social services structures. Even though the personnel reduction target set for the central government productivity programme has been lowered, the overall impact is still expected to be significant. The reform efforts targeted on local government will only yield the anticipated effects in the medium to long term. Local government is expected to remain in slight deficit for the next years and is expected by the Finnish authorities to achieve fiscal balance by 2010.
9. The phasing in of a pension reform and the maintenance of central government spending limits are advancing according to initial plans and targets. The pension reform package is being further supported by legislative changes related to the investment and management of employment pension funds, which is expected to increase the returns on investments. The legislative changes are due to enter into force at the beginning of 2007. The central government spending limits have been successful in containing expenditure and have secured the present government's objective of achieving balance in central government finances under conditions of normal economic growth.
10. Finland has in general made good and timely progress in implementing the specific macro-economic measures outlined in the NRP. The measures should contribute to

the long-term sustainability of public finances and help address long-term challenges arising from population ageing.

Micro-economic policies

11. The 2005-2008 NRP prioritised, within the main micro-economic key challenge of improving competitiveness and productivity, the functioning of markets and competition; knowledge and innovation; entrepreneurship; ICT and transport networks; energy and climate policy.
12. The NRP outlines many valuable micro-economic policy measures that should stimulate growth and jobs and contribute to the central target to increase labour productivity by 2.5% yearly. While this target was announced in the NRP it is not confirmed in the Implementation Report. The low productivity growth in the services sector is partly related to insufficient competition in some branches. The commitment to analyse competition issues in depth is encouraging. A comprehensive study on the Finnish service sector was published this year, which highlights that since the service sector is very heterogeneous, it is difficult to issue common recommendations on reforming this sector. Opportunities for more specific measures targeting specific services where there are clearly identified competition issues are not mentioned. Reform of regulatory bottlenecks would also be beneficial. New legislation has put the Competition Authority in a better position to promote competition. For example, there is a more efficient supervision of anti-competitive practices, the Competition Authority is active in identifying and removing obstacles to competition, and a programme has been introduced foreseeing immunity from and reduction of fines for firms revealing cartels (leniency programme). However, the extent to which the functioning of the Competition Authority has changed in practice is unclear from the Implementation Report. To address the issue of slow procedures in competition cases, the resources of the "market court" (*markkinatuomioistuin*) are further increased. The initiative to review and evaluate state aid policy and reduce the overall aid level is welcome.
13. Finland has set an R&D spending objective of 4% of GDP in 2010. This is ambitious given that current R&D expenditures remained constant at 3.5% of GDP and that public spending on research does not seem to have increased in line with earlier targets. Key challenges identified in the Implementation Report are to convert new knowledge into practical applications and to broaden innovation policy to the service sector. A strategy was presented in June 2006 to develop science and technology clusters and centres of excellence for the programme period 2007-2013 in several sectors. The Structural Funds will be used to promote networking in order to create more regional opportunities for innovation. A significant step was recently taken to protect intellectual property rights. A new law on the intellectual property right to university inventions and an amendment to the law on the right to employee inventions were approved in May 2006, aiming to promote recognition and the commercial use of inventions originating from academic research. The Implementation Report does not refer to specific measures to encourage public procurement of innovative products and services.
14. The reported increase in the number of SMEs is a positive development. Efforts to promote growth-oriented innovative start-ups, for example by increasing the availability of venture capital, are positive steps. Despite the fact that recruitment

procedures are relatively burdensome compared to many other countries, the Implementation Report does not include specific measures regarding the recruitment of the first employee. Finland's Better Regulation programme and the planned impact assessment system have the potential to further improve the business environment. Administrative costs have been limited by reducing the number of notifications businesses are required to deal with, and through the use of electronic data transfer systems. Insolvency legislation will be revised to make restructuring proceedings more efficient. Finland has set the objective of increasing flexibility and competition in public procurement, and has made a commitment to constantly monitor the implementation of the EU public procurement directives. Non-legislative measures undertaken include a public procurement advice centre, jointly established by the Ministry of Trade and Industry and the Association of Finnish Local and Regional Authorities, which provides free advice on tendering procedures. Online public procurement market places have also been set up to facilitate enterprises' access to tender notices and to documentation.

15. Finland is an important producer and user of ICT, but there remains considerable scope for further uptake. The overall objective of the Information Society Programme is to create the conditions to boost productivity in industry and public administration through a more efficient use of ICT. Implementation of the NRP has resulted in rising broadband penetration and increased resources devoted to IT security to bolster confidence in electronic services. One of the technology clusters in the 2006 national strategy is devoted to ICT products and services. The report presents a number of measures aiming at stimulating ICT uptake by SMEs, although most of them are still in the development phase.
16. The Commission welcomes the fact that a national Environmental Technology Action Plan has been drawn up and implementation has started. Finnish estimates of the reasonable potential for increasing the efficiency of energy use are much lower than in the EU Green Paper on Energy Efficiency because most of the proposed measures have already been implemented. No action has been taken regarding the ecological tax reform to promote sustainable development.
17. Overall, Finland has made good progress with the implementation of measures responding to its micro-economic key challenges. Regarding the functioning of markets and competition, it is important to keep momentum behind the planned reform agenda, and to guarantee sufficient resources for the competition authorities and courts.

Employment policies

18. Within the main employment challenge of improving the functioning of the labour market, the NRP identified as key employment priorities: extending working life; improving the incentives of tax and benefit systems; wage formation; and improving the balance between labour demand and supply. The focus is on increasing labour supply at both ends of the working age population. The 2006 APR considered that a stronger response was needed regarding increasing employment of certain categories of workers.
19. Measures to extend careers seem to be having the desired effect, although those for speeding up graduation and postponing retirement are too recent to be assessed

reliably. The employment rate of older workers has increased by more than ten percentage points since 2000 to 52.7% in 2005. Youth unemployment is decreasing but remains relatively high. The Social Guarantee, which calls for early intervention within three months of the beginning of an unemployment spell, is a step towards reinforcing services for young unemployed people. However, further measures are needed to activate young people, especially those in high-risk groups, and also to activate other groups such as the unemployed, the proportion of whom receiving active support has declined since 2003, and the low-skilled. Recent reforms helping to activate labour market support and implement services through the "Labour Force Service Centres" seem to have reduced structural unemployment, which nevertheless remains high. The proportion of job vacancies that is filled has slightly fallen, pointing towards mismatches in the functioning of the labour market. The emphasis in the tax and benefit reform is on low-paid jobs and the effect of this reform on the employment rate needs to be carefully monitored. The exceptionally high number of fixed-term contracts for women (mainly in the public sector) is not discussed. Addressing this issue would help increase the employment rate. A new immigration policy programme was launched in 2006, which seeks to promote employment-based immigration. In 2006 Finland lifted limitations to free movement from EU-10 and decided not to impose limitations for Bulgaria and Romania.

20. Working life development programmes have increased well-being at work and helped encourage workers to remain longer in employment. Some new initiatives have been introduced to increase geographical mobility. No progress has been made in encouraging local wage bargaining systems, as described in the NRP last year.
21. The focus in reforming the framework for human capital investment aimed at the young has been on the age cohort leaving basic education and on minimising early school leaving. The number of pupils continuing education post-basic schooling has risen slightly but consistently. However, the number of early school leavers has increased and is much higher among young men. Addressing this requires a more comprehensive strategy covering the earlier stages of life, and closer co-operation between administrators to increase guidance and counselling at the earliest possible stage. The participation rate in education and training is well above the EU average and has increased in all age groups, except for 55-64 year-olds. Continuing training programmes for the low-skilled are needed to further increase the employment rate among older people.
22. Overall progress in the employment field is encouraging, especially bearing in mind that the effects of many reforms cannot be fully assessed for a number of years. The government target of 100,000 new jobs by next spring is close to being met. However, it is essential, in order to prevent labour market bottlenecks from affecting economic growth, to ensure the availability of skilled labour supply through employment-based immigration and further activation measures for certain groups.

