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COMMUNICATION FROM THE COMMISSION TO THE SPRING EUROPEAN COUNCIL

Strategic report on the renewed Lisbon strategy for growth and jobs: launching the new cycle (2008-2010)

Keeping up the pace of change

KEEPING UP THE PACE OF CHANGE

By re-launching the Lisbon strategy in 2005, and refocusing it on growth and jobs, Europe has come a long way. There has been a significant and permanent change in the way the Union works: a close partnership and a clear division of responsibilities between Member States and the Commission have made possible a big step forward.

The results are already visible. The economy is performing much better than it was in 2005. The growth figures are strong. Almost 6.5 million new jobs have been created in the last two years. Another 5 million are expected to be created up to 2009. Behind these figures stand millions of Europeans who have been lifted out of the misery of unemployment and whose lives have changed for the better.

Of course, some of the current upturn is cyclical. But structural reforms implemented by Member States and the Union within the framework of the Lisbon strategy in the last few years have made a difference, and they are the best protection against a cyclical downturn.

The Lisbon Strategy is the EU's vehicle for accompanying change. This makes it an essential part of the Union's response to globalisation, helping Europeans to shape this new set of challenges and opportunities.

Reform can be tough. It can sometimes be unpopular. But the path of reform is the only one in tune with today's needs. Our success so far should spur us on to further efforts in the next cycle of the Strategy.

This means keeping up the pace of change. Too many Europeans are still unemployed. We do not yet have the best environment for business to grow. Europe is still fragmented when it comes to fostering innovation and research and development; the contribution from the private sector is still insufficient. We have only just begun to transform the EU into a low-carbon economy. Given the risk of a global slowdown in growth, it is essential to press ahead with reform and increase the resilience of our economies.

The Lisbon strategy requires strong leadership. When Europe gives that leadership, action follows. The priority actions agreed by the 2006 Spring European Council have generated real momentum. It is now much easier and quicker to set up a business in most Member States. Common principles on flexicurity have been agreed. This provides a strong basis for a fresh political impetus.

We have to build on this momentum and agree on a focused list of ambitious new actions. Here are a few examples of what we need to do together:

- reduce the number of early school leavers to ensure that no one is left behind in the age of globalisation;
- give Europe a new "fifth freedom", the free movement of knowledge, to allow Europe to capitalise on its creative potential;
- roll out high-speed internet to stimulate innovation and keep Europe at the forefront of the internet age;

– stimulate small and medium sized enterprises through a Small Business Act for Europe;

– improve substantially the energy efficiency of our buildings, using our huge procurement budgets to drive change;

– reinforce the education-research-innovation triangle, notably through the establishment and operation of the European Institute for Innovation and Technology (EIT) and the Joint Technology Initiatives (JTI).

Europe has a unique opportunity to transform itself into a creative, modern innovation-friendly, low-carbon economy, with a dynamic business environment, a highly-skilled work force and high-quality education, underpinned by a strong social model. The Lisbon Strategy for growth and jobs is part of helping Europeans to prosper with an agenda of access, opportunity and solidarity which will enable us to benefit from being open to the wider world and to shape globalisation to reflect European values.

José Manuel Durão Barroso

Brussels, 11th December 2007

TABLE OF CONTENTS

1. Introduction 5

2. Structural reforms implemented during the First Lisbon cycle (2005-2008) 6

3. Deepening the Lisbon Strategy in the next Lisbon cycle 7

3.1. Pressing ahead with reforms at national level 7

3.2. Strengthening economic policy co-ordination 8

3.3. Reforms needed at Community level, including the Community Lisbon Programme 9

3.4. Shaping the external agenda 9

3.5. Integrating national, Community and international action into an effective policy response 10

4. Actions in the four priority areas 10

4.1. Investing in people and modernising labour markets 10

4.2. Unlocking the business potential, especially of SMEs 12

4.3. Investing in knowledge and innovation 13

4.4. Energy and climate change 15

5. Follow-up after the 2008 Spring European Council 16

1. INTRODUCTION

With the re-launch of the Lisbon Strategy in 2005, the European Union and its Member States committed themselves to a new partnership aimed at securing sustainable growth and jobs.

Almost three years later, the results of this partnership are clearly visible. Economic growth has risen from 1.8% in 2005 and is expected to reach 2.9% in 2007 and 2.4% in 2008. While most of the recent upturn is cyclical, structural reforms in the Member States have also contributed. Almost 6.5 million new jobs have been created in the last two years. Another 5 million jobs are expected to be created up to 2009. Unemployment is expected to fall to under 7%, the lowest level since the mid-80's. The employment rate, currently at 66%, has moved much closer to the overall Lisbon target of 70%. For the first time in a decade, strong increases in employment have gone hand in hand with robust productivity growth. Standards of living in the Member States that recently joined the EU are visibly rising.

However, not all Member States have undertaken reforms with equal determination. Reforms in some areas, such as opening up markets and tackling labour market segmentation, have lagged behind. At the same time, the context is becoming less favourable as a result of a global economic slowdown, financial turmoil and higher commodity prices.

At the Informal European Council in Lisbon in October 2007, Heads of State and Government discussed the European response to globalisation[1]. They confirmed the central place of the renewed Lisbon strategy and called for it to be deepened during the next cycle. They also emphasised that the EU should use the Strategy to help shape globalisation in line with its own values and interests. The Union's model of development, combining competitiveness with solidarity and sustainability, and its long experience of economic integration, can be major assets in the age of globalisation. With the signature of the Lisbon Treaty, the EU will enter a new phase. Having resolved key institutional questions, the EU can now turn its attention to the issues that directly affect its citizens in their everyday lives.

The first part of this Communication to the 2008 Spring European Council sets out the Commission's proposals for taking the Strategy forward. While underlining the importance of macro-economic stability, it emphasises the need to implement outstanding reforms to reinforce the fundamentals to sustain solid economic growth in the future and help the EU withstand adverse developments in the global economy.

The second part consists of an assessment of progress made by each Member State (and the euro area) in the implementation of its National Reform Programme and of the country-specific recommendations, as adopted by Council[2]. The third part is a companion document containing a detailed assessment of progress by policy area[3]. The Lisbon package furthermore contains: (1) a proposal for a Council recommendation to update the country-specific recommendations and 'points to watch'; (2) a proposal for a Council recommendation to re-affirm the Integrated Guidelines for growth and jobs; (3) a new Community Lisbon

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1 "The European Interest: Succeeding in the Age of Globalisation" - COM(2007) 581.

2 Council Recommendation 2007/209/EC of 27 March 2007 (OJ L 92, 3.4.2007).

3 As far as the employment part is concerned, this also serves as the basis for the Joint Employment Report. It also includes a summary of the mid-term assessment of the growth initiative.

Programme; and (4) an analysis of the reorientation of the structural funds in support of growth and jobs.

2. STRUCTURAL REFORMS IMPLEMENTED DURING THE FIRST LISBON CYCLE (2005-2008)

Although there is a broad consensus on what needs to be done, the pace of delivery has been uneven. All Member States have implemented substantive reforms since 2005 but some have responded more robustly to the challenge than others. Some signs of "reform fatigue" have become apparent over the last twelve months.

On the positive side, budget deficits have been reduced from 2.5% of GDP in 2005 to a forecasted 1.1% in 2007, whilst public debt has declined from 62.7% in 2005 to just below 60% in 2007. Nonetheless, the opportunity to use the relatively strong growth conditions to reduce structural deficits has not been fully seized, especially in the euro area.

In some Member States, the improving growth conditions have been accompanied by a gradual build-up of imbalances, as witnessed by large current account deficits with signs of overheating, a loss of competitiveness, increasing household indebtedness as well as rapidly rising house prices.

The euro has been an anchor of stability. It has facilitated the functioning of the single market to the benefit of the euro area and the EU as a whole. The potential estimated growth rate of GDP in the euro area has increased by 0.2 percentage points since 2005 to 2.25%, which is partly due to the effects of structural reforms.

Productivity growth reached 1.5% in 2006, compared to an annual growth rate of 1.2% between 2000 and 2005. However, Europe is still lagging behind other leading economies both in investment in information and communication technologies (ICT) and in terms of their use to enhance productivity. Opening up network industries and services to competition has been slow and important obstacles to market entry remain. Some Member States lag behind with the implementation of internal market directives. Likewise, efforts to improve the intellectual and industrial property framework and to speed up standardisation have not borne fruit.

The EU's better regulation agenda is gradually being put in place, although many Member States still need to implement the necessary instruments, including impact assessments and methods to measure and reduce administrative burdens.

It is now much easier and cheaper to start a business in almost all Member States. Europe, as a whole, however, does not yet have a dynamic entrepreneurial culture. Too often, efforts to improve the business environment are made in a piecemeal way as opposed to being part of an integrated approach geared towards the growth of SMEs. Whilst Member States have set targets committing themselves to significantly increasing R&D investments which would help the EU approach its 3% of GDP target by 2010, the evidence does not yet reflect this ambition.

Employment growth has been impressive, although some regions and groups have benefited less. Many Member States have begun to reform their pension and early retirement systems. This has contributed to a large and sustained increase in the employment rate of older workers, although the 50% target is still some way off. The employment rate for women has

increased significantly (at 57.2%, it is approaching the 60% target), even though Member States should take further steps to promote gender equality on the labour market.

About half of the Member States have developed - or are developing - policies on the basis of a 'flexicurity' approach. Yet the policy response remains fragmented. A sustained move from passive to active labour market policies is underway. Member States are reforming social security systems, especially through changes to their tax and benefit systems, so as to balance rights and obligations. More flexible labour contracts for particular categories (e.g. new entrants) have been introduced but have not been backed up sufficiently by opportunities to acquire new skills which can help people to advance in the labour market. The more difficult task of reforming the rules governing other kinds of contracts has received little attention. As a result, many labour markets remain segmented, with well-protected insiders and more precarious outsiders on contracts with uncertain prospects.

Equally, lifelong learning falls far short of what is required, particularly among the low-skilled, who need it most. Education and training systems are not yet sufficiently responsive to labour market needs.

The EU has made the first steps towards transforming itself into a low carbon society. There is progress in meeting the overall EU Kyoto target and, at the Spring 2007 European Council, the EU committed itself to ambitious targets for greenhouse gas reduction and increasing the share of renewable energies by 2020.

A detailed account of progress at Member State level can be found in Part II of this Communication.

3. DEEPENING THE LISBON STRATEGY IN THE NEXT LISBON CYCLE

Although the economy is in better shape than in 2005, the EU goes into the new Lisbon cycle against a background of slowing global growth and risks arising from the financial turmoil and rising oil and commodity prices. Now is therefore the time to decide to deepen the implementation of the Strategy to bolster confidence and strengthen economic fundamentals to weather possible economic downturns.

3.1. Pressing ahead with reforms at national level

The key challenge for Member States during the next cycle is to implement the outstanding reforms, particularly in those areas which are detailed in the country-specific recommendations and 'points to watch'.

Given that it takes time to implement reforms and see their results, the Commission proposes to maintain the current set of recommendations largely unchanged and to fine-tune them in the light of progress made since their adoption in spring 2007.

In order to maximise their impact on growth and jobs, the new generation of EU Cohesion policy programmes are required to "earmark" over 60% of these funds[4] in support of the

[4] The earmarked categories must account for a minimum of 60% in the less developed regions eligible under the Convergence programmes and 75% in the relatively more prosperous regions eligible under

National Reform Programmes (NRPs). € 347 bn will be available for cohesion in the period 2007-2013. This will be complemented by national public and private co-financing of some € 160 bn. In total, € 70 bn will be mobilised annually up to 2013, mostly in support of the NRPs. Now that the programming phase has been completed, it is important to ensure that expenditures reflect the earmarking commitments and are not subsequently shifted to lower priority areas.

Local and regional authorities are already actively involved in the renewed Lisbon Strategy through the programming and implementation of earmarked cohesion programmes. Further efforts are necessary to reinforce wider stakeholder involvement, and to intensify the exchange of experience, ideas and best practice, which is already a major strength of the strategy. In this context, the Commission welcomes the strong interest of the European Parliament, the European Economic and Social Committee and the Committee of the Regions in particular to monitor the extent of stakeholder involvement in the strategy.

3.2. Strengthening economic policy co-ordination

Member States' economies are highly inter-dependent. There are many benefits to be gained if all move in the same direction and if reforms are aligned in time. The new governance of the Lisbon strategy, with its emphasis on partnership between EU and Member States, has proved its worth. The integrated guidelines are a key instrument for closer economic policy co-ordination under the renewed strategy. They offer a general framework within which Member States at different stages of development and with different social systems and institutional frameworks can pursue their own national reform agendas and are sufficiently broad to allow for adjustments in the light of changes to the policy environment. There is broad consensus among Member States and stakeholders that the guidelines should not be changed and that the focus should be kept on implementation[5].

For these reasons, the Commission proposes to re-affirm the current guidelines for the next cycle, whilst updating the explanatory notes which explain the context within which they should be implemented. This includes, for example, putting a stronger emphasis on measures aimed at investing more in people and at modernising labour markets. Member States should review their NRPs to ensure that they are up-to-date for the new cycle and should continue to include a broad range of stakeholders in their development and implementation.

Experience over the last three years has shown that the co-ordination of reforms should be strengthened further. The Commission therefore proposes that Member States discuss their specific policy responses to the country-specific recommendations and 'points to watch' as part of the multilateral surveillance process in Council. To structure the debate, each Member State should, as part of its implementation report, submit an action plan in which it sets out the measures it will take to follow-up the recommendations and/or points to watch.

In addition, the argument for coordinating reforms is even stronger in the euro area. Proposals for more effective co-ordination and governance in the euro area will be part of the review of the functioning of EMU to mark its tenth anniversary, which the Commission will present before summer 2008.

