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GROWTH AND EMPLOYMENT IN THE STABILITY-ORIENTED FRAMEWORK OF EMU

Economic policy reflections in view of the forthcoming 1998 Broad Guidelines

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INTRODUCTION

This Communication comes at a defining moment in the development of the European Union. Within a couple of months, the European Union will decide on which countries will participate in Economic and Monetary Union from the starting date of 1 January 1999. This decision will be based on convergence reports currently under preparation in the Commission and the European Monetary Institute and on a recommendation from the Commission. As a consequence, the present Communication, which, this year, replaces the traditional Annual Economic Report, does not analyse the convergence issue. Instead, it focuses on the current economic situation, examines the main challenges in the years to come and suggests where the main priorities for policies should lie. Its main purpose is to initiate a debate in the European Parliament and the Member States on the policy options to be considered in the forthcoming 1998 Broad Guidelines for the economic policies of the Member States and the Community. These Broad Guidelines will be the first after the initial list of participants in EMU has been decided upon and will put a particular emphasis on growth and employment.

1. ECONOMIC SITUATION AND OUTLOOK

1.1. The present recovery in a longer-term perspective

In the EU, the renewed upturn which begun in the spring of 1996 is gathering momentum and is expected to turn into a self-sustaining expansion. The rebound was initially driven by buoyant export demand from outside the European Union and a marked improvement in competitiveness due to a lower exchange rate against the dollar, moderate wage developments and on-going productivity increases. Given improved competitiveness and assuming that the expected strong export market growth materialises, exports will remain supportive over the short run.

In the years ahead, the growth impulses are expected to stem increasingly from domestic demand, in response to favourable monetary conditions, especially declining risk premiums in long-term interest rates and the strength of the dollar against European currencies, and improved confidence of companies and households. These favourable monetary conditions were brought about by the remarkable progress towards convergence of inflation rates and the correction of excessive budgetary positions in the vast majority of Member States.

Investment is poised to become the engine of growth in the Union, thereby adding to total demand as well as to both productive capacity and to the potential for sustaining growth in future years. Investment in equipment, especially, should expand briskly, being underpinned by improvements in demand prospects, competitiveness and profitability, as well as a continuation in terms of moderate wage developments. Following some slackening in 1997, private consumption is expected to accelerate gently in the years ahead on the back of moderate increases in real wages, a fall in precautionary savings and, increasingly, by rising employment.

On balance, the Commission services' Autumn 1997 forecasts expected that in the EU as a whole, GDP would expand by 2.6 per cent in 1997, accelerating to about 3 per cent in 1998-99.

The progressive acceleration in real GDP growth is expected to have resulted in net employment creation at a rate of 0.5 per cent in 1997 in the EU as a whole, rising to 0.8 % and 1.3 % in 1998 and 1999 respectively. This will correspond to a cumulative net creation of 3.8 million jobs over

the three years. This encouraging performance will, however, not completely compensate for the job losses of the early 1990s (4½ million). In addition, stronger and sustained employment growth over the medium term is required to provide employment opportunities for both the high number of unemployed and the increased number of people wanting to enter the labour force or to re-enter it after a spell of inactivity.

Since labour supply is still expected to grow at about 0.5 per cent per year due to in particular a further rise in the participation of women and fewer men withdrawing from the labour force, the creation of jobs will not lead to an equal reduction in unemployment. In the EU as a whole, the unemployment rate is expected to decrease from a peak of just below 11 per cent in 1996 to 10.7 per cent in 1997, falling gradually further to 9¾ per cent in 1999.

As a result, four years after the adoption of the first Broad Economic Policy Guidelines in late 1993, the Union's economic performance shows a mixed record. On the positive side, all Member States have managed to reduce inflation and budget deficits significantly, having implemented stability-oriented macroeconomic policies over the past years. Conversely, in terms of economic growth and employment, the performance has been disappointing during the first half of the 1990s. This has raised doubts in some circles about the effectiveness and the soundness of the overall policy strategy advocated in the Broad Guidelines.

That the strategy recommended is appropriate and works is demonstrated by the economic performance in countries which have for some time followed sound economic policies, achieved wage trends approximately in line with the Guidelines recommendations, and which have clearly reduced their budget deficits to below 3 per cent of GDP. In these countries, the results in terms of sustainable economic growth and job creation have been favourable and are clearly among the best in the Union (the countries are, Ireland, Luxembourg, the Netherlands, Denmark and more recently Finland).

The perception that the strategy has not yet delivered satisfactory results in the Union at large, is in part due to the sheer size of the challenges at the start of the second stage of EMU and in part to the, at times, insufficient progress in implementing the appropriate policy measures. The disappointing performance of the EU during the period 1991-96 in terms of GDP growth (1.6 per cent p.a.) and employment (-0.4 per cent p.a.) is in sharp contrast with the substantial results achieved in 1986-90 (growth of 3.3 per cent p.a., employment 1.3 per cent p.a.). With hindsight, it becomes increasingly evident that the poor growth and employment performance in the Union over the years 1991-96 was mainly the result of three macroeconomic obstacles to growth within the Union.

(i) An initial overheating of the economy (from 1988 onwards), precipitated by an excessively expansionary macroeconomic policy-mix, fuelled inflation (from 1989) which spiralled into correspondingly higher increases in nominal wages (from 1990). The rekindling of inflationary pressures caused the monetary authorities to adopt a very tight policy, which had a knock-on effect in all the EU countries, but budgetary policy initially remained lax, or even clearly expansionary in some countries. Consequently, rising interest rates and the currency crisis of 1992 led to the stabilising recession of 1992-93, with a substantially negative impact on employment. This stability conflict between budgetary policy, wage developments and monetary policy was a major macroeconomic obstacle to growth.

(ii) A timely moderation of wage increases, sharp rises in productivity and increased competitiveness all contributed in 1993-94 to a healthy upswing, similar to the 1996-97 recovery. Exports and investment led the upswing, which was further supported by a gradual improvement in private consumption and employment. This upturn was, however, abruptly aborted under the combined impact of the currency upheaval of spring 1995 and a marked rise in long-term interest rates. Factors beyond the control of policy-makers in the EU (e.g., the Mexican crisis and the related dollar weakness) undoubtedly played a role in these

developments. The monetary turmoil was, however, largely rooted in insufficiently credible economic policies in the Union, especially a lack of credible budget consolidation plans in several Member States. Such currency upheavals, which have occurred repeatedly in the Union, were another major macroeconomic obstacle to growth.

(iii) The fact that healthy upswings have been repeatedly cut short by stability conflicts and currency upheavals since the first oil price shock and the end of the Bretton Woods system has contributed to a decline in the investment rate in the Union. As a result, the potential rate of economic growth is relatively low (currently at around 2¼ per cent per annum), which in itself constitutes a third obstacle to growth.

If the Union is to achieve a sustained period of healthy economic growth capable of ensuring a significant and lasting reduction in unemployment, it has to find lasting solutions to these macroeconomic obstacles to growth. A more vigorous and credible implementation of the Guidelines strategy over the last two years has set in motion a virtuous circle. The exchange rate disturbances, which occurred during 1995, have been broadly reversed and a higher degree of stability has returned within the ERM. Long-term interest rates have converged towards low levels. Sounder economic policies have led to an improvement in economic confidence and have laid the ground for the current improvement in economic activity. Thus, the economic strategy described in the Broad Economic Policy Guidelines is now delivering its expected results. The stability-oriented policy framework of EMU is likely to help overcome, in a more permanent manner, these obstacles to sustained growth and job creation. The benefits in terms of economic growth and job creation from a good macroeconomic performance will be all the greater the more product, service and labour markets work efficiently. In these areas, although considerable progress has been made in recent years, much remains to be done. It is therefore essential that Member States step up their efforts in these fields.

1.2. Opportunities and risks

(i) After a protracted period of slow growth, the necessary conditions for sustained growth in output and employment in the EU are now in place. Taking into account the combination of very favourable supply-side conditions, improved demand prospects and a further strengthening of confidence, a period of balanced and self-sustaining economic growth could indeed ensue.

Underlying economic fundamentals are sound and, if anything, are as good as or even better than those prevailing at the onset of the 1993-94 upswing or even during the high growth period 1986-1990. Inflation is historically low and contained in almost all Member States. With spare capacity still available and a recovery increasingly supported by capacity-increasing investment, growth can develop without generating inflationary pressures. The profitability of investment is at a level not seen since the late 1960s and is improving further. In such a situation, brightening demand prospects and strengthened confidence can generate a sound and durable recovery. At present, there are still some weaknesses in internal demand. But in the present context, demand cannot be stimulated by fiscal expansion or by significantly stronger wage increases. Internal demand has thus to come from an endogenous process in which the initial external impulse should be progressively replaced by the induced expansion of investment and private consumption. This presupposes favourable monetary conditions, a high profitability of investment and a climate of confidence. These conditions are more and more being met. Interest rates are at an historical low and are converging downwards while intra-EU exchange rates have been very stable and are in line with fundamentals. Finally, business and consumer confidence is being buttressed by several factors. The latter include heightened expectations of a robust recovery, credible and soundly based reductions in budget deficits, an increased political will and determination, both at national and EU level, to tackle the Union's stubborn unemployment problem and the growing perception that a large EMU will be launched on schedule.

(ii) Concerning the Asian crisis, despite the grim economic situation in Asia and the challenges facing the international financial system, there are reasons, given developments so far, for believing that the Asian crisis will only have a small impact on the present recovery in the EU and will have no influence on the arrival of the euro. The trade exposure of the EU to the Asian region is limited. Consequently, the lower demand growth in Asia and the improved competitiveness of the region following the marked depreciation of its currencies will affect EU exports only marginally. The exposure of the financial sectors of some Member States to the region is important, but concentrated in relatively sound economies (namely Hong Kong and Singapore). On the other hand, through lower EU import prices, the Asian crisis may exert a positive influence on inflation in the EU, implying that officially-controlled interest rates could be held lower than they otherwise would have been. Finally, there are no signs as yet that the Asian financial turmoil has affected the spill-over in the EU from external demand to domestic spending, which should become the main driving force of economic growth in 1998. In sum, the financial turbulence in Asia will lead to some reduction in economic growth in the EU in 1998, but the adverse impact is likely to be rather small. A recent simulation with the QUEST model, which suggests that the crisis could knock off about a quarter of a percentage point of output growth in the EU in 1998, corroborates this qualitative assessment.

In part related to developments in Asia, there has also been some concern about the stock market volatility that affected the world economy at large during the second half of 1997 and at the beginning of 1998. In the industrial countries, the correction that took place during this period has, however, been reversed in recent weeks. Nevertheless, renewed falls in stock prices cannot be excluded. Were these to occur, the adverse impact on confidence and economic activity would probably not be very important. Unlike in the United States, market capitalisation is low and the role of shares in households' portfolios is rather limited in continental Europe. Furthermore, any negative effect could be offset by lower interest rates if the liquidity withdrawn from stock markets were to be invested in the bond market or through policy reactions by the monetary authorities.

1.3. Economic policy requirements

Although an increasingly robust cyclical upturn has taken hold, this is not the time for any relaxation of policy effort. The challenges facing policy-makers are twofold:

- in the short run, to maintain monetary stability and market confidence;
- in the medium-term, to transform the upswing into a strong and sustained growth process.

Meeting these challenges is crucial to the realisation of two complementary priority objectives of the EU, namely:

- a smooth transition towards EMU and its successful operation;
- a substantial and lasting reduction in the level of unemployment while significantly increasing the employment rate.

Progress towards a return to sound public finances is instrumental to the fulfilment of these two objectives.

With spare capacity available and with prospects for healthy growth in investment in plant and machinery, solid growth should be able to take place without encountering capacity constraints or generating inflationary tensions. Monetary conditions may thus remain favourable for an extended period. Moreover, the fact that interest rates have converged towards low levels shows that financial markets are confident that the framework for monetary and budgetary policies in EMU will ensure low inflation in the long run.

It is essential to maintain this confidence and to guarantee a smooth transition to EMU through credible policy action. In the monetary field, once the decision has been made as to which

countries will take part in the third stage of EMU from its outset, there is likely to be a need for enhanced monetary co-ordination for two principal reasons. Firstly, to support market stability in the intermediate phase by emphasising the firm commitment to EMU and by underlining a common view on the future single monetary policy. Secondly, to ensure that the ECB inherits a monetary environment consistent with price stability in the prospective euro area and thus to help avoid any sharp movements in interest rates at the beginning of EMU. In the budgetary field, it is essential that Member States fully implement their 1998 budgets and/or their convergence programmes. The objectives set out in these budgetary plans should be considered as ceilings, not targets. In those countries where growth has been quite robust for some years or where the convergence in interest rates in the run-up to EMU would imply a further fall in rates, there may be a particular need to quicken the pace of budget deficit reduction.

Ensuring a transformation of the present recovery into a non-inflationary, high economic growth process over the medium term -- a prerequisite for substantially and durably higher employment -- will require a strengthened programme of macroeconomic and structural policies to address a number of key challenges while allowing the EU economies to better adapt to changing circumstances in the years ahead. In conformity with the Resolution on Growth and Employment from the Amsterdam European Council, durably reducing unemployment will require action over a broad front, with an essential ingredient being macroeconomic policies, including wage developments, that promote sustainable growth and stability. It will also be essential that Member States continue, and where necessary, intensify structural reforms that should, over time, improve the functioning of product, services and labour markets.

2. THE EMPLOYMENT CHALLENGE

2.1. Why an employment challenge?

Article 2 of the Amsterdam Treaty on the European Union states explicitly: "*The Community shall have as its task, by establishing a common market and an economic and monetary union and by implementing common policies or activities [...], to promote throughout the Community a harmonious, balanced and sustainable development of economic activities, a high level of employment and of social protection, equality between men and women, sustainable and non-inflationary growth, a high degree of competitiveness and convergence of economic performance, a high level of protection and improvement of the quality of the environment, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among Member States.*"

Indeed, a common, comprehensive definition of competitiveness in the economy as a whole is as follows. A country is internationally competitive if concurrently:
- its productivity increases at a rate which is similar to or higher than that of its major trading partners with a comparable level of development;
- it maintains external equilibrium in the context of an open free-market economy; and
- it realises a high level of employment.

If one looks at the overall performances of the European Union in terms of productivity and external equilibrium, the picture is satisfactory. During the last 24 years (1974-1997), the growth of labour productivity[1] remained stable at 2 per cent per year on average; i.e. well above the United States (0.7 per cent per year during the same period) and, more recently, even slightly above Japan (1.9 per cent per year in 1986-97). Similarly, the current account of the EU as a whole has always fluctuated within narrow limits, close to equilibrium or in slight surplus thereby allowing for capital export and development aid. However, as regards the labour market, the most dominant feature of the EU is *the mediocrity of its employment growth and level* with respect not only to

[1] Defined as real GDP per employed person.

what the Union was able to sustain during the 1960s but also compared to the United States and Japan.

2.2. The extent of non-employment

According to Eurostat's standardised unemployment definition, the number of unemployed persons in the Union amounted to approximately 18 million in 1997, representing 10.7 per cent of the civilian labour force. Furthermore, the weak employment performance of the Union since the mid-1970s has not only led to a fivefold increase in the unemployment rate but has also resulted in a very low ratio of effectively employed persons with respect to the working-age population. This ratio, the employment rate, fell from 67 per cent in 1961 (a level reached even before the considerable expansion of the female labour force) to about 60 per cent presently whereas it exceeds 74 per cent in the USA and Japan. Such a large fall goes beyond the impact of unemployment alone since activity rates tend to fall when unemployment goes up ("discouraged worker" effect).

The future employment rate will depend on economic and social conditions that may strongly differ from previous periods. However, in the medium to long term, if sufficient jobs are created, the EU employment rate could easily return to a level at least as high as in the early 1960s (67 per cent). In fact, if the female employment rate remains unchanged at the level reached in 1997 and if the male employment rate returns to its high level of the 1960s, then the overall employment rate for the EU could even be 70 per cent. Besides, a further (and likely) increase in female participation would bring the EU to 72 per cent or even close to the US and Japanese levels. These two limits (67 and 72 per cent) imply an employment potential of either 22 or 34 million people, respectively the equivalent of total employment at present in France and Germany[2].

It should also be noted that, in fact, the employment potential is even higher since the present 60 per cent employment rate corresponds to 55 per cent in terms of full-time equivalent posts due to the impact of part-time work of which a part is involuntary and corresponds thus to a form of partial unemployment.

In the short run, the present degree of non-employment is undoubtedly a weakness and the source of a large social cost but the labour reserve associated with it also represents a very important growth potential beyond the growth coming from labour productivity increases. Such a potential is not available in the US and in Japan, and it constitutes an opportunity that should be seized. Indeed, the utilisation of this potential would greatly alleviate Member States' public finances and social security systems[3], facilitating the safeguarding and development of common European social values, as well as the reduction of tax pressure both on companies and on individuals. It would also make the transition towards a more environmentally friendly production mode significantly easier. For the latter, examples of the social and environmental needs that may be fulfilled within the job creation process may be found in recent Commission reports on Employment Pacts and Local Initiatives. In the same spirit, an investment-led, durable growth pattern fits very well with the long term investment strategies proposed by the Commission in its November 1997 Communication on

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[2] Strong economic growth over the medium term combined with a determined implementation of the 1998 Employment Guidelines could result in an increase in the employment rate to 65 per cent within five years in the EU as a whole.

[3] The ratio of people aged 65 and over to those in the active age groups (the so-called grey pressure) will increase by about one third between 1995 and 2020. If the employment rate, i.e. the share of those financing pay-as-you-go pension schemes, remains as low as it is now and unemployment remains above 10 per cent of the labour force, social contributions likewise would have to be increased by 33 per cent if one wants to maintain the present ratio of pensions to earned income. On the other hand, if the employment rate could be raised to the present US or Japanese levels (74 per cent) with a return to (nearly) full employment, the increase in contributors would nearly match the increase in pensioners. Furthermore, the increase in contribution rates required to maintain the same relative pension levels would be negligible. For more details, see *European Economy*, n° 56, 1994, Analytical Study n° 5.

Environment and Employment, so as to promote environmentally sustainable production and consumption patterns.

Finally, strong economic growth in the EU provides considerable help towards a successful transition in the candidate countries and in the less-developed world as a whole.

To exploit the huge labour reserve, two conditions must be met: firstly, the existing workforce must be "employable" and notably meet the changing skill requirements of the economy and, secondly, the economy must create the necessary working posts.

2.3. The employability of labour

The effects of globalisation and the permanent introduction of new technologies are raising the skill requirements for jobs. In this context, in agreement with the recommendation contained in the 1998 Employment Guidelines approved by the Council in December 1997, training policies (broadly defined) should provide the environment needed for the improvement in human capital, which remains a major economic and social goal. It must, however, be noted that given the pressure of competition (both internal and external) and of technological and organisational progress, this need for qualifications applies to **all** members of the potential labour force, both in and out of work. Investment in knowledge is a permanent task and will remain so in the medium to long run.

But it should be kept in mind that in order to produce their full return, training policies must go together with a strong creation of working posts in the economy so that people going through these re-training efforts do indeed find a job at the end of it. If this is not the case, the full potential of these costly efforts cannot be realised and for individuals, it is a strong source of frustration.

It should also be appreciated, at the present time, that both the cyclical (about 2 per cent of the labour force) and nearly one half of the non-cyclical part of unemployment (i.e. about 4 per cent)[4] is composed of persons still in the normal turnover of the labour market, in the sense that they could easily return to work, with some (limited) retraining, provided that new working posts are created for them. This means that from the present 10.7 per cent of the labour force which is unemployed, about 6 per cent could re-enter the job market fairly fast if and when jobs are offered to them. Thus, despite some bottlenecks in a few specific sectors, there is no evidence that the skills offered by a sizeable share of the workforce are basically outdated or insufficient to ensure employability. The true immediate bottleneck is located at the level of net job creation in the economy.

Finally, in a longer term perspective, even part of the structural unemployment stricto sensu (about 5 per cent of the labour force) could be re-integrated into employment by active labour market policies and other structural measures (see section 4.5, below) if the economy creates the required working posts.

2.4. Growth, productivity and employment

To achieve a high employment rate in the EU, which is a requirement of the Treaty (Article 2), it will be crucial to generate, over an extended period of time, economic growth well above the rate coming from increases in labour productivity in the overall economy, whatever the pace of the latter might be. Over the last two decades, overall labour productivity has increased at a stable rate of 2 per cent per year on average in the Union[5]. This has resulted, in more or less equal proportion,

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[4] See, *European Economy*, n° 59, 1995, Analytical Study n °3.

