European Semester 2018 Spring Package explained

The package includes:

- A Communication on the 2018 European Semester: country-specific recommendations;
- Country-specific recommendations (CSRs) for 27 Member States (all Member States except Greece, which is currently under a stability support programme).
- A recommendation to the Council to abrogate the excessive deficit procedure (EDP) under Article 126(12) of the Treaty on the Functioning of the European Union (TFEU) for France;
- Reports on Belgium and Italy under Article 126(3) TFEU, reviewing their compliance with the debt criterion of the Treaty in 2016;
- Warnings to Hungary and Romania on the existence of a significant deviation from the adjustment path toward the medium-term budgetary objective in 2017 and related recommendations for Council recommendations;
- The Commission's opinion on the updated Draft Budgetary Plan (DBP) for Spain;
- A Communication on the review of the flexibility under the Stability and Growth Pact.

Country-specific recommendations

What are the country-specific recommendations?

Country-specific recommendations provide tailored advice to individual Member States on how to boost jobs, growth and investment, while maintaining sound public finances. The Commission publishes them every spring, as part of the European Semester, the EU's annual cycle for economic and social policy coordination. The recommendations adapt priorities identified at EU level in the Annual Growth Survey and at the euro area level in the recommendation for the economic policy of the euro area to the national level. They give guidance on what can realistically be achieved in the next 12 to 18 months to make growth stronger, more sustainable and more inclusive, in line with the EU's long-term jobs and growth plan, the Europe 2020 strategy.

(For more details on the European Semester process and the country-specific recommendations, see the European Semester website).

What is new in the 2018 European Semester and country-specific recommendations?

Against the positive economic outlook, this year's country-specific recommendations seek to promotea forward-looking approach, focussing on building the basis for sustainable, inclusive and long-term growth.

Member States need to pursue structural reforms that improve the business environment and conditions for investment; especially through product and service market reforms, fostering innovation, improving small and medium-sized enterprises' access to finance and fighting corruption.

Member States also need to promote reforms that prepare their workforces for the future and increase digitalisation, reduce income inequalities and foster employment opportunities, for young people in particular.

Finally, Member States need to adopt reforms that strengthen economic resilience in the context of long-term challenges, such as demographic trends, migration and climate change. Only resilient economies can ensure long-term economic convergence and the reduction of social disparities.

The country-specific recommendations also dedicate special attention to social challenges, building on the European Pillar of Social Rights, proclaimed in November 2017. The ensuing recommendations encourage Member States to advance on the three dimensions of the Pillar: equal opportunities and access to the labour market, fair working conditions, and social protection and inclusion. A particular focus is put on the provision of adequate skills, on the effectiveness and adequacy of social safety nets and improving social dialogue.

What progress have Member States made on the country-specific recommendations?

Since the first European Semester cycle in 2011, Member States have fully implemented, made some or substantial progress on over two-thirds of the country-specific recommendations.

They have made most headway in financial services, reflecting the priority given to the stabilisation of the financial sector in response to the economic and financial crisis. There has also been a high implementation rate of reforms to promote job creation on permanent contracts and address labour market segmentation. On the other hand, Member States have not yet fully addressed recommendations in the area of broadening the tax base and in health and long-term care.

Compared to last year, most progress has been delivered in reforming financial sectors and active labour market policies. For instance, Member States have improved the financing conditions and facilitated a durable resolution of non-performing loans or improved banking supervision. Sound progress has also been made in active labour market policies which have become increasingly diverse in nature in recent years, focusing on a more tailored approach to individual needs, in line with the Council recommendations for youth and long-term unemployed. On the other hand, progress has been slow in education and in addressing challenges in the long-term sustainability of public finances. Education reforms, notably those aiming at improving access for disadvantaged groups and raising the overall quality of education, continues to represent a challenge. Rather modest progress has also been recorded on addressing challenges posed by the long-term sustainability of public finances in view of an ageing population. This policy area is addressed in a high number of Member States, but progress has only been limited in spite of posing significant challenges over the coming decades.

