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Special analysis

Commission´s recommendations for 2014

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Introduction

At the beginning of June, the European Commission issued **economic recommendations for individual EU member states**, the intended aim of which is to strengthen the long awaited economic recovery.

The individual recommendations are based on similar economic analyses of member states, based on which the European Commission advises member states regarding how to proceed in many areas for the subsequent period. It attempts **to help improve and maintain already achieved economic growth**, maintain healthy public finances and thus increase competitiveness, including against other world economies. A lot of attention is devoted to **the situation on the labour market**, which has been and remains affected by high unemployment, mainly among young people.

These recommendations are focused on the periods of the subsequent twelve to eighteen months and are based on findings from **the yearly analysis of growth** prepared by the Commission at the end of last year based on the submitted information from mid-term financial plans of individual member states.

Cycle phase

The economic crisis, which hit hard in Europe and elsewhere, showed the need to strengthen the management of economic matters and improve coordination of polities among member states. This coordination shall bear its fruits through contribution of convergence and stability both for the entire EU and for individual member states.

Therefore, the Commission's current recommendations are not a one-time occurrence. Until 2010, tasks for coordination of economic policies were carried out mutually independently. However, it became apparent that it would be necessary to synchronise these approaches and **simplify the entire system**, so that in its individual areas joint objectives would be taken into consideration.

For these reasons, in 2010 EU member states introduced **the European semester** as part of broader reforms. The European semester represents a cycle of coordination of economic and fiscal policies within the EU. During the European semester, member states bring their budget and economic policies in line with objectives and rules agreed upon at the EU level.

The first such consultation occurred in 2011. It was preceded by **the introduction of the Europe 2020 strategy** by the European Commission in March 2010 and its subsequent approval in June of the same year. The Czech Republic approved its first national programme at the end of April 2011.

The already fourth European semester culminated with the approval of individual recommendations by the European Council at the beginning of this June. This European semester includes a clearly defined schedule, in accordance with which member states receive advice at the EU level and then present their policy plans, which need to be assessed at the EU level. After their evaluation, member states are issued **recommendations regarding their domestic budget and reform policies**.

Whenever essential, member states also receive recommendations for correcting macroeconomic imbalances. The aim of this approach is to ensure that member states taken recommendations into consideration when setting their budgets for the subsequent year.

The cycle itself, as specified by the European Council, can be divided into several phases:

- Preparation phase: Analysis of the situation and activities corresponding to the previous year;
- First phase: Political instructions at the EU level;
- Second phase: Individual countries' policies and plans
- Third phase: Implementation.

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Preparation phase: Analysis of the situation and activities corresponding to the previous year

The European semester itself is prepared in November of the preceding year, when the European Commission publishes its yearly analysis and **report regarding the alert mechanism**.

In the yearly growth analysis (carried out at the end of the year), the Commission's opinion regarding the EU's political priorities for the next year is presented. Member states are called upon to consider the specified priorities when formulating their economic policies for the subsequent year.

Macroeconomic development in individual member states is evaluated in the Alert Mechanism Report (AMR). The European Commission may then decide based on that report whether to carry out thorough checks in countries where the risk of macroeconomic imbalance is considered high.

First phase: political instructions at the EU level

At the start of the year, the Council of the EU discusses the yearly analysis of growth, formulates the main directions and adopts conclusions. This yearly analysis is also discussed by the European Parliament, which may issue its own report if it so decides. Then a stance is issued regarding the main aims of employment policy. The European Parliament becomes further involved in the entire process via economic dialogue.

The European Parliament can invite the chairman of the Council, the Commission and the Chairman of the European Council and/or **the head of the Eurozone to discuss issues related to the European semester**. The opportunity to participate in exchanges of opinions can also be offered to individual member states.

Based on a yearly analysis of growth as well as a breakdown carried out by the Council of the EU and its conclusions, the European Council (heads of state and heads of government) provides policy instructions.

Member states are then asked to consider these main aims when preparing their domestic programmes for stability, convergence programmes and national reform programmes, in which their budget policies and policies for supporting growth and competitiveness are highlighted.