PART III: CONCLUSIONS

23. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:

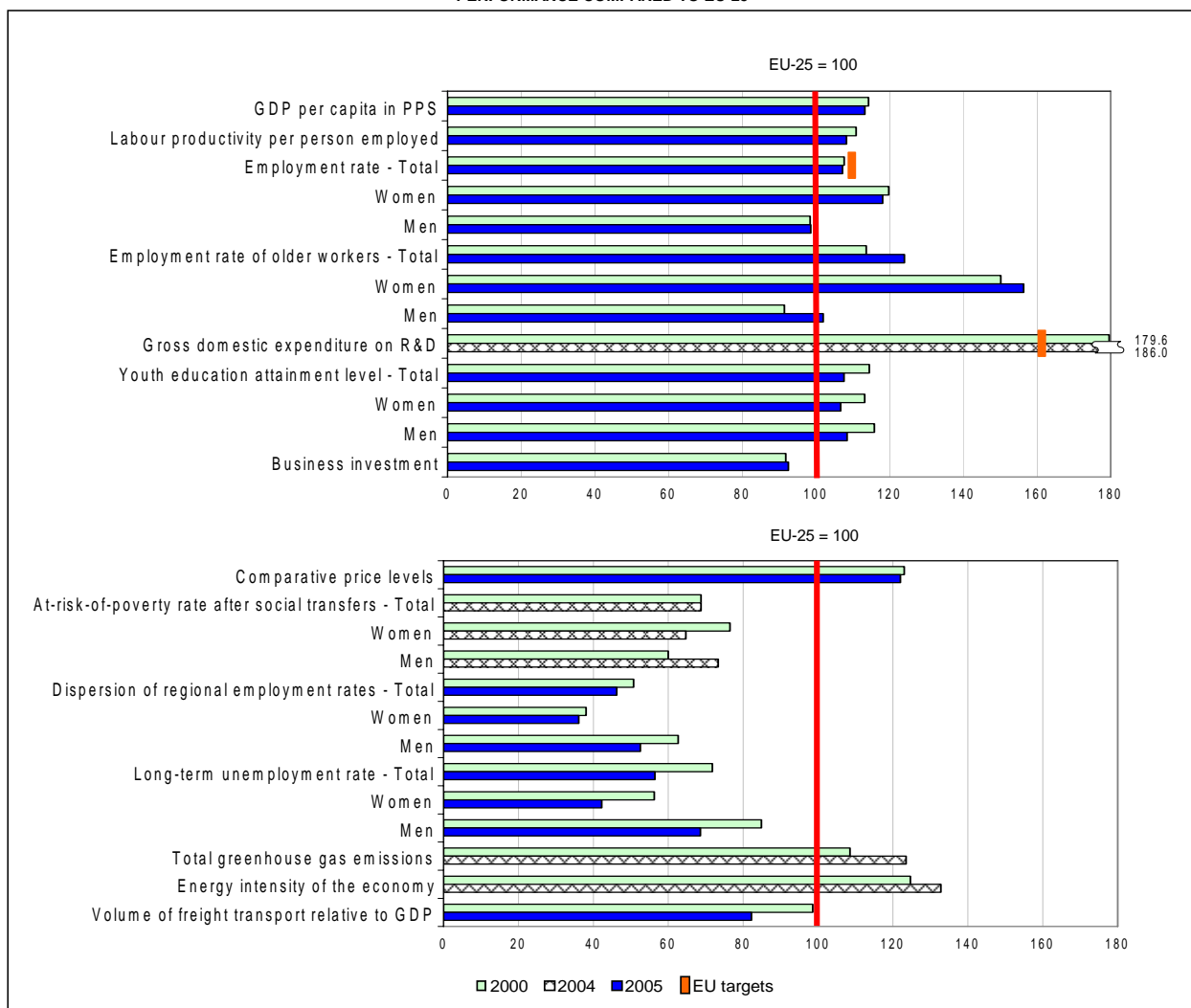
24. Finland is making very good progress in the implementation of its National Reform Programme. Finland is also generally responding well to the commitments made by the 2006 Spring European Council. Progress has been made in particular on the business environment for SMEs.
25. Among the many strengths of the Finnish National Reform Programme and its implementation are: further action to postpone retirement, complementing the already extensive action to strengthen sustainability of public finances and to prepare Finland for the effects of an ageing population; a range of important measures to further improve Finland's excellent knowledge base.
26. It will be important for Finland over the period of the National Reform Programme to focus on: implementing reforms to improve competition and productivity in services; simplifying recruitment procedures for businesses, including through specific measures regarding the recruitment of the first employee; encouraging local wage bargaining systems; and addressing bottlenecks in the labour market, with a particular view to increasing the low participation of youth and tackling high structural unemployment.

PART IV: STATISTICAL GRAPHS AND DATA

FINLAND

	FI							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	114.3	115.5	114.7	112.6	113.7	113.3		100.0	100.0	100.0	
Labour productivity per person employed	110.9	111.8	110.3	108.4	109.4	108.3		100.0	100.0	100.0	
Employment rate							75.0 (2011)				70.0
Total	67.2	68.1	68.1	67.7	67.6	68.4		62.4	63.3	63.8	
Women	64.2	65.4	66.2	65.7	65.6	66.5		53.6	55.7	56.3	
Men	70.1	70.8	70.0	69.7	69.7	70.3	71.2	70.9	71.3		
Employment rate of older workers											
Total	41.6	45.7	47.8	49.6	50.9	52.7		36.6	41.0	42.5	
Women	40.4	45.0	47.2	48.3	50.4	52.7		26.9	31.7	33.7	
Men	42.9	46.6	48.5	51.0	51.4	52.8		46.9	50.7	51.8	
Gross domestic expenditure on R&D	3.34	3.30	3.36	3.43	3.46	3.48	4.0	1.86e	1.86e	:	3.0
Youth education attainment level	87.7	86.1	85.8	85.3	84.5	83.4		76.6	77.1	77.5	
Total	90.0	89.4	89.0	87.6	87.0	85.7		79.5	80.1	80.3	
Women	85.4	82.8	82.6	83.0	81.9	81.0	73.7	74.2	74.7		
Men											
Comparative price levels	123.0	122.8	124.4	125.9	122.9p	122.0p		100.0	100.0p	100.0p	
Business investment	16.8	16.9	15.2	15.2	15.4	16.1		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	11.0	11.0b	11.0	11.0	11.0b	:	16.0e	16.0e	:		
Women	13.0	12.0b	12.0	12.0	11.0b	:	17.0e	17.0e	:		
Men	9.0	10.0b	11.0	11.0	11.0b	:	15.0e	15.0e	:		
Dispersion of regional employment rates											
Total	6.8	7.0	6.7	6.1	5.5	5.5	13.4	12.2	11.9		
Women	7.8	8.1	7.6	6.7	6.2	6.1	20.5	17.3	16.9		
Men	6.2	6.4	6.3	5.7	5.2	5.1	9.9	10.2	9.7		
Long-term unemployment rate											
Total	2.8	2.5	2.3	2.3	2.1	2.2	3.9	4.1	3.9		
Women	2.7	2.3	2.0	2.0	2.0	1.9	4.8	4.7	4.5		
Men	2.8	2.7	2.5	2.6	2.3	2.4	3.3	3.6	3.5		
Total greenhouse gas emissions	98.4	106.0	109.0	120.5	114.5	:	90.7	92.7	:		
Energy intensity of the economy	260.1	263.8	272.2	280.1	272.1	:	208.8	204.9	:		
Volume of freight transport relative to GDP	98.7	92.2	93.6	90.5	90.5	86.1	100.1e	104.6be	104.7e		

PERFORMANCE COMPARED TO EU-25



Sweden

Assessment of National Reform Programme

1. Swedish real GDP growth has been slightly below 3% on average over the last decade and Sweden is in a good position in the EU with respect to GDP per capita (115.6% of EU average in 2006), productivity and employment levels. Labour productivity growth has been just above the EU average. The employment rate is one of the highest in the EU (72.8% in 2006). Employment growth has started to pick up, having been weak over recent years, and the previously increasing unemployment rate (7.3% in 2006) has started to come down.
2. Sweden benefits from a currently strong economic performance. The main challenges are in the medium to long term, in particular given an ageing population. Within stability-oriented macro economic policies, including strong and stable public finances, the ability to finance future increases in welfare expenditures would seem to rely on an increase in the hours worked in the economy. While employment rates are high, they are still lower than in the past. Raising them would require increasing labour supply through strengthening incentives to work and a stronger inclusion in the labour force of certain groups. A higher level of competition would be equally important in contributing to the growth potential.

PART I: GENERAL ASSESSMENT

3. The Swedish 2005-2008 National Reform Programme (NRP) emphasised the need for high levels of labour market participation and hours worked as well as the promotion of a knowledge-based economy with environmentally-efficient production processes. The Commission recommended in its 2006 Annual Progress Report (APR) that further attention be given to enhancing competition in services and to increasing labour supply including via incentives in tax and benefit systems. The 2006 Implementation Report presented as an updated NRP by the new government broadly confirms the overall objectives but puts increased focus on further measures to increase labour supply and conditions for job creation.
4. Sweden is making good progress in taking forward the overall reform agenda. The macroeconomic framework conditions remain beneficial. Sweden has made good progress on SME policy. There are planned increases in public R&D funding which will bring the 1% of GDP target within reach. Some progress has been made in strengthening general competition policy but less in enhancing competition in services. This is, however, an area in which the new government intends to take further steps. There has been good progress towards making work pay through proposed changes in labour taxation and unemployment benefit systems. Some progress has been made in cutting numbers on sick leave but the number of people in more long-term sickness and activity schemes remains high. Measures have been presented with a view to streamlining and increasing the efficiency of the available active labour market programmes. Increasing the lower participation rate of immigrants and the number of hours worked overall remain challenges.