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the Competitiveness and Employment programmes. These thresholds apply on a voluntary basis to Member States that joined the Union after May 2004.

[5] Evaluation of the Integrated Guideline Package for Growth and Jobs, Draft Final Report, October 2007, Eureval and Rambøll Management and Ecofin Council conclusions (13.11.2007).

3.3. Reforms needed at Community level, including the Community Lisbon Programme

The new Community Lisbon programme (CLP) is the Community's contribution to the renewed Lisbon Strategy. It should be seen as the counterpart to the NRPs, setting out those Community actions which add the greatest value to reforms undertaken by Member States, and which will produce the greatest impact on growth and jobs. While some CLP measures only require adoption by the Commission, most also require adoption on a priority basis by the Council and Parliament. There is a need for a concerted political drive by all the EU institutions to reach agreement on these measures in the next cycle to boost growth and jobs. The full CLP is presented in a separate Communication.

It is important at Community level to close the remaining gaps in the single market, particularly in services, so that the full benefits of national reforms can be reaped. The Commission has recently presented its vision for a single market for the 21st century[6]. Some of the proposed measures will be taken forward through the CLP. They aim to empower consumers and small businesses and improve the implementation and enforcement of single market rules, for instance through "single market centres" at national level and regular monitoring of price developments for consumer goods. Enforcing consumer legislation will help consumers exercise choice of producers, thereby promoting competitiveness.

3.4. Shaping the external agenda

Whilst the EU needs to protect its citizens, its interests and its values, protectionism cannot be the solution. As the world's leading trader and investor, its openness allows lower cost inputs for industry, lower prices and a wider choice for consumers, a competitive stimulus for business, and new investment.

Globalisation is the context within which the Lisbon strategy operates and this must be built more effectively into its delivery. This can be done in a number of ways:

– the EU should use all its instruments to ensure that its openness is maintained and matched by increased access to third country markets for its companies:

  Multilateral negotiations, in particular, the successful conclusion of the Doha Trade Round, and on-going bilateral trade deals must be used to open new market opportunities and remove tariff and other barriers to trade[7]. They should also be used to promote a rule-based approach supporting high standards of social and environmental protection. In addition, the Commission will report annually on market access, identifying countries and sectors where significant barriers remain. This should normally give rise to consultations with the countries concerned. If problems remain, the use of Community trade instruments and/or action in the WTO should be considered. Particular attention will be paid to improving access to procurement markets and enforcement of intellectual property rights, fair competition, as well as to market access for SMEs.

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6 "A Single Market for 21st Century Europe" - COM(2007) 724.

7 "Global Europe: Competing in the world – a contribution to the EU's growth and jobs strategy" - COM(2006) 567.

– the EU should upgrade its strategic dialogues with key third countries to develop mutually beneficial solutions, promote higher standards and greater regulatory convergence:

  Thanks to its experience with the single market, the EU can contribute specific expertise (e.g. on market integration, social protection, employment and workers' rights, health care, environmental protection, competition rules, customs) which could be beneficial to its key partners, whilst discussions could also lead to solutions in areas where the EU has strategic interests (e.g. market access, energy, climate change, managing migration, decent work, technological standards and IPR, SME policy). New approaches, taking account of the specificities of each partner, should be developed, such as the recently launched Transatlantic Economic Council. Particular attention should be paid to the neighbourhood of the Union.

3.5. Integrating national, Community and international action into an effective policy response

The 2006 Spring European Council agreed four priority areas as the pillars of the renewed Strategy (knowledge and innovation, unlocking business potential, investing in people and modernising labour markets, energy/climate change). These areas are inter-related; if pursued in parallel, they constitute an integrated policy approach.

In each of these four areas, the 2006 Spring European Council also endorsed a limited number of specific, concrete actions for delivery by the end of the first cycle. The success rate in implementing these actions is good. For example, it is now possible in all but a few Member States to start up a business within one week by means of a one-stop shop. Agreement has been reached on a common set of flexicurity principles. The reduction of administrative burdens was given a strong impetus following the decision of the European Council to set a 25% target. These examples show that the renewed Lisbon Strategy can be used to deliver direct and tangible benefits to business and citizens. All this constitutes a solid platform from which the European Council can provide a further impulse to the implementation of the Strategy by agreeing on a limited set of further actions for delivery by 2010.

The renewed Strategy is built on a partnership approach, which recognises that, to address the common challenges, each level needs to play its full part. The priority areas are a way of bringing the different levels together. Where the actions have to be implemented by Member States, they should find their way into the NRPs; where they require Community-level action, they should be pursued through the CLP. Moreover, many of them can only be realised if they are backed up by a pro-active external policy designed to help the EU shape globalisation and benefit from the opportunities it offers.

4. ACTIONS IN THE FOUR PRIORITY AREAS

4.1. Investing in people and modernising labour markets

'Flexicurity' strikes a balance between flexibility and security on the labour market. It aims at ensuring that all citizens can enjoy a high level of employment security i.e. that they can easily find a good job at every stage of their active life. It helps employees and employers alike to seize the opportunities globalisation offers. After the agreement reached between the social partners, the European Council is invited to endorse the Commission's proposal for

common principles on 'flexicurity'[8]. Member States should now implement them, tailoring them to their own specific situations.

Reinforced efforts to fight poverty and social exclusion and integrate people at the margins, in particular through active inclusion policies, are crucial. Reducing poverty is at the heart of the renewed Lisbon Strategy through its emphasis on growth and jobs and implementing measures which invest in people's capacities, provide equal opportunities, adequate social protection and the provision of good quality jobs. Support for low-skilled workers, migrants and disabled people needs to be reinforced, notably by fostering skills development.

Investing more in education and skills throughout people's lives is not only critical to Europe's success in the age of globalisation, it is also one of the most effective ways to fight inequality and poverty. At a very early age, children develop the ability to acquire knowledge during the rest of their lives. Later on in primary and secondary education, reading skills becomes a pre-requisite for advancement. However, one out of every five 15-year olds in Europe cannot read sufficiently. One out of every six 18 to 24-year olds has dropped out of school with no more than lower secondary education. This makes it very difficult for them to enter and progress in the labour market. Many end up as long-term unemployed. Europe has not made any substantial progress in meeting its targets in this area. A determined effort must be made to raise the basic skills of young people and to drastically reduce early school leaving. What is needed is to concentrate resources over a period of years in order to make a step change.

Learning abroad can be an important stimulus for personal development and language skills. The Erasmus programme has enabled almost two million young Europeans to study abroad. More young people should be able to benefit from it so that, in time, it becomes a standard part of university education.

Ensuring that qualifications learnt on the jobs are recognised across Europe will greatly increase the incentives for people to go on acquiring new skills throughout their working lives. The recently agreed European qualifications framework will help to achieve this, provided Member States move rapidly to relate their national qualification systems and frameworks to it.

Skills development and life-long learning support 'flexicurity' policies by enhancing flexibility, employment security and mobility between jobs. Stronger and more focused vocational training policies must be developed to respond to the challenge of active ageing and contribute to raising productivity and employability. The European Social Fund can contribute significantly to such an effort.

More should be done to forecast and monitor future skills needs and, with pressing labour and skills shortages in an increasing number of sectors, Europe will need to improve regional and national labour mobility, as well as define a regulated immigration policy. Such a policy must be accompanied by measures to improve the economic and social integration of immigrants.

Accompanying the single market review, the Commission has set out its vision for an agenda of access, opportunity and solidarity and launched a public consultation to seek views on these crucial issues. This will feed into a renewed Social Agenda to be adopted by mid-2008.

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[8] "Towards common principles of flexicurity – more and better jobs through flexibility and security" - COM(2007) 359.

*To **invest more in people** through a **life-cycle approach in employment and education**, to **modernise labour markets** and to reinforce **social inclusion**:*

Community action:

*- the Commission will propose a renewed **Social Agenda** by mid-2008 based on opportunities, access and solidarity, taking account of Europe's new social realities and covering notably issues such as youth, education, migration and demography;*

*- the Commission will make proposals to address the skills gap by improving the forecasting and monitoring of **future skills requirements** in Europe;*

*- the Commission will make proposals for a common policy on **immigration** in 2008.*

Member States should:

*- implement the agreed common principles on **'flexicurity'** by defining national pathways within their NRPs by end 2008;*

*- increase the availability and affordability of quality **childcare** in line with national and Community targets;*

*- draw up action plans and set targets to substantially reduce **early-school leaving** and improve basic **reading skills**;*

*- link up national and regional programmes to the **Erasmus programme** to increase the number of students participating in international exchanges;*

*- by 2010, draw up national **qualification frameworks** aligned with the European framework.*

4.2. Unlocking the business potential, especially of SMEs

The business environment in Europe has been improved as a result of Member States implementing the 2006 Spring European Council decisions to introduce one-stop shops and reduce the time to set up a business to one week or less. The EU now needs to go further and agree an integrated policy approach which tackles obstacles at all stages of SME development and which enables more of its small businesses to grow into bigger companies that compete successfully in the global market place. This approach could be encapsulated in a Small Businesses Act, setting out both principles and concrete measures to support SMEs throughout their life-cycle.

A clear priority for the Union is to close the important gaps in the single market, particularly in services, so that the full benefits of national reforms can be reaped. The complete and timely implementation of the services directive will not only create a genuine single market for services but also offer a major opportunity to streamline procedures, remove red tape, facilitate market access and accelerate the introduction of interoperable e-government applications.

Europe's better regulation agenda is starting to produce results and administrative burdens should be reduced by 25% at EU level. Member States have committed themselves to equally ambitious targets at national level. An important part of improving the business environment for SMEs, and an underestimated source of innovation, is the modernisation of public

administrations, notably as regards their uptake of interoperable ICTs. As part of the better regulation agenda, many administrations are already responding to growing expectations; treating businesses and citizens as customers, using new technologies, promoting social innovation and making organisational changes to provide a transparent, predictable service and effective means of redress. The Commission will promote the exchange of good examples.

Unlocking business potential:

Community action:

*- adopt a **European Small Business Act** setting out an **integrated policy approach** to unlock the growth potential at every stage of the life-cycle of **SMEs**;*

*- move towards the target to reduce EU **administrative burdens** by 25% by 2012 and implement an ambitious **simplification programme**;*

*- strengthen the **single market**, increase **competition in services** and take further steps to integrate financial services markets.*

Member States action should:

*- undertake sustained and consistent efforts to implement the **services directive** by end 2009; complete the screening and assessment of national legislation before end 2008 and, in parallel, set up single contact points and electronic procedures and introduce an effective system of administrative cooperation across borders;*

*- set and announce national **administrative burden reduction** targets before the 2008 Spring European Council;*

*- make full use of the opportunities offered by the implementation of the services directive and the better regulation agenda to continue **modernising public administrations**.*

4.3. Investing in knowledge and innovation

Following decisions by the 2006 Spring European Council, Member States have set targets and taken steps to increase investments in research and development. The European Research Council and several Joint Technology Initiatives are being launched, based on Commission proposals. The European Institute for Innovation and Technology (EIT) is expected to start work in 2009. Under the new cohesion policy programmes, more than € 85 bn will be made available for investments in knowledge and innovation.

These are good first steps, but much more is needed to achieve Europe's ambitions. Member States should take additional measures to meet their R&D investment targets for 2010. This is particularly urgent as the EU's R&D ratio fell back slightly in 2006, as growth in R&D investment did not keep up with stronger GDP growth.

With globalisation, R&D is increasingly outsourced to other parts of the world. In Europe, the costs of protecting and enforcing innovations remain too high. Licences for distributing content are still nationally-based. The procedures for setting interoperable standards are far too slow. Spectrum is still managed in a fragmented way putting a brake on the development of new high-tech products and cross-border services. Too many barriers, including legal ones,

prevent universities, research institutes, companies and researchers from working together. This also holds back one of Europe's traditional strengths: the creativity and inventiveness of its people.

To reverse this trend Europe needs a "fifth freedom" – the freedom of knowledge – completing the four freedoms of movement of goods, services, people and capital. This "fifth freedom" should spur the EU's transition to an innovative, creative knowledge economy:

– one dimension is a genuine European research area where not only the framework conditions are in place to stimulate and reward innovation, but where the EU and national R&D programmes complement each other; where resources are allocated competitively geared towards excellence, where it is easy for universities and businesses to co-operate, where degrees are fully recognised and students, academics, researchers and skill workers can move around freely and cooperate easily with the worldwide scientific community;

– Europe must also pool its resources for a new generation of large-scale facilities for future laboratories and instruments which are indispensable for staying at the forefront of frontier research over the next decades. A common agenda identifying the priority research facilities ranging from lasers, telescopes and marine exploration to databases for cancer research has been agreed. As the resources needed to launch them exceed the capacity of any individual Member State, national decisions need to be taken now on how to join forces;

– information and communication technologies, driven by high-speed internet are key to raising productivity and stimulating innovation in Europe. Too many small businesses and citizens are not yet connected to high-speed internet which hampers their development and their innovation potential. Alongside increasing competition in telecoms markets, national plans are needed to ensure that, by 2010, 30% of Europe's population uses high-speed internet.