[5] With the productivity trend stable at 2 per cent per year, a trend growth of real GDP of 2 per cent per year will simply keep employment constant. Furthermore, since labour supply is still likely to grow by about 0.4 to 0.5 per cent per year in the medium term, a real GDP growth rate of higher than 2.5 per cent is needed to reduce unemployment.

from the incorporation of technological and organisational progress (total factor productivity) and a substitution of labour by capital at the macroeconomic level[6].

Since technological progress is the main source of wealth and improvement in the quality of living standards over the long run, policies should be directed at maintaining, and even accelerating, the pace of technological change. This is also necessary in order to safeguard the Union's competitiveness in an ever closely integrated world economy. Furthermore, there are powerful forces at work, such as globalisation, the completion of the internal market and the move towards a knowledge-based economy, which are expected to sustain the trend of total factor productivity but also of labour to capital substitution in the Union in the future.

On the other hand, with respect to substitution of capital for labour at the macroeconomic level, the Union's economy has traditionally been characterised by a comparatively strong degree of substitution, implying a stronger increase in the capital intensity of its production process than for instance in the United States. However, the analysis of the 1986-90 data shows that the combination of wage moderation (hence, profitability increases) combined with good demand prospects and strong growth in capacity-expanding investment may reduce significantly the rate of labour to capital substitution. Thus, if the evolution of wages continues to be appropriate, a further slowing-down of this substitution process is to be expected. Simultaneously, through increased profitability, it reinforces the foundations for higher, investment-supported, economic growth as demand prospects brighten. By incorporating new technologies, the new investment will contribute to sustaining total factor productivity growth and, to the extent it is capacity widening, slow down the substitution process[7]. For another way to weaken the substitution process, see section 4.5.

3. EMU AND MACRO-ECONOMIC POLICIES CONDUCIVE TO GROWTH AND EMPLOYMENT

3.1. The established consensus of the Broad Guidelines and the favourable, new, policy framework in EMU

Within the framework of the Broad Economic Policy Guidelines a solid EU-wide consensus has been established on a common macroeconomic policy strategy to achieve sustained, investment-supported, output growth and job creation over the medium term without inflationary tensions. This strategy contains three essential ingredients, which may be summarised as follows:

- a stability-oriented monetary policy;
- sustained efforts to consolidate the public finances in most Member States consistent with the objectives of the Stability and Growth Pact;
- nominal wage trends consistent with the price stability objective; at the same time, real wage developments with respect to increases in productivity should take into account the need to strengthen the profitability of investment and to support the purchasing power of workers.

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[6] For a detailed analysis, see "1997 Annual Economic Report", *European Economy*, n° 63, 1997.

[7] The experience of Ireland seems to bear this out in an even clearer way. In Ireland, macroeconomic wage moderation since the mid-1980s was much stronger than in the Union on average (e.g. over the period 1991-97, in Ireland real wages grew by 1.5 percentage points less than the labour productivity trend of 4 per cent p.a. whereas in the EU they rose by 1.1 percentage point less than the labour productivity trend of 2 per cent p.a.). This has resulted in a significant slowing down of capital-labour substitution, but the growth of labour productivity has been maintained, helped by higher capacity-widening investment which incorporated technical progress. Simultaneously, in Ireland, economic activity and employment grew at a strong pace (average annual rate of growth of 6½ per cent and 2½ per cent, respectively). On the other hand, in the Netherlands wage moderation in combination with labour market reforms (especially part-time work) since 1983 has led to a slowdown in capital-labour substitution but also in apparent labour productivity growth.

The underlying reasoning is that "the more the stability task of monetary policy is facilitated by appropriate budgetary measures and wage developments, the more monetary conditions, including exchange rates and long-term interest rates, will be favourable to growth and employment"[8].

The framework for macroeconomic policies in EMU, as laid down in the Treaty and supplemented by the Stability and Growth Pact and the new exchange rate mechanism (ERM2), reflects, builds on and will reinforce this consensus. Consequently, the realisation of EMU enhances the prospects of avoiding the three principal reasons or obstacles that have, on repeated occasions, brought economic growth and job creation in the Union to a premature halt (see above, section 1.1). This holds because in EMU:

- *exchange rate turbulence will be ruled out among participating countries* and the euro exchange rate with non-participating Member States is likely to be stable, especially if they participate in the ERM2, as countries with a derogation are expected to do. The more countries take part in the single currency, the greater the benefits of the Single Market will be. Moreover, given the economic importance of the prospective euro-zone in the world economy, the euro could help stabilise world currency relationships. This possibility is further enhanced by the commitment of policy-makers on both sides of the Atlantic to pursue stability-oriented macroeconomic policies. Thus, extra-EC trade (representing only about 10 per cent of Community GDP) would probably also be favoured;
- *stability conflicts will be more easily avoided.* The Treaty provisions (Art. 104 to 104c)[9] and the Stability and Growth Pact with its goal of an underlying budgetary position close to balance or in surplus in "normal" cyclical conditions decisively reduce the risk of conflicts between budgetary and monetary policies. This also makes it possible to durably achieve a low level of long-term interest rates. Moreover, given that exchange rate changes between participating countries are ruled out and given the price stability task of the ECB, the responsibilities of the two sides of industry in setting wages are increased. These two factors will also make it easier for them to settle wage agreements in conformity with stability and growth. Finally, the conditions and incentives for wage and price discipline will be enhanced in EMU by increased product market integration and competition;
- *a more stable and less risk-prone environment for investment will be created.* The single currency will create a zone of macroeconomic stability and low inflation and will thus provide a stable framework in which companies can plan and invest. The investment process will thus benefit from the stability context in the sense that its expansion will not be abruptly and prematurely interrupted by stability conflicts or monetary turbulence. Besides, reduced volatility in exchange rates, inflation, interest rates and economic activity will reduce the required rate of return on investment decisions. The euro will be a complement to the Single Market, boosting competition and providing new opportunities to invest. For these reasons, the stability provided by the EMU regime will make a decisive contribution to overcoming the third obstacle to growth, namely the insufficient growth of productive capacity with respect to the labour productivity trend.

In sum, EMU will help to lock in the fundamental change in the macroeconomic policy mix which has been progressively achieved in the Union and which has started to deliver its expected results.

As emphasised in the Luxembourg European Council Resolution on "Economic policy co-ordination in stage 3 of EMU", the policy mix under EMU will require closer Community surveillance and co-ordination of economic policies, both among Member States and between the

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[8] See "1997 Broad Economic Policy Guidelines", *European Economy*, n° 64, 1997.

[9] Art. 104: ban on the monetary financing of government deficits; Art. 104a: ban on privileged access for the public authorities to the financial markets; Art. 104b: the Community and the public authorities of the Member States are prohibited from assuming liability for the debts of other public authorities; Art. 104c: excessive government deficits and debts must be avoided.

parties involved in economic decision-making. This notably implies the close monitoring of macroeconomic developments in Member States and of the euro exchange rate, the surveillance of budgetary positions and policies, the monitoring of structural policies in labour, product and services markets and of cost and price trends, the fostering of tax reform to raise efficiency and discourage harmful tax competition.

The enhanced co-ordination will adhere to the principle of subsidiarity, respecting the prerogatives of national governments in determining structural and budgetary policies subject to the provisions of the Treaty and the Stability and Growth Pact. It will respect too the independence of the ESCB and the role of the ECOFIN Council as the central decision-making body and will respect national traditions and the competence of the social partners in the wage formation process.

Finally, the Broad Economic Policy Guidelines should be developed into an effective instrument for ensuring sustained convergence and should provide more concrete and country-specific guidelines and focus more on measures to improve Member States' growth potential, thus increasing employment.

3.2. Monetary policy

Monetary policy in the euro-area will be under the responsibility of the ECB and the ESCB. In conformity with Article 105(1), the primary objective of monetary policy will be to maintain price stability and, subject thereto, to support the economic objectives of the Union, including in particular sustained, non-inflationary, growth and a high level of employment, as laid down in Article 2 of the Treaty.

The credibility of the ECB in delivering price stability is of paramount importance in achieving low long-term interest rates and positively influencing the behaviour of price and wage setters. This credibility is an important asset in realising higher levels of investment, growth and employment.

The credibility of the ECB in delivering price stability is underpinned not only by the clarity of its objective but also by the Treaty guaranteed independence of the ECB and of its governing council. The credibility of the ECB and the euro will therefore from the outset be as high as that of any existing central bank and major world currency. This has been clearly confirmed by developments in the financial markets in the run-up to EMU. In the countries that have shown a determination to meet the convergence criteria and participate in EMU, long-term interest rates have fallen towards the best performers in the ERM. Moreover, long-term interest rates have even fallen to record low levels in Germany, the country that is traditionally viewed as having had the most credible central bank and most stable money. Record-low nominal interest rates in Germany and other countries are an unmistakable sign that the credibility of the euro and the ECB is, from the outset, comparable with that of the best performing Member States.

Finally, and not least importantly, the more the stability task of monetary policy is facilitated by a sound budgetary policy, inspired by the Stability and Growth Pact, and by appropriate wage developments, in line with stability and growth, the less monetary policy is overburdened and the more monetary conditions, including the euro exchange rate and long-term interest rates, can develop in a way that is favourable to growth and employment. This will represent clear progress over the earlier, "pre-EMU", times.

For the European Central Bank this implies, in line with Art. 105 (1) of the Treaty, that it pursues its primary objective of maintaining price stability with emphasis and credibility, but it implies also that, "without prejudice to the objective of price stability", it support(s) the general economic policies in the Community with a view to contributing to the achievement of the objectives of the Community as laid down in Art. 2", including the objectives of growth and employment.

3.3. Budgetary policy

Budgetary policies will remain the responsibility of national governments in EMU but will be subject to the constraints of the Treaty and the Stability and Growth Pact, which emphasises the need to balance the budget in "normal" economic conditions and clarifies the key Treaty provisions on budgetary policy. These legal provisions reflect the recognition that sound budgetary policies are an essential condition for sustained, non-inflationary growth and a high level of employment. This is so because sound budgetary policies, apart from facilitating the task of monetary policy in maintaining price stability, will:

- by helping to reduce long-term interest rates, *generate a crowding-in of private investment.* Since in such circumstances governments no longer absorb private saving, but make a positive contribution to savings in the economy, the increase in the investment rate can - other things being equal - take place without pressures on the balance of payments and long-term interest rates;
- *create the necessary room to cope with adverse cyclical developments.* This will be particularly important after the introduction of a single currency, because the adjustment to country-specific shocks will then, to a higher degree, rest with budgetary policy;
- by curbing public debt ratios and hence reducing the debt service burden, facilitate the needed *restructuring of government spending towards more productive uses and lowering of taxes and social security contributions, while making the taxation system more employment friendly.* It will also help prepare for the budgetary consequences of population ageing.

Budgetary issues will also form an integral part of the strengthened multilateral surveillance and co-ordination of economic policies agreed at the Luxembourg European Council. Such policy co-ordination will facilitate the maintenance of appropriate budgetary policies in each participating Member State and in the euro-zone as a whole, taking into account the current and prospective stance of monetary policies, the economic situation and prospects, etc.

Critics have argued that this commitment to disciplined budgetary policies will result in an unduly restrictive budgetary stance, hence risking exacerbating fluctuations in economic activity. However, this does not take into account that, given the "virtuous circle" effects of the considerable efforts already made, of the fall in interest rates and the general reduction in the public debt burden, it will be much easier to bring budget deficits from 3 per cent of GDP to zero, if the medium term growth path develops as expected, than it was to bring them to 3 per cent of GDP in the first place.

Critics also ignore the fact that the possibility to use the stabilising function of fiscal policies has been increasingly lost over the last three decades. In this period, Member States with relatively high deficits and debt levels have often found themselves compelled to follow restrictive budgetary policies during periods of economic slowdown. Budgetary consolidation will help regain that margin.

Budgetary positions close to balance or in surplus in normal cyclical positions allow sufficient scope to deal with all but the most severe disturbances without breaching the 3 per cent reference value. In exceptional circumstances (as specified in the Stability and Growth Pact), Member States will be allowed to surpass this value. Some Member States will, however, actually have to plan budget surpluses in favourable economic conditions to comply with the Pact's objective of ensuring a sustainable public finance position over the full range of the economic cycle. Sound budgetary policies will in all likelihood also increase the effectiveness of the automatic stabilisers. Proven budgetary discipline will strengthen the confidence of economic agents that a rising deficit during a recession will not permanently disrupt the public finances, thereby alleviating the adverse effects through higher interest rates.

Over the last year, Member States have submitted new or updated convergence programmes setting out their medium-term budgetary objectives. They all aim for a continuing budgetary improvement in the years to come, thus making steady progress towards the objective of budgetary positions close to balance or in surplus. The improvement in the public finances is helped by the expected upswing in growth and employment. In many countries, the full effect of recent years' sharp reduction in interest rates also still has to come through. In most cases, these cyclical and interest rate induced gains are accompanied by further, if moderate, improvements in the structural budget positions net of interest payments.

Given the important efforts made in recent years, showing already positive results, it is essential that Member States stick to the budgetary objectives set out in their recent convergence programmes. The opportunities offered by the improving economic cycle must be seized in order to improve the state of the public finances and to fulfil the objective of close to balance or in surplus at the earliest possible date. It is equally important that policy mistakes are avoided in other areas, notably policies which might add to labour cost and inflation pressures and thus could precipitate a rise in interest rates or a premature halt in business expansion and investment dynamism.

In order to be consistent with the Broad Economic Policy Guidelines, budget deficit reductions should be achieved mainly through continued expenditure restraint rather than through tax increases. Until now, for the EU as a whole, the impressive budgetary consolidation effort (from a deficit of 6.1 per cent of GDP in 1993 to 2.6 per cent in 1997) was indeed entirely made by a contraction in the level of total expenditures in GDP (from 52.4 per cent in 1993 to 48.7 per cent in 1997) since the overall tax pressure remained practically constant (at 46.3 per cent of GDP in 1993 and 46 per cent in 1997).

However, having reduced their budget deficits to 3 per cent of GDP or below, some Member States (especially the Netherlands, but recently also Germany) have embarked, or are contemplating doing so, on a strategy of simultaneously curbing the budget deficit and the burden of taxation. Such a programme is motivated by the need both to control government expenditure growth and to promote economic dynamism, thereby strengthening the conditions for sustained growth and employment creation. In view of the important distortions and disincentives emanating from a high level of taxation, such a strategy is certainly appropriate provided that it does not jeopardise further, steady, progress towards sound budgetary positions.

The successive Broad Guidelines exercises have identified two general principles for focusing the expenditure structure: (i) priority of controlling public consumption, public pensions provisions, health care, passive labour market measures and subsidies; (ii) priority in favouring productive activities such as investment in infrastructure, human capital, and active labour market initiatives. To the extent that such a restructuring would lead to a reduction in the number of people of working age receiving social transfers and/or to an increase in employment, it would help to improve budgetary positions over the medium term. However, *ex post facto*, it appears that a number of Member States had difficulties in applying these principles. For instance, the EU average share of public capital formation in GDP fell from 2.9 per cent in 1992 to 2.2 per cent at present and the shift from passive to active labour market policies seems to be somewhat slow. It may therefore be asked whether, in the future, such expenditures should not be better preserved from the general consolidation process.

As regards the structure of taxation, the Broad Guidelines and the 1998 Employment Guidelines recommended, for most Member States, a reduction in the social contribution burden or in tax wedges as a whole, in order to reverse the trend towards an increase in the tax burden borne by employed labour (which rose from 35 per cent in 1980 to more than 42 per cent at present). It is essential that the timing and modalities of efforts to reduce the tax burden on labour are decided upon with a view to maximising their employment effects while fostering sound public finances. In

a broader perspective, apart from an overall reduction in the general level of taxation, as called for by the Amsterdam European Council and the 1997 Broad Guidelines, the Commission regards it as essential to achieve greater fiscal coherence throughout the Union. To this end, following the adoption of a code of conduct in December 1997 and in conformity with the Luxembourg European Council Resolution on Policy Co-ordination, which asks explicitly for "... tax reform to raise efficiency and the discouragement of harmful tax competition", the Commission will endeavour to reach agreement in other important areas, such as the taxation of capital income and a Community framework for the taxation of energy products. These points will be further covered in sections 4.4 and 4.5.

3.4. Wage developments

In EMU, wage setting will remain the responsibility of the social partners at the national, regional, sectoral or even at a more decentralised level following their respective traditions. As underlined in the Amsterdam Resolution on "Growth and employment", the social partners are responsible to reconcile high employment with appropriate wage settlements and to set up a suitable institutional framework for the wage formation process. The social dialogue is important for achieving the right results. For that reason, the Broad Guidelines urged the Commission to continue to develop the European social dialogue, especially on macroeconomic issues, on the basis of the Broad Guidelines. National governments retain a considerable responsibility for wage setting, both because of their role as a large employer and because they set the macroeconomic framework and determine the labour market rules and regulations in which the social partners operate.

The requirements for employment-friendly wage trends in EMU are no different from those already specified in the Broad Economic Policy Guidelines: (i) nominal wage increases must be consistent with price stability; (ii) real wage increases with respect to productivity should take into account the need to strengthen the profitability of investment and to support the purchasing power of wage earners; and (iii) collective agreements should better reflect, in a pragmatic way, productivity differentials according to qualifications and skills, regions and, to some extent, sectors. These recommendations concern wage developments in countries which will participate in EMU but also in the other Member States as they should be equally committed to stability-oriented policies[10].

The credibility of the EMU macroeconomic framework and the increased competition in the single currency zone is likely to strengthen wage and cost discipline. The *conditions* for maintaining appropriate wage trends will be improved because EMU will provide low inflation, secured by the ECB, as well as lower inflation variability because sudden shifts in exchange rates are ruled out among participating countries. The known and credible price stability objective will facilitate agreement on moderate and appropriate wage increases. In countries where the social partners agree on moderate wage increases in order to help strengthen employment, they no longer risk seeing the job benefits of their moderation undermined by currency appreciation relative to EMU partners. The *incentives* for wage discipline will be improved too because irresponsible and inappropriate wage increases can no longer be accommodated by national monetary and exchange rate policies.

If there were to be national or regional wage agreements not in line with these general rules, this would not necessarily imply an acceleration of inflation in the entire monetary union. Even in the country or region concerned, the impaired competitiveness would probably lead less to higher inflation but more to higher imports from other regions, since in the monetary union and with the internal market the elasticity of supply will be high. As the reduced competitiveness would risk resulting in lower employment in the country or region, it is probable that the social partners would avoid such an outcome.

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[10] See also, "Wage policy and employment in Economic and Monetary Union", Opinion of the Economic Policy Committee to the Ecofin Council, October 1997.

On the other hand, national or regional differences in wage developments will continue to be possible and necessary in EMU, especially if a healthy catching-up process is developing. Catching-up countries tend to have a higher trend in productivity growth in the exposed sector and therefore have room for higher real wage increases while maintaining competitiveness and profitability. Developments in Ireland since the mid-1980s clearly illustrate this point. Continued moderation of nominal wage increases has led to higher investment and higher productivity growth which in turn permitted a rise in real wages that lay clearly above the EU average, without affecting inflation and competitiveness and allowing for strong growth and employment (see also footnote 7, page 8).

While the responsibility of the social partners for employment trends will be enhanced in general, two special cases merit attention. Firstly, the increased transparency of wage and costs levels between Member States due to the existence of a single currency and the elimination of exchange rate fluctuations, may lead to a certain increase in labour mobility but may also give rise to wage claims in lower-wage countries to close the gap with higher wage countries. As noted above, an increase in wages faster than warranted by productivity levels in a country or region would lead to a deterioration in competitiveness and investment profitability and therefore to reduced attractiveness as a production location. The country or region's export performance would suffer, investment would be deterred and unemployment would increase. Through a process of labour shedding and capital-labour substitution, labour productivity could gradually increase to match the higher level of wages. But such a process would entail further job destruction and higher unemployment. For these reasons, "wage imitation" must be avoided[11].