5. Progress towards meeting the commitments made by the 2006 Spring European Council is in general good. The youth unemployment rate is high and increased in 2005, but nearly all youth receive a new start within the targeted six months. However, no information is provided on setting up a single administrative contact point for recruiting the first employee.
6. Consultation and efforts to develop ownership of the NRP have been substantial. The political visibility of the Strategy for Growth and Jobs has been improved by assigning responsibility at ministerial level. The Programme has been presented to Parliament for discussion. Contributions to the Implementation Report have been received from social partners, including local and regional public authorities. Discussions with civil society representatives have taken place. The National Strategic Reference Framework has been prepared in line with the NRP.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The macro-economic strategy presented in the 2005 NRP is confirmed in the 2006 Implementation Report. This strategy aims for sound public finances within the national rules-based framework, low and stable inflation guaranteed by the independent central bank and wage setting in line with productivity. Overall, in the medium to long term, reaching a high level of employment and raising hours worked in the economy are key objectives to sustain public welfare commitments. This is to be achieved through increased labour market participation and a higher rate of job creation. As regards fiscal policy, this continues to be set with the objective of a general government budget surplus of 2% of GDP on average over the economic cycle and with rolling three-year nominal expenditure ceilings. The Implementation Report confirms the commitment to the national budgetary rules but announces that a review will be initiated to develop them further.
8. The general government budget balance surplus was 3% of GDP in 2005 and is expected to be of a similar magnitude in 2006. This is in line with the national objective of a 2% of GDP surplus. In addition, local authorities' financial position has improved markedly. The inflation rate has remained low, although in the light of a projected increase in inflation, the central bank (Riksbanken) has implemented a series of interest rate increases. Employment growth has improved and unemployment decreased. The 2007 budget includes proposals for changes in tax and benefit systems strengthening incentives to work. Wage developments have remained in line with productivity trends and in this respect the outcome of the 2007 private sector wage round will be an important test of the credibility of the wage-setting framework, given the currently strong cyclical position.
9. The 2005 NRP mentioned ongoing investigations in a number of areas such as the efficiency of the welfare insurance system and how the responsibilities are divided across different levels of government. The NRP also signalled the intention to conduct a general overview of the efficiency of the tax system since the 1990/91 reform. The Implementation Report does not provide any further information on the status and progress of these investigations. However, it does contain a number of measures and objectives for tax and benefit systems.

10. Overall, the stability-oriented framework is well-rooted. The short-term outlook remains conducive to Sweden continuing to achieve its macro-economic policy objectives.

Micro-economic policies

11. The government aims to strengthen R&D by providing additional funds over the period 2007-2009. With these budgetary increases, Sweden would come very close to reaching the 1% of GDP target for public R&D and with some further efforts the target is definitely within reach. Measures to improve the regulatory framework for the protection of intellectual property, particularly for smaller companies, are welcome. Initiatives have been taken to promote R&D in SMEs. However, there is scope for a stronger emphasis on the role of SMEs in the R&D and innovation system, including further measures focusing on research-driven and innovative SMEs, particularly encouraging links with larger firms and with the university sector. Improved linkage between industrial and research priority setting would also contribute to leveraging private R&D funding and the commercialisation of high-tech products and services. The implementation of the six sectoral industrial strategies presented in late 2005 should contribute to this. Clearer delimitation of the roles of the various public sector actors in the R&D and innovation system (ministries, agencies) would facilitate a better link between policy objectives and implementation. A review of the existing model for cooperation between public and private actors, in order to establish better cooperation in the framework of long-term development projects, would also be useful.
12. Progress in improving the business environment through better regulation is mixed: simplification measures are being taken and an ambitious overall target to reduce administrative burdens by at least 25% by 2010 has been set. However, improvement of the impact assessment system and development of a more coherent approach to better regulation is still pending. To stimulate entrepreneurship, work by international comparisons, work to create a more competitive business environment is being stepped up, as are measures to facilitate access to risk capital and reduce or phase out taxes and insurance contributions. Measures are also foreseen to encourage entrepreneurship among women, immigrants and young people. Apart from measures to promote needs-motivated R&D, the six sectoral industrial strategies also focus on skills provision, test and demonstration projects, export and investment promotion and cooperation with the business community, all with the aim of strengthening the competitiveness of the industrial base.
13. The Implementation Report acknowledges the need to strengthen competition law and its implementation. Proposals for regulations spelling out heavier fines for serious infringements are envisaged. Furthermore, the expected adoption of a new law on public procurement is expected to remedy some of the (acknowledged) problems in the area of direct procurement. The Competition Authority has recommended that bidding for public contracts be facilitated, that coordinated purchasing should not be too extensive and that public procurement rules be simplified. However, further efforts to enhance competition, especially in services, are needed. The increased focus on ensuring equal conditions of competition for public and private operators is a welcome development in this regard.

14. As regards improving public sector efficiency and services to citizens and business, the e-government proposals are appropriate, but would gain from being accompanied by a precise timetable for implementation. The initiated project for benchmarking local government performance in terms of quality and productivity is welcome.
15. Sustainable use of resources remains a high priority for Sweden. Measures encouraging consumption of energy from renewable sources, promoting climate-related research and investment, and improving incentives for households and industry to increase energy efficiency are combined with measures that could drive growth over time by promoting environmentally friendlier technologies, fuels and vehicles.
16. The Commission's assessment of the innovation and ICT strategies is positive. There are strong measures to promote entrepreneurship. Despite some encouraging progress on improving the business environment and boosting competition, additional micro-economic measures, following the work of the committees of inquiry concerned, could usefully be taken to promote a more effective market for services and to improve the efficiency of the public services.

Employment policies

17. The 80% employment rate and 4% unemployment target mentioned in the NRP are no longer official government policy objectives. The Implementation Report does not refer to new national employment targets but increasing labour supply and hours worked remains a priority. The report includes several proposals to make work pay in order to increase labour supply. Unemployment benefits will be further restricted in duration and level, while taxes will be reduced, especially for low and middle income earners, in order to make work more attractive. Furthermore, it will be mandatory to belong to an unemployment insurance fund and employees' own contributions will increase. To strengthen the incentive to employ – in particularly those furthest from the labour market - the government has proposed that the employers' contribution will be abolished for people who have been receiving benefits and social welfare assistance for more than a year and for newly arrived immigrants ("New Start Jobs"). To facilitate young people's entry into the labour market, a special allowance in employers' contributions will be introduced. Given the persistently high employment gap between immigrants and the native-born population (15 percentage points in 2005) and the high unemployment rate among young people these measures are welcome.
18. A job and development guarantee is planned for those who have received unemployment benefit for 300 days. To increase incentives to return to work, changes will also be made in the sickness benefit system, coupled with measures to promote more active rehabilitation. The employers' obligation to pay 15% of the employees' sickness benefit after two weeks on sickness leave will be abolished. The Implementation Report includes, however, few alternative measures to reduce the large number of people in sickness- and activity schemes. A number of active labour market programmes which have proved inefficient will be abolished. This may, in the short term perspective, lead to an increase in measured unemployment rates. The National Labour Administration will be reformed to improve the matching of unemployed candidates with appropriate vacancies.

19. While there are no proposals to change the overall employment protection legislation, which in general provides good conditions for combining security on the labour market with a high level of employment, the government intends to return to a proposal that treats older and younger workers equally regarding notice of dismissal. Permanent employment contracts are still the norm although fixed-term contracts will be allowed more widely and for longer periods at the same employer in order to open up broader paths into the labour market. A proposed tax reduction on household services aims to facilitate reconciliation of work and family life and decrease undeclared work.
20. Sweden is performing well on lifelong learning. Educational attainment is high – the proportion of 22 year olds having completed at least upper secondary education is 87.8% and participation in lifelong learning exceeds the EU average. Few new measures are proposed by the new government but its intention is to consider new ways to encourage individuals and employers to allocate resources to lifelong learning. The government's main emphasis is on improving the quality of the whole education system, for example by: improving teachers' skills; early prevention to identify pupils with problems achieving basic skills; reform of upper secondary school with the objective of introducing a clearer vocational orientation; and a new apprenticeship programme. These measures should also contribute to inclusive labour markets by reducing youth unemployment and the employment disparity between immigrants and native-born Swedes.
21. Sweden is performing well in most employment areas. The new measures proposed to boost labour supply are welcome, especially the measures to reform the tax and benefit system, which are likely to be implemented in the short term. To further boost the number of hours worked, especially for certain groups - particularly immigrants, people on sickness related schemes and young people - remains a challenge for Sweden.