The Commission makes public the thorough examination of the macroeconomic imbalance, which has been carried out in member states where the risk of such imbalance is deemed high.

Based on such examination, **the Commission may prepare proposed recommendations** for the affected countries for the purpose of correcting the specified imbalance. These proposals can be prepared together with the publication of the thorough examination or in a later phase of the process, together with other recommendations for individual countries.

Second phase: individual countries' policies and plans

Member states submit their policy plans, if possible by 15 April, but no later than by the end of April:

- **stability and convergence programmes**, in which the mid-term budget strategy of states is highlighted;
- **national reform programmes**, in which member states' plans related to structural reforms focused on supporting growth and employment are specified.

In the subsequent months, the European Commission evaluates the policy plans of individual member states and presents proposed recommendations for individual countries, and the Council of the EU discusses the proposals and approves the final recommendations for individual countries. These recommendations are then submitted to the European Council for confirmation.

The Council of the EU adopts recommendations for individual countries, and member states are called upon to implement them.

Third phase: Implementation

Beginning in July, member states consider the specified recommendations when deciding at the national level regarding the state budget for the upcoming year, which enables them to implement policies in the planned manner.

The entire cycle is restarted at the end of the year, when the Commission presents an overview of the economic situation as part of its yearly analysis of growth for the upcoming year. The Commission begins already in this phase to consider the progress that individual countries have achieved when implementing the recommendations.

Member states that use financial assistance bound to economic recovery programmes do not need to present stability programmes and are not subjected to potential thorough examination related to macroeconomic balance.

Receiving financial assistance is conditioned on thorough implementation of a recovery programme, which already includes all of these policy areas.

COMMISSION´S 2014 RECOMMENDATIONS FOR MEMBER STATES

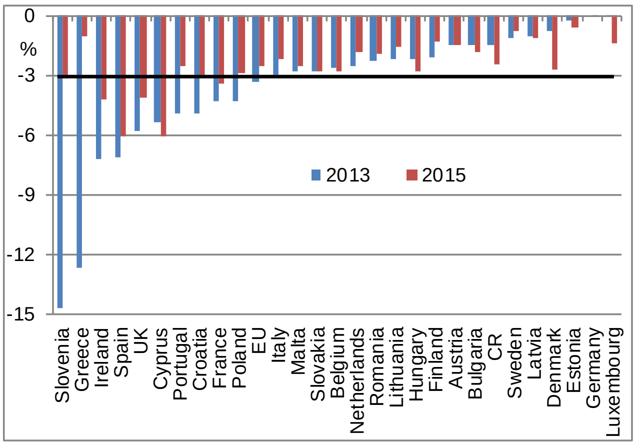
This year recommendations were issued for 26 member states. However, recommendations were not issued for Greece and Cyprus, where economic recovery programmes are ongoing. The recommendations reflect progress and positive results, which have been achieved since 2013:

- **After the economic crisis, the economy returned to growth in most countries affected by the crisis.** An economic decline is expected this year only in Cyprus (-4.8% of GDP) and Croatia (-0.6% of GDP). However, in 2015, all of the states without exception are expected to report economic growth.
- **The balance of public finances continues improving.**

  In 2014, it is expected that the total budget deficit of the EU states will drop to below 3% for the first time since the crisis hit and will amount to 2.6% of GDP.