Secondly, as a consequence of the transfer of national monetary and exchange rate policies to the Union level, the role of other adjustment instruments will be enhanced in the event of possible country-specific disturbances. It will be particularly important to assure that wage adjustment plays a positive role in re-establishing output growth and employment following asymmetric shocks (see also section 4.2).

4. EMU AND STRUCTURAL POLICIES FOR GROWTH AND EMPLOYMENT

4.1. Concepts, subsidiarity and Community coherence

The Maastricht convergence process has championed greater clarity and a remarkable consensus on the role of macroeconomic policies in bringing about higher growth and employment. A similar degree of understanding has not yet emerged with respect to structural policies. However, at the EU level, considerable progress towards a more rational debate is taking place, fostered by the procedures established by the Internal Market programme, the Broad Economic Policy Guidelines and the Employment Title of the Amsterdam Treaty.

There can be no doubt that structural policies have a key role to play in stimulating economic growth, restoring competitiveness and raising employment levels. In economic terms, their key role is to help ensure a tension-free macroeconomic growth process, to reinforce the EU's competitiveness (and therefore increasing the potential growth of productivity), to increase the employment-content of growth and to make growth more respectful of the environment. However, to reach their full effectiveness, they must be coherent with the pursuit of sound macroeconomic policies. In this respect, it is essential that the budgetary costs of structural reform are kept under control and do not jeopardise the achievement of sound budgetary positions. Their economic benefits also emerge only gradually over time and they are clearly more efficient in a context of higher economic growth.

[11] The analysis of present labour cost differences between regions in Europe suggests that these differences largely reflect the existing discrepancies in labour productivity.

Most structural policies are the responsibility of national governments and of the social partners. It is obvious that in these fields the principle of subsidiarity must be respected. It is, however, equally clear that in implementing structural policies, Member States must take into account a certain number of principles and the necessity of coherence at the level of the Union. These principles include *inter alia* (i) respect of the Treaty principle of an open market economy, with free competition; (ii) the need not to impede the proper functioning of the internal market; (iii) consistency with the macroeconomic strategy; (iv) respect of certain social values and the equality of opportunity and, finally, (v) respect for the environment. In full respect of the principle of subsidiarity, a combination of Community surveillance, joint actions and exchange of national practices offers the potential of strengthening the competitiveness, growth and job performance of the Member States and the Union.

Finally, the Resolution on "Growth and employment" adopted by the Amsterdam European Council asked that the Broad Economic Policy Guidelines put more emphasis on growth and employment through the co-ordination of macroeconomic and structural policies. The Resolution also contains a request for the Community itself to complete national measures by all relevant Community policies having an impact on growth and employment, like e.g. the TEN's and R&D policies and by an increased responsibility of the European Investment Bank in financing the development of high-tech projects in SMEs, in studying interventions in education, urban renewal and environmental protection and in increasing its interventions in the field of the high-priority TEN projects adopted in Essen. The Commission has also proposed the creation of a Research Fund in the field of Coal and Steel following the expiration of the CECA Treaty.

4.2. Enhanced need for structural adjustment in EMU

In the EU, the implementation of structural reform has so far been uneven, with considerable progress in some fields, particularly product markets, and rather less in other areas, especially labour markets. Justified efforts aimed at further correcting structural deficiencies, which are deeply rooted in the European economies, are made all the more pressing by the imminence of EMU. The introduction of a single currency reduces the instruments available to the national authorities to tackle disturbances that affect their economy differently. It will no longer be possible to absorb or dampen them through nominal exchange rate adjustments.

Some observers have expressed doubt whether EMU Member States will be sufficiently well equipped to cope with economic shocks, especially asymmetric shocks that have differential effects across countries. The first point to recall is that the exchange rate instrument is only suitable to deal with shocks that are country-specific, real and temporary. Already today, such shocks are exceptional. Furthermore, in EMU, there are grounds for believing that the incidence of asymmetric shocks will be limited for various reasons. In the past, the asymmetric character of shocks was considerably amplified by diverging monetary, exchange rate and budgetary policies. In EMU, with a common monetary policy and exchange rate and with consensus and limits on budgetary policies, such developments will become much more rare and much smaller, leading to better prospects for more cyclical convergence. Finally, while most Member States already have highly diversified industrial structures -- more diversified than in the United States -- increased product market integration may possibly, in line with the historical experience of the Union, stimulate intra-industry trade between Member States and further enhance the diversification of industrial structures.

When asymmetric shocks do occur, the correct policy response would depend on the nature of the shock. In the case of a temporary domestic demand disturbance, the automatic stabilisers and possibly other budgetary measures to cushion the negative demand impact will be desirable and sufficient. As already noted, when it will reach its cruising speed, the Stability and Growth Pact allows sufficient room for this to occur. The automatic budgetary stabilisers in fact will provide more stabilisation in EMU Member States than is the case for instance in individual US states even

though the latter benefit from net budgetary transfers from the Federal government. But in addition to budgetary stabilisers, some shocks, notably those that affect the competitiveness or the external balance of the economy, may require adjustment of relative prices which in EMU can only come about through changes in the rate of wage growth, profit margins or productivity growth. This underscores the need for EU Member States to further reform product, services and labour markets to enhance flexibility and efficiency.

Failure to make resolute headway in bringing about a greater flexibility of the Member States' economies will have serious consequences; economic growth will not be sufficiently bolstered, employment levels will not be significantly raised and progress towards greater economic and social cohesion among the Member States will be jeopardised. On the other hand, EMU itself is likely to act as a catalyst for structural reform. The single currency will unleash competitive forces that will strengthen the incentives for structural reforms, thereby improving the chances for reducing unemployment. Policy makers have recognised the importance of flexible markets to help in adjusting to shocks and to make their economies more efficient. With the adoption of an Action Plan for the Single Market and the 1998 Employment Guidelines, the Council took decisive actions last year. It is essential to carry these plans through and to complement them, especially at the national level, with measures in other fields.

4.3. Sectoral changes in the growth process and structural policies

Technical progress and globalisation lead to permanent structural changes in the growth process. They put constant pressure on the economy to maintain and improve competitiveness and productivity and unleash a dynamic process of job creation and job destruction. In sectors with high increases in productivity, fierce international and intra-EU competition leads to falling relative prices which in turn allow productivity gains, for a large part, to be passed on to the rest of the economy through the price mechanism. This market-induced transfer of purchasing power allows for rising relative prices in sectors with low productivity gains and less competitive pressure, thereby permitting the creation of profitable jobs in these sectors.

This is an age-old process, for which there is clear statistical evidence, and which requires that the price mechanism operates effectively. To a large extent the opening-up of markets and the liberalisation and deregulation of previously closed sectors have met this condition. Nevertheless, in order for this process to create sufficient jobs there are two further prerequisites: (i) sectoral change must be accepted, including more labour mobility, and be assisted by strengthened efforts to improve human capital formation, in particular with respect to low-skilled labour, and has to occur in a socially acceptable manner; (ii) the growth rate in the economy at large must be sufficiently high for the balance between sectoral job creation and sectoral job losses to be positive and large enough to bring about a fall in unemployment.

These two conditions are interrelated. The stronger the overall economic growth, the easier the process of sectoral change will be, and the more readily its social effects can be cushioned. Only if efforts to increase competitiveness and productivity are accompanied by correspondingly high growth and rising employment levels can the potential prosperity gains from technical progress, globalisation and the internal market be fully exploited. On the structural side, it will be necessary to ensure that product and services markets function efficiently and that the labour force is employable and adaptable, thereby underscoring the need for a determined implementation of the specific recommendations contained in the 1998 Employment Guidelines.

4.4. Better functioning product and service markets

The functioning of product and services markets covers many aspects.

The process of sectoral change and the interplay of relative prices described in section 4.3 require that the price mechanism works fully in the EU. Price flexibility will be of even greater importance after the introduction of a single currency. Competition policy will thus remain of critical importance under EMU in order to ensure that neither private, nor public behaviour undermines effective competition in more globalised and integrated markets.

All too often, the product and services markets in the EU are still submitted to outdated or corporatist regulations that hamper their full development. The suppression or modernisation of these regulations when made in a socially acceptable way is likely to favour entrepreneurship and to allow a faster growth without tensions in the relevant sectors. These deregulation efforts are all the more needed to promote the start up of firms and to encourage the development of self-employment. In that way, environmentally sustainable production and consumption patterns and further development of eco-industries could also be promoted.

Improved functioning of markets for goods and services will also require timely and full completion of the internal market programme, in conformity with the Commission's Action Plan. The Single Market represents the cornerstone of Economic Union. By favouring an efficient allocation of resources and reinforcing competition, it will contribute to the good functioning of markets, which is essential to the sustainability of Monetary Union.

In the EU, significant barriers to market access still exist in sectors accounting for approximately half of the GDP of the EU. In the field of goods, the main barriers are to be found in the fields of public procurement and construction (which alone accounts for 10% of GDP). For services such restrictions are frequent in services sold to other enterprises (producer services) as well as in those sold to the final consumer (consumer services). They include on the one hand key services for industry such as energy, telecommunications and transport, financial services and business, particularly professional, services and on the other hand such services as commerce and distribution, household and welfare services.

Amongst the services with the tightest restrictions are to be found most of the sectors with the highest job creation potential. In their search for the most efficient forms to organise production, companies have externalised services that have formerly been provided within the company itself. This process has been driving the growth of producer services, as has the growing intangible content of products.

Several infrastructure services have in the past been delivered predominantly by monopoly suppliers. Here, liberalisation of markets may initially lead to significant job losses amongst established suppliers as they quickly exploit the latent potential for productivity gains attainable in these industries. However, the consequences of liberalisation are the growth of new market entrants, the development of new products using infrastructure services and the increased investment in infrastructure capital goods. This means that job creation has proved positive overall in those countries where liberalisation has been achieved. The leading example is telecommunications. A competitive market in this field is also a necessary requirement for the development of the information society and the introduction and expansion of electronic commerce.

The job creation potential of services supplied to consumers is particularly significant, because most of them occur in a geographically limited area and are little traded. Therefore, they are not exposed to pressure from third countries with low wages, despite being labour-intensive. In addition, the changing structure of demand in developed countries means that these services have

one of the highest output growth rates. A comparison with other developed countries demonstrates that particularly the job creating component of service growth has been significantly less than in North America and Japan.

In the framework of the Commission's Action Plan, and in line with the Resolution on economic policy co-ordination attached to the Luxembourg European Council conclusions, all factors affecting the efficiency of Member States' economies as well as the structural impediments which diminish their growth and job-creation potential will have to be scrutinised. This requires that special attention be paid to policies in the areas of product- and services-market competition, taxation, state aids and the labour market, while fully respecting the principle of subsidiarity. Such an exercise of multilateral surveillance of structural factors would be a natural complement to the on-going macroeconomic multilateral surveillance. It would aim to ensure, not only the sustainability of EMU, but also its success in terms of deeper integration and a more solid and flexible economic union.

At the Community level, simplification and modernisation is going on. In its work programme for 1998, the Commission will notably draw conclusions from the second phase of the pilot scheme for the simplification of legislation for the internal market (SLIM) and the work of the Business Environment Simplification Task Force (BEST) with a view to simplifying administrative formalities and easing regulatory constraints, especially for SMEs. In 1998, the Commission will launch phase III (dealing with legislation related to social security rights and insurance markets) and phase IV of SLIM.

The Internal Market and overall globalisation exert a strong pressure to improve competitiveness, but the latter is also linked to national or Community policies in the field of R&D and, notably, the information society. The logistic environment of firms is also critical for a smooth development of trade relations and warrants a strengthening of efforts in TEN and national infrastructure projects both in keeping an adequate share of public investment in overall public expenditure and by searching for joint ventures with the private sector where appropriate.

Finally, the opening-up of the markets of third countries for both goods and services from the European Union can have an important impact on job creation. Barriers to market entry in third countries for services are a frequent case, while at the same time advances in communications technology make many more services directly tradable across borders. Restrictions on inward investment and inadequate protection of intellectual property rights also weaken European industry's capacity to penetrate foreign markets and reduce the returns on past intangible investments. Significant progress to open third-country markets has been made through the Uruguay Round and WTO. Effective implementation of this agreement along with enlargement of the Union to the Central and Eastern European Countries constitute significant levers for action of the European Union.

4.5. Policies for efficient labour markets

The European Union has developed a strategy in the field of employment based on two pillars. At the economic policy level, including macroeconomic and structural elements, the Broad Economic Policy Guidelines define an overall policy mix favourable to growth and employment in the stability framework of EMU and this aspect should be strengthened in the future, in agreement with the Resolution on "Growth and employment" adopted by the Amsterdam European Council. At the same time, in anticipation of the Employment Title of the Amsterdam Treaty, the Council adopted in December 1997 Employment Guidelines for labour market policies. These Employment Guidelines are co-ordinated with the Broad Economic Policy Guidelines in order to make them consistent and mutually supportive. They will also be transposed into National Action Plans, which will be discussed for the first time at the Cardiff European Council in June 1998.

These Employment Guidelines propose basically four lines of action:

- Improve the "employability" of manpower;
- Promote entrepreneurship;
- Encourage the adaptability of firms and workers;
- Strengthen the policies for equal opportunity.

From an economic viewpoint, the first line of action (employability) covers all policies (training and improvement in human capital, active measures in favour of the young or long-term unemployed) which aim at avoiding tensions on the labour market particularly when unemployment starts to fall significantly during the growth process and at making better use of the growth potential offered by the labour reserve. The conditions for the sound working of these measures have already been dealt with in section 2.3 above.

The second line of action (entrepreneurship) is closely linked to reforms on the product and service market (section 4.4 above) and is directly concerned with the most important bottleneck on the labour market at present, i.e. the insufficient creation of new job posts.

Finally, allied to equity objectives, the last two areas of action (adaptability and equal opportunities) aim at increasing the employment rate and at making growth more employment creating. The third line of action (adaptability) seeks to encourage a more dynamic approach to improving the employment situation by making enterprises more productive and competitive. This includes, notably, actions by governments and the social partners aimed at modernising work organisation (including working time, new forms of contracts, etc.) while achieving the right balance between flexibility and security. The fourth line of action (equal opportunities) aims at increasing the employment rate by tackling gender gaps, reconciling work and family life, facilitating reintegration into the labour market and promoting the integration of people with disabilities into working life.

As regards the increase in the labour content of growth, structural reforms have the effect that apparent labour productivity grows more slowly, so that more jobs could be generated for a given rate of GDP growth. Obviously, the purpose is neither to hamper productivity at the sectoral or company level, nor to reduce the organisational and technical progress, since it would be damaging for competitiveness and general welfare. In this reasoning, the slowdown in the apparent labour productivity at the macroeconomic level may result from:

(i) less substitution of labour by capital;
(ii) a greater sharing of working time (reorganisation and reduction of working time, including part-time jobs).

(i) Slowdown of labour by capital substitution via a widening of the wage scale

As already presented in section 2.4, from a macroeconomic viewpoint, a process of moderate overall wage increases, within a given wage structure, and which does not distribute the increase in productivity coming from capital-labour substitution into real wages, as happened in 1982-89 and 1992-96, would act in the right direction but will take some time to bring significant effects, unless the moderation is very intense. On the other hand, these substitution effects would be completed with strong, immediate, profitability effects thanks to the reduction in real unit labour costs. The latter, in turn, have a powerful potential impact on employment in making possible a stronger classical, investment-supported, growth exceeding the productivity trend when demand prospects are good.

An alternative approach would be to assume that the wage scale could be strongly opened, especially downwards. At present, it is deemed that the EU economies are not using all the employment opportunities, especially in low-skilled, low-productivity activities that are presently priced out of the market by too high wage costs. Should the conditions be created permitting the

full use of these opportunities, re-introducing in the production process activities with below-average productivity would, all other things being equal, entail a reduction in the apparent productivity of labour.

There are basically two ways to "price in" activities with excessive wage costs relative to the productivity level in the activity concerned.

- Widen the wage distribution downwards -- In order to reach its target, a downward widening of the wage scale would imply a fall in the wage cost of low-skilled activities by about 20 to 30 percent, as happened, for instance, in the United States during the 1970s and 1980s. Furthermore, in order to be efficient, the downward extension of the wage distribution would require in Europe a corresponding lowering of unemployment compensations and social protection schemes in order to eliminate the so-called "poverty trap".

  This would, *ceteris paribus*, widen the income distribution towards larger inequality and, at the limit, would create "working poor" groups, unable to survive decently from their wages. Such an evolution would introduce in Europe a form of exclusion just as damaging for social cohesion as unemployment and it is worth noting that in the United States, these consequences are now deemed to be sufficiently serious for warranting a switch towards a less extreme system and welfare support in the form of the so-called ''Earned-Income Tax Credit''. In Europe, this would mean that part of the saving in unemployment compensation would have to be switched to other forms of social transfers and would therefore not alleviate the public budget constraints.

  This form of wage-cost reduction would thus be difficult to apply in the EU although pragmatic collective agreements between the social partners, including entry level wages for the long-term unemployed, may make some contribution to it.

- Reduce non-wage labour costs -- In most countries, social security contributions form by far the largest part of taxes on labour. Often they have a complex structure which, besides their undesirable aspect of a tax on the use of labour, also makes them weigh relatively more heavily on low wages. Furthermore, these systems were created as an expression of social solidarity at a time when the number of contributors was high (low unemployment and a high employment rate), budgets were balanced and the degree of solidarity could increase. At present, the employment rate and thus the number of contributors has fallen (cf. section 2.2), social expenditures are growing and significant reductions in the degree of generosity are politically difficult to implement. This resulted in a vicious circle of ever-increasing social contributions and tax wedges on a decreasing proportion of working persons in the total number of potential beneficiaries. For instance, the share of social security contributions in GDP, which was about 10.5 per cent in 1970 is presently at about 16 per cent for the EU as a whole and represents only a part of the total tax wedge in overall wage costs.

  Initially, between 1970 and 1981, the increase in the tax wedge went together with an increase in total labour costs per unit of output, i.e. the share of the overall wage bill in GDP. Indeed, during those years, the wage share in GDP increased by 4.6 percentage points. However, between 1981 and 1997, the strong wage moderation has more than compensated for this increase. Between 1981 and 1997 the wage share in GDP decreased by 6 percentage points, bringing wage costs per unit of output below their level of 1970. Thus, the increase in the tax wedge has been totally passed on to wage income. This evolution is expected to continue in the near future, thereby contributing to a further improvement in profitability (see section 3.4 above).

  But, in spite of this favourable development of overall labour costs per unit of output, it is indisputable that, at the individual level, the tax wedge remains very high and is especially

harmful at the low end of the wage scale where it causes pricing-out of the market for low-skilled, low-pay jobs and an increase in "black market" activities.

Given the dimension of the tax wedge, there is room for a cut in wage costs for the employers without reducing the net wage income of wage earners. However, a general, across the board, reduction would have no more effect on unit labour costs than a few years of further wage moderation but would either imply a strong reduction of social benefits or have a high budget cost which would go well beyond the automatic stabiliser effects of a lower number of unemployed. This reduction would thus need to be compensated for by other fiscal reforms (including, where appropriate, higher environmental taxes) which should of course have as little negative side effects (in terms of inflation, for instance) as possible, a constraint that is not easy to satisfy. On the other hand, cuts in the tax wedge would be most efficient when targeted at specific labour force groups at the low end of the wage scale (young workers, long-term low skilled unemployed) where their impact might be more substantial, especially when combined with active labour market measures in education, apprenticeship schemes, vocational training and re-training, etc., which could be partly financed by using social transfers such as unemployment benefits in a more active way and new forms of partnerships with the private sector. In that way, the budgetary consequences may remain within manageable limits. In this context and to maximise the employment impact, care needs also to be taken to reduce as much as possible substitution and dead-weight effects resulting from targeted cuts in the tax wedge.

These reductions of the tax wedge should be inserted in the general reforms of the social security systems and the tax structure that are needed for many other reasons (ageing, explosion of health expenditure, elimination of "poverty traps", introduction of environmental taxes, etc.).

Thus, a sustained attention to the relationship between wages and productivity, integrated into the normal process of collective wage negotiations, combined with fiscal reform where applicable, would help to make growth more employment creating by fostering market conditions conducive to the return, and the development, of activities currently priced out of the market and by reducing the "black" economy[12].