Current level of implementation of 2011-2017 recommendations (multiannual assessment)

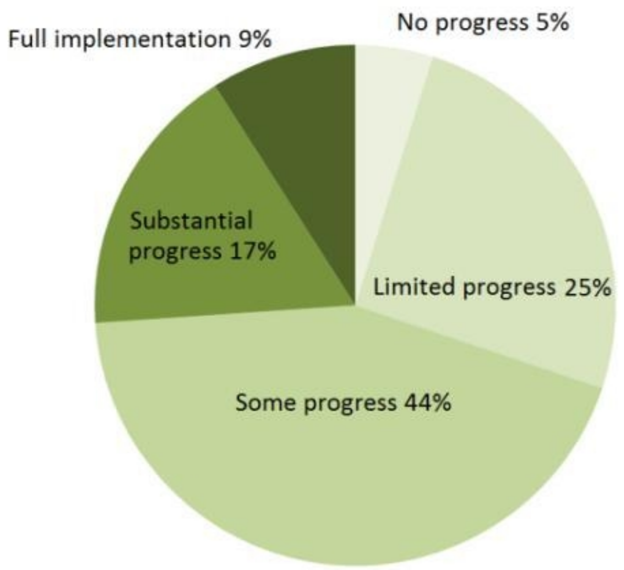


Figure 2: Implementation of country-specific recommendations: annual assessment in each consecutive year since 2011 versus implementation to date

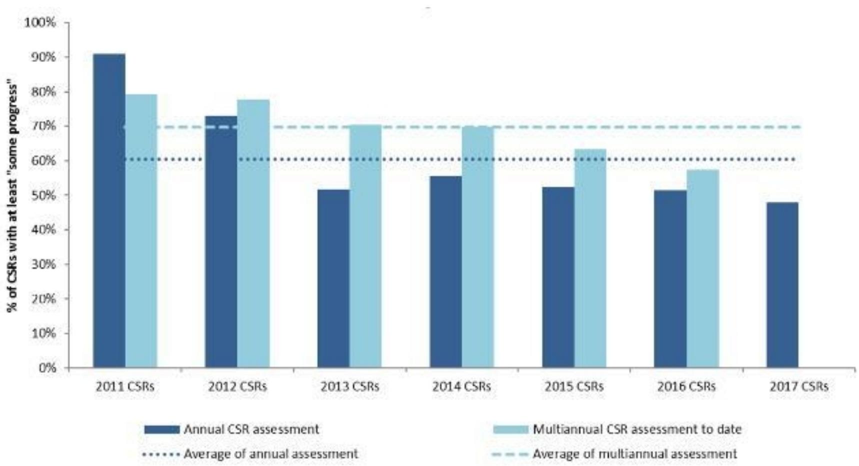
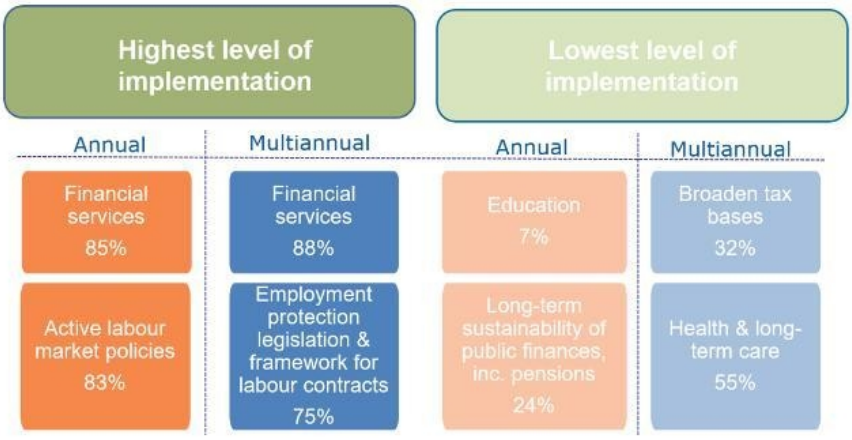


Figure 3: Policy areas displaying highest and lowest level of CSR implementation



What are the main challenges for Member States in 2018-2019?

The overall objective of the country-specific recommendations is to encourage Member States to use the current favourable economic climate to further strengthen the resilience of their economies.

Given the positive cyclical conditions, all Member States should prioritise reforms that increase their growth potential and make it more inclusive, improve the institutional and business environment, remove bottlenecks to investment, support the creation of quality jobs, reduce inequalities, address skills challenges, ensure effective, resilient and accessible healthcare and improve social safety nets.

How is the Commission helping Member States to implement recommendations?

The Commission promotes reform implementation by engaging in an open dialogue with Member States, by using our monitoring and surveillance tools to identify opportunities and vulnerabilities and by providing technical and financial support to Member States.

The continuous policy dialogue with Member States has intensified over the past few years. Like last year, we have consulted Member States on the analytical parts of their Country Reports prior to publication. In recent months, we have conducted additional consultations with national authorities and stakeholders on how the key challenges identified could translate into country-specific recommendations.