Making the "fifth freedom", the free movement of knowledge, a reality:

Community action:

*- improve the key **framework conditions** for innovation through an integrated patent jurisdiction and a single affordable patent; streamline the currently fragmented IPR rules, particularly to facilitate the circulation of content; accelerate the setting of interoperable standards and move towards more common spectrum management ; and improve access to venture capital;*

*- remove obstacles to the cross-border **mobility of researchers** based on a European "passport";*

***- pool EU and Member States' R&D resources to ensure their more effective use**, by agreeing by end 2008 areas for joint programmes and launching common calls for projects by end 2010;*

*- launch a **new generation of world-class research facilities** by drawing up by end 2009 roadmaps for the launch of the 35 commonly agreed projects[9]. For those projects of a global scale, launch a dialogue with interested international partners during 2008;*

*- improve competition for **high-speed internet** by adopting the telecoms review by May 2009.*

Member States should:

*- better co-ordinate efforts to improve framework conditions for **innovation**;*

*- indicate how national **R&D investment targets** for 2010 will be met and how their R&D strategies will contribute to realising a European research area;*

*- remove obstacles to the **mobility of researchers** between public and private research centres;*

*- draw up, by end 2008, national strategies identifying the **new generation of world-class research facilities** in which they will participate;*

*- as part of their NRPs, set national targets for **high-speed internet** usage[10] aiming at a 30% penetration rate of the EU population and connection of all schools by 2010.*

4.4. Energy and climate change

The 2007 Spring European Council committed itself to transform Europe into a low carbon economy with secure, sustainable and competitive energy. It agreed ambitious targets to cut greenhouse gas emissions, increase energy efficiency and boost the use of renewable energy by 2020. The challenge during the next cycle will be to put the framework and instruments in place to deliver these targets and to work with the rest of the world to agree similarly ambitious action within the UN framework.

The whole economy will need to gear up to reach such far-reaching goals. Market-based instruments, such as the emissions trading scheme (ETS), provide incentives to economic actors to reduce their emissions in the most cost effective way. A strengthened ETS should be complemented by action to realise legally-binding national targets on greenhouse gases and renewables: this will involve a mix of targeted regulation, effective use of economic instruments, such as subsidies, tax incentives or procurement, as well as steps to increase transparency, such as labelling or green accounting. The earliest gains can be made in the area of energy efficiency where governments can play a pioneering role. All of these efforts will need to be accompanied by sustained investment in research and development and active take up of new technologies, as outlined recently in the Commission's proposal for a Strategic Energy Technology Plan[11].

A more competitive and integrated internal energy market will make a major contribution to achieving secure, sustainable and competitive energy for the Union. This involves new

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9 European Strategy Forum for Research Infrastructures (ESFRI), European Roadmap for Research Infrastructures, Report 2006 + Conclusions of the Council on 21-22.5.2007.

10 The Commission will monitor the development of the EU internet economy through a broadband performance index to be launched in 2008.

11 "Towards a European Strategic Energy Technology Plan" - COM(2006) 847.

investments to improve infrastructures and interconnections, better stocks management, solidarity mechanisms and a more diversified energy mix. At the same time, all policies will need to adapt to the impact of climate change. Whilst climate change can be contained at acceptable levels with decisive global action, it cannot be prevented. Policies need to factor in this reality and minimise the social, environmental and economic impacts, while developing the potential of new technologies to enhance the competitiveness of EU industry.

Transform Europe into a low carbon and energy-efficient economy:

Community action:

*- adopt legislative proposals to complete the **internal electricity and gas markets** and the **climate change package** in order to put in place the framework to achieve at least a 20% reduction in greenhouse gas emissions and reach a renewables energy share of 20% by 2020;*

*- promote an industrial policy geared towards **more sustainable production and consumption**, focusing on renewable energies and low-carbon and resource-efficient products, services and technologies;*

***- review the energy tax directive** to link it more closely to the EU's energy and environmental objectives;*

*- strengthen the requirements in the **energy performance of buildings** directive.*

Member States should:

*- **review** their **economic instruments**, including taxation, subsidies and charging, to ensure that they contribute to the fight against climate in a cost-effective way;*

*- urge contracting authorities to systematically include **energy efficiency** as one of the award criteria for public procurement;*

- set mandatory energy reduction targets for government buildings;

*- improve **inter-connection of energy grids**.*

5. FOLLOW-UP AFTER THE 2008 SPRING EUROPEAN COUNCIL

The renewed Lisbon Strategy for growth and jobs is already delivering results. Europe now has a common integrated agenda, a set of instruments to work in partnership on common challenges as well as an effective yearly monitoring of progress by the Spring European Council.

Everything is in place for the 2008 Spring European Council to **launch an ambitious next cycle**, by:

- adopting the actions within the four priority areas as set out in Section 4;
- re-affirming the integrated guidelines for the next three years;

- endorsing the Commission's proposals for country-specific recommendations and 'points to watch';

- calling on Member States to implement the remaining reforms in their National Reform Programmes and ensure that they have up-to-date NRPs for the new cycle; invite Member States as part of their annual implementation reports to present to Council and Commission concrete action plans setting out their specific policy responses and time-tables to implement the country-specific recommendations and 'points to watch';

- endorsing the new Community Lisbon programme;

- calling on Member States to work with national and regional parliaments with a view to organising annual debates on the implementation of their NRPs and country-specific recommendations;

- calling on Member States to ensure that cohesion funds are used in accordance with the earmarking provisions so that they produce maximum impacts on growth and jobs;

- encouraging the Lisbon National Co-ordinators to continue to exchange experiences on reform, in particular in the four priority areas and on strengthening stakeholder involvement;

- calling on the European Parliament to play an active role throughout the next cycle, including through its dialogue with national parliaments.

COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 11.12.2007
COM(2007) 803 final
PART II

COMMUNICATION FROM THE COMMISSION TO THE SPRING EUROPEAN COUNCIL

Strategic report on the renewed Lisbon strategy for growth and jobs: launching the new cycle (2008-2010)

Keeping up the pace of change

Assessment of the National Reform Programmes

Statistical Annex to the Country Fiches – explanatory notes

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

The full database of Structural indicators, including data and metadata relating to the EU Member States, the Acceding and Candidate countries, USA, Japan and EFTA countries, is publicly available on the Eurostat Structural indicators website: http://ec.europa.eu/eurostat/structuralindicators. For each EU Member State, all 14 indicators are presented in one table and two charts.

The 14 short-listed indicators

GDP per capita in PPS	Gross Domestic Product (GDP) in Purchasing Power Standards (PPS) (EU-27 = 100)
Labour productivity per person employed	GDP in Purchasing Power Standards (PPS) per person employed relative to EU-27 (EU-27 = 100)
Employment rate*	Employed persons aged 15-64 as a share of the total population of the same age group
Employment rate of older workers*	Employed persons aged 55-64 as a share of the total population of the same age group
Gross domestic expenditure on R&D (GERD)	Gross domestic expenditure on R&D as a percentage of GDP
Youth education attainment level*	Percentage of the population aged 20 to 24 having completed at least upper secondary education
Comparative price levels	Comparative price levels of final consumption by private households including indirect taxes (EU-27 = 100)
Business investment	Gross fixed capital formation by the private sector as a percentage of GDP
At-risk-of-poverty rate after social transfers*	Share of persons with a disposable income below the risk-of-poverty threshold, which is set at 60% of the national median disposable income
Dispersion of regional employment rates*	Coefficient of variation of employment rates across regions (NUTS 2 level) within countries

Long-term unemployment rate*	Long-term unemployed (12 months and more) as a percentage of the total active population
Total greenhouse gas emissions	Index of greenhouse gas emissions and targets according to Kyoto Protocol / EU Council Decision for 2008-2012 (Actual base year = 100)
Energy intensity of the economy	Gross inland consumption of energy divided by GDP (at constant prices, 1995 = 100), measured in kilogram of oil equivalent per 1 000 Euro
Volume of freight transport relative to GDP	Index of inland freight transport volume relative to GDP, measured in tonne-km / GDP (at constant prices, 1995 = 100)

* Indicators disaggregated by gender

The table

The country-specific table presents data from 2000, 2003-2006 for that country and the EU-27 average. The following flags are used in the data tables:

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

The charts

The 14 indicators are presented in two charts which compare the actual value with the EU-27 value[1], illustrating in which areas a particular Member State is performing better or worse than the European average.

The "At risk of poverty" indicator measures relative poverty in a particular country and the EU-27 average is computed as a population-weighted average of individual national values. A comparison of national values with the EU-27 average can therefore be difficult to interpret, and may give a different result than if risk-of-poverty rates were computed based on a common reference threshold. During the transition to data production under the new EU-SILC regulation by all Member States with effect from 2005, indicators were drawn from national sources which were not fully harmonised. The indicators are computed using an income definition which until 2007 excludes imputed rent revenues and mortgage interest payments.

[1] Values in the chart = Current national value / Current EU-27 value * 100.

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

- First chart; those indicators for which increasing values indicate a positive trend, i.e. where a value of the indicator above 100 when compared to EU-27 is a relatively good performance;

- Second chart; those indicators for which decreasing values indicate a positive trend, i.e. where a value of the indicator below 100 when compared to EU-27 is a relatively good performance.

The charts also display the two central EU targets of reaching 3% of expenditure on Research and Development and an overall employment rate of 70% by 2010. In the same way as the indicators are compared to the EU-value, the targets have been converted to a ratio which compares the EU target to the real EU-27 value in 2006 (or latest year available).

Data sources

All indicators were extracted from the Eurostat database on 19 November 2007. The source of the information is Eurostat in all cases except for Greenhouse gas emissions (European Environment Agency and European Topic Centre on Air Climate Change) and Gross Domestic expenditure on R&D (Eurostat and OECD).

The European Council has invited Member States to set up national targets on the employment rate and on the gross domestic expenditures on R&D as a share of GDP. The national targets presented are those that respond to this invitation and have been extracted from the respective National Reform Programs.

Explanation of abbreviations

EU-27: European Union (27 countries)

Euro Area: Euro Area (13 countries for all years)

Belgium

1. Economic growth in Belgium reached 2.8% in 2006 and should remain broadly the same in 2007. The unemployment rate is forecast to decline from 8.2% in 2006 to around 7.5% in 2007, slightly above the euro area average. The 2006 employment rate was 61%. It is expected to rise in 2007, but remains well below the EU average, especially for older people. Labour productivity is among the highest in the EU and expected to grow in line with the euro area average. After a government budget surplus of 0.4% of GDP in 2006, the budgetary outturn for 2007 is likely to be a small deficit. The debt-to-GDP ratio remains on a downward trend.

2. Economic policy focuses on controlling labour costs, creating a more dynamic labour market and stimulating innovation. To preserve competitiveness, wage negotiations are based on a bi-annual national indicative wage norm agreed by the social partners, the most recent covers 2007-2008 and takes into account developments in Germany, France and the Netherlands. Measures to further reduce the tax burden on labour need to be reconciled with budgetary targets necessary to reduce the still high debt level and prepare for the cost of an ageing population. Policies to increase employment combined with efforts to curtail public expenditure could enhance medium-term growth and improve the long-term sustainability of public finances. Economic growth could be fostered by removing barriers to competition in services markets (including some network industries) and implementing reforms to boost innovation.

PART I: GENERAL ASSESSMENT

3. Overall, the Belgian Implementation Report shows good progress on implementing the 2005 National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have decreased over the last year, due to the fact that the current federal government is a caretaker government since elections in June 2007. The continuation of such a situation is likely to delay the implementation of further necessary budgetary measures and thereby also jeopardise targets for 2008.

4. Overall, there has been some progress on responding to the two country specific recommendations adopted by the Council. Belgium has made some efforts to further reduce the tax burden on labour, although it remains high above the EU average. Some measures were also taken to reduce regional unemployment and employment disparities, but not through a comprehensive economic strategy and the disparities are increasing.

5. With regard to the other areas on which the Council concluded Belgium should focus, there has been some progress over the 2005-2007 period, but the pace slowed in 2007. There has been most progress on policies to reduce emissions.

6. Last year's Commission Annual Progress Report concluded that Belgium had launched a series of measures to respond to the commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been some progress on most of the

commitments with a deadline of end 2007, but limited development in the flexicurity domain.

7. The Implementation Report specifically addresses the recommendations issued to the euro area countries. Belgium has made some progress on competition in services, although legislative action is still required in professional services. Progress is limited in the fields of the quality of public finance, employment protection, labour mobility and the development of a coherent flexicurity strategy. The budgetary balance is considerably better than the euro area average.

8. Consultation and efforts to develop ownership of the NRP by central and regional governments and the social partners continue. The Belgian federal government involves regional authorities in drafting the report. Social partners are extensively consulted and provide advice on policy areas, on some implementing measures and on the reporting process. Governance of the implementation of the NRP is strongly linked to structural funds programmes. EU Structural funds are being directed satisfactorily towards improving access to employment and promoting innovation and entrepreneurship.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. Belgium kept its budget balanced from 2000 until 2004. It planned to do so in 2005, but an exceptional and one-off assumption of debt from the railway company SNCB left a deficit of 2.3% of GDP. The 2006 government budget surplus of 0.4% of GDP exceeded the NRP's balanced-budget objective, but included revenue-raising one-off measures worth about 0.8% of GDP. For 2007, a budget surplus of 0.3% of GDP was planned, but the actual turnout is projected to be a small deficit as many one-off measures, initially budgeted at 0.5% of GDP, will not be executed by the caretaker government. Assuming no policy changes, the projected deficit would increase slightly to 0.4% of GDP in 2008-2009. The current federal government as a caretaker government is not in a position to contain an increase in the public deficit. The debt-to-GDP ratio continues to decline and should reach 84.6% of GDP in 2007 from 94.2% at end-2004.

10. The Council recommended Belgium to undertake further efforts while continuing fiscal improvement, to reduce the tax burden on labour towards the average of its neighbouring countries, especially by reducing the tax wedge on low-skilled workers. Following the income tax reform decided in 2001 and fully implemented in 2006, a further easing of fiscal pressure on earned incomes will follow, notably from a lump-sum reduction in income tax in the Flemish region, the upward revision of the fixed deductible amount for professional spending, and further tax reductions on high-skilled workers, shift work, night work and overtime work. However, the tax burden on labour remains above the EU average. Moreover, the measures seem insufficient to give low-skilled workers more incentives to take up work or to substantially improve the employment rate of older workers.