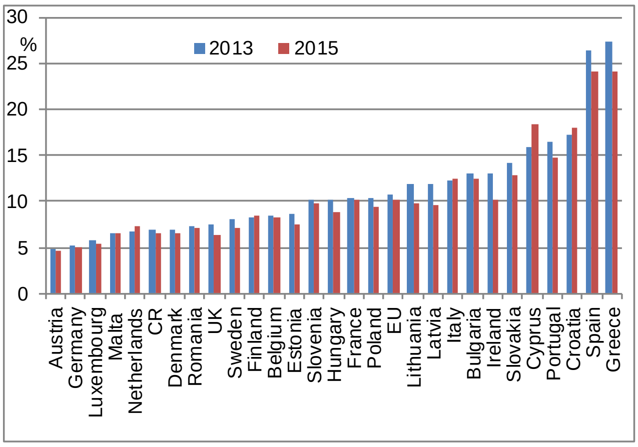
  The Commission has recommended to Belgium, the Czech Republic, Denmark, the Netherlands, Austria and Slovakia that they end the excessive deficit procedure, as a result of which the number of countries still subjected to this procedure would fall to 11. In 2015, the situation with public budgets is expected to continue improving, and the average for the European Union will likely drop by another 0.1%.
- **Balance is being restored**, which is improving several countries' financial situation. In March 2014, the Commission, for the first time since the procedure for handling macroeconomic imbalances was implemented, concluded that two countries, Denmark and Malta, would no longer encounter any imbalances and that in Spain the imbalance would cease to be excessive.
- **Beginning this year, employment growth is expected to be levelled out**, and the unemployment level is expected to drop by 2015 to about 10%, with a half-year or longer delay existing between developments on the labour market and development of GDP.

Public budget deficit to GDP (in %)



Source: European Commission

Unemployment level in the EU



Source: European Commission, AMECO

Several member states, including Spain, Portugal, Italy and France, have carried out major reforms at boosting the strength of the labour market.

According to the European Commission, certain recovery of the economy and its growth should occur also in 2015, when unlike in 2013 in most EU member states the unemployment level is expected to drop (the EU average is expected to drop in 2015 by 0.7% from 10.8% in 2013). The highest unemployment levels, in Greece and Spain, are expected to fall to under 25%.

In view of the recent economic crisis and recovery, it is necessary for member states to continue with their structural reforms.

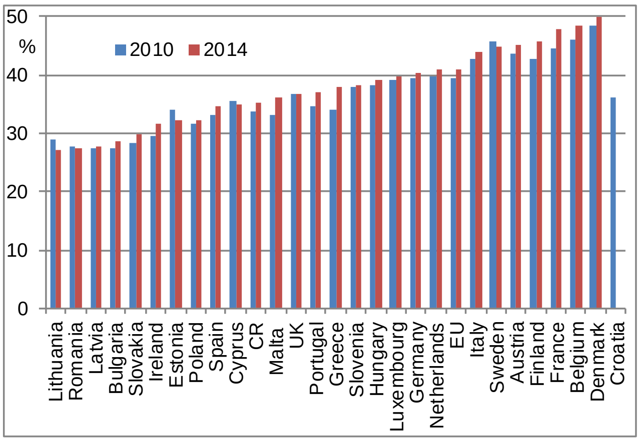
Therefore, the Commission recommends these specific measures:

- **Tackling high unemployment, inequality and poverty:** The crisis in the European Union has deeply and over the long term been reflected in the unemployment level. In 2013, the EU's average unemployment level was still very high at 10.8%, while among individual states the differences ranged from 4.9% in Austria to 27.3% in Greece.

  This situation requires the continuation of employment policy reforms, in order to improve the education and social security systems.

  Special attention is devoted in the recommendations to resolving youth unemployment, which in some states exceeds 50%, in particular by implementing a system of guarantees for young people. The long-term unemployed are another group that remains negatively affected.

Overall tax burden in % of GDP



Source: EC, AMECO, data of 2014 for Croatia are not available

- **Reorganisation of the tax system, so that it supports employment more:** During the crisis, many countries relied more on tax increases than cuts in spending, and so the total tax burden grew. The total tax burden (including taxes and contributions for social security) in the EU has grown since 2010 by 1.4% to 41% in 2014.

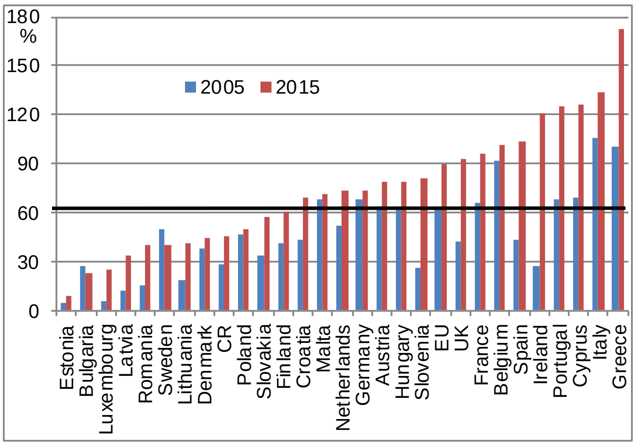
  Since from the point of view of public finances there is limited manoeuvring space, the recommendations have in many cases been focused on shifting the tax burden from work to periodic taxes on real estate, consumer taxes and environmental taxes, on better fulfilment of tax obligations and on combating tax fraud.