The Commission is also making sure that EU funding is steered towards EU and national priorities. The European Structural and Investment Funds are the principal investment tools for delivering on the Europe 2020 goals. There is a need to use this funding in conjunction with financial engineering techniques, loans and schemes to facilitate SME financing, in order to enhance the impact on the EU economy. The Juncker Plan’s European Fund for Strategic Investments also serves this purpose. In addition, for the long-term budget for the period 2021-2027, the Commission will propose a reform delivery tool which would provide financial support to Member States committing to structural reforms, including those identified in the European Semester.

Effective implementation of structural reforms requires both political will and adequate administrative capacity. The Commission is providing technical support to the Member States through the Structural Reform Support Service (SRSS). Countries can request from the Commission tailor-made technical support to prepare, design, and implement growth-enhancing structural reforms. This covers reforms in the areas of governance and public administration, public financial management, business environment, labour markets, health and social services, financial sector and access to finance. This year, the SRSS will support reforms in 24 Member States through more than 140 projects, most of them addressing challenges identified in the European Semester. This will bring the total number of support projects to over 440.

In its proposals on the deepening of the Economic and Monetary Union of 6 December 2017, the Commission advocated strengthening this technical support and presented a pilot tool to deliver reform that offers Member States new possibilities for financial support. Building on these initiatives, the Commission will shortly present a new streamlined instrument for the post-2020 multiannual financial framework that will provide both technical and financial support for the implementation of national reform commitments in order to further enhance the resilience of the Economic and Monetary Union.

What should countries do to make public finances more supportive of growth?

As economic conditions steadily improve, Member States with high levels of debt should rebuild fiscal buffers while Member States with a budget surplus should use the available fiscal space to make their economies more resilient and support growth.

To ensure that public finances are available for medium-to-long-term investment projects, close attention should be paid to their composition. Appropriately allocating public revenues and expenditures across various policy areas would result in a mix more conducive to growth. Further efforts are also needed to make taxation and expenditure more efficient and more effective at all levels of government. Rigorously implemented spending reviews are a useful tool to improve the allocation of taxpayers’ money.

The impact of an ageing population on national budget warrants reforms of the pension, healthcare and long-term care systems. These are crucial to ensure the long-term sustainability of public finances as well as adequate and accessible social security and healthcare.

Finally, further efforts are necessary to address high levels of labour taxes while safeguarding the necessary revenue for public policies, to increase incentives to work and support job creation for more vulnerable population groups.

What are the priorities for reform in the financial sector?

The resilience of the financial sector has been strengthened in a number of Member States since last year, as both the stock and the flows of non-performing loans have been reduced. Steps have been taken to improve the insolvency framework, to strengthen the supervisory framework and reduce non-performing loans, including through asset management companies. Further actions are recommended in some Member States to strengthen the supervision of the financial sector in those segments that are under the competence of national authorities. The proposals for country-specific recommendations adopted today also point to the remaining large shares of non-performing loans in some EU countries.

Developments in the housing market can have a destabilising impact on the financial sector, requiring action in some Member States. Housing is generally the main asset held by households, and real estate is also routinely used as collateral for loans by companies. Preventing booms and busts would thus increase the resilience of economies to potential shocks, especially if there is correction in housing prices. A number of Member States are recommended to reduce bottlenecks to housing supply. Reducing the debt bias created by the tax system, such as mortgage interest deductibility, would also contribute to decrease high levels of household debt.

How can Member States foster productivity growth?

Investment in infrastructure as well as research and development is essential to boost productivity growth. Ensuring that innovation investment is channelled to the most productive areas requires various steps: regulatory obstacles need to be removed, the business environment improved and entrepreneurship supported.

Priorities vary significantly across Member States.

Digitalisation levels vary considerably across countries in terms of infrastructures or the availability of digital skills. Even those Member States with good overall performance may show significant internal differences across regions.

Strengthening public or private research and development in terms of investment or effectiveness through better targeting is recommended for a number of Member States. Others should promote closer collaboration between business and research institutions.

At the same time, sustained investment in network infrastructure is necessary to lower the cost of starting or operating a business, and interconnections between Member States and regions are crucial to benefit from the full potential of the Single Market.

Reforms to create competitive and dynamic markets would open up new growth opportunities that firms could easily take advantage of in good economic times.

The introduction of ICT technologies has contributed to increasing productivity in some sectors where productivity performance had remained low for many years. Grocery markets and retail banking are good examples of this.