11. The Council also referred to the need to focus on the long-term sustainability of public finances. Belgium had already taken a number of relevant measures in the

past, including the Silver Fund and the Generation Pact. In 2007, Belgium established a "Fund for the future of the health system" to offset the medical costs of an ageing population. These measures are only a first response to the major budgetary challenge that ageing poses in Belgium, especially given the low effective retirement age. Responding to this challenge crucially hinges on maintaining high primary surpluses and strict control of government primary expenditure growth. The expected cost of age related expenditure has been upwardly revised from 3.5% to 4.4% of GDP between 2006 and 2030. Combined with expected budgetary deterioration in 2007, additional structural budgetary measures may therefore be needed. These should be complemented by growth and productivity enhancing reform measures encompassing the welfare system and product and labour markets.

12. Between 2005 and 2007, Belgium has achieved some progress in addressing the macro-economic challenges set out in its NRP. The country-specific recommendations and points to watch have to some extent been addressed but require further efforts, and they therefore remain valid.

Micro-economic policies

13. Belgium introduced some new measures in 2007 and continued implementing previously taken initiatives to address the its micro-economic challenges. An R&D forum brought together all levels of governance and the private sector to pinpoint Belgium's R&D weaknesses and make recommendations to stop recent declines in investment. Existing initiatives such as fiscal incentives for R&D have been strengthened and public spending on R&D has increased. However, public R&D investment remains well below the EU average.

14. ICT measures continue to be implemented and the federal regulator should now progress with the analysis of the broadband market. The transposition deficit of EU legislation, including the EU Financial Services Action Plan measures, has improved significantly. However, three important directives are still only partially transposed and the public procurement package not yet at all. Work is on-going to reduce the time to start up a business from 26 days to 3 days. Simplification efforts have continued and the institutional set up for better regulation has further improved but no target for reducing administrative burden has been set. Round Table proposals on upgrading legislation could lead to more competition, especially in professional services where legislative action is still required. Competition authorities should enforce competition more actively, particularly in network industries.

15. The Council referred to the need to focus on improving competition in gas and electricity markets and on identifying further emission reduction measures. The measures taken by the federal government and the regions are insufficient, particularly to neutralise the incumbents' market power. The spot market for electricity has been extended, but to be effective, further interconnection capacity is required to remove congestion at the border. Liberalisation of the residential users market in 2007 has been only a partial success, with particularly slow progress in Brussels. The incumbents' presence in transmission and distribution network operators is still high. In Wallonia the incumbent exercises control over nearly all distribution networks. A recent anti-trust decision referred to concerns related to the gas incumbents' anti-competitive behaviour. Measures to ensure independent, clearly mandated, and adequately staffed regulators must be reinforced to ensure effective

regulation of the transmission and distribution network operators and the incumbents. Market rules and their effect on market transparency need reviewing to facilitate new entry.

16. Belgium took appropriate additional emission reduction measures in 2007 and should reach its Kyoto commitments. Financial incentives have been introduced to achieve further energy efficiency and some emission rights will be bought abroad. However, more measures to achieve the renewable target for electricity are needed.

17. Belgium has succeeded in implementing a significant number of measures to deliver on the micro-economic key challenges outlined in the NRP. Good progress has been made on better regulation and the time required to start-up a company. A coherent R&D policy with better coordination across all levels of governance is needed to further increase the level and the impact of public R&D funding if Belgium's R&D is to reach the target of 3% of GDP. The point to watch on competition in the gas and electricity markets has not been addressed sufficiently, and significant challenges remain. The point to watch on reducing emissions represents a good policy response and is therefore no longer merited.

Employment policies

18. Since 2005, Belgium has taken important initiatives covering active ageing, the quality of education and the rights and obligations of people receiving unemployment insurance. However, the overall employment rate (61.0%) and the employment rates for women (54.0%) and older workers (32.0%) remain considerably below the EU goals and getting further from the EU average. Further attention is needed to promote labour market adaptability. Progress over 2005-2007 with regard to the implementation of policies to address Belgium's labour market challenges is therefore mixed.

19. The Council recommended that Belgium should take further measures aimed at reducing regional disparities in unemployment and employment. Regional authorities have reacted to some extent. Data transmission between different public employment services has been improved and job vacancies in the regions are now systematically exchanged. Regional public employment services are also reinforcing language training and the active follow-up of jobseekers. Nevertheless, regional disparities in unemployment and employment have further widened. A comprehensive strategy in accordance with the flexicurity approach should reinforce policy measures taken to improve labour market performance.

20. The Council also referred to the need to focus on increasing the employment rate for older workers and vulnerable groups. New measures improve the transition from school to work but a coherent youth strategy is still to be further developed. To promote active ageing Belgium is gradually implementing an important number of measures agreed in the 2005 Generation Pact. Steps have been taken to encourage adaptability in the labour market, including diversity plans, one-to-one coaching, and concentration of older workers and vulnerable groups in active labour market policies. Further reductions of the tax burden on low wages may improve the integration of outsiders. This is a necessary policy response to Belgium's challenges in this area.

21. Recent policy initiatives are inspired by the flexicurity approach, such as a rebalancing between social security and active labour market policies. Overall however, Belgium is not yet addressing flexicurity in a fully integrated way; measures to tackle segmentation remain at the conceptual stage. Although the NRP underlines the importance for Belgium of enhancing participation in lifelong learning to foster flexibility and security in the labour market, opportunities for lifelong learning should be improved, particularly in-company training.

22. Between 2005 and 2007, Belgium has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. Some progress has been made to address the country specific recommendation on regional disparities. A first important package of measures have been taken towards increasing the employment rate of older workers and vulnerable groups, but this needs to be monitored to check whether further measures are required. Belgium requires a comprehensive labour market strategy to improve the performance of the labour market across the territory and the Commission therefore considers a recommendation merited in this area.

PART III: CONCLUSIONS

23. In the light of Belgium's 2007 Implementation Report and the Commission's assessment of progress made to implement key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

24. Belgium has made good progress in implementing its National Reform Programme over the 2005-2007 period. Belgium has shown some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

25. The Implementation Report shows some policy response to the Council recommendations, but further reform is still necessary. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

26. Among the strengths shown by the Belgium's 2007 Implementation Report are the emission reduction policies and the promising results of the guidance and monitoring system of unemployed people.

27. The policy areas in the Belgian National Reform Programme where challenges need to be tackled with the highest priority are reducing the tax burden on labour whilst strengthening fiscal consolidation and improving labour market performance. Against this background it is recommended that Belgium:

- continues efforts to further reduce the tax burden on labour towards the average of its neighbouring countries, especially by reducing the tax wedge on low skilled workers, while strengthening fiscal consolidation;

- reinforces the policy measures to improve the performance of its labour market through a comprehensive strategy, in accordance with an integrated flexicurity approach, to enhance labour market participation, lower regional disparities, and increase participation in lifelong learning.

28. In addition, it will be important for Belgium to focus on the following challenges: to fully implement the strategy aiming to ensure the long term sustainability of public finances, including expenditure restraints, fiscal surpluses, and a persistent reduction of government debt; urgently take further measures to improve competition in gas and electricity markets, including through independent and effective regulators and additional measures concerning transmission and distribution operators; to increase substantially its commitment to stimulating R&D and innovation notably by increasing both the level and impact of public funding and developing a coordinated policy mix at all levels; continuing the implementation of the measures to increase the employment rate for older workers and vulnerable groups, monitor their impact and, if need be, take further activation measures.

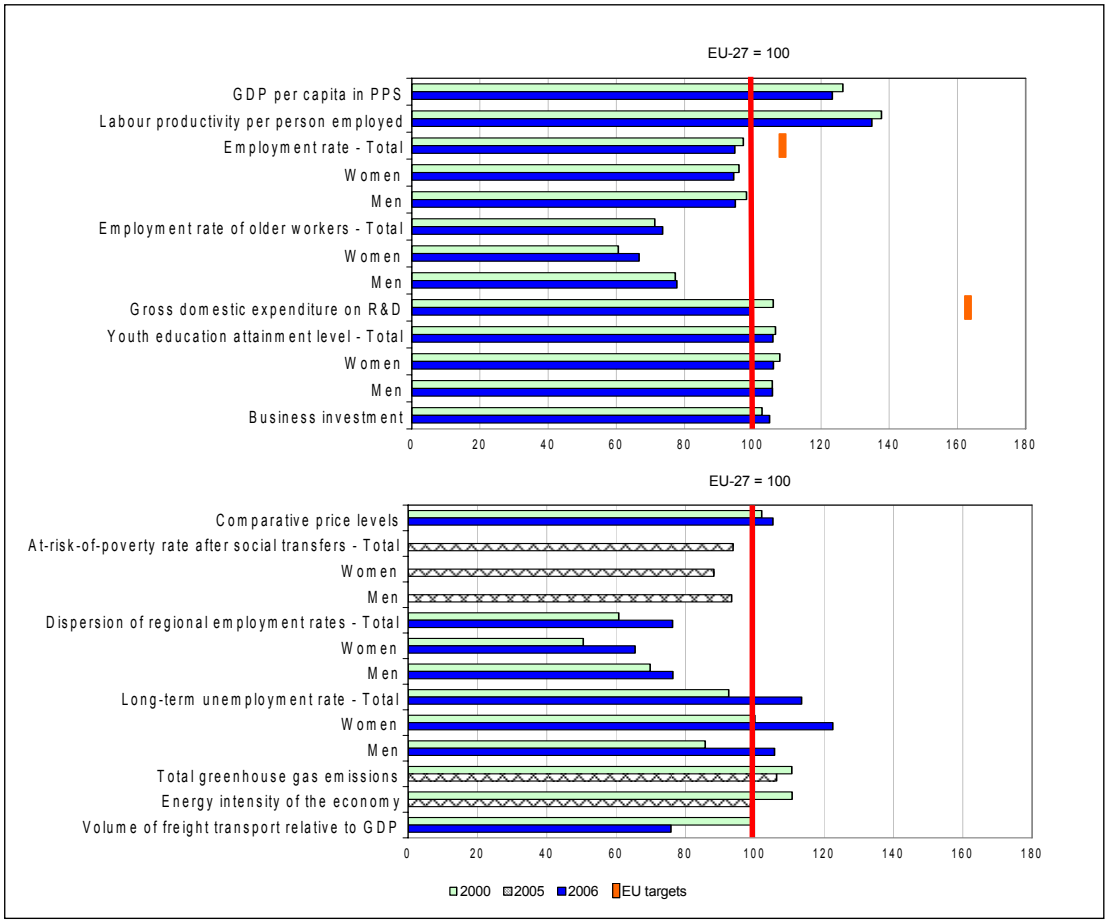
PART IV: STATISTICAL GRAPHS AND DATA

BELGIUM

		BE						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		126.4	123.5	124.5	124.4	123.3		100.0	100.0	100.0	
Labour productivity per person employed		137.7	134.4	135.6	135.2	134.9		100.0	100.0	100.0	
Employment rate	Total	60.5	59.6	60.3	61.1	61.0	70.0*	62.2	63.4p	64.4p	70.0
	Women	51.5	51.8	52.6	53.8	54.0		53.7	56.2p	57.2p	
	Men	69.5	67.3	67.9	68.3	67.9		70.8	70.8p	71.6p	
Employment rate of older workers	Total	26.3	28.1	30.0	31.8	32.0		36.9	42.3p	43.5p	
	Women	16.6	18.7	21.1	22.1	23.2		27.4	33.5p	34.8p	
	Men	36.4	37.8	39.1	41.7	40.9		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.97	1.88	1.87	1.84	1.83	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	81.7	81.2	81.8	81.8	82.4		76.6	77.4	77.8	
	Women	85.6	84.6	84.8	85.3	85.6		79.3	80.1	80.7	
	Men	78.0	77.9	78.9	78.4	79.1		73.8	74.7	74.8	
Comparative price levels		102.0	106.5	105.7	105.1	105.2		100.0	100.0	100.0	
Business investment		18.9	17.1	18.0	18.6	19.1		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	13.0	15.0b	15.0	15.0	:		:	16.0e	:	
	Women	14.0	16.0b	16.0	15.0	:		:	17.0e	:	
	Men	12.0	14.0b	14.0	14.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	7.9	7.7	8.7	8.4	8.7		13.0	11.9	11.4	
	Women	10.1	9.1	10.7	10.5	10.6		20.0	16.8	16.2	
	Men	6.7	6.9	7.2	6.8	7.1		9.6	9.7	9.3	
Long-term unemployment rate	Total	3.7	3.7	4.1	4.4	4.2		4.0	4.1p	3.7p	
	Women	4.6	4.2	4.7	5.0	4.9		4.6	4.5p	4.0p	
	Men	3.0	3.3	3.7	3.8	3.7		3.5	3.8p	3.5p	
Total greenhouse gas emissions		100.4	100.8	100.5	97.9	:		90.7	92.1	:	
Energy intensity of the economy		236.1	217.4	207.4	205.7	:		213.1	208.1	:	
Volume of freight transport relative to GDP		98.0	95.0	89.3	83.7	80.9e		99.1e	105.4e	106.7e	

* National target: 70% as soon as possible

PERFORMANCE COMPARED TO EU-27



Bulgaria

1. Bulgaria's GDP growth rate has averaged around 4% over the last ten years, accelerating to above 6% per year since 2004. Accordingly, GDP per capita reached 37.1% of the EU average in 2006, but remains among the lowest in the EU. Although the employment rate increased from 49.7% in 2001 to 58.6% in 2006, it is still below the EU average. The unemployment rate fell to 9% in 2006, down from 19.5% in 2001, and is estimated to decline further to below 8% in 2007. Macro-economic imbalances have been increasing substantially in recent years, with widening external deficits and rising inflationary pressures. Moreover, the labour market has tightened since 2006, triggering an acceleration of wage growth to around 20% in the first three quarters of 2007, clearly outpacing productivity growth.