(ii) Reduction in working time

The secular reduction in the number of hours worked in industrial countries has undoubtedly been a factor of social progress and welfare in this century. But it must be noted that most progress in this field was made during periods of fast growth and high employment and were part of a "work versus leisure" choice. The trend is, in fact, nothing more than a distribution of productivity growth, with lower working times and less growth in real income. A return to this secular trend when growth recovers may therefore be expected and would be quite normal and welcome as an improvement in working conditions and quality of life.

In periods of recession and high unemployment, however, it is often put forward that a massive, across the board, compulsory reduction in working time would be the fastest and most efficient solution for a significant reduction of unemployment. This approach, in fact considers the amount of work available to be somehow fixed and that the only way to reduce unemployment is thus to redistribute it over the whole labour force, with less hours worked per individual.

Such a solution nevertheless raises a number of questions:

[12] A slowdown of capital for labour substitution could for instance result from well-designed measures supporting pent-up demand for new activities, notably in services to persons and communities, without a fall in the productivity level of existing production.

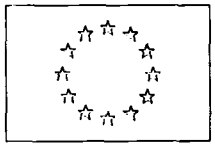
- A compulsory reduction in working time may have adverse consequences in firms where labour and capital are used in a fixed proportion at a given point in time. If the firm is organisationally unable to maintain the total number of hours worked (through additional hiring and/or decoupling between labour hours and capital hours), its productive capacity is likely to be reduced, even if productivity per hour increases[13] somewhat. This entails a reduction in potential output growth (i.e. in the potential creation of wealth and income) which could be negative in the long run for employment.
- If one wants to avoid a deterioration of profitability which would negatively affect investment and thus compress even more the productive potential, the growth of real wages per capita would have to be adjusted downwards in order to avoid a deterioration in real unit labour costs. Such a reduction may be difficult to obtain and cause severe and conflicting problems in terms of income distribution.

However, this should not exclude specific measures of working time reduction at the microeconomic level where it is warranted by local conditions, negotiated by the social partners and is either reversible or can be seen as integrated into the secular trend of reduction in working time.

In this context, some initiatives suggest that measures combining a reduction of working time with job creation and fiscal advantages could entail positive results.

Another approach for increasing the labour content of growth would be to encourage, if need be by revision of existing legislation, the maximum use of *voluntary* part-time and new forms of employment. The possibilities in that field are obviously very different in Member countries given the very large differences in the proportion of part-time workers that one may observe at present.

[13] This is the major reason why a reduction of working hours would have to be significant in order to have a positive employment effect.



EUROPEAN COMMISSION

GROWTH AND EMPLOYMENT IN THE STABILITY-ORIENTED FRAMEWORK OF EMU

Economic policy reflections in view of the forthcoming 1998 Broad Guidelines

STATISTICAL ANNEX

TABLES

GRAPHS

Table 1

The European economy [*] – Key Indicators

(% change p.a. if not otherwise indicated)

	61-73	74-85	86-90	91-96	1990	1991	1992	1993	1994	1995	1996	Forecasts Autumn 1997 1997	1998	1999
Economic growth (real % change p.a.)														
Private consumption	4.9	2.2	3.7	1.5	2.9	2.2	1.8	-0.3	1.7	1.8	2.1	2.1	2.5	2.6
Government consumption	3.8	2.5	2.0	1.1	2.1	1.8	1.5	1.2	0.3	0.5	1.0	0.8	1.2	1.5
Gross fixed capital formation	5.7	-0.1	5.7	-0.1	3.6	-0.4	-0.9	-6.6	2.5	3.6	1.3	2.6	4.7	5.5
of which equipment	-	2.1	7.2	0.0	5.4	0.2	-3.7	-11.5	4.3	7.5	3.0	4.5	6.3	7.0
of which construction	-	-1.0	4.9	-0.1	3.4	-0.3	1.1	-3.7	1.2	1.3	0.0	1.2	3.3	4.2
Exports of goods and services[a]	8.0	4.3	5.0	5.3	6.6	5.0	3.7	1.7	9.0	7.9	4.7	7.9	7.4	7.2
Imports of goods and services[a]	8.7	2.8	7.4	3.9	6.1	4.1	3.9	-3.0	7.7	6.7	3.9	6.7	7.0	7.2
GDP	4.8	2.0	3.3	1.6	2.9	1.5	0.9	-0.5	2.9	2.4	1.8	2.6	3.0	3.1
Demand Components : Contribution to changes in GDP (%)														
Consumption	3.6	1.7	2.6	1.1	2.1	1.6	1.4	0.0	1.1	1.2	1.5	1.4	1.7	1.8
Investment	1.3	0.0	1.2	0.0	0.6	-0.1	-0.2	-1.4	0.5	0.7	0.3	0.5	0.9	1.1
Stockbuilding	0.0	-0.1	0.1	0.0	-0.1	-0.4	-0.1	-0.5	0.9	0.2	-0.3	0.2	0.1	0.0
Domestic demand	4.9	1.6	3.8	1.1	2.6	1.2	1.0	-1.9	2.5	2.1	1.4	2.1	2.7	2.9
Exports[b]	-	0.4	0.1	0.6	0.3	0.3	0.4	1.4	0.9	0.9	0.9	1.4	1.1	1.1
Final demand[b]	-	2.1	3.9	1.9	3.1	1.5	1.5	-0.4	3.4	3.0	2.3	3.5	3.9	4.1
Imports[b] (minus)	-	-0.1	-0.6	-0.4	-0.2	0.0	-0.5	0.0	-0.5	-0.5	-0.6	-0.9	-0.9	-1.0
Net exports	-	0.4	-0.5	0.4	0.1	0.2	-0.1	1.4	0.4	0.4	0.3	0.5	0.2	0.1
Savings and Investment in % of GDP														
Private sector	21.2	21.1	20.6	20.9	20.8	20.1	20.6	21.0	21.3	21.7	20.7	19.9	19.8	19.8
of which households[c]	10.3	12.5	10.0	9.1	9.8	10.0	9.1	9.3	8.7	8.9	8.5	8.1	7.9	7.7
of which enterprises[c]	10.9	8.6	10.8	11.8	11.0	10.1	11.5	11.7	12.6	12.8	12.2	11.8	11.9	12.1
General government	4.1	0.5	0.2	-1.7	0.2	-0.4	-1.7	-2.7	-2.3	-1.8	-1.3	-0.2	0.4	0.9
National savings	25.3	21.6	21.0	19.2	21.0	19.7	18.9	18.3	19.0	19.9	19.4	19.8	20.2	20.7
Gross capital formation	24.7	21.9	20.8	19.4	21.7	21.1	20.1	18.4	19.0	19.4	18.7	18.7	19.0	19.4
Current account	0.4	-0.4	0.1	-0.3	-1.0	-1.9	-1.7	-0.1	0.0	0.6	0.9	1.3	1.4	1.4
Determinants of investment														
Capacity utilisation ratio	-	-	83.1	80.8	84.9	82.5	80.5	77.7	79.8	83.0	81.2	82.0	-	-
GDP gap	-	-1.9	1.1	-1.3	2.2	1.2	-0.2	-2.7	-2.0	-1.7	-2.1	-1.7	-1.1	-0.6
Profitability index (1961-73=100)	100.0	72.9	88.1	94.8	90.5	90.0	90.5	89.2	96.6	99.6	102.6	107.0	111.0	113.6
Growth potential														
Capital/Output ratio (C/GDP)	3.0	3.3	3.3	3.4	3.3	3.3	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.3
Capital intensity	4.5	2.9	1.2	2.6	1.2	2.5	4.0	3.9	2.3	1.4	1.9	1.5	1.3	1.1
Growth of capital stock (real)	4.9	2.9	2.5	2.2	2.9	2.6	2.5	1.9	1.9	2.0	2.0	2.0	2.2	2.4
GDP growth (real)	4.8	2.0	3.3	1.5	2.9	1.5	0.9	-0.5	2.9	2.4	1.8	2.6	3.0	3.1
Productivity growth (GDP/pers.empl.)	4.4	2.0	1.9	2.0	1.2	1.3	2.4	1.4	3.3	1.9	1.5	2.1	2.1	1.8
Employment and Unemployment														
Employment	0.3	0.0	1.3	-0.4	1.7	0.1	-1.4	-1.9	-0.4	0.6	0.2	0.5	0.8	1.3
Activity Rate as % of pop.15-64	-	-	67.3	67.8	67.8	68.3	68.1	67.6	67.6	67.6	67.7	-	-	-
Employment rate (benchmark) [d], %	67.5 (1960)	65.2 (1974)	61.3	60.9	62.6	62.7	61.8	60.4	60.1	60.3	60.3	-	-	-
Employment rate, full-time equivalent%	-	-	57.0	56.0	58.0	58.0	57.0	55.6	55.1	55.2	55.0	-	-	-
Unemployment rate % of active pop. [e]	2.3	6.4	8.9	10.2	7.7	8.2	9.3	10.7	11.2	10.8	10.9	10.7	10.3	9.8
Prices and wages														
Nominal wages	9.9	12.4	6.2	4.7	7.6	7.1	7.0	4.1	3.4	3.2	3.4	3.2	3.2	3.5
Real wages [f]	5.0	1.5	1.9	0.8	2.6	1.4	2.2	0.1	0.1	0.2	0.8	1.1	1.0	1.2
Nominal unit labour costs	5.3	10.2	4.2	2.7	6.3	5.7	4.5	2.7	0.1	1.3	1.9	1.1	1.0	1.6
Real unit labour costs	0.0	-0.3	-0.6	-0.9	0.9	0.2	0.0	-0.9	-2.4	-1.6	-0.5	-0.8	-0.9	-0.6
GDP deflator	5.2	10.6	4.9	3.6	5.4	5.5	4.5	3.6	2.6	2.9	2.4	1.8	2.0	2.2
Private consumption deflator	4.7	10.7	4.3	3.9	4.9	5.6	4.7	4.0	3.3	3.0	2.6	2.1	2.2	2.2
Terms of trade	0.4	-1.3	1.7	0.2	0.6	0.4	1.2	0.1	-0.7	-0.4	0.3	-0.2	-0.1	-0.1
General government budget, % of GDP														
Expenditure	-	46.3	46.2	50.9	46.2	49.4	50.8	52.4	51.3	51.0	50.4	48.7	47.9	47.1
Current revenues	-	42.7	44.9	45.8	44.7	45.2	45.6	46.3	45.9	45.9	46.1	46.0	45.6	45.3
Net borrowing	-	3.6	3.3	5.0	3.5	4.2	5.1	6.1	5.4	5.1	4.2	2.7	2.2	1.8
Net borrowing cyclically adjusted	-	3.4	3.9	4.8	5.2	5.3	5.5	5.1	4.8	4.7	3.8	2.1	2.0	1.9
Debt	-	-	54.9	65.7	55.3	56.0	60.4	66.0	67.9	70.9	73.0	72.3	71.3	69.7
Monetary conditions														
Long-term interest rate (1)	-	-	9.8	8.6	11.1	10.3	9.8	7.8	8.2	8.3	7.1	6.2	6.1	6.2
Short-term interest rate (2)	-	-	9.8	8.2	11.7	11.0	11.2	8.6	6.6	6.7	5.1	4.6	4.4	4.5
Yield curve (1-2)	-	-	0.0	0.4	-0.6	-0.7	-1.4	-0.8	1.5	1.6	2.0	1.6	1.7	1.7
Long-term interest rate adjusted for inflation[g]	-	-	4.7	5.0	5.4	4.6	5.1	4.0	5.4	5.5	4.8	4.2	3.3	-
DEM/USD	3.76	2.38	1.84	1.57	1.61	1.66	1.56	1.65	1.62	1.43	1.50	1.75	1.81	1.80
Nominal effective exchange rate	0.3	-4.1	5.9	-1.6	12.6	-3.7	2.5	-12.5	-2.2	3.9	2.3	-4.6	0.4	-0.2
Real effective exchange rate (Index: 1991=100)	93.3	95.5	93.5	95.8	103.0	100.0	104.7	92.7	89.6	92.8	94.9	89.2	88.3	87.1

[*] EU including the new German Länder from 1991; for percentage changes from 1992.
[a] Including intra-EU trade.
[b] Extra-EU trade.
[c] EUR12 until 1993.
[d] 1960 figure from the national accounts (Ameco).
[e] Eurostat definition.
[f] Private consumption deflator.
[g] GDP deflator.

Source: Commission services.

Table 2

Main Economic Indicators, 1995-1999 (Autumn 1997 forecasts)

1997	Population	GDP national currency (bln)	GDP in ECU (bln)	GDP p/head ECU (thou)	GDP p/head PPS EUR=100
B	10.2	8622	212.6	20.9	113.0
DK	5.3	1078	144.0	27.3	117.1
D	82.2	3658	1862.6	22.7	109.5
EL	10.6	32679	105.6	10.0	66.2
E	39.3	77389	466.6	11.9	77.5
F	58.6	8151	1230.9	21.0	106.1
IRL	3.6	49	65.7	18.0	103.7
I	56.8	1946520	1009.6	17.8	102.4
L	0.4	556	13.7	32.6	161.7
NL	15.6	701	317.2	20.3	108.6
A	8.1	2502	181.0	22.4	109.6
P	9.4	17843	90.0	9.6	69.2
FIN	5.1	607	103.3	20.1	99.6
S	8.9	1745	201.5	22.7	99.5
UK	59.0	789	1141.2	19.3	96.6
EUR	**373.1**	-	**7145.8**	**19.2**	**100.0**
USA	267.6	8074	7185.9	26.9	144.7
JAP	125.9	512777	3825.4	30.4	118.0

GDP at constant prices (annual % change)

	1995	1996	1997	1998	1999
B	2.1	1.5	2.4	3.0	3.1
DK	2.6	2.7	3.5	3.3	3.2
D	1.9	1.4	2.5	3.2	3.3
EL	2.0	2.6	3.3	3.5	3.9
E	2.8	2.3	3.3	3.5	3.6
F	2.1	1.5	2.3	3.1	3.1
IRL	11.1	8.6	8.6	8.1	7.6
I	2.9	0.7	1.4	2.5	2.8
L	3.8	3.0	3.4	3.8	4.0
NL	2.3	3.3	3.1	3.6	3.3
A	1.5	1.6	1.9	2.8	3.3
P	1.9	3.3	3.5	3.7	3.7
FIN	5.1	3.3	4.6	4.0	3.6
S	3.6	1.1	2.1	2.9	3.3
UK	2.5	2.3	3.3	2.1	2.3
EUR	**2.4**	**1.8**	**2.6**	**3.0**	**3.1**
USA	2.4	2.8	3.6	2.6	2.5
JAP	1.4	3.5	1.3	2.3	2.9

Domestic demand at constant prices (annual % change)

	1995	1996	1997	1998	1999
B	1.4	1.1	1.7	2.3	2.4
DK	4.4	2.6	4.4	3.3	3.2
D	2.1	0.8	1.2	2.4	3.1
EL	3.2	3.4	4.1	4.1	4.3
E	3.1	1.4	2.5	3.9	4.2
F	1.8	0.9	1.0	2.7	2.9
IRL	6.4	8.4	7.6	6.7	7.4
I	1.9	0.4	1.5	2.2	2.7
L	3.2	1.9	3.8	1.3	2.9
NL	2.0	3.5	3.4	3.0	3.0
A	2.0	1.5	1.4	2.1	2.7
P	1.5	3.3	4.6	3.9	4.0
FIN	4.8	3.3	3.8	3.3	3.2
S	2.3	0.0	1.0	2.4	2.8
UK	1.5	2.7	4.0	3.1	2.4
EUR	**2.1**	**1.4**	**2.1**	**2.8**	**3.0**
USA	2.3	3.0	4.0	2.8	2.3
JAP	2.2	4.6	0.2	2.2	2.8

Deflator of private consumption (annual % change)

	1995	1996	1997	1998	1999
B	1.7	2.3	1.7	1.8	1.8
DK	2.0	2.1	2.1	2.5	2.7
D	1.9	1.8	2.1	2.2	2.2
EL	9.3	8.5	6.0	4.5	3.5
E	4.7	3.4	2.1	2.2	2.3
F	1.6	1.9	1.3	1.5	2.0
IRL	2.0	1.1	1.4	2.5	3.0
I	5.8	4.3	2.2	2.2	2.0
L	0.7	1.4	1.6	1.7	1.8
NL	1.5	1.3	2.1	2.4	2.6
A	1.4	2.5	1.9	2.1	2.2
P	4.2	3.3	2.2	2.1	2.3
FIN	0.3	1.6	1.3	2.0	2.0
S	2.4	1.2	1.8	2.0	2.3
UK	2.6	2.6	2.4	2.4	2.3
EUR	**3.0**	**2.6**	**2.1**	**2.2**	**2.2**
USA	2.2	2.4	2.1	2.4	3.0
JAP	-0.5	0.2	1.5	1.1	1.0

Gross fixed capital formation in equipment at constant prices (annual % change)

	1995	1996	1997	1998	1999
B	5.5	3.3	4.8	5.0	5.3
DK	12.6	3.7	7.8	5.3	4.9
D	2.0	2.4	4.3	7.7	8.8
EL	5.1	14.1	11.8	11.5	11.8
E	12.1	5.9	8.9	8.9	8.4
F	6.6	0.7	-0.5	4.2	6.1
IRL	4.0	11.8	10.0	9.0	12.0
I	13.4	1.3	2.0	6.0	7.0
L	-	-	15.0	-9.5	5.0
NL	10.6	10.9	6.9	3.9	6.5
A	3.1	2.9	5.0	7.5	7.5
P	1.3	8.2	9.1	7.5	7.0
FIN	25.5	11.6	2.9	1.9	6.0
S	29.2	6.5	5.8	5.5	5.1
UK	5.1	2.2	6.6	6.0	4.1
EUR	**7.5**	**3.0**	**4.5**	**6.3**	**7.0**
USA	10.3	10.1	10.4	10.9	6.6
JAP	10.2	7.2	4.6	6.1	7.1

Compensation of employees per head (annual % change)

	1995	1996	1997	1998	1999
B	2.9	1.4	2.3	2.6	2.6
DK	3.6	3.1	3.8	4.4	4.6
D	3.6	2.5	2.0	2.5	3.0
EL	12.5	11.5	10.5	7.5	6.1
E	2.2	4.4	2.7	3.0	3.1
F	2.5	2.6	2.4	2.7	3.2
IRL	1.6	2.2	5.5	5.3	5.3
I	4.8	5.5	5.3	3.2	3.3
L	2.2	1.8	3.3	3.3	3.4
NL	2.1	2.0	3.2	3.6	3.6
A	3.1	1.7	1.7	2.3	2.8
P	4.5	5.7	4.7	4.1	4.2
FIN	4.0	3.6	2.4	2.6	3.0
S	2.9	7.3	4.5	3.9	3.9
UK	2.4	3.5	4.2	4.3	4.2
EUR	**3.2**	**3.4**	**3.2**	**3.2**	**3.5**
USA	3.5	3.4	3.2	3.8	5.2
JAP	1.6	0.8	1.2	2.4	2.8

Note: As usual, the forecasts are conditioned upon, inter alia, the technical assumption of "no policy change". This means that specific policy measures, especially in the budgetary field, which have not yet been disclosed are not taken into account. As a result, projections for 1999 are essentially an extrapolation of expected trends in 1997/98.

Source: Commission services.

Table 2 continued.