Exposing services markets to competition has also proven to increase productivity in markets where competition was stifled by regulations restricting entry. Markets for professional services remain a pending issue in this regard in several Member States. Opening these markets to competition is important to increase productivity within them as well as in markets using those services as inputs.

Finally, technological developments are contributing to making productivity growth possible in more areas of the services sector. E-commerce is the clearest best known example of this, but the number is expanding in the ever increasing field of the collaborative economy, for instance.

What should Member States do to improve employment?

Although employment is at a record high in Europe, significant gaps persist in the labour market participation of different population groups. In particular, labour market opportunities and outcomes need to be further improved for the low-skilled, the young, older people, people with disabilities and people with a migrant background.

While targeted measures are needed to tackle specific obstacles to labour market participation for each of these groups, providing access to high-quality and labour market relevant education as well as to training is key for all of them.

In addition, improving care services (childcare as well as healthcare and long-term care services), facilitating work-life balance and removing disincentives to work are important to increase overall participation in the labour market.

What should Member States do to improve social inclusion and protection – and to tackle inequalities?

This Commission renewed the emphasis on social priorities, which are at the heart of the European project. While labour market conditions are improving across the board, further efforts are needed to ensure that all groups benefit from the recovery.

Policy measures should aim to create truly inclusive labour markets. This would contribute to reducing inequalities and poverty risks. Access for all to high-quality education and training is particularly important in this respect. With the right skills, people are better equipped for taking up high-quality jobs and for job transitions when shocks occur. Raising skill levels and preparing our people for the jobs of tomorrow is the first way to address inequalities.

Member States should also tackle the gender gap in terms of employment rate and pay level, often caused by a lack of adequate care services and work-life balance opportunities or disincentives enshrined in the tax and benefit system.

In addition, the impact of social transfers on reducing poverty is weakening in the EU. As a result, tax reforms are needed in some Member States to protect the revenue for adequate social protection and to improve the capacity of the welfare system to reduce poverty and inequalities.

What is the role of education for economic growth? Which challenges do Member States need to address?

Investing in education and skills is essential to sustain innovation and productivity growth, especially in the current context of rapid technological change and an ageing population across Europe. Reskilling and upskilling are key to make labour markets more dynamic and inclusive, so that everyone can participate fully in society or engage in entrepreneurship.Transitions from lower- to higher-skilled career opportunities should be supported, with resolute policy action and adequate investment.

Educational inequality represents a threat to social cohesion and the long-term prosperity of European societies, and is often inherited across generations. Efforts should therefore focus on reducing unequal access to quality education and training, in particular for disadvantaged groups such as Roma, people with a migrant background and people with disabilities.

How does the Social Scoreboard for the European Pillar of Social Rights feed into the Semester?

The Social Scoreboard supports the identification of employment and social challenges faced by Member States in delivering on the principles of the European Pillar of Social Rights. It is used as a screening device that is integrated with a wider analysis at country-specific level. As such, the scoreboard supports the analysis presented in the Joint Employment Report and in the Country Reports, as a key analytical tool.

This year the Country Reports contain a box on the European Pillar of Social Rights reporting on Member States' state of play under the headline Social Scoreboard indicators, according to the methodology developed for the Joint Employment Report. Member States are evaluated according to their performance under the scoreboard dimensions, ranging from "critical situation" to "best performer". All headline and secondary social scoreboard indicators are reported in the statistical annex of the country reports.

The Commission does not apply a strict correspondence between proposed CSRs and challenges identified according to the indicators in the Social Scoreboard. The assessment of each situation is country-specific and based on a number of analytical sources – not only the Social Scoreboard, but also other tools like the Joint Assessment Framework, the Employment Performance Monitor (EPM) and the Social Protection Performance Monitor (SPPM).

Why do some countries have more detailed recommendations?

The level of detail and specificity of an individual country-specific recommendation depends on the specific economic situation of the country concerned. Member States which face more urgent and/or encompassing challenges, such as those experiencing excessive imbalances, receive more detailed and comprehensive recommendations than other Member States.

For Member States where economic performance is overall satisfactory and challenges are more specific, the recommendations are less comprehensive and detailed.

Fiscal development and decisions: what has the Commission decided today?