PART III: CONCLUSIONS

22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
23. Sweden is making very good progress in the implementation of its National Reform Programme. It addresses most of the commitments made by the 2006 Spring European Council. The stability oriented macro-economic framework is appropriate and performs well. A strong effort is being made to strengthen incentives to work. Additional measures are needed to enhance competition in services.
24. Among the strengths of the Swedish National Reform Programme and its implementation are: the progress made on increasing public investment in R&D and in bringing forward measures to encourage innovation; the vigorous approach to encouraging entrepreneurship; Sweden's performance on encouraging the sustainable use of energy, which is among the best in the EU; progress in increasing labour supply; measures to make it simpler and more profitable to run a business by phasing out taxes and reducing administrative burdens; and proposals to enhance incentives to work, notably changes in labour taxation and benefit systems.

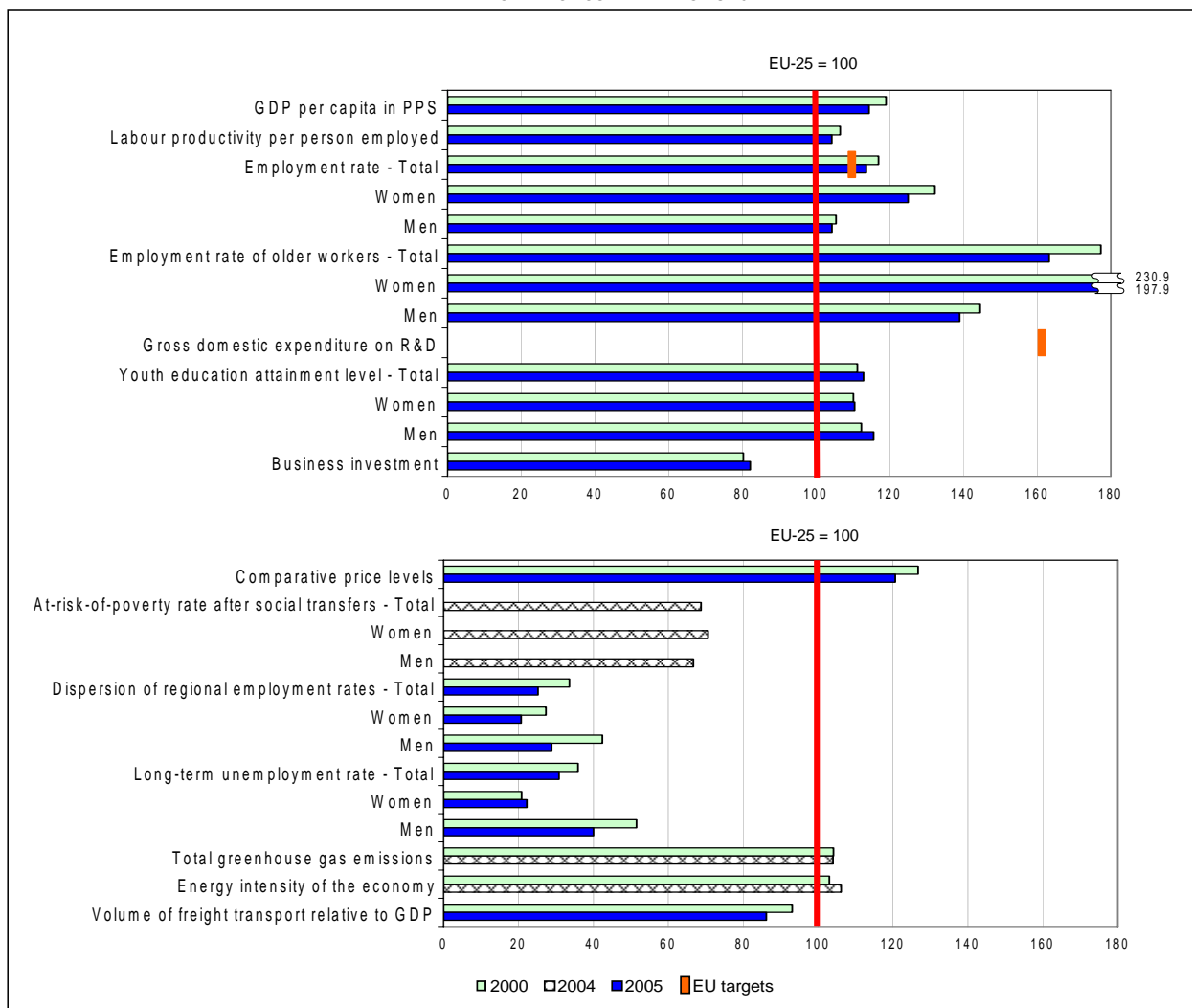
25. It will be important for Sweden over the period of the National Reform Programme to focus on: taking further regulatory measures to increase competition, notably in services; implementing rapidly planned improvements to the impact assessment system; taking a more coherent approach to better regulation, strengthening its strategy to increase labour supply and hours worked, including through the implementation of proposals to increase incentives to work, as well as stronger measures to increase the employment rate of immigrants and young people and to reintegrate people on sickness-related schemes;

PART IV: STATISTICAL GRAPHS AND DATA

SWEDEN

	SE							EU25					
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target		
GDP per capita in PPS	119.0	115.2	113.6	115.6	116.8	114.4	:	100.0	100.0	100.0	70.0		
Labour productivity per person employed	106.6	102.5	101.4	103.9	106.0	104.3		100.0	100.0	100.0			
Employment rate	73.0	74.0	73.6	72.9	72.1	72.5b		62.4	63.3	63.8			
Women	70.9	72.3	72.2	71.5	70.5	70.4b		53.6	55.7	56.3			
Men	75.1	75.7	74.9	74.2	73.6	74.4b		71.2	70.9	71.3			
Employment rate of older workers	64.9	66.7	68.0	68.6	69.1	69.4b		36.6	41.0	42.5			
Women	62.1	64.0	65.6	66.3	67.0	66.7b		26.9	31.7	33.7			
Men	67.8	69.4	70.4	70.8	71.2	72.0b		46.9	50.7	51.8			
Gross domestic expenditure on R&D	:	4.25	:	3.95	:	3.86		4.0	1.86e	1.86e		:	3.0
Youth education attainment level	85.2	85.5b	86.7	85.8	86.0	87.5			76.6	77.1		77.5	
Women	87.6	86.8b	88.3	87.2	87.2	88.7			79.5	80.1		80.3	
Men	82.8	84.2b	85.2	84.3	84.8	86.4			73.7	74.2		74.7	
Comparative price levels	126.7	117.0	121.1	124.0	121.1p	120.6p			100.0	100.0p		100.0p	
Business investment	14.7	14.3	13.3	12.9	13.3	14.3			18.3	17.1		17.4	
At-risk-of-poverty rate after social transfers	:	9.0	11.0b	:	11.0b	:	16.0e		16.0e	:			
Women	:	:	12.0b	:	12.0b	:	17.0e		17.0e	:			
Men	:	:	10.0b	:	10.0b	:	15.0e		15.0e	:			
Dispersion of regional employment rates	4.5	4.2	4.6	4.3	4.4	3.0	13.4		12.2	11.9			
Women	5.6	4.6	4.8	4.8	4.3	3.5	20.5		17.3	16.9			
Men	4.2	4.0	4.5	4.1	4.8	2.8	9.9		10.2	9.7			
Long-term unemployment rate	1.4	1.0	1.0	1.0	1.2	1.2p	3.9		4.1	3.9			
Women	1.0	0.8	0.8	0.8	1.0	1.0p	4.8		4.7	4.5			
Men	1.7	1.2	1.2	1.2	1.4	1.4p	3.3	3.6	3.5				
Total greenhouse gas emissions	94.4	95.3	96.7	97.9	96.4	:	90.7	92.7	:				
Energy intensity of the economy	215.0	228.9	224.3	217.1	217.5	:	208.8	204.9	:				
Volume of freight transport relative to GDP	93.2	88.9	90.6	90.6	88.9	90.2	100.1e	104.6be	104.7e				

PERFORMANCE COMPARED TO EU-25



United Kingdom

Assessment of National Reform Programme

1. The UK's real GDP grew 2.8% on average in 1996-2005 and it is expected to reach 2.7% in 2006. Inflation remained low and stable over this period. In 2006, the employment rate at 71.7% is expected to exceed the target set for the EU as a whole under the Lisbon Growth and Jobs Strategy. The unemployment rate has been broadly stable and low, albeit edging up to 5.6% in 2006. There has been a decline in employment rates in the youngest age group as more stay in education, offset by increasing participation among women and older workers. Youth unemployment has increased. Labour productivity is growing, but from a low level.
2. The UK's steady growth and employment performance is mainly facing a productivity challenge. Labour, capital and product markets are very flexible. Further improvements to intermediate skills and to R&D intensity would contribute to productivity growth. The proposed reform of the pension system would help to increase the low level of private saving and to promote labour supply from older workers, while reducing potential future risks to sustainability of the public finances.