2. Bulgaria joined the EU on 1st January 2007. Its economy is at present performing strongly, but is showing signs of overheating with a high and growing external deficit, growing labour shortages, strong wage growth including in the public sector and rapid increases in credit growth which have fuelled inflationary pressures. The challenge for Bulgaria consists of further tackling these macro-economic vulnerabilities by maintaining a tight fiscal policy and speeding up structural reforms to strengthen its competitiveness. Improving administrative capacity is a prerequisite for a successful implementation of structural reforms.

PART I: GENERAL ASSESSMENT

3. Since the Bulgarian National Reform Programme (NRP) was submitted in March 2007, the Commission's assessment is mainly based on the quality of the policy response as well as on first steps taken towards its implementation. The NRP identifies five key challenges for the period 2007-2009: maintaining macro-economic stability; infrastructure; improving the business environment; improving the quality of human capital; and activating labour supply through using a flexicurity approach. Furthermore the NRP identifies improving administrative capacity as an overarching challenge.

4. The NRP identifies the right challenges. The NRP clearly prioritises and introduces the correct sequence for addressing the numerous challenges which the country faces. It is also rightly recognising that improving administrative capacity is an absolute prerequisite to achieve progress in other priority areas. The presentation of the NRP is operational. For each priority, based on a clear problem analysis, it briefly lays out the planned measures, the actions, the targets, the associated budgets, responsible services and timelines. The NRP is however weak in presenting concrete policy measures in some areas, in particular strengthening administrative capacity and cutting red tape. The implementation report does not provide sufficient additional information on concrete measures in those two areas.

5. In spite of some progress achieved so far, Bulgaria's economic and social development is still hampered by weak public administration. Corruption still affects the business environment and access to and quality of the public services. Significant

improvements on these aspects are urgently needed. In this context Bulgaria presented a report on the implementation of the Action Plan under the Strategy for Transparent Governance and for Prevention and Counteraction of Corruption. Progress in this area is monitored through the Commission's cooperation and verification mechanism.

6. Whereas legislation to reform the administration was adopted in 1998, the effects are not yet visible. The NRP and the Implementation report contain only measures either of a general or of a technical nature to improve administrative capacity. It does not address the need to develop a comprehensive human resources policy aimed in particular at tackling the high-turnover of senior staff, raising the independence of the civil service, increasing performance-based pay and career development schemes.

7. Furthermore, whereas the NRP rightly prioritises by focusing on only 5 policy areas that Bulgaria needs to tackle as a matter of urgency, this prioritisation is not reflected sufficiently in the planned measures to raise administrative capacity. This weakness could be remedied by recognising that the administrative capacity must first of all be improved in those departments (and regulatory authorities) that are in charge of elaborating and implementing policy measures in those 5 priority areas.

8. The NRP foresees several measures to meet the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. It foresees the establishment of one-stop shops for setting up a business but greater effort will need to be made to ensure adequate simplification. Several projects in the field of entrepreneurship education are on-going, but their scope is limited.

9. Political ownership of the NRP is strong, with the appointment of a national Lisbon coordinator at political level and the quarterly monitoring of progress by the Prime-Minister and the Council of Ministers. Consultation of stakeholders, parliament and the social partners has been substantial. Pursuing this dialogue with stakeholders during the implementation phase will be important. Taking a strongly integrated policy approach across government departments will be key to the successful implementation of the NRP. Meeting the NRP's ultimate aim - to catch up with the rest of the EU by growing robustly and increasing the employment rate – will depend on maintaining strong political commitment throughout its implementation phase.

10. Bulgaria is eligible for € 6.852 billion from the Structural Funds in the period 2007-2013. The links between the priorities in the NRP and the programmes under the Structural and Cohesion Funds are fairly strong. Bulgaria needs to stay focused on strategic priorities and realistic targets, with Structural Funds-assisted activities complementing and not replacing policy developments set out in the NRP. To ensure the efficient absorption and delivery of cohesion policy programmes, the administrative capacity must be further reinforced at national, regional and local level.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

11. Maintaining macro-economic stability in the context of the currency board arrangements through tight fiscal policy, preserving long-term sustainability of public finances, and further structural reform is rightly identified as a key challenge in Bulgaria's NRP. The NRP shows ambition with regard to the medium-term budgetary surpluses (in the order of 1.5%-2% of GDP), but could be more ambitious with regard to the acceleration of structural reforms.

12. The current account deficit rose to around 19% of GDP in the first half of 2007 due largely to buoyant growth of domestic demand and especially investments. This, combined with accelerated wage growth and increasing food and energy prices, contributed to annual inflation rising to over 10% in September 2007. Despite comparatively low employment rates, growing shortages and skills gaps in the labour market have implied a significant acceleration of wage growth. Although Bulgaria targets a budgetary surplus, given rising macro-economic imbalances and signs of overheating, Bulgaria faces risks regarding the sustainability of its growth path. Structural reforms must be accelerated in order to reinforce the economy's ability to adjust, whilst sticking to tight fiscal and income policies to contain domestic demand.

13. The Implementation Report confirms the commitment to high medium-term budgetary surpluses and to avoiding pro-cyclical fiscal easing. Fiscal policy has been tightened in recent years, with the fiscal surplus projected to reach 3% of GDP in 2007. Maintaining this tight fiscal stance is essential given the rising external deficit and inflation. With wage growth in the public sector accelerating during 2007 and a scheduled increase of minimum wages by over 20% in 2008, ensuring that public sector wage policy contributes to wage moderation will be crucial to control inflation and to preserve competitiveness. Moreover, improving the efficiency of public expenditures will also be important to strengthen potential growth. The presentation of the 2008 budget on a programme basis and the envisaged public expenditure reviews, notably in health care and education, are important positive steps in this respect.

14. Bulgaria faces a demographic challenge to its long-term financial sustainability. To limit the expected negative budgetary impact, the NRP acknowledges the need for continued pension and health reform. A special demographic reserve fund has been capitalised to underpin the first-pillar pension system, but the respective legislation is still to be adopted. Furthermore, pensions have been increased twice by 10% in 2007, contrary to existing legislative provisions on pension indexation. Refraining from such discretionary measures would be important to support long-term sustainability. After several delays, a draft national health strategy has been elaborated which provides for an increase in public health expenditure, but needs to be complemented with concrete measures aimed at improving efficiency.

15. In summary, maintaining tight fiscal and income policies while improving public expenditure efficiency and accelerating structural reforms to ease labour market

pressures, improve skills and to increase competitiveness of product and service markets will be crucial to contain external imbalances and inflationary pressures.

Micro-economic policies

16. The NRP identifies improving the business environment and modernising infrastructure as the micro-economic challenges. The Commission subscribes to these priorities. Improving the business environment, transport, telecommunications and energy infrastructure, and opening network markets and the services sector will require an integrated policy approach.

17. The NRP sets out some measures, but of a rather general nature, to improve the business environment, such as a better regulation agenda, the introduction of impact assessment for new laws, the introduction of a new electronic-based commercial register, introduction of single form schemes for payments at borders and one stop shops at all levels of administration. Although these measures are a clear step in the right direction, progress should be seen against the backdrop of continued overregulation, long delays in obtaining authorisations, time-consuming settlement of contractual and legal disputes and continued corruption. Besides implementing the better regulation agenda, further urgent structural measures are needed to reduce the number of authorisations and time for their delivery, introduce more transparency and recourse. These measures can assist the public administrations in delivering a better service to the citizen and businesses. Judicial procedures must equally be made more transparent. The introduction of single contact points and electronic-procedures and other obligations deriving from the implementation of the Services Directive must be seized as an opportunity to streamline procedures.

18. The NRP recognises the importance of R&D in the broader context of innovation, and lists a number of problems mainly relating to the limited involvement of the business sector in R&D activity. However, concrete measures are yet to be proposed to address the major problem of reforming the public research base, and Bulgaria has yet to set a target for R&D intensity. In order to ensure long-term productivity growth, it is vital to boost private R&D investment and reform public R&D to be both efficient and relevant to industrial needs. This should be achieved by increasing the share of competitive funding and focusing on few priorities. Better synergy between education and R&D policies is also needed.

19. The NRP and Implementation Report fully recognise the importance of ICT, in particular the development of e-government and broadband infrastructure to facilitate the move towards a knowledge-based society. The NRP sets out in general terms a range of initiatives, most of which will draw on Structural Funds investments, to improve transport, telecommunications, energy infrastructure and competitiveness but underestimates the administrative capacity constraints. Management structures for project implementation covering the whole project cycle, notably project feasibility assessment, project design, tendering and procurement strategies and project/works management must be further reinforced. Urgent measures must be taken to ensure the staffing, independence and proper functioning of regulatory authorities to increase competition in the network industries and in particular in the area of telecommunications, through the rapid and effective implementation of EU legislation.

20. Bulgaria would benefit from an integrated approach in the micro-economic domain. The effects of policies are unclear given the absence of such an approach. The proposed steps to cut red tape and consequently improve the business environment are insufficient to address the challenges.

Employment policies

21. Bulgaria is facing increased labour shortages as a result of fast growth, strong job creation, outward migration and insufficient skill levels in specific sectors. Nonetheless, employment rates remain low and structural unemployment relatively high so that there is, in principle, still a large source of untapped labour. Against this backdrop, activating the labour supply along with improving the adaptability of workers by improving access to and quality of education and training are rightly addressed as main priorities in the NRP.

22. Labour market policies currently focus on activating vulnerable groups and increasing literacy among low-skilled persons. Sustainable economic growth is at risk if further measures are not taken to put into place an integrated active labour market policy approach. So far, notwithstanding some initial measures, there has been limited progress to reform the design and scope of active labour market policies as employment programmes tend to create predominantly subsidised low-skilled jobs providing little opportunity to increase workers' employability through training. Further efforts are needed to assess, analyse and improve the effectiveness, efficiency and adequacy of active policies. More sustainable and integrated policies are necessary to encourage people to participate in the labour market and remain in employment through further opportunities for vocational training and through more far-reaching youth employment policies facilitating school-to-work transition, with special attention to Roma. Strengthening the capacity of labour market institutions to implement policies and adequately deliver employment services should also become a high priority area. The Implementation Report does not foresee further actions to address the need for strengthening the capacity of the Employment Agency and improve its effectiveness, including its role in unemployment prevention.

23. Bulgaria faces major challenges with respect to the financial efficiency and the quality of the education system. Further steps should be taken to reform education and training systems to ensure correspondence between skills supplied and labour market needs, including establishing a reliable labour market monitoring system. In order to tackle persistently high early school leaving, Bulgaria should take an integrated policy approach by focusing more on students at risk, either because of social or geographical background, in particular Roma. A comprehensive and coherent life-long learning strategy should be adopted and implemented to increase participation levels while encouraging employers to invest in training.

24. Recently adopted legislative amendments are first steps towards introducing a flexicurity approach in Bulgaria but an integrated approach must be further elaborated and involving social partners in all policy areas, particularly in life-long learning where their role has been weak. Making contractual arrangements more flexible and tackling the high level of undeclared work can further help increase labour supply. Some progress has been made in tackling undeclared work through compulsory registration of employment contracts and reduction of social insurance

contributions. However, more efforts are necessary to strengthen the administrative capacity of labour inspectorates and improve compliance.

25. Overall, Bulgaria has made some initial progress in the employment policy field. However, despite the current trend of falling unemployment, Bulgaria needs to take a more integrated and better-sequenced approach to increase activity and employment in the formal economy for all; ensure correspondence between skills and labour market needs; and raise the skills potential of the labour force.

PART III: CONCLUSIONS

26. In the light of Bulgaria's 2007 Implementation Report and the Commission's assessment of its National Reform Programme and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

27. Overall, the National Reform Programme focuses on the right challenges, but in some areas lacks concrete and substantial measures in particular as regards strengthening administrative capacity. Furthermore the National Reform Programme lacks measures aimed at urgently and significantly reducing red tape to make the business environment more dynamic and competitive. Given the growing economic imbalances it is particularly important for Bulgaria to accelerate the implementation of its National Reform Programme in order to create the necessary conditions for sustainable growth and jobs in the medium to longer term.

28. The National Reform Programme's strengths include a clear problem analysis and right prioritisation and sequencing of reforms as well as strong political ownership. Important provisions for a tight monitoring of progress at the highest political level have been put in place, which should prove an effective tool for ensuring a rapid and effective implementation of the National Reform Programme. The National Reform Programme is furthermore underpinned by a tight fiscal policy which offers a solid basis for accelerating the needed structural reforms to ensure long-term growth.

29. The policy areas in the Bulgarian National Reform Programme where challenges need to be tackled with the highest priority and budgetary impacts of measures and details on the monitoring and evaluation procedures should be clearly spelled out are: administrative capacity; macro-economic imbalances; red tape; and the functioning of the labour market. Against this background, Bulgaria is recommended to:

- urgently strengthen administrative capacity in particular focus on key government functions, including regulatory authorities, and the judiciary.

- contain the growing current account deficit and inflationary pressures, in particular by a tight fiscal policy, improving the quality of public expenditure and promoting wage moderation in order to keep wage developments in line with productivity gains;

- take rapid measures substantially to cut red tape and shorten procedural delays in order to improve the business environment (in particular for SMEs and facilitating start-ups), which will also help in the fight against corruption;

- increase the quality of labour supply and the employment rate by improving the efficiency and effectiveness of active labour market policies and further reform the education system to raise skills to levels that better match labour market needs and reduce early school leaving.