Based on the assessment of the 2018 Stability and Convergence Programmes, the Commission has also taken a number of steps under the Stability and Growth Pact:

- The Commission recommends that the Excessive Deficit Procedure be closed for **France.** This would leave only one Member State (Spain) under the corrective arm of the Pact, down from 24 countries in 2011.
- The Commission also adopted reports for **Belgium** and **Italy** under Article 126(3) TFEU, in which it reviews their compliance with the debt criterion of the Treaty. In the case of Italy, the analysis suggests that the debt criterion should be considered as currently complied with, notably as Italy was found broadly compliant with the preventive arm of the Pact in 2017. For Belgium, as there is no sufficiently robust evidence to conclude that Belgium did not comply with the preventive arm requirements, the report could not fully conclude as to whether the debt criterion is or is not complied with. The Commission will reassess next year the two countries' compliance with the Stability and Growth Pact on the basis of the ex-post data for 2018, to be notified in Spring 2019.
- The Commission addressed a warning to **Hungary** and **Romania** on the existence of a significant deviation from the adjustment path toward the medium-term budgetary objective (MTO) in 2017. The Commission proposes that the Council adopt a recommendation for Hungary to take appropriate measures in 2018 with a view to correcting this significant deviation. For Romania, which is already subject to a significant deviation procedure, the Commission recommends that the Council issue a decision on non-effective action and a recommendation to take measures in 2018 and 2019 to correct the significant deviation.
- The Commission also publishes today its Opinion of the updated Draft Budgetary Plan (DBP) for **Spain**, as the one submitted last October was based on a "no policy change" scenario. The Commission considers the updated Draft Budgetary Plan is broadly compliant with the requirements under the Stability and Growth Pact, since the Commission's Spring 2018 Economic Forecast projects that Spain's headline deficit will be below the Treaty reference value of 3% of GDP in 2018. Nonetheless, the Opinion notes that neither the headline deficit target nor the fiscal effort called for in the 2016 Council notice are projected to be met this year.

Why is the Commission recommending that the Council closes the excessive deficit procedures (EDP) for France?

France achieved a headline deficit of 2.6% of GDP in 2017, thus fulfilling the EDP target of 2.8%. The deficit is projected to decline further to 2.3% in 2018 before increasing to 2.8% in 2019. This points to a durable and timely correction of the excessive deficit as required to close the EDP.

When will France move to the preventive arm of the Stability and Growth Pact?

EU finance ministers are expected to discuss the Commission's recommendations in the Economic and Financial Affairs Council (ECOFIN) next month. If the ECOFIN Council decides to abrogate the EDP, France will move from the corrective to the preventive arm of the Stability and Growth Pact (SGP) as of 2018.

Under the preventive arm of the SGP, France should progress towards its medium-term budgetary objective at an appropriate pace, including respecting the expenditure benchmark, while complying with the deficit and debt criteria. France would have to comply with the rules of the SGP's preventive arm as of this year.

How many Member States are currently in an excessive deficit procedure?

If the Council follows the Commission's Recommendation for closing the EDP for France, only Spain would remain in EDP. In spring 2011, 24 Member States were in EDP.

What is a report under Article 126(3) of the Treaty?

The Article 126(3) report represents the first step in assessing the case for launching a possible Excessive Deficit Procedure. It assesses the Member State's deficit and/or debt position. A Member State is non-compliant with the deficit requirement if its general government deficit is above 3% of GDP, unless the excess over the reference value is only exceptional and temporary and the deficit ratio remains close to the reference value. As regards debt, the criterion for non-compliance is a general government debt level greater than 60% of GDP and not declining at a satisfactory pace.

The SGP defines a satisfactory pace as a reduction of the gap between a country's debt ratio and the 60% of GDP reference value of the Treaty by 1/20th annually on average over three years. If a Member State does not meet one or both of the criteria, the Commission prepares a report under Article 126(3) of the Treaty, which considers in detail a series of factors and assesses the case for opening an EDP.

Why is the Commission recommending that the Council opens the Significant Deviation Procedure for Hungary and Romania?

Based on the Commission 2018 Spring forecast and the 2017 outturn data validated by Eurostat, the observed deviation from the required structural adjustment path in 2017 was above the threshold of significance of 0.5% of GDP according to both indicators in both countries.

In Hungary, the growth of government expenditure, net of discretionary revenue measures and one-offs, was well above the applicable expenditure benchmark rate in 2017, pointing to a significant deviation from the required structural adjustment. In 2017, from a position of -1.8% of GDP in 2016, the structural balance deteriorated to -3.1% of GDP, also pointing to a significant deviation. An overall assessment leads to the conclusion that the observed deviation from the medium-term budgetary objective (MTO) in 2017 is significant.