PART I GENERAL ASSESSMENT

3. The main challenges for the UK as described in the 2005-2008 National Reform Programme (NRP) were: 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 endorsed these in its 2006 Annual Progress Report (APR). Among points requiring further attention, the APR noted budgetary consolidation; boosting R&D expenditure; transport infrastructure; and addressing skills and employment prospects for the most disadvantaged.
5. The UK has made good progress towards meeting all the challenges, with action on all the areas where new measures were indicated in the NRP. However, despite initial progress, further measures on R&D, childcare and, especially, skills will be necessary, as well as progress in implementing the proposals for reform of the pensions system.
6. The Implementation Report takes account of the priorities identified by the 2006 Spring European Council and identifies recent action in those fields, for example to make it possible to set up a business in 24 hours. However, no target for total investment in R&D has been set for 2010, corresponding to the timetable for the EU's overall 3% objective. The UK has instead set a target for 2014.
7. Governance is strong in terms of coordination across the different parts of central government. Devolved administrations in Scotland, Wales and Northern Ireland have also been involved in preparing the Implementation Report, in relation to their own

policy responsibilities. The Implementation Report, like last year's NRP, shows a strong degree of internal coherence. The medium-term priorities in government expenditure will be reviewed in 2007. New targets under Public Service Agreements, which underpin the reform agenda in the UK and are used to monitor individual government departments, will be established corresponding to the key Lisbon Growth and Jobs objectives. There has been extensive consultation on many individual policy elements, including a series of Green or White Papers on major reforms. Specific consultation in preparing the Implementation Report included a stakeholder seminar and web-based consultation. The Implementation Report includes several references to the contribution of EU Structural Funds. It cross-references the recent consultation on the forthcoming National Strategic Reference Framework for the investment of those funds.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. In macro-economic policy, pension reform, the quality of public finance and fiscal sustainability have been identified as specific challenges. The existing monetary and fiscal framework is reaffirmed in the Implementation Report. The report focuses on expenditure policy issues and their links with the objectives of the Growth and Jobs Strategy. The Implementation Report also presents the government's proposals to reform the pension system. The NRP does not directly highlight the issue of the projected, but not yet implemented, fiscal consolidation.
9. The pension reform proposals involve increasing the value and coverage of the state pension, while raising the state pension age, and building stronger incentives to work longer and to increase private saving for retirement. These proposals are a significant reform and would help reduce the risk of insufficient provision of retirement income while moderating the risks to the sustainability of the public finances. Some aspects of the reform proposals still need clarification. For example, more detail of the reforms to increase private saving for retirement are expected in a forthcoming White Paper. The impact of pension reforms in terms of changing behaviour will inevitably only be fully evident once they are implemented.
10. The Implementation Report reviews progress against targets to improve the efficiency of public spending, including improving management of government assets and cost-saving relocation of public sector employees away from south-east England. A number of indicators to measure progress are reported, whilst highlighting the risks and the need to strengthen measurement methodologies.
11. The Implementation Report outlines a series of studies which will provide a background for the allocation of expenditure in the UK government's 2007 Comprehensive Spending Review. The strategic and evidence-based approach is welcome, as prioritisation of expenditure will be crucial. While the fiscal outlook has marginally improved since last year's programme, the UK authorities will need to continue to pursue medium-term fiscal consolidation as currently projected. To avoid an increase in the tax burden, a moderation of expenditure growth is required. The UK has acknowledged the need to progressively increase housing supply to reduce

house price pressures in the medium-term, without which there could be an effect on future growth prospects.

12. Overall, some progress in macro-economic policy is being made. Further medium-term fiscal consolidation is required but long-term sustainability of the public finances is not currently at high risk. Successfully implementing proposed pensions reform should remove one risk to sustainability, while helping to increase currently low levels of private savings in the economy and labour supply from older workers.

Micro-economic policies

13. In terms of microeconomic policies, the UK has identified R&D and innovation and the encouragement of entrepreneurship as key micro-economic challenges.
14. The UK has made progress in implementing, monitoring and updating its ten-year Science and Innovation Investment Framework. Particular attention has been paid to maintaining high standards in the public science base and to delivering the UK Technology Strategy. Further development of the policy package is under consideration. This will be needed to achieve the government's own 2.5% of GDP R&D intensity target for 2014. No target for 2010 has been set. When establishing post-2008 public spending priorities and policies, continued account should be taken of the need to strengthen the incentives for private sector investment in R&D and innovation and to continue to increase R&D at regional level. The development of innovation clusters, transnational cooperation and knowledge transfer is being addressed, along with policy measures aiming to stimulate the demand side both at regional and national level. These need to be strengthened within a clearer and more coherent framework. The UK aims to achieve this through the Technology Strategy Board, working with the devolved authorities.
15. Some progress has been made in implementing the announced measures on the business environment, encouraging entrepreneurship and promoting better regulation. The measures taken to integrate entrepreneurship into education are a particular strength. The minimum time for registering a business has been reduced to 24 hours, but VAT registration remains time-consuming. The one-stop-shops for business set-ups are useful but could be more widely publicised. Measures to facilitate SMEs' bidding for public R&D contracts are welcome. Some progress has been made in making smaller public contracts available to SMEs through a web portal, which matches suppliers to public sector opportunities.
16. Funding of rail infrastructure has increased substantially. The London congestion charge is successful and the transport Trans-European Network priority projects have moved forward. However, specific transport needs remain outside the South East, particularly regarding accessibility to local employment opportunities. The implementation of the recently published Eddington Study on the long-term impact of transport decisions provides an opportunity to address this.
17. The UK is advanced in energy market opening. Security of supply, competitiveness, and sustainability are addressed in the July 2006 Energy Review and promoting renewable energies is part of Climate Change Programme 2006. However, more could be done to increase energy efficiency and to promote environmental technologies and the generation of electricity from renewable sources. In this context

recent recommendations by the Stern Review on climate change have relevance not only for the UK but also for other Member States. Implementing these recommendations would constitute an extremely important step forward.

18. Progress on Better Regulation has been strong. The ambitious baseline measurement of administrative burdens in legislation is providing a useful example which can be applied to similar measurements EU-wide, while the recent Davidson review is an example of good practice in making the implementation of EU legislation at national level more efficient and reducing business burdens. Competition policy is also being developed and is working well to continue the development of open and dynamic markets and benefiting consumers in the UK. The implementation of the EU Financial Services Action Plan is well advanced. The implementation of the spectrum review should aim at creating more competition and innovation in electronic communications.
19. Overall, concerning micro-economic policies, progress has been made in each area. However, if the UK is to reach its own R&D intensity target, it will need to implement measures under consideration to further strengthen incentives for private sector investment and engagement in R&D and innovation. On better regulation, the UK demonstrates good practice in piloting many new initiatives over the full range of policy areas, particularly in relation to risk-based approaches to enforcement.

Employment policies

20. The key challenges identified in the NRP were to open up opportunities for sections of the population with low employment rates; and raising the skill levels in the workforce.
21. The government aspires to an employment rate of 80%, which it sees as key to tackling poverty and promoting inclusion. The NRP makes connections to the National Report on Strategies for Social Protection and Social Inclusion. The most important development since the NRP has been the proposed law on welfare reform. Incapacity benefit is to be replaced with an allowance rewarding job seeking while there will be more services to help people back into work. The Pathways to Work programme has been expanded after long pilot projects. For lone parents, there will be a combination of new requirements and rewards for job search. There have been developments to assist other groups with low employment rates, notably the low-skilled unemployed, and to tackle geographic concentrations of unemployment and to improve health at work. In most cases these involve reallocation of money rather than extra spending. While youth unemployment has increased in the past year it is still relatively low in the UK, partly thanks to the effectiveness of existing measures. The government aims to further increase the number of older workers by a million, using policies that combine incentives with other measures. Legislation against age discrimination recently came into force. Good progress from a low base has been made to increase the availability of childcare, but further progress needs to be made. The need for further measures to narrow the wide gender pay gap is acknowledged.
22. The NRP states that "the reform agenda is designed to deliver security throughout the lifecycle by balancing flexibility and fairness". Proposed pension reform, in

particular proposals to extend the coverage of supplementary pensions, and expansion of access to lifelong learning should improve both flexibility and security.

23. A strategy for basic skills has been established in recent years. Programmes for the unemployed lacking basic skills and - in England - for employees lacking qualifications have been expanded in the past year. The strategy for intermediate level qualifications in England is undergoing significant change with new funding arrangements, reform of the curriculum and qualifications, a Green Paper on further education, and the promise of more financial support for individuals. The emphasis of public support nonetheless remains on basic and foundation skills. Based on an earlier review, proposals for further education colleges are being carried out. The new qualifications that are being developed aim for more flexibility, but there is a need to ensure clarity so that qualifications are useful for both individuals and employers. The new measures to encourage training among those in work are likely to lead to positive developments, provided that adequate resources are allocated.
24. Overall, a well-balanced package of policies and wide consultation on areas where fundamental reforms are proposed - such as welfare benefits, pensions, and further education - has led to sound progress in addressing the employment challenges identified last year. Nevertheless, as the report of the Leitch review on training and skills acknowledged, more will need to be done, beyond meeting existing targets, if the UK is to fully realise its ambitions in terms of improving intermediate skills compared with other economies.