Main Economic Indicators, 1995-1999 (Autumn 1997 forecasts)

Number of unemployed as % of the civilian labour force

	1995	1996	1997	1998	1999
B	9.9	9.8	9.7	8.8	8.0
DK	7.2	6.9	6.0	5.4	5.1
D	8.2	8.9	10.0	9.8	9.1
EL	9.2	9.6	9.5	9.3	9.2
E	22.9	22.1	21.0	19.8	18.7
F	11.7	12.4	12.5	12.3	11.9
IRL	12.3	11.8	10.8	9.5	7.9
I	11.9	12.0	12.1	11.9	11.8
L	2.9	3.3	3.6	3.8	3.9
NL	6.9	6.3	5.5	4.8	3.9
A	3.9	4.4	4.4	4.2	3.9
P	7.3	7.3	6.8	6.7	6.3
FIN	16.3	15.4	13.8	12.6	11.7
S	9.2	10.0	10.4	9.9	9.3
UK	8.7	8.2	6.4	5.8	5.5
EUR	10.8	10.9	10.7	10.3	9.7
USA	5.6	5.4	5.0	4.7	5.1
JAP	3.1	3.4	3.3	3.1	3.1

Total employment (annual % change)

	1995	1996	1997	1998	1999
B	0.5	0.0	0.2	1.1	1.0
DK	1.6	1.1	2.2	0.9	0.6
D	-0.3	-1.2	-1.3	0.3	1.5
EL	0.9	1.3	1.6	1.7	1.8
E	1.7	1.5	2.5	2.4	2.5
F	1.0	0.0	0.3	1.1	1.4
IRL	4.8	3.7	4.5	3.8	4.0
I	-0.2	0.2	0.1	0.3	0.5
L	2.5	2.4	1.8	2.2	2.2
NL	1.4	1.8	1.9	2.0	2.0
A	0.2	-0.7	0.0	0.7	1.3
P	-1.0	0.6	1.5	0.7	0.6
FIN	1.7	0.9	2.4	1.8	1.5
S	1.5	-0.6	-1.1	0.7	1.2
UK	1.2	1.2	1.5	0.5	0.5
EUR	0.6	0.2	0.5	0.8	1.3
USA	1.5	1.4	2.4	1.8	0.9
JAP	0.2	0.4	1.2	1.0	1.2

Balance of current transactions (as a % of GDP)

	1995	1996	1997	1998	1999
B	4.5	4.5	5.0	5.4	5.7
DK	0.8	0.8	0.2	0.3	0.4
D	-1.2	-1.2	-0.6	-0.2	-0.2
EL	-2.7	-2.6	-2.9	-3.0	-3.1
E	0.4	0.3	1.0	0.5	0.1
F	1.5	1.6	2.4	2.5	2.8
IRL	4.5	3.8	3.3	2.9	1.4
I	2.4	3.5	3.7	4.0	4.4
L	17.2	16.0	14.6	16.2	17.0
NL	5.5	5.7	5.4	5.4	5.5
A	-2.1	-1.8	-1.6	-1.4	-1.3
P	-2.0	-2.5	-2.4	-2.3	-2.4
FIN	4.1	3.8	3.7	4.9	5.9
S	1.1	1.2	1.9	2.2	2.6
UK	-1.9	-0.1	0.0	-0.5	-0.7
EUR	0.6	0.9	1.3	1.4	1.4
USA	-1.9	-1.7	-1.9	-2.0	-1.9
JAP	2.2	1.4	2.3	2.5	2.3

General government net lending(+) or borrowing(-) (as a % of GDP)

	1995	1996	1997	1998	1999
B	-3.9	-3.2	-2.6	-2.3	-2.2
DK	-2.4	-0.8	1.3	1.9	2.4
D [1]	-3.3	-3.4	-3.0	-2.6	-1.7
EL	-9.8	-7.6	-4.2	-3.0	-2.7
E [2]	-7.3	-4.7	-2.9	-2.4	-2.2
F	-5.0	-4.1	-3.1	-3.0	-2.6
IRL	-2.1	-0.4	0.6	1.2	2.1
I	-8.0	-6.8	-3.0	-3.7	-3.6
L	2.0	2.6	1.6	1.0	0.5
NL [3]	-4.0	-2.3	-2.1	-1.9	-1.5
A	-5.0	-3.8	-2.8	-2.6	-2.4
P	-5.8	-3.2	-2.7	-2.4	-2.2
FIN	-5.0	-3.1	-1.4	-0.2	0.5
S	-7.1	-3.7	-1.9	-0.2	0.2
UK	-5.5	-4.9	-2.0	-0.6	-0.3
EUR	-5.1	-4.2	-2.7	-2.2	-1.8
USA	-2.3	-1.4	-0.3	0.3	0.8
JAP	-3.7	-4.4	-3.4	-3.0	-2.5

Cyclically adjusted lending (+) or borrowing (-) of general government (as a % of GDP)

	1995	1996	1997	1998	1999
B	-3.3	-2.2	-1.9	-2.1	-2.4
DK	-1.8	-0.3	1.3	1.6	1.8
D	-3.2	-2.7	-2.3	-2.2	-1.6
EL	-9.1	-6.9	-3.8	-3.0	-3.1
E	-6.2	-3.5	-2.1	-2.0	-2.2
F	-4.4	-3.3	-2.4	-2.8	-2.7
IRL	-2.1	-1.0	-0.5	-0.1	0.8
I	-7.9	-6.2	-2.3	-3.3	-3.7
L	-	2.2	1.7	1.4	0.8
NL	-3.3	-1.9	-1.8	-2.1	-1.8
A	-5.0	-3.4	-2.2	-2.1	-2.4
P	-4.6	-2.3	-2.1	-2.1	-2.2
FIN	-3.1	-1.8	-1.3	-0.6	-0.2
S	-6.3	-2.4	-0.7	0.3	-0.2
UK	-5.0	-4.5	-2.2	-0.7	-0.3
EUR	-4.7	-3.6	-2.1	-2.0	-1.9

General government gross debt (as a % of GDP)

	1995	1996	1997	1998	1999
B	131.2	126.9	124.7	121.3	117.7
DK [4]	73.8	71.6	67.0	62.2	57.0
D	58.0	60.4	61.7	61.4	60.0
EL	111.3	112.6	109.3	106.4	104.2
E	65.3	70.1	68.1	66.5	64.8
F	52.5	55.7	57.3	58.2	58.2
IRL	82.2	72.7	65.8	59.2	52.3
I	124.4	123.8	123.2	121.9	120.0
L	5.9	6.6	6.7	6.9	7.6
NL	79.1	77.2	73.4	71.5	69.4
A	69.3	69.5	66.1	65.6	64.8
P	66.5	65.6	62.5	60.8	59.5
FIN	58.1	58.0	59.0	57.3	55.8
S	78.2	77.8	77.4	75.3	71.2
UK	53.8	54.4	52.9	51.5	49.8
EUR	71.0	73.0	72.4	71.4	69.8

[1] Not including unification related debt and asset assumptions by the federal government in 1995 (Treuhand, eastern housing companies and Deutsche Kreditbank), equal to DEM 227.5 bn.

[2] Figures complying with Eurostat's recommendations of February 1997 establishing a common and harmonised interpretation of the rules of ESA 2nd edition. The figures for 1995 and 1996 are 6.4 % of GDP.

[3] Not including for 1995 a net amount of 32.84 bn NLG of exceptional expenditure related to the reform of the financing of the social housing societies.

[4] Government deposits with the central bank, government holdings of non-government bonds and public enterprise related debt amounted to some 16 % of GDP in 1996.

Source: Commission services.

Table 3

Economic policy-mix in the EU: favourable to growth and employment

	Real effective exchange rate [1] (Unit labour costs) (1993 = 100)		Change in short-term interest rates since Q1 1995 (3-month interbank)	Change in long-term interest rates since Q1 1995 (10-year benchmark)	Change in cyclically-adjusted budget balance [2]		Nominal compensation per employee		Nominal unit labour cost		Real unit labour cost [3]	
							Percentage change					
	Q1 1995	Q4 1997	Jan 1998	Jan 1998	1996/97 annual average	1998	1997[4]	1998[4]	1997[4]	1998[4]	1997[4]	1998[4]
B	107.2	98.7	-2.2	-3.3	0.7	-0.2	2.3	2.6	0.1	0.7	-1.2	-1.1
DK	102.9	102.6	-2.5	-3.7	1.6	0.3	3.9	4.3	2.5	1.9	-0.2	-0.8
D	106.3	92.0	-1.5	-2.5	0.4	0.2	2.0	2.5	-1.7	-0.4	-2.5	-2.0
EL	110.6	128.2	1.1	n.a	2.7	0.8	10.5	7.5	8.7	5.6	1.7	0.7
E	90.7	91.8	-4.3	-6.5	2.1	0.1	2.7	3.0	2.0	1.9	0.1	-0.3
F	102.8	98.4	-3.0	-3.1	1.0	-0.4	2.4	2.7	0.4	0.7	-0.8	-0.6
IRL	95.3	91.4	-0.6	-3.4	0.8	0.4	6.5	5.3	1.1	1.1	-0.3	0.4
I	88.2	101.6	-3.8	-6.6	2.8	-1.0	5.3	3.2	4.0	1.0	1.4	-1.0
NL	103.2	97.6	-1.6	-2.7	0.8	-0.3	3.2	3.6	2.0	1.9	0.1	-0.4
A	104.7	95.5	-1.0	-2.5	1.4	0.1	1.7	2.3	-0.2	0.2	-1.5	-1.4
P	108.6	106.2	-5.5	-6.3	1.3	0.0	4.7	4.1	2.6	1.1	-1.0	-1.2
FIN	113.9	106.1	-2.5	-4.9	0.9	0.7	2.4	2.6	0.3	0.5	-0.6	-1.6
S	97.3	108.9	-3.6	-5.2	2.8	1.0	4.5	3.9	1.2	1.7	-0.7	-0.3
UK	99.2	119.6	0.8	-2.6	1.5	1.5	4.2	4.3	2.3	2.7	-0.4	0.0
EUR[5]	**101.6**	**96.2**	**-2.1**	**-3.6**	**1.3**	**0.1**	**3.2**	**3.2**	**1.1**	**1.1**	**-0.7**	**-0.9**
USA	**102.6**	**115.0**	**-0.6**	**-2.0**	**0.2**	**-0.1**	**3.2**	**3.8**	**2.0**	**3.0**	**-0.1**	**0.7**

[1] Relative to 22 industrialised countries.
[2] A minus sign indicates a deterioration, i.e. a rise in the deficit.
[3] Deflated by GDP deflator.
[4] European Commission Autumn 1997 forecast.
[5] Exchange rate relative to 9 industrial non-EC countries.

Source: Commission services and OECD.

Table 4

Labour market situation, EUR[1)]

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
a) Non activity rate, as % of population 15-64 year (a = 100-b)	33.6	33.3	33.0	32.7	32.3	32.2	31.7	31.9	32.4	32.4	32.4	32.3
b) Activity rate, as % of population 15-64 year (b = c+f)	66.4	66.7	67.0	67.3	67.7	67.8	68.3	68.1	67.6	67.6	67.6	67.7
c) Employment rate, benchmark series, % of population 15-64 year (c)	59.8	60.1	60.5	61.1	62.1	62.6	62.7	61.8	60.4	60.1	60.3	60.3
d) Full-time equivalent employment rate [2)]	55.8	56.0	56.3	56.9	57.7	58.0	58.0	57.0	55.6	55.1	55.2	55.0
e) Effect of part-time employment (e=c-d)	4.0	4.1	4.2	4.2	4.4	4.6	4.7	4.8	4.8	5.0	5.1	5.3
f) Unemployment rate, as % of population 15-64 year (f=b-c)	6.6	6.6	6.5	6.2	5.6	5.2	5.6	6.3	7.2	7.5	7.3	7.4
g) Unemployment rate, as % of civilian labour force[3)]	10.0	9.9	9.7	9.1	8.3	7.7	8.2	9.3	10.7	11.2	10.8	10.9

[1)] Variables c, d and g are original input. Other variables are derived from these.
[2)] Taking into account part-time and over-time in relation to national legislative number of working hours per week.
[3)] Definition Eurostat.

Source: Commission services.

Table 5

Labour market situation, individual Member States [1)]

	B	DK	D	EL	E	F	IRL	I	L	NL	A	P	FIN	S	UK	EUR
a) Non activity rate, as % of population 15-64 year (a = 100-b)																
1985	40.8	16.7	32.0	38.3	43.7	31.0	38.1	41.9	34.0	37.1	30.2	30.5	20.9	17.4	25.3	33.6
1990	41.4	15.9	30.8	39.5	40.6	30.9	38.2	40.9	27.8	33.7	27.9	30.6	22.6	15.7	22.2	32.2
1993	38.2	16.5	30.5	39.6	40.3	31.6	37.5	41.2	22.3	32.4	26.1	29.1	26.5	19.9	23.6	32.3
1996	37.2	18.9	31.3	37.0	39.4	31.2	36.2	41.6	18.2	30.5	27.0	28.8	27.1	21.9	24.0	32.3
b) Activity rate, as % of population 15-64 year (b = c+f)																
1985	59.2	83.3	68.0	61.7	56.3	69.0	61.9	58.1	66.0	62.9	69.8	69.5	79.1	82.6	74.7	66.4
1990	58.6	84.1	69.2	60.5	59.4	69.1	61.8	59.1	72.2	66.3	72.1	69.4	77.4	84.3	77.8	67.8
1993	61.8	83.5	69.5	60.4	59.7	68.4	62.5	58.8	77.7	67.6	73.9	70.9	73.5	80.1	76.4	67.7
1996	62.8	81.1	68.7	63.0	60.6	68.8	63.8	58.4	81.8	69.5	73.0	71.2	72.9	78.1	76.0	67.7
c) Employment rate, benchmark series, % of population 15-64 year (c)																
1985	53.1	77.4	63.1	57.3	44.1	62.0	51.4	53.1	64.1	57.7	67.3	63.5	74.3	80.1	66.2	59.8
1990	54.7	77.6	66.3	56.6	49.7	62.9	53.5	53.7	71.0	62.2	69.7	66.2	74.9	82.8	72.4	62.6
1993	56.3	75.1	64.0	55.2	46.1	60.4	52.7	52.7	75.6	63.2	70.9	66.9	61.1	72.5	68.5	60.4
1996	56.6	75.5	62.6	56.9	47.2	60.3	56.3	51.4	79.1	65.1	69.8	66.0	61.7	70.3	69.8	60.3
d) Full-time equivalent employment rate [2)]																
1985	50.9	67.6	58.9	55.8	42.8	59.1	49.7	52.3	54.3	47.6	63.5	61.9	70.7	70.6	58.0	55.8
1990	51.7	68.3	60.6	55.4	48.4	59.6	51.3	52.8	53.0	50.2	65.8	64.5	71.2	72.8	63.2	58.0
1993	52.7	66.1	59.1	54.1	44.4	56.7	49.8	51.8	52.6	50.8	66.8	64.8	58.1	63.6	59.1	55.6
1996	52.7	67.3	57.0	55.6	45.1	56.1	53.0	50.2	51.0	51.7	65.0	63.8	58.5	63.3	59.8	55.0
e) Effect of part-time employment rate (e=c-d)																
1985	2.2	9.8	4.2	1.5	1.3	2.9	1.7	0.8	9.8	10.1	3.8	1.6	3.6	9.5	8.2	4.0
1990	3.0	9.3	5.7	1.2	1.3	3.3	2.2	0.9	18.0	12.0	3.9	1.7	3.7	10.0	9.2	4.6
1993	3.6	9.0	4.9	1.0	1.7	3.7	2.9	1.0	23.1	12.4	4.1	2.0	3.0	8.8	9.4	4.8
1996	3.9	8.2	5.6	1.3	2.1	4.2	3.3	1.2	28.1	13.4	4.8	2.2	3.2	7.0	10.0	5.3
f) Unemployment rate, as % of population 15-64 year (f=b-c)																
1985	6.1	5.9	4.9	4.4	12.2	7.0	10.5	5.0	1.9	5.2	2.5	6.0	4.8	2.5	8.5	6.6
1990	3.9	6.5	2.9	3.9	9.7	6.2	8.3	5.4	1.2	4.1	2.4	3.2	2.5	1.5	5.4	5.2
1993	5.5	8.4	5.5	5.2	13.6	8.0	9.7	6.1	2.1	4.5	3.0	4.0	12.4	7.6	7.9	7.2
1996	6.2	5.6	6.1	6.1	13.4	8.5	7.5	7.0	2.7	4.4	3.2	5.2	11.2	7.8	6.2	7.4
g) Unemployment rate, as % of civilian labour force[3)]																
1985	10.3	7.1	7.2	7.0	21.6	10.1	16.9	8.5	2.9	8.3	3.6	8.7	6.0	3.0	11.5	10.0
1990	6.7	7.7	4.8	6.4	16.2	8.9	13.4	9.1	1.7	6.2	3.2	4.6	3.3	1.8	7.0	7.7
1993	8.9	10.1	6.0	8.6	22.8	11.7	15.6	10.3	2.7	6.6	4.0	5.7	16.9	9.5	10.4	10.7
1996	9.8	6.9	8.8	9.6	22.1	12.4	11.8	12.0	3.3	6.3	4.4	7.3	15.4	10.0	8.2	10.9

[1)] Variables c, d and g are original input. Other variables are derived from these.

[2)] Taking into account part-time and over-time in relation to national legislative number of working hours per week.

[3)] Definition Eurostat.

Source: Commission services.

Table 6

Growth, employment and productivity trends, EUR, USA and Japan

(Average annual growth rates, in %)

	1961-73	1974-96	1974-85	1986-96	1986-90	1991-96
1. Real GDP growth						
EUR	4.7	2.2	2.0	2.3	3.2	1.5
USA	3.9	2.4	2.3	2.5	2.8	2.1
JAP	9.6	3.3	3.7	3.0	4.6	1.7
2. Labour supply						
EUR	0.3	0.6	0.7	0.4	0.9	-0.1
USA	1.9	1.7	2.1	1.3	1.5	1.1
JAP	1.2	1.0	0.9	1.2	1.4	0.9
3. Employment						
EUR	0.3	0.1	0.0	0.3	1.4	-0.5
USA	1.9	1.7	1.9	1.5	1.9	1.1
JAP	1.3	0.9	0.8	1.1	1.5	0.6
4. Labour productivity[1] (≅ 1-3 ≅ 5+6)						
EUR	4.4	2.0	2.0	2.0	1.9	2.0
USA	1.9	0.7	0.5	1.0	0.9	1.0
JAP	8.1	2.4	3.0	1.9	3.1	1.1
5. Total factor productivity[2]						
EUR	2.8	1.1	1.0	1.2	1.5	1.0
USA	1.6	0.6	0.4	0.8	0.9	0.8
JAP	6.3	1.1	1.4	0.7	2.0	-0.3
6. Labour to capital substitution[3]						
EUR	1.6	0.9	1.0	0.8	0.4	1.0
USA	0.3	0.1	0.1	0.1	0.0	0.2
JAP	1.8	1.3	1.6	1.1	1.1	1.3

[1] Real GDP per employed person.
[2] Average of capital and labour productivity, weighted by factor income shares in GDP.
[3] Discrepancy between labour productivity and total factor productivity.

Source: Commission services.

Table 7

General government net lending / borrowing (% of GDP)

Convergence programme projections

	Date[1]	1996	1997	1998	1999	2000	2001
B	1/97	-3.4	-2.9	-2.3	-1.7	-1.4	
DK	6/97	-1.4	0.7	0.7	0.9	1.1	[2]
D[3]	1/97	-3.9	-2.9	-2.5	-2.0	-1.5	
EL	7/97	-7.4	-4.2	-2.4	-2.1		
E	4/97	-4.4	-3.0	-2.5	-2.0	-1.6	
F	1/97	-4.0	-3.0	-2.8	-2.3	-1.8	-1.4
IRL	4/97	-0.9	-1.5	-1.5	-1.1		
I	6/97	-6.7	-3.0	-2.8	-2.4	-1.8	
NL	12/96	-2.6	-2.2	-2.25			
A	10/97	-4.0	-2.7	-2.5	-2.2	-1.9	
P	3/97	-4.0	-2.9	-2.5	-2.0	-1.5	
FIN	9/97	-3.1	-1.3	-0.1	0.3	1.0	1.9
S[4]	9/97	-2.5 (-3.7)	-1.9 (-1.6)	0.6	0.5	1.5	
UK[5]	9/97	-4.2	-1.6	-0.3	-0.1/0.4	0.5/1.5	0.9/2.4

1) Date when most recent version of convergence programme was submitted.
2) Government surplus of 2.8% of GDP projected for 2005.
3) Taking into account revised estimates (for 1996 and 1997) provided by the German authorities in February 1997.
4) Main series according to Swedish national accounts, figures in brackets for 1996 and 1997 according to ESA accounting principles.
5) Financial year ending in March of the following calendar year.

Source: Commission services.