- **Underestimating of private investments:** In Italy, Greece, Spain, Lithuania, Slovakia, Croatia and Cyprus, it is still difficult to obtain bank financing, mainly for SME. The recommendations cite the need to stabilise the banking sector further and support alternative forms of financing, such as programmes involving credit guarantees or business bonds.

- **Increasing the competitiveness of EU economies:** There has been only minor progress in structural reforms of key sectors compared to in 2013. In several of this year's recommendations, additional reforms are emphasised, in relation to the service sector, energy, traffic and transport infrastructure, research and development systems and regulations governing economic competition.

- **Debt reduction:** According to the most recent spring economic prognosis from this year, public debt will reach its maximum due to ongoing debt accumulation, and it is necessary for debt accumulation to begin declining, particularly in the most affected states, which are Belgium, Ireland, Greece, Spain, Italy, Cyprus and Portugal, where public debt still exceeds 100% of GDP.

Public debt to GDP in the EU (in %)



Source: European Commission, AMECO

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In terms of public finances, it will be a demanding task to manage expenditures related to the ageing population (particularly expenditures for pensions and healthcare) and to maintain pro-growth expenditures for areas such as education, research and innovation.

Budget decisions

The European Commission has continued to recommend to the Council of Ministers that it end the excessive budget procedure for six states: Belgium, the Czech Republic, Denmark, the Netherlands, Austria and Slovakia.

The Commission also concluded that two countries (Poland and Croatia), in reaction to the recommendations issued by the Council during the excessive deficit procedure, had adopted effective measures.

RECOMMENDATIONS FOR THE CZECH REPUBLIC FOR 2014-2015

The recommendations from this June do not differ much from those of previous years. Like in previous years, there are seven of them:

- **Maintain a healthy fiscal situation during this year corresponding to correction of the excessive budget.**

  Significantly boost budget strategy in 2015 to ensure achievement of mid-term objectives and to maintain that achievement. Expenses focused on growth shall be given priority. It is also recommended to implement fiscal rules for local and regional governments and improve coordination between all levels of administration.
- Another point is focused **on improving fulfilment of tax obligations** (especially with a focus on VAT) and the effort to reduce costs for tax collection and payment through simplification of the tax system and harmonisation of VAT bases for individuals and assessment bases for contributions to social security and health insurance.

  Emphasis is also placed on reducing differences in the tax area between employees and self-employed people.
- **Improve the efficiency and effectiveness of public services** related to employment, mainly by implementing a system for measuring performance.

  Address unregistered young people and provide individualised services. Significantly increase the availability of affordable and quality facilities and services for child care, with a focus on children up to age three.

  A very drastic reduction in the number of preschool facilities has occurred in the past, particularly daycare centres. However, there was certain progress, when in January 2014 the Czech Republic approved a bill regarding children's groups.
- **Ensure that accreditation, management and financing of universities** contribute to improvement of their quality and to a better focus on the labour market. Speed up the processing and implementation of new methods for evaluating research and for allocating financial resources, in order to increase the share of financing provided to research institutions based on their performance.

  Make the teaching profession in elementary education more attractive, implement a comprehensive evaluation framework and support schools and pupils with poorer results. Increase education inclusiveness and support for participation of Roma and other socially disadvantaged children, particularly in preschool education.
- **In the area of reforms of regulated professions**, speed up their progress and focus on eliminating unjust and unreasonable demands.
- **Adopt and implement the state service act this year** and speed up and strengthen the fight against corruption by implementing the remaining legislative measures defined in the anti-corruption strategy for 2013-2014.
- **More quickly increase the legally set age for beginning retirement** with clearer tying of this age with changes in the middle part of life and thereby ensure long-term sustainability of the public pension system. It is also recommended to support employment of older workers and examine the mechanism for valorisation of pensions.