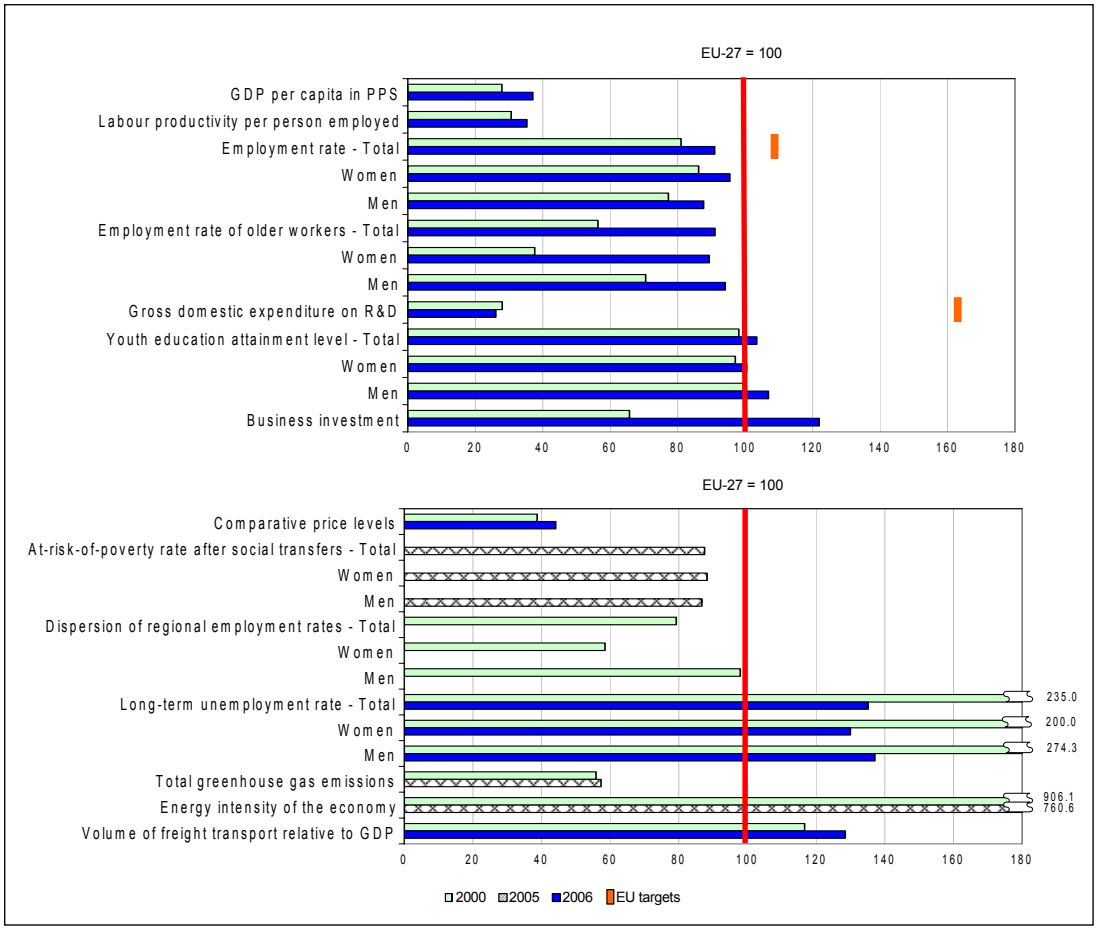
30. In addition, it will be important for Bulgaria over the period of the National Reform Programme to focus on: taking further measures to ensure the long-term sustainability of public finances, in particular with regard to potential risks in terms of adequacy and sustainability of pensions; creating all necessary pre-conditions for strong competition in network industries; elaborating an integrated policy for R&D and innovation notably aimed at reforming the public R&D system, shifting public support to R&D- based on an overall R&D intensity target for 2010- towards more competitive funding focused on key priorities; tackling undeclared work by strengthening institutional capacity to perform inspections and ensure legal enforcement; completing the lifelong learning strategy and increasing participation.

PART IV: STATISTICAL GRAPHS AND DATA

BULGARIA

		BG						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		27.9	32.6	33.6	35.2	37.1		100.0	100.0	100.0	
Labour productivity per person employed		30.6	33.4	33.5	34.1	35.3		100.0	100.0	100.0	
Employment rate	Total	50.4	52.5	54.2	55.8	58.6	61.0 (2009)	62.2	63.4p	64.4p	70.0
	Women	46.3	49.0	50.6	51.7	54.6		53.7	56.2p	57.2p	
	Men	54.7	56.0	57.9	60.0	62.8		70.8	70.8p	71.6p	
Employment rate of older workers	Total	20.8	30.0	32.5	34.7	39.6		36.9	42.3p	43.5p	
	Women	10.3	21.0	24.2	25.5	31.1		27.4	33.5p	34.8p	
	Men	33.2	40.5	42.2	45.5	49.5		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.52	0.50	0.50	0.49	0.48	:	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	75.2	76.3	76.1	76.5	80.5		76.6	77.4	77.8	
	Women	77.0	77.3	77.5	77.1	81.1		79.3	80.1	80.7	
	Men	73.4	75.4	74.9	75.9	80.0		73.8	74.7	74.8	
Comparative price levels		38.7	40.7	41.7	42.4	44.1		100.0	100.0	100.0	
Business investment		12.1	16.6	17.6	20.0	22.2		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	14.0	14.0	15.0	14.0	:		:	16.0e	:	
	Women	15.0	16.0	17.0	15.0	:		:	17.0e	:	
	Men	13.0	12.0	13.0	13.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	10.3	6.8	7.0	7.1	:		13.0	11.9	11.4	
	Women	11.7	8.8	8.9	8.0	:		20.0	16.8	16.2	
	Men	9.4	5.8	5.9	7.0	:		9.6	9.7	9.3	
Long-term unemployment rate	Total	9.4	8.9	7.2	6.0	5.0		4.0	4.1p	3.7p	
	Women	9.2	8.6	7.0	6.0	5.2		4.6	4.5p	4.0p	
	Men	9.6	9.2	7.3	6.1	4.8		3.5	3.8p	3.5p	
Total greenhouse gas emissions		50.7	52.7	52.2	52.8	:		90.7	92.1	:	
Energy intensity of the economy		1931.1	1769.2	1595.3	1582.4	:		213.1	208.1	:	
Volume of freight transport relative to GDP		115.6	127.1	138.4	147.9	137.1		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Czech Republic

1. The Czech Republic grew at an annual rate of 6.4% of GDP over 2005 and 2006. Growth in 2007 is expected to be almost 6%, and to remain close to its potential of 5% in 2008 and 2009. GDP per capita is currently 79% of the EU average. This strong economic growth, mainly driven by domestic demand, has positively affected the labour market with the employment rate projected to reach 68% in 2007. The unemployment rate decreased below 6% in 2007 and is projected to drop to 5% by 2009. However, although falling, the proportion of long-term unemployed remains high.

2. Further structural reform focused on labour market flexibility, increasing human capital, and active policy measures to tackle skill mismatches, are now important. High growth rates create a good environment for further fiscal consolidation and a reallocation of spending towards growth-enhancing activities. Whilst the level of government debt is relatively low, at about 30% of GDP, it is anticipated to rise steeply mainly due to the ageing population and the structure of the pension and healthcare systems, putting the long-term sustainability of public finances in the Czech Republic at high risk.

PART I: GENERAL ASSESSMENT

3. Overall, the Implementation Report shows some progress on implementing the National Reform Programme (NRP) over the 2005-2007 period, with a slight acceleration in 2007.

4. There has been some progress on the recommendations issued by the Council to the Czech Republic. Steps have been taken to improve the long-term sustainability of public finances by reforming the pension and healthcare systems. The recommendation on R&D has been partly addressed. Policy measures in the employment, and education and training areas represent important steps forward though continuing effort is now needed.

5. With regard to the other areas on which the Council concluded the Czech Republic should focus, progress has been mixed. Good progress has been achieved in developing a coherent approach towards improving the regulatory framework for enterprises. An active ageing strategy is being implemented, and regional disparities have slightly decreased, but more progress is needed. Although unemployment amongst disadvantaged groups decreased, the Czech Republic has to move forward significantly to support the better integration of disadvantaged groups into the labour market, reconciling work and family life, and in terms of reducing the high gender pay gap.

6. Last year's Commission Annual Progress Report concluded that the Czech Republic had made mixed progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been further mixed progress on most of the commitments with an end 2007 deadline.

7. Consultation and efforts to develop ownership of the NRP within government and with the social partners are quite good. The Office of the Vice-Prime Minister for European Affairs is responsible for the coordination, preparation and evaluation of the Implementation Report, supported by an inter-ministerial working group. Other stakeholders are consulted but more efforts are needed to support implementation at regional and local levels. The Implementation Report provides a clear overview and timetable. Links between the NRP implementation and the structural and cohesion funds are fairly strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The Czech Republic has made partial progress over the 2005-2007 period in addressing its macro-economic challenges. On fiscal consolidation, the budget deficit is likely to worsen to 3.4% of GDP in 2007, mainly due to increases in social spending (likely to cost over 1% of GDP) without compensating measures in other areas. A package of measures to improve fiscal stability in the medium term was introduced in September 2007. This Package includes expenditure cuts above the level of revenue reductions. On the revenue side, these include the introduction of a 15% flat tax rate on personal income from 2008, a gradual decrease in corporate income tax from 24% to 19% in 2010, an increase of the reduced VAT rate from 5% to 9%, and the introduction of new environmental taxes. The package shifts the tax burden from direct to indirect taxation. On the expenditure side, substantial cuts in mandatory spending aim at improving the flexibility of public expenditure toward growth enhancing public spending. Overall, the reform package and the 2008 budget approved by the government should reduce the deficit to 2.9% of GDP in 2008.

9. The Council recommended the Czech Republic to take steps to implement reforms of the pension and healthcare systems. A pension reform has been prepared, including an extension of the retirement age to 65 and the introduction of a fully-funded pillar. Healthcare reform is also under preparation, aiming to transform health insurance companies into joint-stock companies in order to increase their transparency and establish competition among healthcare institutions. The Stabilisation Package introduced co-payments for some medical services. These represent first valuable steps in the right direction.

10. The Czech Republic has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. New measures approved in September 2007 should contribute to fiscal consolidation in the short and medium term, although further efforts will be needed for the long-term. The proposed pension reform should be given a concrete time frame for its implementation as soon as possible in order for the Czech Republic to prepare for the negative impact of population ageing on public finances and potential economic growth.

Micro-economic policies

11. Important steps have been taken over the 2005-2007 period towards improving the business environment. In 2007, most progress has been achieved on the regulatory

framework, while progress in other areas, for example e-government and access to venture capital, was more modest. The timely and effective implementation and application of EU legislation needs attention.

12. The Council recommended that the Czech Republic increase the level and efficiency of R&D expenditure. Public R&D expenditure is projected to increase in 2007, improving the chances of the Czech Republic reaching the target in the NRP. The major challenge now is to increase the effectiveness of spending. Alongside this, R&D expenditure financed by the private sector has increased from 0.66% of the GDP in 2004 to 0.88% in 2006. The private contribution now amounts to 57% of total R&D spending. In addition to expenditure increases, the Czech government has committed to better targeting and to a higher structural fund contribution to R&D. It will also invest more in innovation infrastructure that promotes cooperation between public and private research actors. More pronounced action is now needed to avert research personnel shortages.

13. The Council also referred to the need to focus on: improving the system of patenting and the protection of intellectual property rights, speeding up progress in the ICT area, meeting targets for reducing the administrative burden on enterprises, further developing access to finance for innovative companies, developing links between foreign-owned and domestic companies and introducing entrepreneurship education into the curricula.

14. The Czech Republic lags behind in terms of European patenting, although it performs well on national patenting. The effective enforcement of intellectual property rights remains a challenge. ICT up-take is improving, for which the structural funds have been an important investment source. However, the adoption of several legal acts in the field of e-government and electronic communication needs to be accelerated, and implemented. An insufficient level of interconnection between public authority databases is still a serious obstacle for effective e-government, and the relatively low ICT use by citizens must be addressed. The "Smart Administration Strategy" provides a coherent approach for improving the regulatory framework for enterprises and set a target of a 20% reduction in the administrative burden. This represents a good policy response, but continued reform is essential.

15. A lack of finance for innovation still hampers the development and commercialisation of new products and services, despite the increased use of EU funds. Further promotion of the venture capital market is therefore important. Good progress has been achieved in strengthening cooperation between foreign-owned and domestic companies, again notably through the support of structural funds programmes. The Czech government recognises the economic importance of SMEs. In 2006 it approved "the conception of support for small and medium-sized enterprises 2007-2013". However, it is neither clear how SMEs will directly benefit from this, nor which main areas of support fall under this concept. Better information on the key elements of SME support would be welcome. Although entrepreneurship education has been integrated into the “Framework Educational Programmes” the coverage of these programmes is limited. Action is also needed to simplify the recruitment of the first employee.

16. The Czech Republic has partially succeeded in implementing measures to deliver on the micro-economic commitments of the NRP. Significant progress has been made in

promoting better regulation and the Commission therefore considers that this point to watch is no longer merited. There has been some progress in addressing the recommendation on R&D and the points to watch in the area of intellectual property, ICT, financing for innovation and entrepreneurship education where an increased pace of reform is now needed. The Commission therefore considers that the recommendation and the points to watch in these areas remain valid.

Employment policies

17. Continued economic growth has helped increase employment in the Czech Republic. The employment rate is now approaching the 2008 targets, with the exception of older workers. Although decreasing, youth and long-term unemployment remain high.

18. The Council recommended the Czech Republic to further modernise employment protection, including legislation and tax and benefit systems; improve efficiency and equity in education and training, especially in their responsiveness to labour market needs; provide incentives to invest in training, particularly for older workers and the low-skilled; and increase the diversification of tertiary education supply.