Table 8

Receipts and expenditures of general government - EUR [a])

(in % of GDP)

	1961	1970	1973	1982	1989	1993	1994	1995	1996	1997
					Current receipts					
1. Total (2+3+4+5)	**34.3**	**37.4**	**38.2**	**44.3**	**44.8**	**46.3**	**45.8**	**45.9**	**46.1**	**46.0**
of which:										
2. Indirect taxes	13.9	13.5	12.9	13.2	13.5	13.6	13.8	13.7	13.8	14.0
3. Direct taxes	8.7	10.2	10.7	12.4	13.3	12.9	12.6	12.8	12.8	12.9
4. Social security contributions	10.2	10.7	11.8	14.7	14.6	16.0	15.9	16.0	16.1	15.8
5. Other current receipts	1.5	2.9	2.8	4.0	3.4	3.8	3.5	3.4	3.4	3.3
					Total expenditure					
6. Total (7+8+9+10+11)	**33.6**	**36.9**	**38.7**	**49.3**	**47.2**	**52.4**	**51.3**	**51.0**	**50.4**	**48.7**
of which:										
7. Current transfers	11.5	14.7	16.0	21.6	20.7	23.7	23.5	23.3	23.1	22.5
7bis. *of which*: Households	:	12.1	13.0	17.9	17.1	20.0	19.9	19.8	19.7	19.3
8. Actual interest payments	3.1	1.8	1.7	4.1	4.6	5.4	5.2	5.4	5.4	5.0
9. Public consumption	13.7	15.4	16.4	19.6	18.2	19.6	19.2	19.0	18.9	18.7
10. Net capital transfers	0.8	0.7	0.9	1.0	0.9	1.1	0.8	0.8	0.6	0.3
11. Gross capital formation	4.5	4.2	3.7	2.9	2.8	2.8	2.7	2.5	2.4	2.2
					Memory items					
12. Gross saving (1-7-8-9)	6.0	5.2	4.1	-1.0	1.2	-2.4	-2.1	-1.8	-1.3	-0.2
13. Net lending(+)/ borrowing(-) (1-6)	0.7	0.3	-0.6	-5.1	-2.4	-6.1	-5.4	-5.1	-4.2	-2.6
14. Gross public debt[b)]	65.2	38.8	35.3	45.6	54.1	66.1	68.1	71.1	73.2	72.6

a) 1961 : EUR 15 excluding Greece, Portugal, Austria, Sweden and Finland; 1970: EUR15 excluding Greece, Portugal and Finland, 1973 : EUR 15 excluding Luxembourg, Greece and Portugal.

b) 1970: EUR 15 excluding Denmark, France , the Netherlands and Portugal 1973 : EUR 15 excluding France and the Netherlands.

Source: Commission services.

Table 9

Sectoral change in the EU [1]

(% p.a.)

Indicator	Period	Total	Agriculture	Industry[2]	Services
Value added	1961-73	4.9	1.8	5.5	5.6
	1974-85	2.0	1.4	1.5	2.7
	1986-90	3.2	1.3	2.6	3.4
	1991-94	1.1	0.9	0.1	1.8
Employment	1961-73	0.3	-4.6	0.5	1.6
	1974-85	0.2	-2.9	-1.6	1.7
	1986-90	1.2	-3.3	-0.2	2.0
	1991-94	-0.8	-3.8	-3.3	0.5
Labour productivity	1961-73	4.6	6.5	5.0	4.0
	1974-85	1.8	4.3	3.1	1.0
	1986-90	2.0	4.6	2.8	1.4
	1991-94	1.9	4.7	3.4	1.3
Relative prices	1961-73	0.0	-0.4	-1.0	0.7
	1974-85	0.0	-2.6	-0.7	0.6
	1986-90	0.0	-1.6	-1.3	0.8
	1991-94	0.0	-6.1	-1.4	0.7
Relative weight of value added (in % of total in current prices)					
	1960		7.6	35.5	41.3
	1973		4.8	33.7	49.5
	1985		3.0	29.4	56.9
	1990		2.6	26.9	60.1
	1994		2.0	24.3	63.5
Occupied population per sector (in % of total)					
	1960		15.9	30.8	41.4
	1973		8.6	31.6	49.1
	1985		6.0	26.6	59.0
	1990		4.8	23.9	61.7
	1994		4.2	21.6	65.0

[1] EUR15 excluding Greece, Spain, Ireland, Luxembourg and Portugal. For the period 1961-73 comparable data is only available for EUR5 (Belgium, West Germany, France, Italy and the Netherlands) and for 1974-85 EUR 8 (Belgium, Denmark, West Germany, France, Italy, Finland, Sweden, the UK).

[2] Excluding building and construction.

Source: Commission services.

Table 10

Wage dispersion in the EU

	ECHP [1]	OECD(96)	ECHP [1]	OECD (96)	ECHP [1]	OECD (96)
	Overall Dispersion (D9/D1)	Overall Dispersion (D9/D1) [2]	Upper-Half Dispersion (D9/D5)	Upper-Half Dispersion (D9/D5)	Lower-Half Dispersion (D5/D1)	Lower-Half Dispersion (D5/D1)
B	2.42	2.25	1.64	1.57	1.47	1.43
DK	2.10	2.17	1.53	1.57	1.37	1.38
D [3]	2.95	2.32	1.76	1.61	1.68	1.44
EL	2.50	n.a.	1.60	n.a.	1.56	n.a.
E	3.64	n.a.	2.04	n.a.	1.78	n.a.
F	3.20	3.28	1.98	1.99	1.62	1.65
IRL	4.18	n.a.	2.00	n.a.	2.08	n.a.
I	2.13	2.80	1.52	1.60	1.40	1.75
L	3.38	n.a.	1.94	n.a.	1.74	n.a.
NL	2.33	2.59	1.62	1.66	1.44	1.56
A	n.a.	3.66	n.a.	1.82	n.a.	2.01
P	4.20	4.05	2.63	2.47	1.60	1.64
FIN	n.a.	2.38	n.a.	1.70	n.a.	1.40
S	n.a.	2.13	n.a.	1.59	n.a.	1.34
UK	3.73	3.38	1.94	1.87	1.92	1.81
EUR12	**3.05**	**n.a.**	**1.83**	**n.a.**	**1.66**	**n.a.**
USA	n.a.	4.39	n.a.	2.10	n.a.	2.09

1) EC Household Panel.

2) (D9/D1) = (D9/D5) * (D5/D1)

3) OECD data referring to Western Germany only.

Note: Based on (provisional) data of the ECHP-94, the earnings dispersion have been calculated on normal gross monthly earnings (for NL : net monthly earnings) for full-time employees. Figures are ratios of upper/lower deciles in the distribution of earnings. The ratios for EU12 have been calculated as the sum of the dispersion rates for each Member States, weighted with the respective share in total employment (from Labour Force Survey 1994).

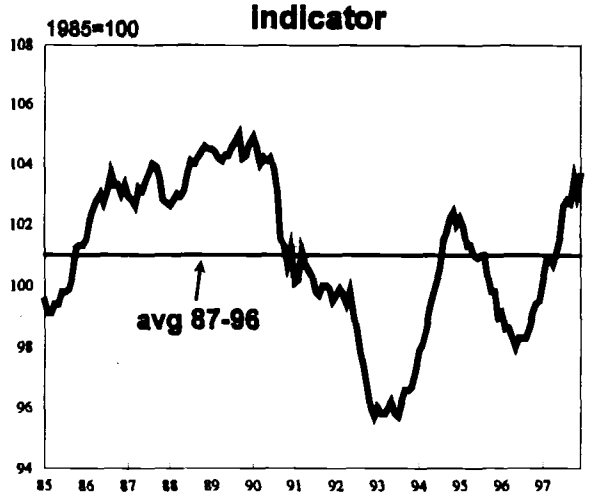
Source: Commission services and OECD.

Graph 1

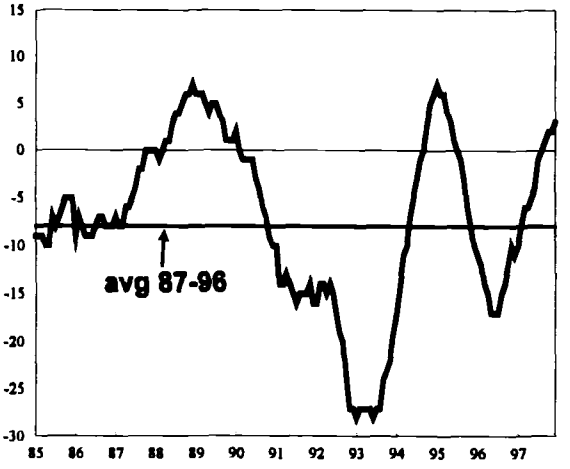
Survey indicators - EUR

(balance between positive and negative answers)

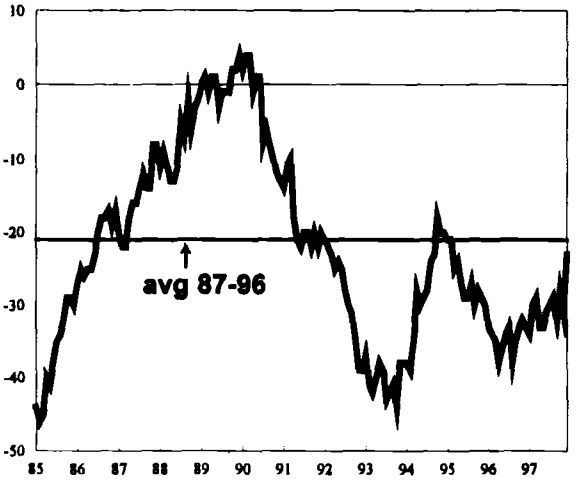
Economic confidence indicator



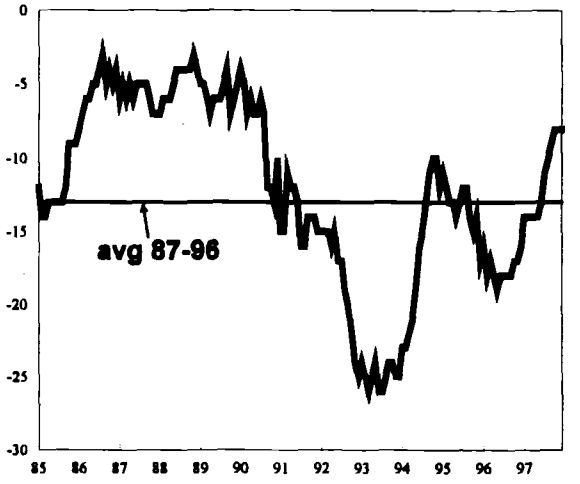
Industrial confidence



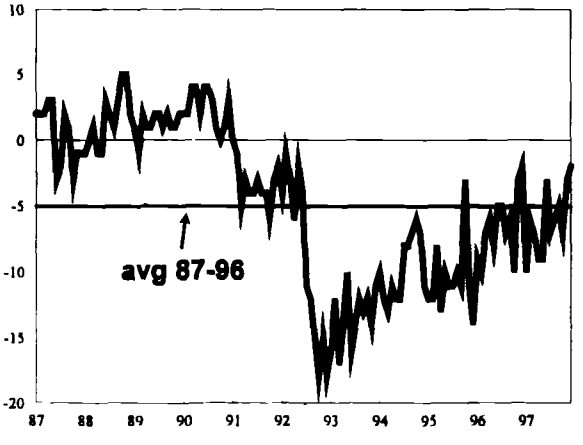
Construction confidence



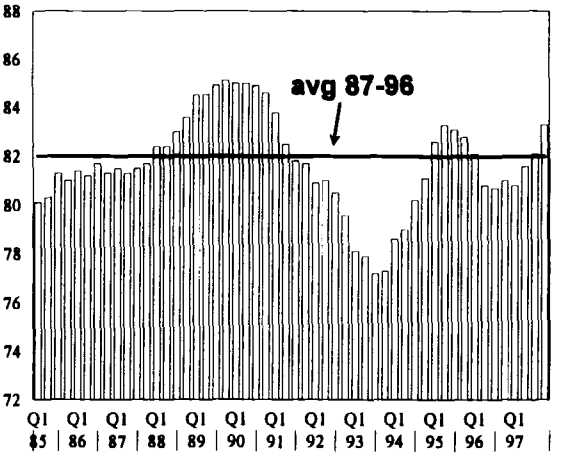
Consumer confidence



Retail trade confidence indicator



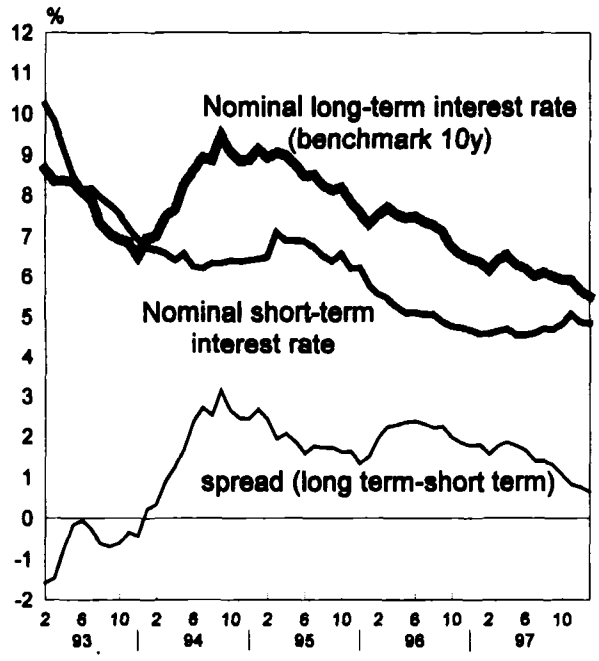
Capacity utilisation rate

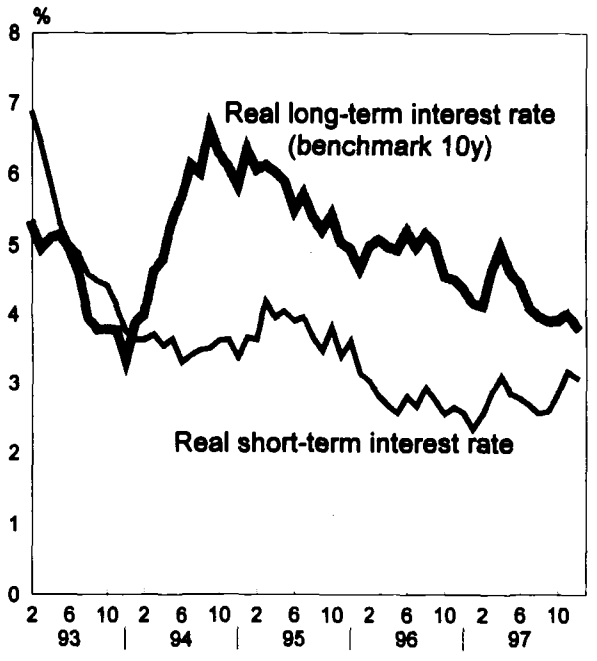


Source: Commission services.

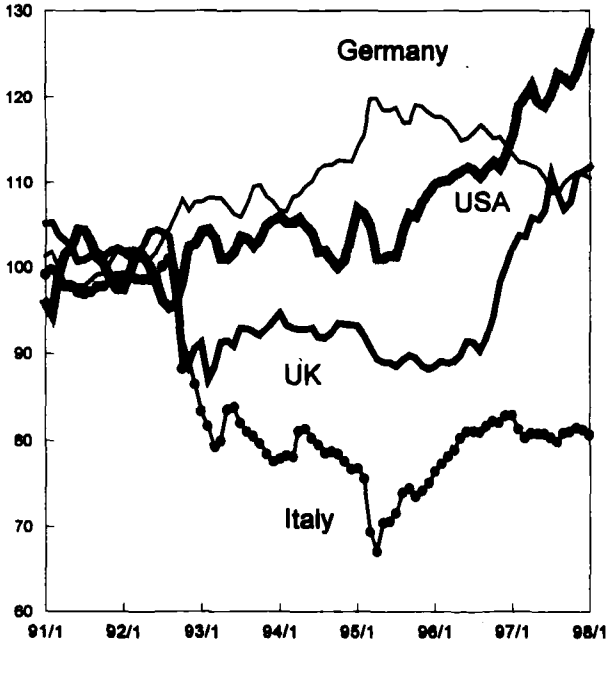
Graph 2

Interest rates and effective exchange rates - EUR

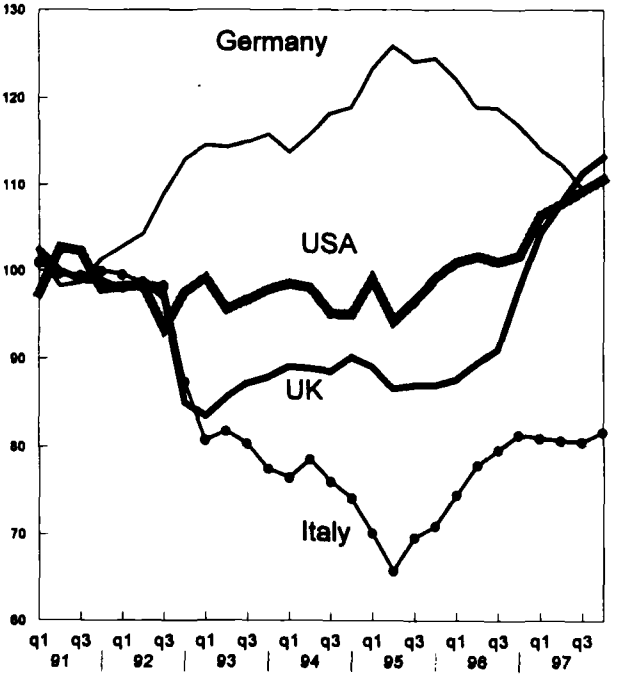




Nominal effective exchange rates (1991=100)



Real effective exchange rates, adjusted by ulc; (1991=100)

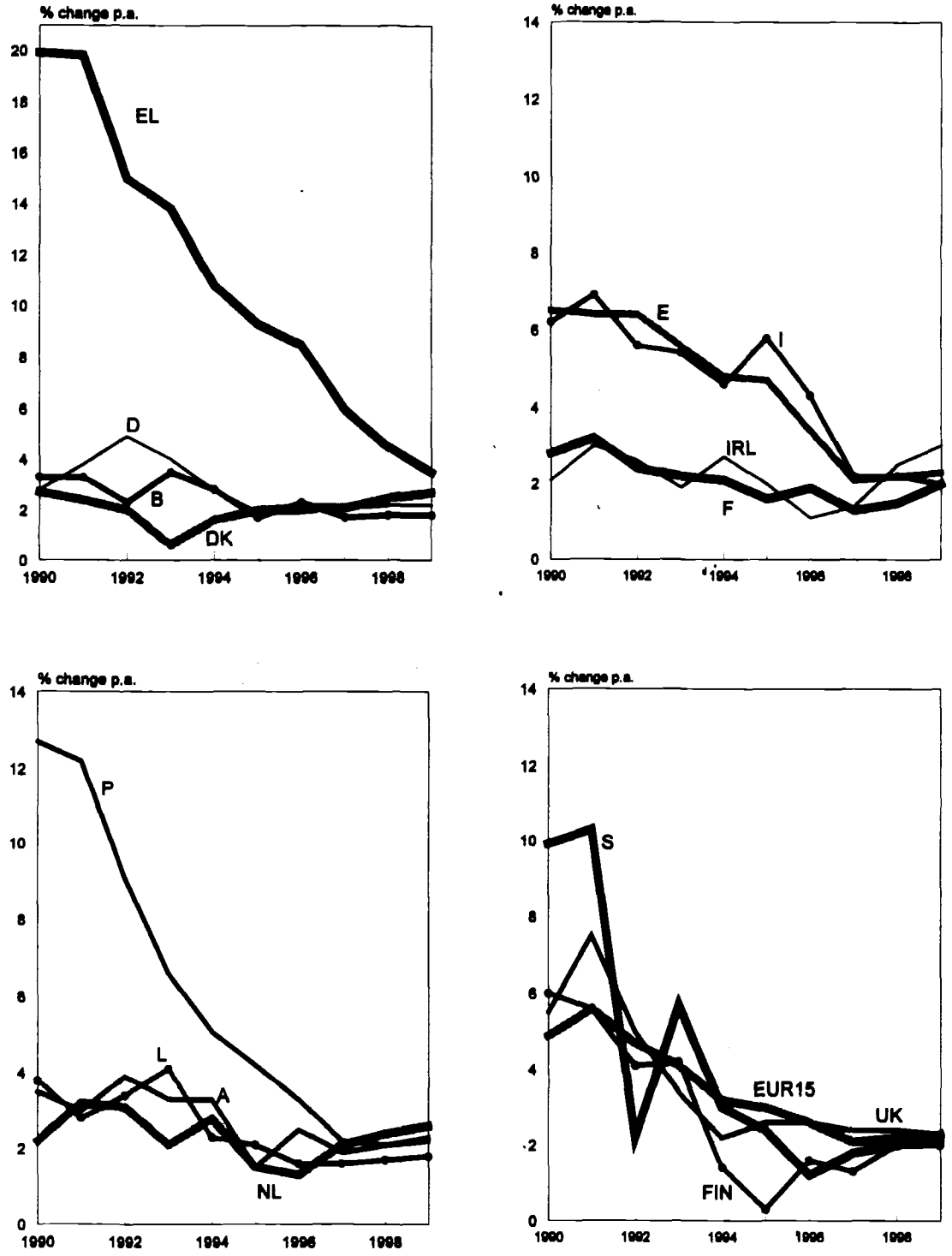


Source: Commission services.