PART III: CONCLUSIONS

25. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
26. The UK is making good progress in the implementation of its National Reform Programme and of the commitments made by the 2006 Spring European Council. Solid progress has been made in all policy areas, particularly in micro-economic and employment policy. In macro-economic policy, plans for fiscal consolidation and pension reform have been drawn up and still need to be implemented. The UK has made greater efforts to involve stakeholders.
27. The particularly strong points in the UK reform implementation are in encouraging entrepreneurship, promoting better regulation, and undertaking welfare reforms. Many other successful reforms have already taken place, such as energy market opening, increasing investment in transport infrastructure, and in introducing charging policies, for example the London road transport congestion charge. The UK has also undertaken innovative reforms to improve the quality of public expenditure that are still in the course of implementation.
28. The policy areas in the UK National Reform Programme where weaknesses need to be tackled with the highest priority are: improving skill levels compared with other economies; and taking further measures to tackle disadvantage and exclusion in the labour market. Against this background, it is recommended that the UK:

increase basic and intermediate skills, in order to raise productivity, and further improve employment prospects for the most disadvantaged.

29. In addition, it will be important for the UK over the period of the National Reform Programme to focus on: ensuring that the current proposals on pension reform are effectively implemented; progressively increasing housing supply to reduce house price pressures in the medium-term, without which there could be an effect on future growth prospects; implementing its science and innovation strategy, in the context of which an intermediate R&D target for 2010 should be set and measures should be taken to further strengthen investment incentives and to increase private sector engagement; and improving access to childcare.

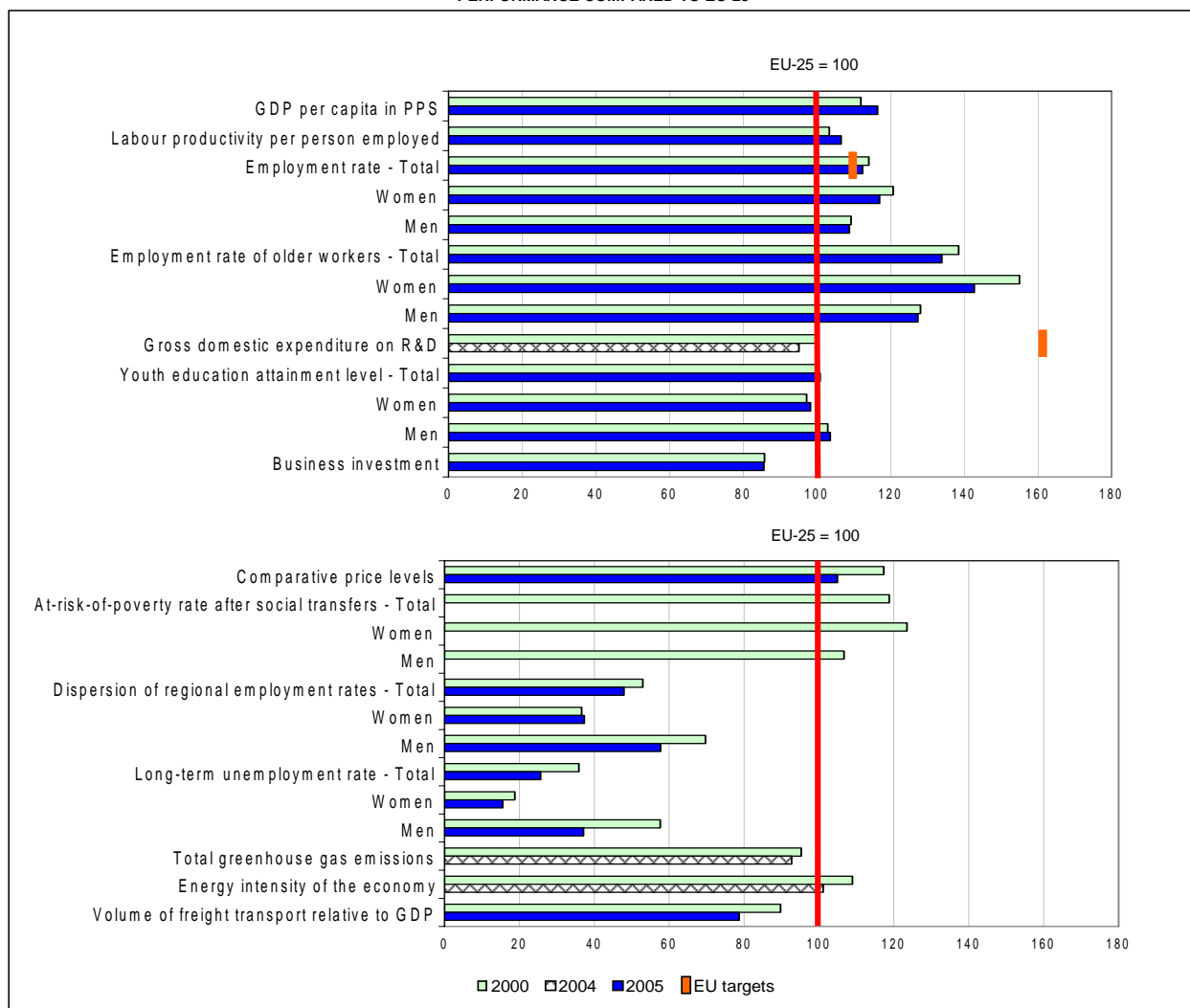
PART IV: STATISTICAL GRAPHS AND DATA

UNITED KINGDOM

	UK							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	112.0	113.1	116.0	116.4	117.1	116.5f		100.0	100.0	100.0	
Labour productivity per person employed	103.4	104.9	107.3	107.0	107.2	106.6		100.0	100.0	100.0	
Employment rate							*				70.0
Total	71.2	71.4	71.3	71.5	71.6	71.7		62.4	63.3	63.8	
Women	64.7	65.0	65.2	65.3	65.6	65.9		53.6	55.7	56.3	
Men	77.8	78.0	77.6	77.7	77.8	77.6		71.2	70.9	71.3	
Employment rate of older workers											
Total	50.7	52.2	53.4	55.4	56.2	56.9		36.6	41.0	42.5	
Women	41.7	43.0	44.5	46.3	47.0	48.1		26.9	31.7	33.7	
Men	60.1	61.7	62.6	64.8	65.7	66.0		46.9	50.7	51.8	
Gross domestic expenditure on R&D	1.86	1.87	1.89	1.88	1.77e		2.5 (2014)	1.86e	1.86e		3.0
Youth education attainment level											
Total	76.6	76.9	77.1	78.7	77.0	78.2		76.6	77.1	77.5	
Women	77.3	78.4	77.6	78.9	78.0	78.9		79.5	80.1	80.3	
Men	75.9	75.4	76.6	78.4	76.0	77.4		73.7	74.2	74.7	
Comparative price levels	117.3	114.3	110.7	103.8	105.6p	104.9p		100.0	100.0p	100.0p	
Business investment	15.7	15.2	15.1	14.3	14.6	14.9		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	19.0	18.0	18.0	18.0				16.0e	16.0e		
Women	21.0	19.0	19.0	19.0				17.0e	17.0e		
Men	16.0	17.0	17.0	17.0				15.0e	15.0e		
Dispersion of regional employment rates											
Total	7.1	6.8	6.6	6.1	5.8	5.7		13.4	12.2	11.9	
Women	7.5	7.2	7.0	6.7	6.5	6.3		20.5	17.3	16.9	
Men	6.9	6.6	6.5	5.8	5.7	5.6		9.9	10.2	9.7	
Long-term unemployment rate											
Total	1.4	1.3	1.1	1.1	1.0	1.0		3.9	4.1	3.9	
Women	0.9	0.8	0.7	0.7	0.6	0.7		4.8	4.7	4.5	
Men	1.9	1.7	1.4	1.4	1.2	1.3		3.3	3.6	3.5	
Total greenhouse gas emissions	86.4	87.4	84.9	85.7	85.9			90.7	92.7		
Energy intensity of the economy	227.3	223.7	214.5	212.1	207.2			208.8	204.9		
Volume of freight transport relative to GDP	89.8	87.3	85.5	84.7	84.1e	82.4e		100.1e	104.6be	104.7e	

* National target: 80% following the national definition

PERFORMANCE COMPARED TO EU-25



Euro Area Member States

Assessment of National Reform Programme

1. The euro area's economic performance considerably improved in 2006: economic growth accelerated to 2.6% from 1.4% in 2005 and unemployment declined from 8.6% in 2005 to 7.8% in September 2006. Since the euro area accounts for almost three quarters of economic activity in the EU-25, this improvement had a considerable impact on the growth performance of the EU as a whole. These positive developments do not appear to be purely cyclical developments. In particular, resilient employment growth coupled with the substantial drop in unemployment in 2006, suggests that there has been some structural improvement in the functioning of labour markets.
2. Over the last eight years, the euro has embedded economic stability in euro area countries, shielding them from exchange rate turbulence. In addition to favourable interest rates, euro area countries have benefited from becoming more integrated and interdependent due to the combined effects of EMU and the Internal Market. While EMU has undoubtedly been a success, a recent appraisal by the Commission² suggests that economic policies and governance structures may not yet have fully adjusted to draw the full benefit from the monetary union. This calls for a broad agenda of policy actions: euro area countries need to run their national fiscal policies more prudently, make markets for goods and services more flexible, accelerate financial market integration, and promote wage setting mechanisms which reflect the implications of monetary union. Such policy actions are not unique to the euro area. Indeed, they lie at the core of the Strategy for Jobs and Growth which applies to the whole EU. But, for the euro area, due emphasis and focus within the Strategy must be placed on reforms that are especially relevant for the smooth functioning of monetary union, i.e. reforms which cater for the fact that euro area countries can no longer make independent use of interest or exchange rate policies by developing alternative instruments to help their economies adjust to economic shocks and competitiveness pressures.