In case of Romania, on 16 June 2017, the Council decided that a significant observed deviation from the MTO occurred in Romania in 2016. On 5 December 2017 the Council found that Romania had not taken effective action in response to that recommendation concerning 2017. In 2017, the growth of net primary government expenditure was well above the expenditure benchmark, pointing to a significant deviation. The structural balance deteriorated to -3.3% of GDP from a position of -2.1% of GDP in 2016, also pointing to a significant deviation from the recommended structural adjustment. An overall assessment leads to the conclusion that the observed deviation from the requirements of the preventive arm of the SGP in 2017 is significant.

What is the follow-up if a significant deviation is confirmed for 2017 for Hungary and/or Romania?

In the event of a significant observed deviation from the adjustment path towards the medium-term budgetary objective (MTO) in a Member State, a warning is addressed to that Member State. Within one month of the date of the adoption of the warning, the Council should address a recommendation to the Member State concerned to take the necessary policy measures to correct the significant observed deviation. The regulation foresees that the recommendation will set a deadline of no more than five months for the Member State to address the deviation. Within that deadline, the Member State should report to the Council on action taken in response to this recommendation.

Why is the Commission publishing today an assessment of the updated Draft Budgetary Plan (DBP) for Spain?

The Draft Budgetary Plan submitted by Spain last October was based on a "no policy change" scenario. Spain submitted a fully-fledged Draft Budgetary Plan in April 2018 with additional policy measures.

Why is the Commission adopting a Communication on the review of the flexibility under the Stability and Growth Pact?

At the start of 2015, the Commission adopted a Communication on "Making the Best Use of the Flexibility within the Stability and Growth Pact". Building on this Communication and following extensive discussions between the Commission and Member States, a Commonly Agreed Position on Flexibility was achieved (and endorsed by the ECOFIN Council in February 2016).

The use of Flexibility in the Stability and Growth Pact was enhanced along three axes:

- The structural reform clause
- The investment clause
- The matrix of requirements, which allows for a more nuanced modulation of fiscal effort at national level depending on public debt and the business cycle.

The Commonly Agreed Position on Flexibility required the Commission to review the application of the structural reform clause and investment clause by the end of June 2018. Thus, the Commission is adopting the Communication on Flexibility under the Stability and Growth Pact in line with this requirement.

What are the main findings of the review of the flexibility under the Stability and Growth Pact?

The review shows that the key objectives of the Commonly Agreed Position on Flexibility have been met to a large extent. It provides a predictable and transparent framework that has allowed the Commission to apply the existing rules of the Pact in a country-specific and balanced manner.

The flexibility allowed under the Pact has allowed striking a good balance between the objective of ensuring prudent fiscal policy and stabilising the economy. The European Commission spring forecast 2018 shows that public debt and deficits declined, while economic activity picked up since 2016.

The cyclical modulation encourages Member States to increase their fiscal effort in good times to make our economies more resilient. With the economic expansion in Europe in its fifth year, the time is ripe to build up fiscal buffers, which would give Member States more manoeuvring space in the next downturn.

What are the next steps in the implementation of the budgetary decisions?

The Council is invited to adopt the Commission's Recommendations:

- on closing the Excessive Deficit Procedure (EDP) for France
- on issuing a decision on non-effective action on the Significant Deviation Procedure open for Romania
- on opening a Significant Deviation Procedure for Hungary and Romania

The Economic and Financial Committee (EFC) will provide its opinion on the Article 126(3) reports for Belgium and Italy within two weeks.

The Commission assesses compliance with the SGP continuously throughout the year as part of the European Semester of economic policy coordination.

For further information:

Press release on the European Semester 2018 Spring Package

Chapeau Communication on the country-specific recommendations 2018

Country-specific recommendations 2018

Excessive Deficit Procedure for France

Significant Deviation Procedure for Hungary

Significant Deviation Procedure for Romania

Article 126.3 report for Belgium

Article 126.3 report for Italy

Opinion on the updated Spanish Draft Budgetary Plan

Key employment and social figures factsheet

2018 Convergence Report press release

European Economic Forecast Spring 2018

European Semester timeline

Recommendation for the Euro Area 2018

European Semester Winter Package 2018

Communication on Country Reports 2018

Country Reports 2018

European Semester Autumn 2017 Package: Striving for sustainable and inclusive growth

Alert Mechanism Report 2018

Annual Growth Survey 2018

European Pillar of Social Rights

The EU Economic Governance Explained

Commonly Agreed Position on Flexibility under the SGP

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