Graph 3

Convergence in the EU

a. Inflation trends[1)]



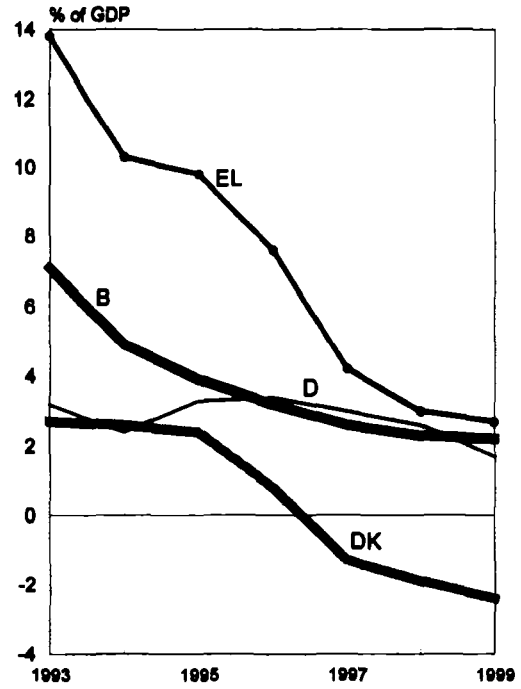
1) Private consumption price deflator.

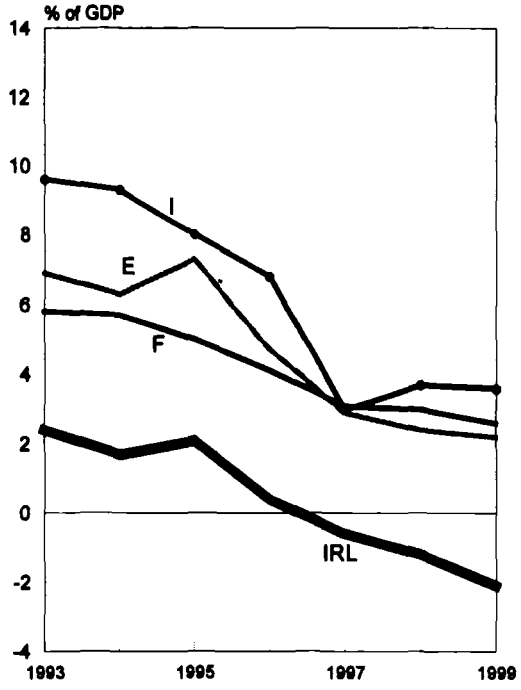
Source: Commission services.

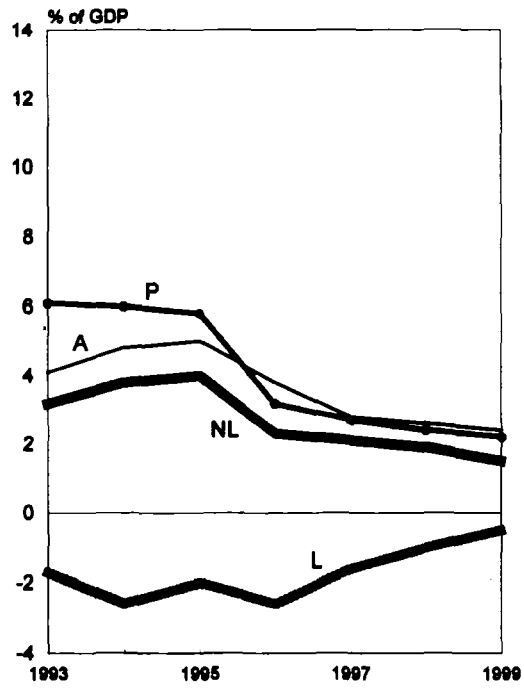
Graph 3

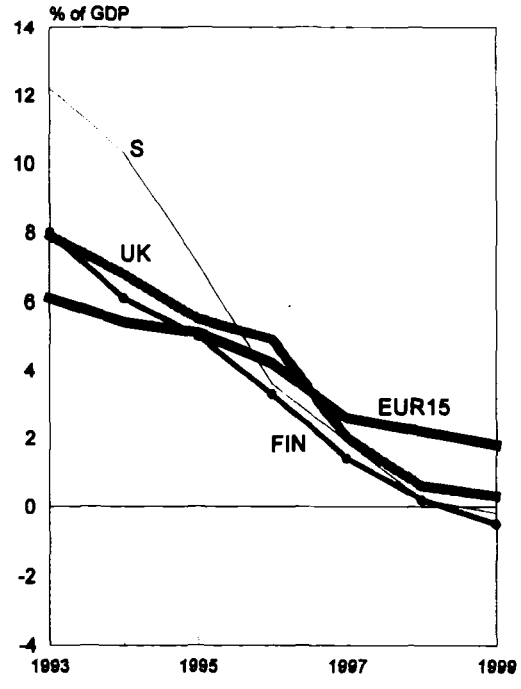
Convergence in the EU

b. General government deficits







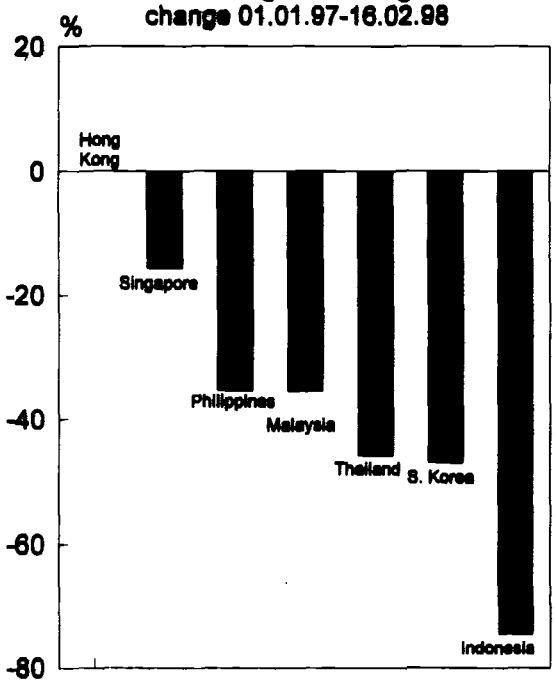


Source: Commission services.

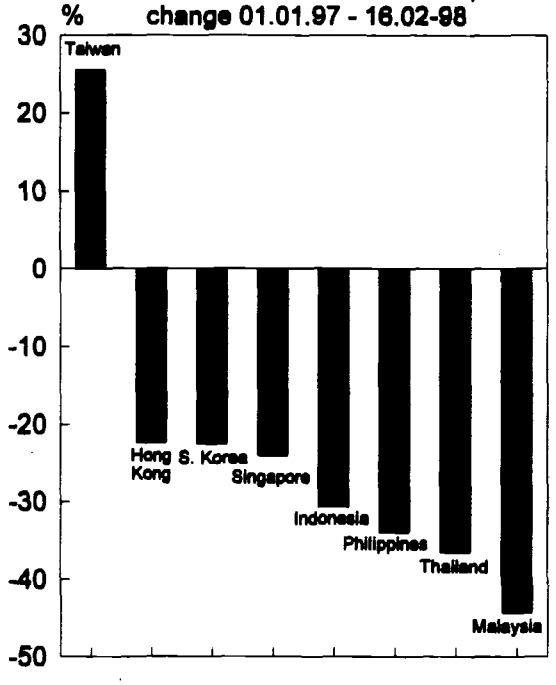
Graph 4

Asia

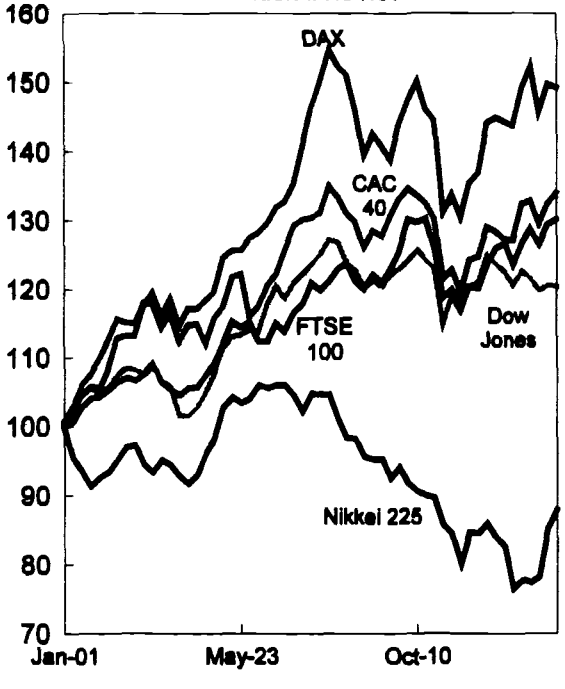
Bilateral exchange rates against USD
change 01.01.97-16.02.98



Stockmarket indices Asia,
change 01.01.97 - 16.02-98



Stockmarket indices EUR,
index 01.01.97



Bilateral trade flows

Selected bilateral trade for EU, US and Japan in 1996 (%)

		Origin of exports			
		EU15		USA	Japan
Destination:		Extra-EU15 exports	Total exports		
Asia		24	9	30	44
of which	Japan	6	2	11	-
	China	2	1	2	5
	Korea	2	1	4	7
	Tigers*	4	2	4	12
USA		18	7	-	27
EU15		-	62	21	15
Eastern Europe +FSU		14	5	1	1
OPEC-Indonesia		6	2	3	2
Latin America		4	2	7	3
Africa		6	2	1	1
Rest of World-EU		27	10	36	6
World-EU		100	36	79	85

* Thailand, Philippines, Malaysia, Indonesia

Source: Commission services.

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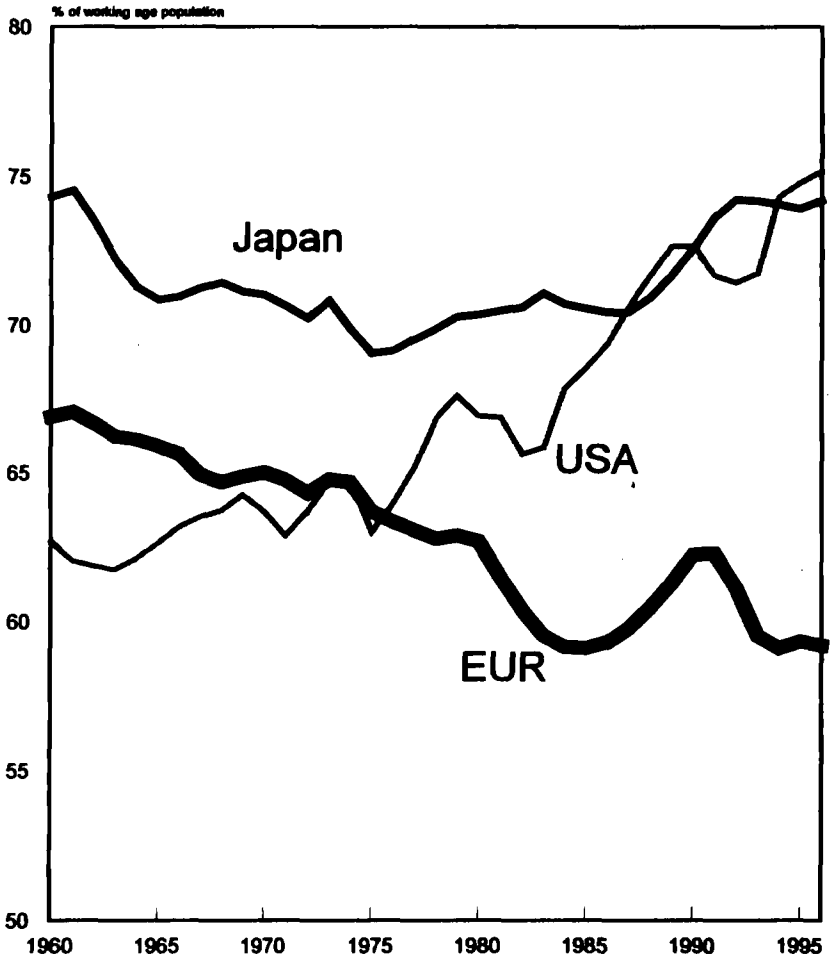
Graph 5 + 6

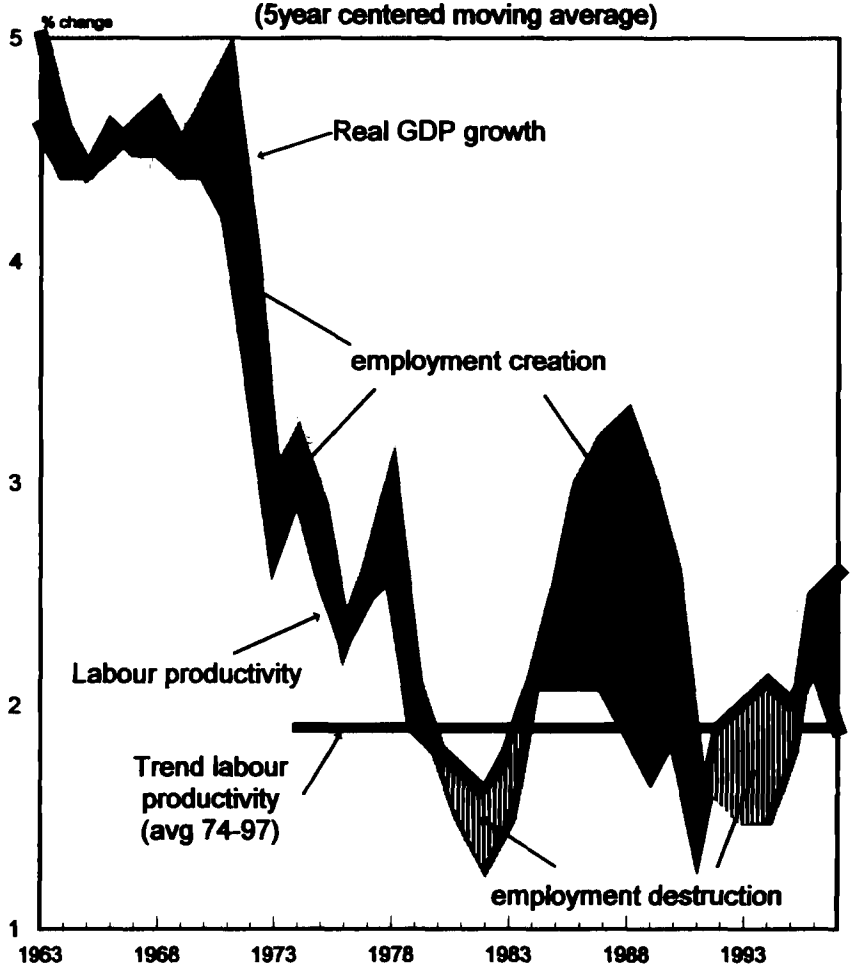
Employment rates and employment creating growth - EUR

Employment rates; EUR, USA and Japan



Employment-creating growth - EUR[1)]

(5year centered moving average)

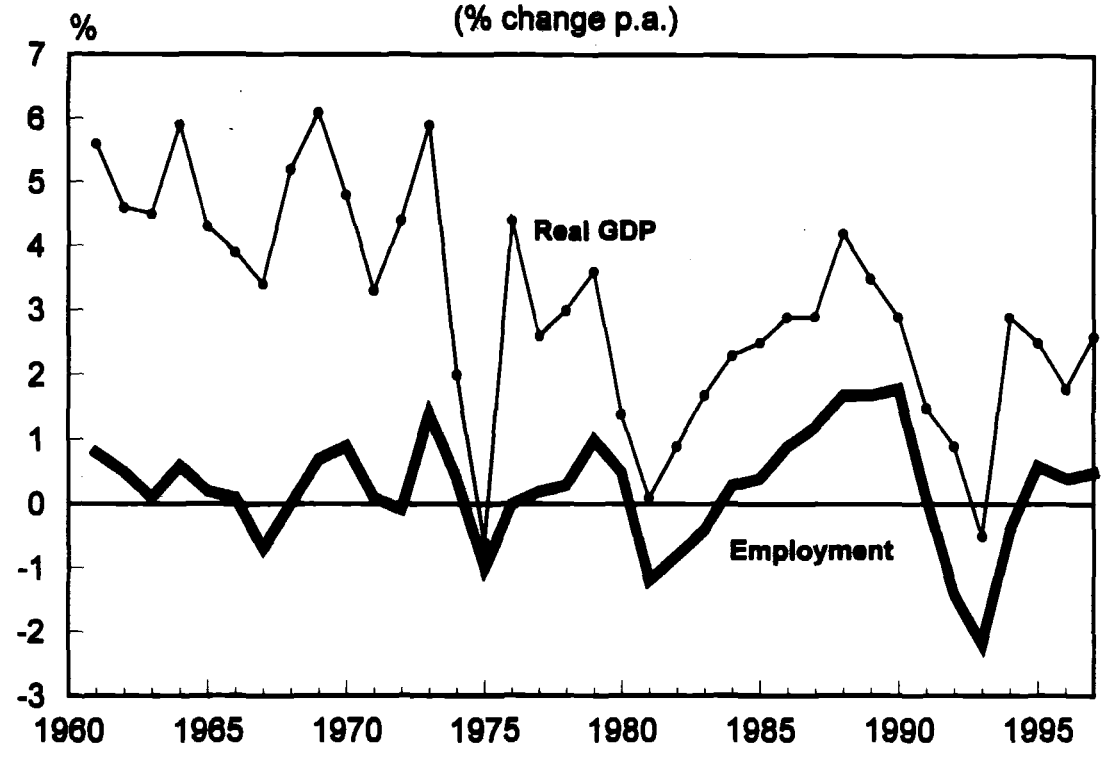


Source: Commission services.

[1)] As from 1992 (5 year centered moving average 1990-1994) EUR includes Unified Germany.

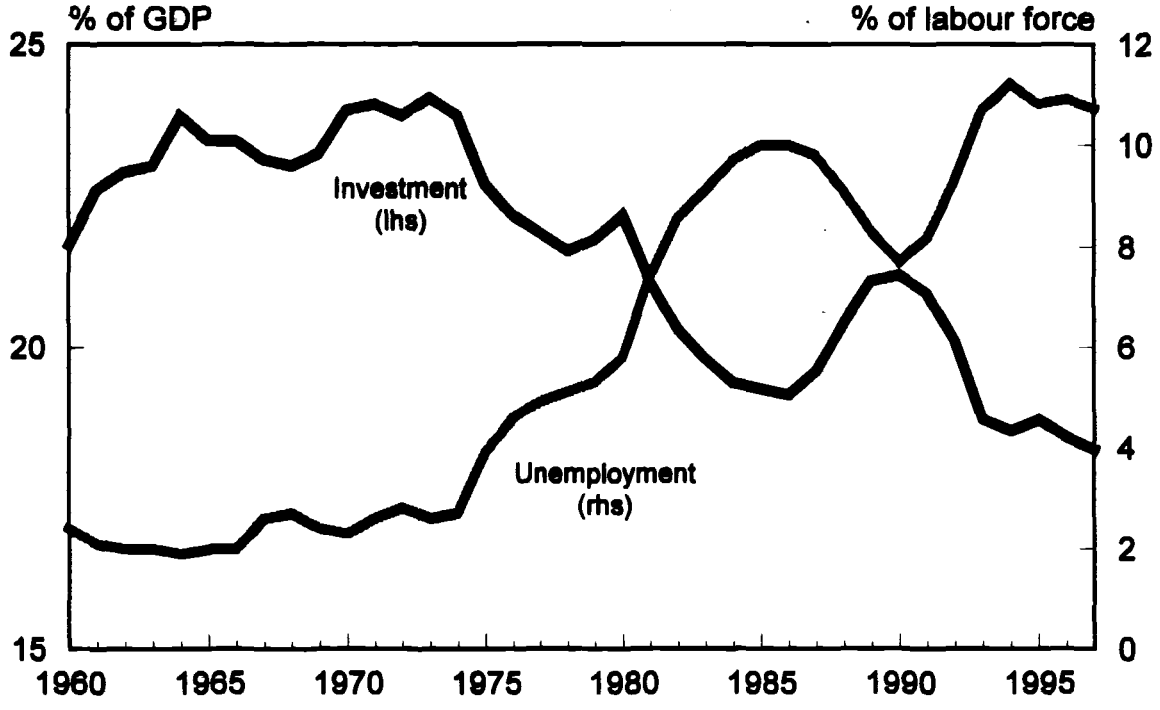
Graph 7

Growth and employment - EUR



Graph 8

Investment and unemployment - EUR



Source: Commission services.