The Czech government has accepted the individual recommendations. They mostly correspond with the government's programme. However, a certain controversial point is the retirement age, since the Czech government does not agree with faster increasing of the retirement age, even because of worse employment levels among older people.

The retirement age in the Czech Republic is among the lowest in the EU, but continued life expectancy is lower as well. Continued Life expectancy (65), the average lifespan, expresses the number of years on average that a person age 65 will still live, assuming that for the duration of the remainder of the person's life particular demographic indicators do not change.

Period of economic activity and continued life expectancy in the EU in 2012

	Continued life expectancy (65)		Period of economic activity	
	Women	Men	Women	Men
France	23.4	19.1	32.6	36.5
Spain	22.8	18.7	31.9	37.4
Italy	22.1	18.5	25.4	35.3
Finland	21.6	17.8	36.7	38.0
Luxembourg	21.4	18.4	29.4	35.5
Belgium	21.3	17.7	29.6	34.7
Austria	21.3	18.1	34.2	39.4
Portugal	21.3	17.6	35.0	38.7
Germany	21.2	18.2	34.9	39.9
EU	**21.1**	**17.7**	**32.2**	**37.6**
Ireland	21.1	18.0	30.1	37.9
Slovenia	21.1	17.1	32.1	34.9
Sweden	21.1	18.5	39.3	41.8
Greece	21.0	18.1	27.8	36.0
Malta	21.0	17.6	23.7	38.9
Netherlands	21.0	18.0	37.0	42.2
UK	20.9	18.5	35.1	41.0
Cyprus	20.4	17.9	32.4	39.9
Estonia	20.3	14.8	35.7	36.7
Denmark	20.2	17.5	37.8	40.7
Poland	19.9	15.4	29.5	34.6
CR	**19.2**	**15.7**	**30.9**	**37.5**
Lithuania	19.2	14.1	34.2	33.7
Croatia	18.7	15.0	28.7	33.3
Latvia	18.5	13.6	34.9	35.2
Slovakia	18.5	14.6	29.7	35.6
Hungary	18.1	14.3	28.2	32.5
Romania	17.7	14.5	29.2	34.5
Bulgaria	17.3	13.9	30.3	32.7

Source: EC, Eurostat

Retirement age in EU states

	Retirement age men and women (2009)	Retirement age men and women (2020)
Belgium	65/65	65/65
Bulgaria	63/60	65/63
CR	**62/56y8m-60y8m**	**63y10m/60y6m-63y10m**
Denmark	65/65	66/66
Germany	65/65	65y9m/65y9m
Estonia	63/61	64/64
Ireland	66/66	66/66
Greece	65/60	67/67
Spain	65/65	65-66y4m/65/66y4m
France	60-65/60-65	62-67/62-67
Croatia	65/60	65/62y6m
Italy	65y4m/60y4m	66y11m/66y11m
Cyprus	65/65	65+/65+
Latvia	62/62	63y9m/63y9m
Lithuania	62y6m/60	64/63
Luxembourg	65/65	65/65
Hungary	62/62	64/64
Malta	61/60	63/63
Netherlands	65/65	66y8m/66y8m
Austria	65/60	65/60
Poland	65/60	67/62
Portugal	65/65	66/66
Romania	63y4m/58y4m	65/61
Slovenia	63/61	65/65
Slovakia	62/57y6m-61y6m	62+/62+
Finland	63-68/63-68	63-68/63-68
Sweden	61-67/61-67	61-67/61-67
UK	65/50	66/66

Source: European Commission; note: y = years, m = months, 2009 = the situation in 2009, 2020 = member states' plans for 2020

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Conclusion

The presented **recommendations for individual countries** will be discussed by top officials and ministers from member states. On 8 July, EU finance ministers will formally accept them.

Then it will be up to member states **to fulfil the recommendations** and take them into consideration when preparing their state budgets and strategies for 2015.