PART I: GENERAL ASSESSMENT

3. When assessing last year's reform priorities, the Commission called upon the euro area countries to pay further attention to measures that reinforce public finance sustainability. Reversing the upward trend in the debt ratio was highlighted, and some Member States were explicitly asked to undertake more permanent adjustment measures. R&D and innovation policies, competition in services and a better functioning of the Internal Market, as well as increased adaptability were indicated as points requiring further attention for a better functioning of the euro area.
4. The overall response of the euro-area Member States to the conclusions of the 2006 Spring European Council has been adequate, though more remains to be done in

² See the work on adjustment capacity of the euro area in The EU Economy: 2006 Review, Communication from the Commission - COM(2006) 714.

some Member States. Progress has been made with budgetary consolidation in the euro area in 2006. Regarding the four priority areas indicated by the Heads of State and Government at the 2006 Spring European Council, most progress has been made in the field of “R&D and innovation” and “Unlocking business potential”. Less widespread have been measures in the areas of “Employment opportunities for priority categories” and “in the Energy sector”.

5. The 2006 Spring European Council recognised that euro area Member States need to ensure better coordination of their economic and budgetary policies. In addition, to achieve higher growth and employment following a period of subdued economic performance, as well as to be able to adjust smoothly to changing economic conditions and competitiveness pressures, the Council also recognised the essential importance for euro area countries of budgetary sustainability and structural reforms. This, however, must be placed in the context of a broader EU perspective so that key overlapping interests of all Member States are strengthened, not diluted, by euro area members' targeted policy efforts. A better functioning euro area would benefit all EU Member States, not least countries that have not yet joined the monetary union but for whom the euro remains an important policy anchor. Overall, Member States' National Reform Programmes address many of the most important reform areas needed to raise growth and employment. However, in some cases, more prominence could be given to the specific dimensions of structural reforms that are particularly relevant for ensuring the smooth functioning of the euro area.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

6. The euro area countries have a single monetary policy and exchange rate. National fiscal policies play therefore a key role in supporting the monetary policy objective of maintaining price stability. Achieving sound budgetary positions also ensures that countries have the necessary fiscal leeway to cope with fluctuations in growth over the economic cycle, and contributes to public finance sustainability in the face of ageing populations. Progress is being made in this direction, as the combined euro area budget deficit is forecast to decline from 2.4% of GDP in 2005 to 2.0% in 2006 and 1.5% in 2007, an adjustment marginally stronger than that foreseen in the EU-25. Nevertheless euro area countries do not seem to take full advantage of more favourable economic conditions in order to more rapidly progress towards reaching their Medium Term Objectives (MTOs) in terms of public deficit. At this stage while six Member States of the euro area have already achieved the MTO, several are set to achieve their MTO target within the term of their stability programme while five Member States have still to set a date for achieving this target. Still, it is reassuring that euro-area Member States with the highest budget deficits are expected to record relatively strong improvements in their structural balances in 2006 and/or 2007. On the revenue side, Member States benefited from buoyant tax revenues, while on the expenditure side they started to implement both stricter controls and spending cuts.
7. The focus on efforts to improve the long-term sustainability of public finances notably in the area of pensions was considered as a strength in the programmes of the euro-area countries last year. During 2006, measures in the area of pension and health reform have been adopted or announced in a number of euro area countries,

including in countries considered to face a medium or high risk to the sustainability of their public finances.

8. Wage growth has again been contained in 2005 and 2006. Unit labour costs in the area as a whole increased by around 1%, which is in line with the price stability objective. However, two aspects of wage developments in euro area countries warrant continued vigilance. First, above average wage growth in excess of productivity gains occurred in several countries: if sustained, such developments can lead to a loss of competitiveness against other euro area countries. Secondly, wages in many euro area countries appear to adjust slowly in response to changes in economic conditions, and sometimes wages are not sufficiently linked to productivity developments at sectoral and local level. Overall, there is scope for wages to play a stronger role in helping economies adjust and more attention needs to be paid to the wage setting process in euro area countries. Many countries have sought to address these issues, mostly through measures to reduce non-wage labour costs which have often targeted specific groups such as the low-paid. More attention should also be paid to the role of labour mobility, across regions and occupations, as an adjustment mechanism in the euro area.
9. Overall, while macro-economic policies are contributing to fostering stability in the euro area and creating the conditions for higher growth potential, the challenge now facing euro area countries is to exploit the favourable economic climate to pursue further budgetary consolidation and structural reforms.

Micro-economic policies

10. Structural reforms can support macroeconomic stability and public finance sustainability by raising the speed limits of growth and mitigating sources of inflationary pressure, thereby enabling interest rates to be kept low and providing the right incentives for further productive investment and sustained consumption. Structural reforms can also boost the capacity of economies to cope with changing economic conditions by making the re-allocation of resources across companies and sectors easier. The entire range of microeconomic policies included in the Strategy for Jobs and Growth - designed to ensure open and competitive product and service markets - are essential to raise the growth and jobs potential. But two areas of reform are especially relevant for the euro area: first, enhanced competition in services could help foster price flexibility; second, more financial market integration would enable households and business to better finance investment and consumption thereby making the area more resilient to economic shocks.
11. In order to improve the functioning of the euro-area services markets, the adoption of the Directive on Services in 2006 represented notable progress. It would need to be followed up by a quick implementation especially by the euro area Member States in order to transform more services into tradable items, subject to higher degrees of competition. Many Member States address competition issues in network industries (notably gas and electricity sector but also electronic communications). Nevertheless, greater efforts are needed in many countries in respect of issues such as the separation of network management and supply as well as the resources and independences of the regulator. Within the area of competition in services many Member States are taking positive steps towards reform in the key area of professional services, while major efforts are still needed on the part of other Member States. Many euro area Member

States have taken policy actions to encourage R&D and innovation and to create a more attractive business environment, especially by reviewing regulation. Upon implementation of the announced plans, R&D spending would increase to 2.8% of GDP by 2010 from 1.9% of GDP in 2004. An additional issue, potentially relevant for the euro area, is the need for removing the tax incentives to invest in housing, that could have contributed to housing price acceleration in some Member States, entailing strong adjustment costs in case of trend reversal.

12. The single currency crucially enhanced the integration of financial markets among the euro area Member States, but more needs to be done to tap unused potential and maximise the benefits. Greater financial integration can smooth the impact of economic shocks on incomes and on national credit markets. In this regard, full transposition and enforcement of the Financial Services Action Plan and ongoing efforts to enhance financial market integration should deliver further significant results. At the EU level, some initiatives of particular importance for the euro area are advancing, namely the directive on payment services, the results of the Commission's inquiry into competition in financial services and the application of a code of conduct on clearing and settlement of securities. Some progresses in the transposition of the Single Market Directive for banking and financial markets are noted in some euro-area Member States.
13. The assessment of reform efforts in the field of goods and services markets in the euro area show signs of progress. While all euro-area countries took actual policy actions to promote better regulation, encourage R&D and the spread of innovation, the measures proposed or taken could be more ambitious in order to effectively address the challenge of low productivity growth in the service sector. The Internal Market Review to be presented in 2007 will propose essential actions that euro area Member States especially must take.