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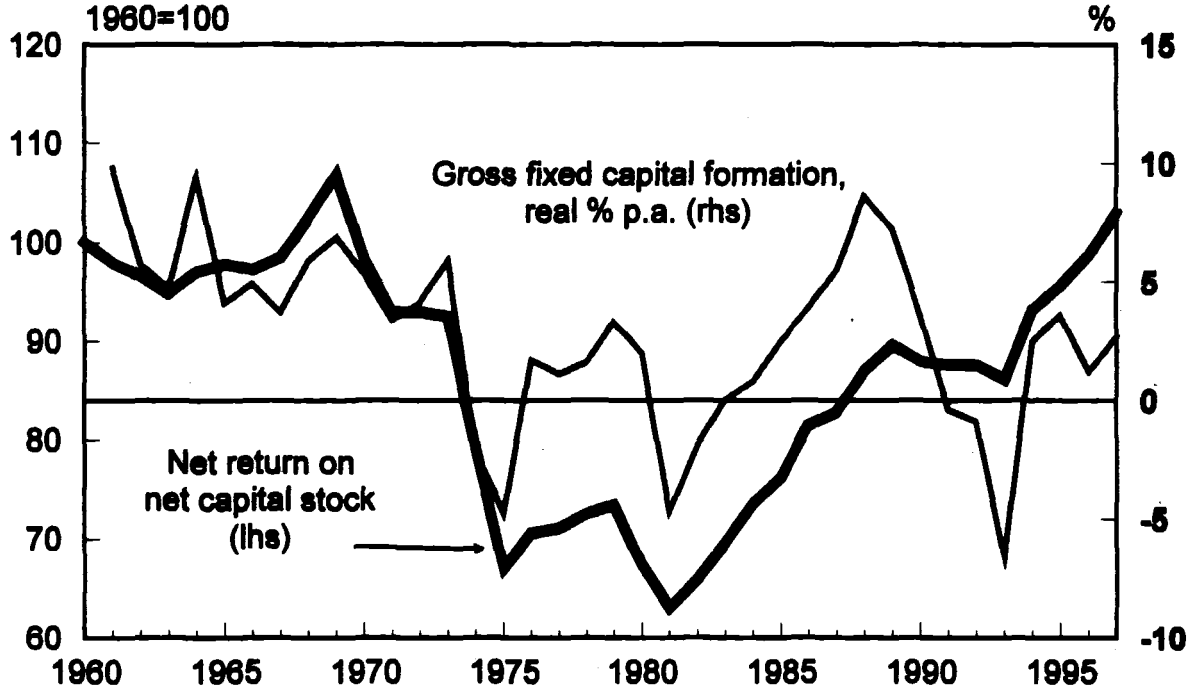
Graph 9

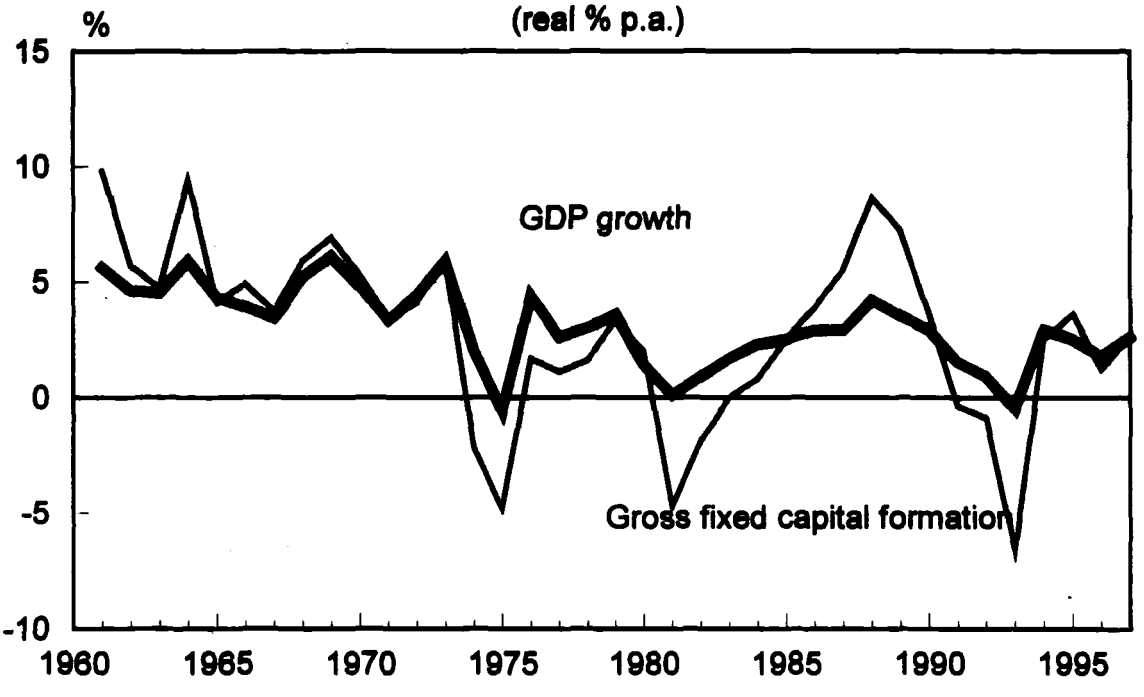
Profitability and investment - EUR



Graph 10

Growth and investment - EUR

(real % p.a.)

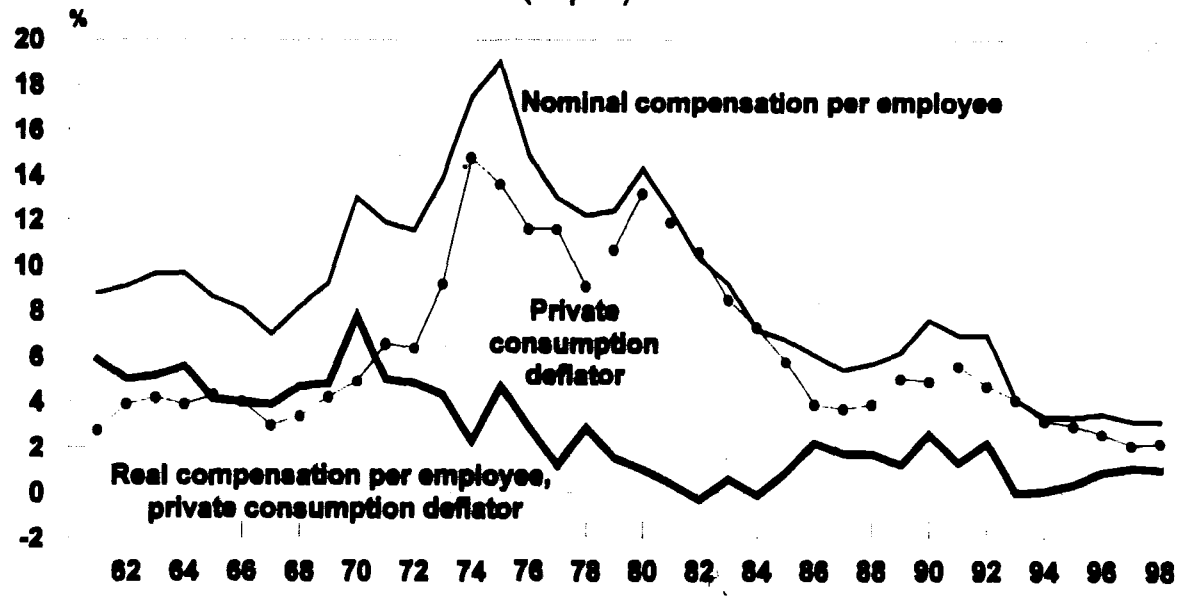


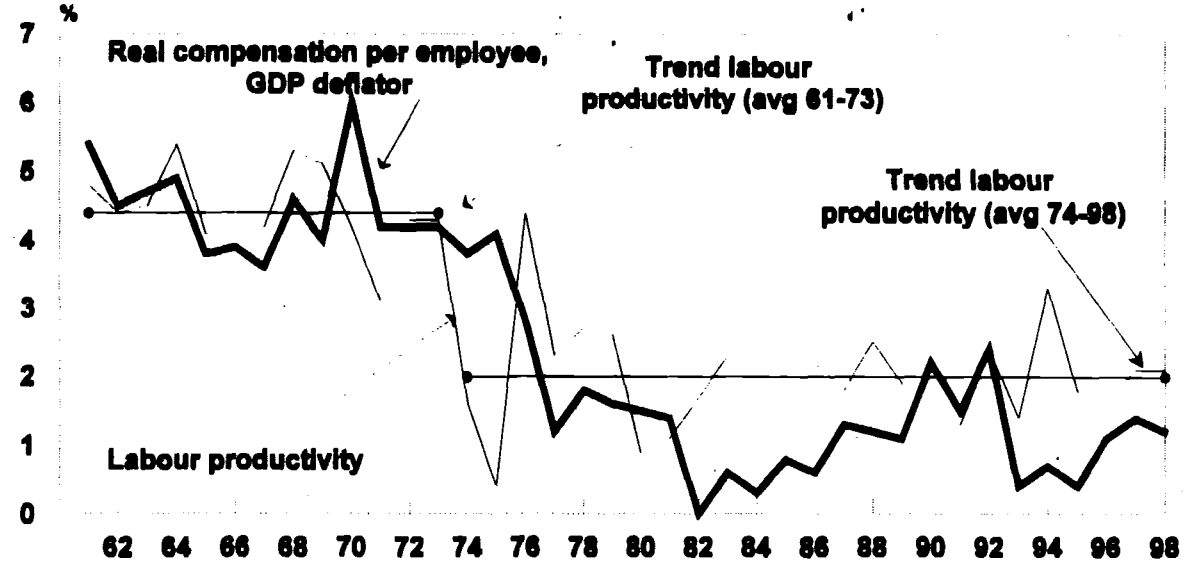
Source: Commission services.

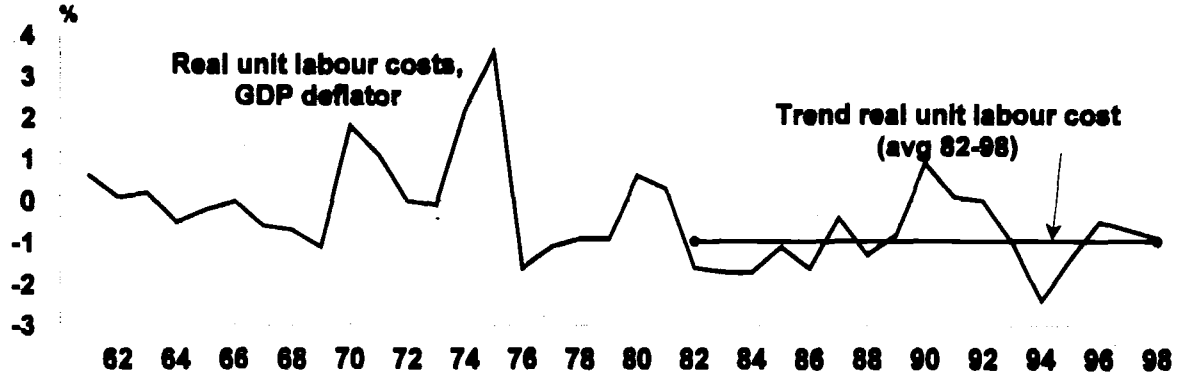
Graph 11

Wage developments - EUR

(% p.a.)



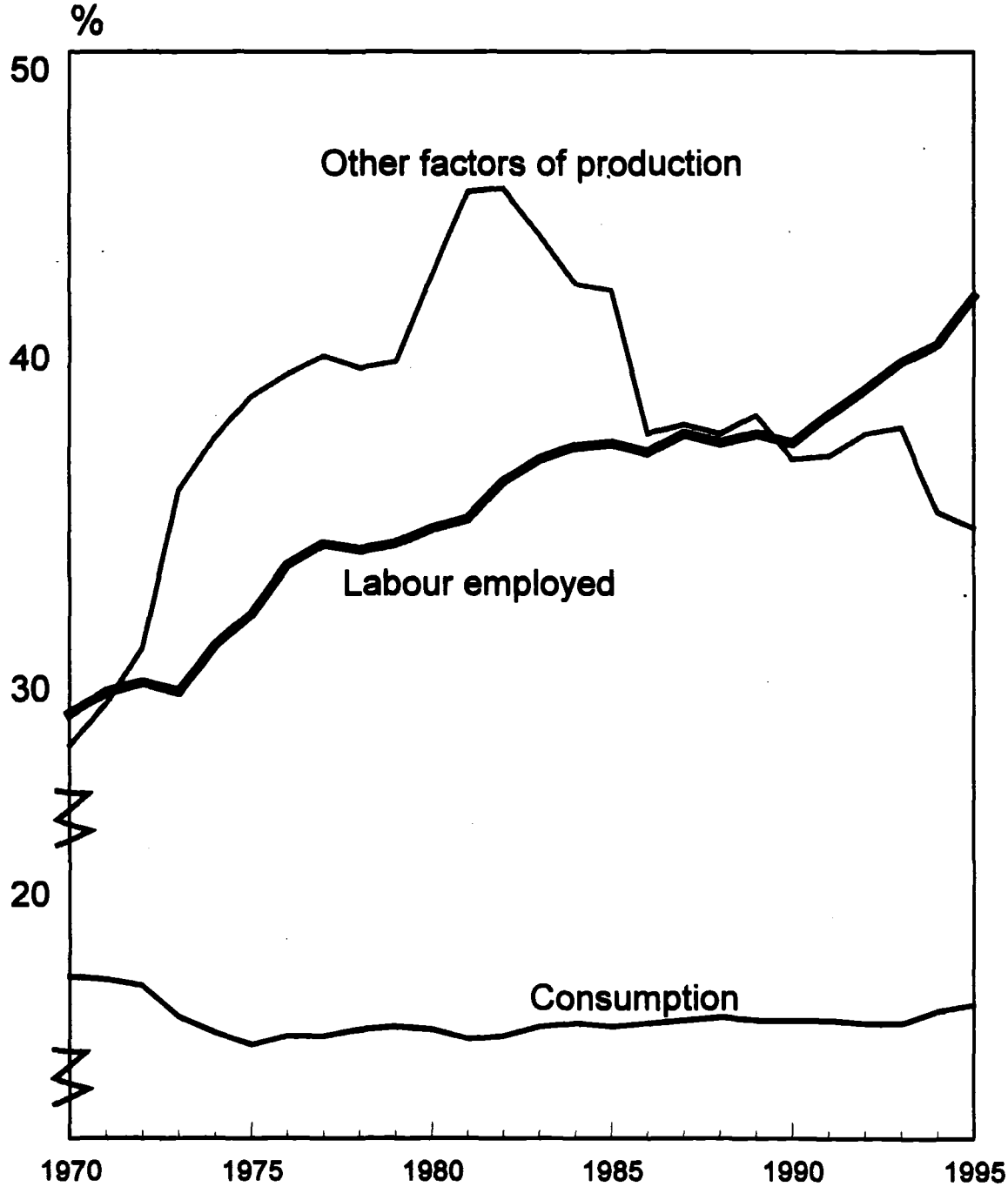




Source: Commission services.

Graph 12

Implicit tax rates[1] - EUR[2]



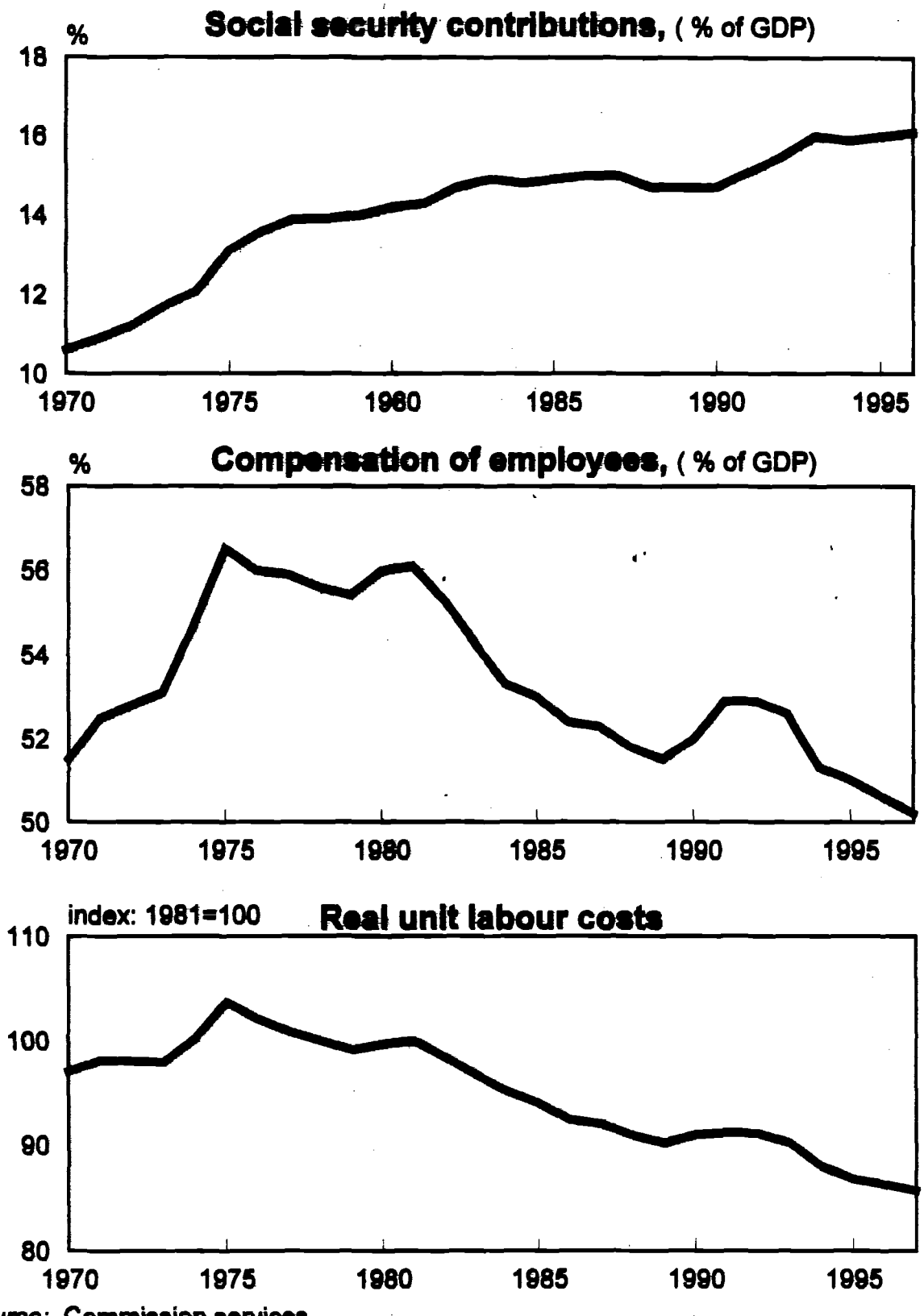
[1] Tax rates calculated by dividing the taxes on the economic activity by the appropriate tax base. For further definitions see Eurostat publication "Structures of the taxation systems in the European Union, 1970-1995" (1997).

[2] 1970-72 EUR6, 1973-85 EUR9, 1986-94 EUR12 1995 EUR15.

Source: Commission services.

Graph 13

Wages and non-wage labour costs - EUR



Source: Commission services.