19. A new Labour Code entered into force in January 2007 to facilitate flexible work organisation. However, it did not address employment protection of permanent contracts. The announced introduction of ceilings on social and health insurance contributions is a positive step for reducing non-wage labour costs. Stricter conditions for unemployment and social benefits have contributed to decreased benefit dependency, but this should be combined with more effective active labour market policies. The integration of employment and social administrations is under preparation, aiming to improve the coherence and efficiency of employment and social policies. Within the framework of the public finance reform, benefit reform has been approved which should further increase incentives to work. Extensive educational reform continues. A reform of curricula for primary and secondary education is ongoing, and the number of tertiary students and study programmes is increasing, particularly in technical and natural sciences. A comprehensive lifelong learning strategy was approved, and gives greater access to training and incentives for schools to provide training for adults. However, limited progress has been made to provide incentives for individuals and employers to invest in training. These policy measures are important first steps in the right direction that now need complementing.

20. The Council also referred to the need to focus on a better integration of disadvantaged groups into the labour market, reducing regional employment disparities, reconciling work and family life, tackling the gender pay gap and implementing an active ageing strategy. Although overall unemployment is shrinking, further efforts and resources are needed to help disadvantaged groups, in particular people with disabilities and the low-skilled. The situation of the Roma minority requires further attention. No additional measures have been taken to reduce regional disparities. To help address a high gender pay gap, the new flexible duration of maternity leave contains financial incentives to encourage women to return rapidly to the labour market. In order to better reconcile work and family life this measure needs to be complemented by an increase in childcare facilities. A rapid implementation of the active ageing strategy is now required.

21. The Czech Republic partly addresses flexicurity in an integrated way. Permanent contracts continue to be the norm. Active labour market policies lack funding and are not as effective as they could be, and adult participation in lifelong learning remains low. However, a range of measures enhancing labour market flexibility and modernizing the social security system have been implemented. In addition, a broad range of reform measures are being implemented to modernize all levels of education to bring them closer to employment needs.

22. In general, the Czech Republic has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. There has been mixed progress over 2005-2007 in addressing the challenges faced by the Czech Republic in terms of labour market flexibility, greater inclusion in the labour market of groups at the margins, and of improving education. The country specific recommendation and points to watch have been addressed to some extent. The Commission considers the measures taken so far a limited response to the challenges the Czech Republic faces in the fields concerned. It is now important to step up the pace of reform.

PART III: CONCLUSIONS

23. In the light of the 2007 Czech Republic Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

24. The Czech Republic has made some progress in implementing its National Reform Programme over the 2005-2007 period. The Czech Republic had made some progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas.

25. The Implementation Report shows some policy response to the recommendations adopted by the Council. There has been some policy response on the additional areas requiring attention, as identified in the Council conclusions.

26. Among the strengths shown by the 2007 Czech Republic Implementation Report are the coherent strategy to improve the regulatory framework for enterprises, reforms to make work pay, of the curricula for primary and secondary education, to increase participation in tertiary education, and the adoption of the lifelong learning strategy.

27. The policy areas in the Czech Republic National Reform Programme where challenges need to be tackled with the highest priority are the long-term sustainability of public finances in the context of an ageing population, fulfilling the commitments for public R&D expenditure and further increasing its effectiveness, improving security and flexibility in the labour market, improving the efficiency and equity in education and training and increasing participation in lifelong learning. Against this background it is recommended that the Czech Republic:

- with a view to improving the long-term sustainability of public finances, implements the announced reform programme of the pension system without delay, and implements reforms announced in the healthcare system;

- meets the targets for public R&D expenditure and increases its effectiveness, notably by promoting a better collaboration between business, universities and public R&D institutions, and by providing the necessary human resources for research and development;

- within an integrated flexicurity approach, further modernises employment protection, including legislation, improves the efficiency and equity of education and training, especially its responsiveness to labour market needs, provide incentives to invest in training particularly for older workers and the low-skilled, and increases the diversification of tertiary education supply.

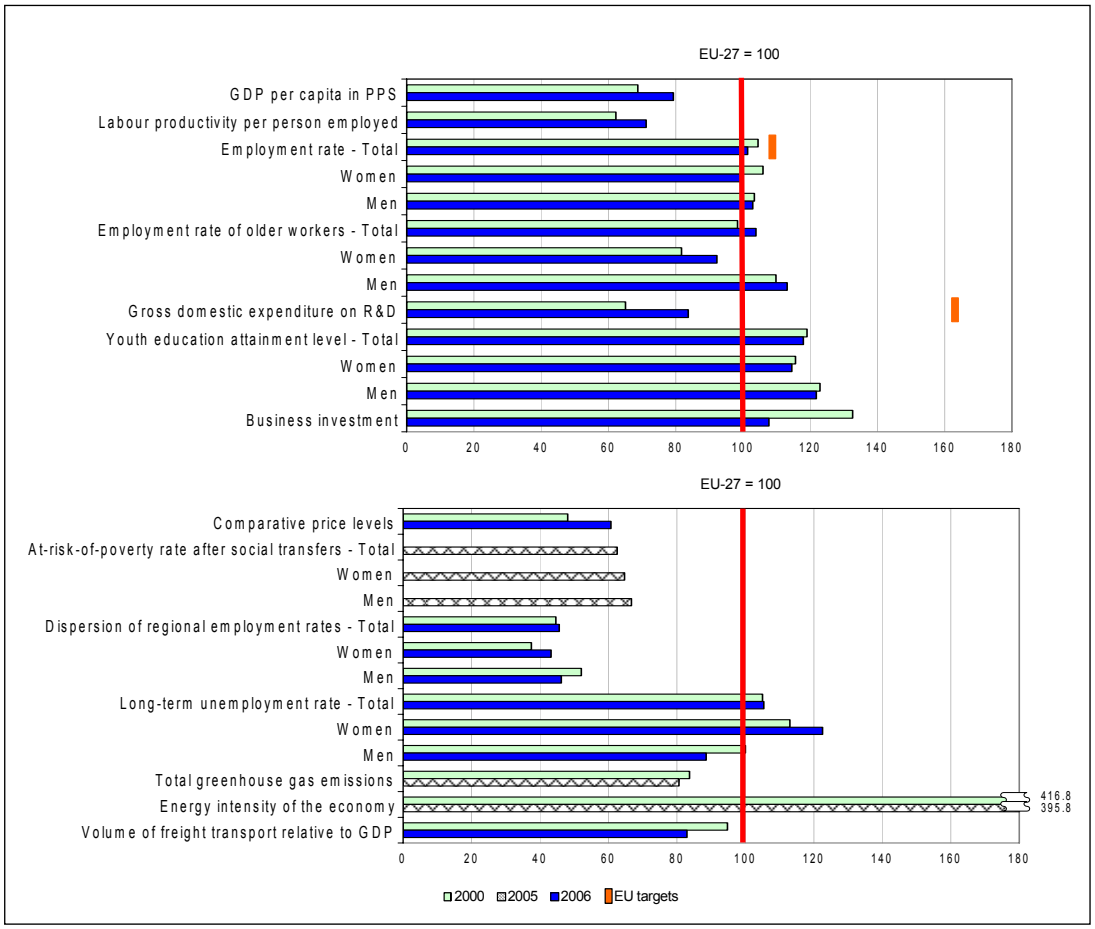
28. In addition, it will be important for the Czech Republic to focus over the period of the National Reform Programme on the following challenges: improving the protection of intellectual property rights; speeding up progress in the ICT area, including by implementing and monitoring a fully enabled legal environment for e-government; improving access to finance for innovative companies, in particular through further developing the venture capital market; increasing the coverage of entrepreneurship education; better integrating disadvantaged groups into the labour market; reducing regional disparities; reconciling work and family life; tackling the gender pay gap; and implementing the active ageing strategy.

PART IV: STATISTICAL GRAPHS AND DATA

CZECH REPUBLIC

		CZ						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		68.7	73.7	76.1	77.0	79.3		100.0	100.0	100.0	
Labour productivity per person employed		62.2	66.5	68.6	69.3	71.2		100.0	100.0	100.0	
Employment rate	Total	65.0	64.7	64.2	64.8	65.3	66.4 (2008)	62.2	63.4p	64.4p	70.0
	Women	56.9	56.3	56.0	56.3	56.8		53.7	56.2p	57.2p	
	Men	73.2	73.1	72.3	73.3	73.7		70.8	70.8p	71.6p	
Employment rate of older workers	Total	36.3	42.3	42.7	44.5	45.2		36.9	42.3p	43.5p	
	Women	22.4	28.4	29.4	30.9	32.1		27.4	33.5p	34.8p	
	Men	51.7	57.5	57.2	59.3	59.5		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.21	1.25	1.25	1.41	1.54	2.06	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	91.2	92.1	91.4	91.2	91.8		76.6	77.4	77.8	
	Women	91.7	91.5	91.8	91.1	92.4		79.3	80.1	80.7	
	Men	90.7	92.8	91.0	91.3	91.1		73.8	74.7	74.8	
Comparative price levels		48.1	54.5	54.9	58.1	60.7		100.0	100.0	100.0	
Business investment		24.4	22.1	21.0	20.1	19.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	:	:	:	10.0b	:		:	16.0e	:	
	Women	:	:	:	11.0b	:		:	17.0e	:	
	Men	:	:	:	10.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	5.8	5.8	5.6	5.5	5.2		13.0	11.9	11.4	
	Women	7.5	7.4	6.6	6.7	7.0		20.0	16.8	16.2	
	Men	5.0	4.9	5.1	4.8	4.3		9.6	9.7	9.3	
Long-term unemployment rate	Total	4.2	3.8	4.2	4.2	3.9		4.0	4.1p	3.7p	
	Women	5.2	5.0	5.3	5.3	4.9		4.6	4.5p	4.0p	
	Men	3.5	2.9	3.4	3.4	3.1		3.5	3.8p	3.5p	
Total greenhouse gas emissions		75.9	75.2	75.0	74.2	:		90.7	92.1	:	
Energy intensity of the economy		888.4	891.2	874.4	823.4	:		213.1	208.1	:	
Volume of freight transport relative to GDP		93.9	98.7	92.5	83.0	88.5		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Denmark

1. Denmark performs well with regard to both growth and jobs. In recent years GDP growth has been particularly strong (above 3% in 2005 and 2006), driven by private consumption and a booming housing market, and is now constrained by labour shortages. With employment increasing rapidly, unemployment reached 3.3% in mid-2007, the lowest level in 30 years, and the lowest in the EU. Denmark also has the highest employment rates in the EU at 77.4% in 2006, while levels for productivity and working time are relatively close to the EU-15 average.

2. Denmark has continued to consolidate its public finances to prepare for the ageing of the population and to this end welfare systems have been reformed. Structural unemployment has been reduced through labour market reforms within the flexicurity approach. Given the already high employment level, the potential for further enhancing labour supply lies especially in increasing hours worked, and augmenting participation rates among, in particular, older workers, immigrants and their descendants.

PART I: GENERAL ASSESSMENT

3. Overall, Denmark has made very good progress with implementing the 2005 National Reform Programme (NRP) over the 2005-2007 period. Compared to the large number of actions taken in the first half of 2006, the pace of progress appears to have decreased somewhat over the last year. Progress remains nevertheless good. In August 2007, Denmark presented the "Denmark 2015" plan outlining the medium-term objectives and requirements to ensure long-term fiscal sustainability. The plan also envisages proposals to increase labour supply, improve public sector efficiency and for public investments. Alongside the plan, there are proposals to improve the quality of public services and it has been agreed to lower the taxation on wage income gradually in 2008 and 2009.

4. No country-specific recommendations were issued for Denmark, but the Council concluded that special attention should be paid to: increasing labour supply over the medium term; following through proposed reforms in competition law; improving the functioning of electricity and gas markets; emission reduction policies and measures; and improving primary and secondary education and completion rates of upper-secondary and tertiary education. Within these areas there has been good progress in the past year, notably with regard to the reform of the competition law. The focus on increasing labour supply has been maintained, but a significant part of the measures announced to increase labour supply have yet to be implemented. Progress to improve energy interconnection has been limited. Denmark has taken several initiatives in the area of education but uncertainty remains as to whether they are sufficient. Measures identified to reduce green house gas emissions have been for the most part identified and will now need to be adopted and implemented.

5. Last year's Commission Annual Progress Report concluded that Denmark had responded well to the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and

energy. Since then, there has been good progress on the commitments with an end 2007 deadline.

6. Consultation and efforts to develop ownership of the NRP amongst all levels of government and with the social partners continue to be positive. The Lisbon Coordination Committee with representatives from various ministries and stakeholder organisations is consulted on the Danish contribution. The Implementation Report presents a wide range of initiatives over the 2005-2008 period and includes initiatives and contributions to the Lisbon process from social partners and interested parties. Regional and municipal reform has coincided with the start of the new structural and cohesion fund period, making it feasible to improve coherence between the implementation of the NRP and the programmes under the structural and cohesion funds. Structural funding is largely earmarked to achieve Growth and Jobs objectives.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. Denmark is coping well with its macro-economic challenge of preparing for the ageing of the population and is maintaining fiscal sustainability. Price and exchange rate stability, and high employment, are the cornerstones of its medium-term fiscal strategy. Key here is the "Denmark 2015" plan which aims at maintaining fiscal sustainability by maintaining fiscal surpluses while allowing public expenditure to grow in line with GDP rather than at a more restrained rate. The "tax freeze" is maintained implicitly constraining local government spending. To ensure sustainability, new initiatives are needed to increase employment whilst at least maintaining current working hours unchanged. These initiatives now need to be implemented to achieve the objectives.

8. In general, Denmark is delivering on the macro-economic commitments expressed in its NRP and progress over the 2005-2007 period has been very good.

Micro-economic policies

9. Denmark has made good progress over the 2005-2007 with the implementation of policies to address the micro-economic challenges of improving competition in certain sectors; enhancing public sector efficiency; developing a knowledge society; securing environmental sustainability and energy; and encouraging entrepreneurship.