Employment policies

14. Though it has improved in recent years, the labour market performance of many euro area countries has been disappointing in terms of low employment rates as well as high and persistent levels of unemployment. Pursuit of the entire range of employment policies included in the Strategy for Jobs and Growth is essential to raise jobs and growth potential. However, the labour market has an especially important role to play in ensuring the smooth functioning of the euro area; in particular, it needs to be more flexible and adaptable to be able to cope with shocks to the economy. Particularly helpful would be labour market reforms that make work pay, improve flexibility and security, and increase labour mobility.
15. The policy to attract and retain more people in employment is a key challenge to tap potential labour supply and reduce labour market mismatches, especially in a context of fast ageing populations. Looking at the actual progress, a number of countries have adopted further measures to increase labour supply through interventions targeted towards particular groups (women, older workers, the young, immigrant, disabled people), but rarely does this constitute an integrated life-cycle approach to work. To make work pay, a number of countries have adopted measure to reduce income taxes, so as to make work more attractive for everybody or targeted at long-term unemployed, low paid, young and older workers. Several countries have also taken measures in the field of unemployment and welfare-related benefits, consisting in

increasing activation, for example by tightening the eligibility rules or the reintegration obligations, but also by improving public employment services. Few actions have been taken to increase the training opportunities of unemployed. Non-financial incentives to work, through for example access to child care still need to be further developed in many countries.

16. Better job allocation will require a better responsiveness of labour demand to changing structures. In order to give more employment security to job-mobile workers, policies should aim at more investment in human capital, more efficient active labour market policies, rebalancing employment protection between permanent and temporary contracts and fostering a more flexible work organisation. This approach should help the workforce to better adapt to the firms' new needs, while reducing employees' exposure to uncertainties in the labour market. As regards active labour market policies, the reforms remain quite piecemeal in the euro area, especially as to the development of efficient training. A limited number of actions were undertaken to rebalance employment protection between permanent and temporary contracts.
17. Most Member States made progress with the implementation of programmes to foster human capital formation. However, the tendency has been to focus mostly on education for young persons and less on training for adults already in the workforce. It is critical that the right incentives are put in place to encourage employers to invest in their staff and employees to invest the necessary effort in their own professional development.
18. With respect to the adjustment capacity of labour markets in the euro area, labour mobility should also be encouraged across regions and countries to accommodate shocks and feed the job opportunities where they emerge. While some euro-area Member States have taken different initiatives to tackle regional differences, no real progress has been made in 2006 on the portability of pension rights and the recognition of professional qualifications. Policy action is required in order to speed up the adoption and implementation of the relevant measures of the Lisbon Community Programme.
19. The general assessment of the labour market reforms is fairly positive in terms of the number of policies initiated in the areas of increasing labour supply and making-work pay. There are still insufficient actions when it comes to increasing the incentives for older workers to stay longer in the labour force and reforms of unemployment benefit systems in terms of their degree of activation. Only limited actions have been taken in the area of employment protection. Within the area of human capital investment, more attention needs to be paid to ensure that clear priorities are set and financial means, particularly from the Structural Funds, are spent in the most efficient manner. Finally, the adoption by the Council and the European Parliament of the Lisbon Community programme to promote labour mobility should be speeded up.

PART III: CONCLUSIONS

20. In light of the analysis presented above and based on the Integrated Guidelines for Growth and Jobs, it is concluded that:

21. The Implementation Reports of the Member States of the euro area show that progress is being made overall, reflecting substantive action in many countries. With the euro area growing in line with its potential and a number of reforms under way, some indicators are starting to turn more positive in this direction. But the closer economic and financial interdependence generated by having a single currency makes it necessary for its Member States to be more ambitious and for the euro area as a whole to go beyond what is specifically required at the level of Member States. Effective policy coordination at euro area level would help to promote policy action in Member States so to ensure fiscal discipline and structural reforms. This is necessary to increase the growth potential of the economy, enhance the capacity for absorption of asymmetric shocks and thereby preserve price stability while promoting economic dynamism in the euro area.
22. Among the strengths of the implementation of the National Reform Programmes of euro area Member States is that promising reforms are being undertaken or are planned to increase labour utilisation, boost R&D, human capital, innovation and to create a more attractive business environment, notably via policies to further better regulation. It remains however to be seen whether the concrete measures are sufficiently systemic and ambitious to achieve the stated objectives.
23. Building upon the policy conclusions identified for each individual euro area Member State based on their National Reform Programmes, action for the euro area as a whole is needed most urgently in policy areas that would improve the functioning of EMU, where weaknesses are evident. On the budgetary side, while progress is being made to reduce deficits, some countries need to accelerate the pace of budgetary consolidation and continue reforming pension and health care systems also to significantly address the budgetary impact of ageing populations. To ensure a more dynamic internal adjustment in EMU, markets could be made to function better, namely to ensure better factor mobility, a rapid adaptation of prices and wages, and to foster innovation and productivity growth, so to avoid excessive or protracted divergences in relative competitiveness in EMU. Financial markets have a key role in smoothing internal adjustment. The Internal Market Review to be presented in 2007 will propose essential actions that Member States, especially euro area countries, must take. In the meantime, however, it is evident that more competition in service markets would contribute to smoothen adjustment in EMU: hence the importance of the rapid and effective implementation of both the Services Directive and the Financial Services Action Plan. A review of the functioning of wage setting and measures to enhance labour mobility in euro area countries is also warranted. Against this background, the euro-area Member States are recommended to:
- make use of the favourable cyclical situation to aim at more ambitious budgetary consolidation towards the medium-term objective of close to balance or in surplus, hence striving to achieve an annual structural adjustment of at least 0.5% of GDP as a benchmark;
 - enact measures that lead to more competition, especially in services, and step up measures that promote the full integration of financial markets and the competition in financial retail services;

- improve flexibility and security on labour markets inter alia by better aligning wage and productivity developments, balancing employment protection and security in the market and enacting measures to promote labour mobility across borders and occupations.
24. In view of the spillovers and synergies arising from national policies and local developments within the monetary union, euro area Member States should aim at deepening policy co-ordination and strengthening governance, especially in the context of the Eurogroup, but also in international fora. This would significantly contribute to more effectively address policy challenges within the euro area and in the global economy.

PART IV: STATISTICAL GRAPHS AND DATA

EUROAREA

	EUROAREA							EU25			
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target
GDP per capita in PPS	109.0	108.5	107.6	107.2	106.5	106.3		100.0	100.0	100.0	
Labour productivity per person employed	108.5	107.8	107.0	106.6	106.0	105.9		100.0	100.0	100.0	
Employment rate							:				70.0
Total	61.5	62.2	62.4	62.6	63.0	63.5		62.4	63.3	63.8	
Women	51.4	52.4	53.1	53.6	54.5	55.2		53.6	55.7	56.3	
Men	71.6	72.0	71.7	71.6	71.6	71.8		71.2	70.9	71.3	
Employment rate of older workers											
Total	34.4	35.2	36.5	37.9	38.6	40.4		36.6	41.0	42.5	
Women	24.3	25.2	26.6	28.0	29.0	31.5		26.9	31.7	33.7	
Men	44.9	45.6	46.7	48.2	48.6	49.7		46.9	50.7	51.8	
Gross domestic expenditure on R&D	1.85e	1.87e	1.88e	1.88e	1.86e		:	1.86e	1.86e		3.0
Youth education attainment level											
Total	72.9	72.6	72.7	72.6	73.3	73.5		76.6	77.1	77.5	
Women	76.3	75.9	76.0	75.9	77.0	77.1		79.5	80.1	80.3	
Men	69.5	69.2	69.4	69.3	69.6	70.0		73.7	74.2	74.7	
Comparative price levels	99.9	100.3	101.1	102.9	102.7p	102.4p		100.0	100.0p	100.0p	
Business investment	18.9	18.4	17.8	17.5	17.7	18.0		18.3	17.1	17.4	
At-risk-of-poverty rate after social transfers											
Total	15.0e	15.0e	:	15.0e	17.0e	:		16.0e	16.0e	:	
Women	16.0e	:	:	16.0e	18.0e	:		17.0e	17.0e	:	
Men	14.0e	:	:	14.0e	15.0e	:		15.0e	15.0e	:	
Dispersion of regional employment rates											
Total	12.9	12.7	12.1	11.5	10.5	10.5		13.4	12.2	11.9	
Women	21.6	20.9	20.0	19.1	17.0	16.8		20.5	17.3	16.9	
Men	8.2	8.3	8.0	7.9	7.8	7.8		9.9	10.2	9.7	
Long-term unemployment rate											
Total	3.9	3.6	3.6	3.9	4.0	3.8		3.9	4.1	3.9	
Women	5.2	4.6	4.6	4.8	4.9	4.6		4.8	4.7	4.5	
Men	3.0	2.8	2.9	3.2	3.4	3.3		3.3	3.6	3.5	
Total greenhouse gas emissions	99.2e	100.2e	100.2e	101.7e	102.2e		:	90.7	92.7		
Energy intensity of the economy	188.6	190.0	184.9	186.3	184.7		:	208.8	204.9		
Volume of freight transport relative to GDP	104.3e	103.9e	104.7e	102.9e	110.3be	109.7e		100.1e	104.6be	104.7e	

PERFORMANCE COMPARED TO EU-25