10. Denmark continues to make good progress within a systematic and comprehensive system for identifying and addressing sectors with competition problems. In addition, new initiatives have been launched to increase the effectiveness of merger control, to fight against cartels, and to enforce public procurement rules.

11. Denmark continues to be one of the best performing countries in the development of the knowledge society. Good progress has been achieved in the areas of R&D and innovation in the period 2005-07, in line with announced plans. The budgetary framework for R&D, agreed in 2006, has been made more concrete so that the objective of increasing public R&D investment to 1% GDP in 2010 is realistic. A

number of initiatives have been launched to stimulate private R&D and innovation. Denmark is leading in broadband penetration and in the use of the digital signature. Policy continues to focus on the integration of ICT systems and on standardisation. Public sector efficiency is addressed in a package of proposals, some of which have been agreed, but most await adoption and implementation. Following transition-related problems after structural, municipal and regional reform, it will be important to reap efficiency gains in the near future.

12. Denmark is further improving its attractive business environment, in particular regarding fast-growing enterprises and the reduction of administrative burdens, for which a 25% reduction target has been set. The one-stop shop for start-ups is a fully web-based system, allowing immediate company registration online. The integration of VAT registration into the online system is planned for January 2008. Measures on entrepreneurship education are planned for all students in primary and secondary school. Progress has also been made in consulting SMEs on the legislative process and facilitating their access to public procurement. Administrative costs have been lowered by 9.7% over the 2001-2006 period.

13. The Council referred in the micro-economic domain to the need to focus on following through proposed reforms in competition law and ensuring that new competition powers are vigorously exercised by the relevant authorities; additional measures in energy interconnection supply, in order to improve the functioning of the electricity and gas markets; and identifying further emission reduction policies and measures.

14. Denmark has made good progress with regard to the improvement of the competition law to fight cartels. A new leniency programme has been introduced in the amendment to the Competition Act of July 2007 and the powers of the Danish Competition Authority have been strengthened. The effectiveness of this new regime has now to be proven. The Commission will continue to follow progress on the actual implementation of the new regime.

15. Denmark has previously taken action regarding the improvement of energy interconnection. The capacity of the electricity link between Denmark and Germany has been expanded by 15-20% and further expansion is being negotiated. An East-West Denmark link is under construction and will be fully operational in 2010. An expansion of the link between Denmark and Norway is envisaged. Although competition in the energy sector has increased as markets have gradually been liberalised, implementation of measures to increase electricity and gas interconnection capacity is still needed to improve market integration.

16. Denmark performs very well on environmental sustainability, especially with regard to indicators such as energy intensity, electricity produced from renewable sources, and environmental technologies. Several measures have been put forward in 2007 addressing climate change, transport, air pollution and waste management and a comprehensive Energy Strategy 2025 is awaiting adoption. The Danish plan to tackle green house gas emissions outlines measures Denmark has identified to meet its Kyoto target. However, this plan still contains a series of unspecified elements where foreseen emission reductions depend on measures still to be identified.

17. Overall, Denmark is implementing measures to deliver on most of the micro-economic commitments expressed in its NRP. There has been good progress in the field of competition. Measures to reduce green house gas emissions have been mostly identified, and measures to enhance energy inter-connectivity are progressing.

Employment policies

18. Denmark already fulfils the Lisbon employment rate target and performs very well on other employment indicators. The Welfare Agreement (2006) addressed the long-term challenge of an ageing population, by increasing the retirement age gradually from 2019. However, this did not address concerns in the short and medium term. In recent years labour supply has risen due to an increase in average working hours and in the activity rates of the young, older people and immigrants. Among the young the activity rate has increased from 68.1% in 2005 to 72.6% in 2007, while the overall activity rate increase from 79.8% to 80.3% over the same period. Total working hours have increased by 2.2% from 2005 to 2006. Over 2005-2007 Denmark has made progress in addressing the labour market challenge of increasing the labour supply. However, labour shortages remain a challenge both in the private and in the public sector.

19. The Council referred to the need to focus on measures aimed at increasing labour supply over the medium term, up until 2015, including further initiatives to improve incentives to work and additional steps to integrate older workers and immigrants into the labour market. The "Denmark 2015" plan and further future measures aim to raise labour supply by the equivalent of some 8,000 full-time employees. Denmark furthermore aims at strengthening employment by an additional 20,000 jobs by 2015, whilst at least maintaining the current level of average working hours. The Danish government has recently taken initiatives to improve incentives to work, better match the unemployed with vacancies, speed up education reform, improve the employment of older workers and immigrants, and encourage immigration. There remains further room for improving incentives for older workers to stay in work rather than resort to early retirement. Overall, the Commission considers the Danish response to be positive, but efforts must be sustained in this area as the labour market will remain tight.

20. The Council also referred to the need to reinforce existing well-targeted measures to improve primary and secondary education and increase the number of students finalising upper-secondary or tertiary education, if the measures prove insufficient to reach the ambitious targets set. Denmark has taken a number of initiatives, including strengthening teachers' education; tests and evaluations starting from second grade compulsory education; faster completion of education and training via a premium on starting tertiary education within two years of finalising upper secondary education, and a reinforcement of business-related youth educational programmes. Public expenditure on education is the highest in the EU at 7.9% of GDP in 2005. It is important to ensure the quality of these investments as reflected in their cost-effectiveness. Effective implementation of existing initiatives, their evaluation and, if required, consideration of additional measures, will be important to reach the ambitious education targets.

21. The close collaboration between the social partners and the government on the four components of flexicurity is the hallmark of the Danish labour market. Flexible

contractual arrangements giving a large degree of freedom to hire and fire are combined with a high level of unemployment benefits that secure income. Continuous efforts to enhance active labour market policies and an improved life-long-learning strategy allow the labour market to adapt to changing economic conditions. The Danish flexicurity model is continuously adapted by adjusting the incentives in order to make sure that people able to work become employed. The social partners are fully involved in all related policy areas

22. In general, Denmark has succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. Although the areas requiring particular attention have been well addressed, further initiatives and implementation is required, and the Commission therefore considers these points to watch as remaining valid.

PART III: CONCLUSIONS

23. In the light of the 2007 Danish Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

24. Denmark has been making very good progress in implementing its National Reform Programme over the 2005-2007 period. Denmark has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

25. The Implementation Report shows a good policy response to the areas identified by the Council as requiring attention.

26. Among the strengths shown by the 2007 Danish Implementation Report is the comprehensive and integrated approach to reform planning and implementation, within a framework for ensuring long-term fiscal sustainability, combined with the active participation of stakeholders.

27. It will be important for Denmark over the period of the National Reform Programme to focus on the following challenges: continuing to implement measures on energy interconnection in order to improve the functioning of the electricity and gas markets; increasing labour supply and hours worked over the medium term, including further initiatives to work and additional steps to integrate older workers, immigrants and their descendants into the labour market; reinforcing, in a cost-effective manner, measures to improve primary and secondary education and the number of students finalising upper-secondary or tertiary education to reach the ambitious targets set.

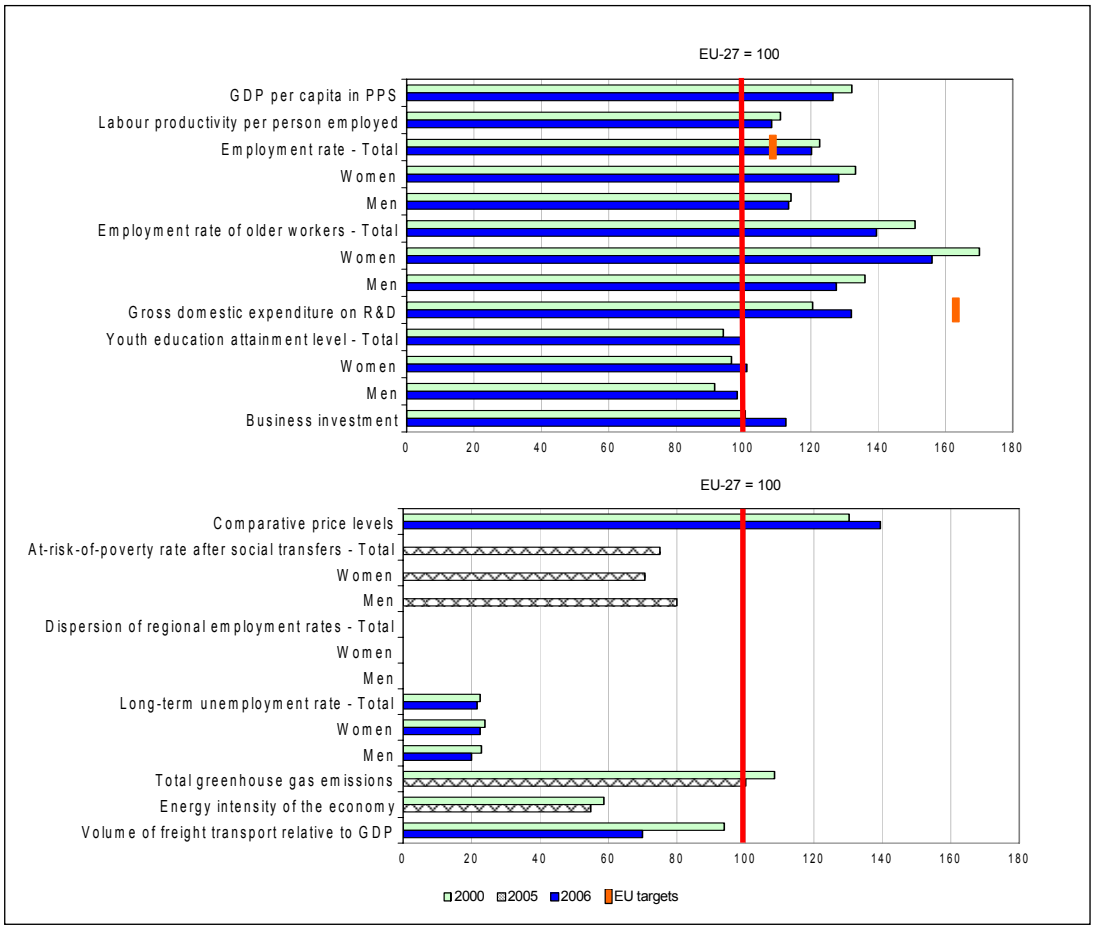
PART IV: STATISTICAL GRAPHS AND DATA

DENMARK

		DK						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		132.2	124.7	124.5	126.3	126.6		100.0	100.0	100.0	
Labour productivity per person employed		111.0	106.4	106.8	108.5	108.4		100.0	100.0	100.0	
Employment rate	Total	76.3	75.1	75.7	75.9	77.4	:	62.2	63.4p	64.4p	70.0
	Women	71.6	70.5	71.6	71.9	73.4		53.7	56.2p	57.2p	
	Men	80.8	79.6	79.7	79.8	81.2		70.8	70.8p	71.6p	
Employment rate of older workers	Total	55.7	60.2	60.3	59.5	60.7		36.9	42.3p	43.5p	
	Women	46.6	52.9	53.3	53.5	54.3		27.4	33.5p	34.8p	
	Men	64.1	67.3	67.3	65.6	67.1		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		2.24	2.58	2.50	2.45	2.43	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	72.0	76.2b	76.2	77.1	77.4		76.6	77.4	77.8	
	Women	76.5	78.5b	78.1	80.5	81.5		79.3	80.1	80.7	
	Men	67.5	73.8b	74.3	73.8	73.4		73.8	74.7	74.8	
Comparative price levels		130.3	141.1	139.6	140.1	139.4		100.0	100.0	100.0	
Business investment		18.5	17.7	17.6	18.7	20.5		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers*	Total	:	12.0b	11.0	12.0	:		:	16.0e	:	
	Women	:	12.0b	11.0	12.0	:		:	17.0e	:	
	Men	:	11.0b	11.0	12.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	0.9	1.1	1.2	1.1	0.8		4.0	4.1p	3.7p	
	Women	1.1	1.0	1.3	1.2	0.9		4.6	4.5p	4.0p	
	Men	0.8	1.2	1.1	1.1	0.7		3.5	3.8p	3.5p	
Total greenhouse gas emissions		98.4	107.0	98.4	92.2	:		90.7	92.1	:	
Energy intensity of the economy		125.0	126.1	121.1	114.1	:		213.1	208.1	:	
Volume of freight transport relative to GDP		93.0	87.9	87.5	84.3	74.6		99.1e	105.4e	106.7e	

* Alternative computation for Denmark using income definition including rent revenue and mortgage interest payments: 2003 10.0b, 2004 10.0 and 2005 10.0

PERFORMANCE COMPARED TO EU-27



Germany

1. GDP growth in Germany was sluggish during the first half of the decade, before peaking at 2.9% in 2006 and slightly decelerating in 2007 to an expected 2.5%. The potential rate of GDP growth stands at 1.7% for 2007. GDP per capita is projected to be 119% of the EU average in 2007. The employment rate was 67.5% in 2006, reflecting a steep rise in the employment rate of older workers from 45.4% in 2005 to 48.4% in 2006, which is above the EU average. The unemployment rate stood at 10.3% in 2006 and is forecast to fall to 8.1% in 2007.

2. Being highly export-oriented and with a technologically strong manufacturing sector, Germany has held up well in the face of intensifying international competition, benefiting from globalisation. Despite the recent upswing, Germany's growth potential is still held back by a relatively high level of structural unemployment and sluggish productivity growth. To re-invigorate growth and job-creation, Germany is confronted with the task of tackling these structural bottlenecks, while safeguarding the achieved consolidation of public finances.

PART I: GENERAL ASSESSMENT

3. Overall, the 2007 Implementation Report shows there has been good progress with the implementation of the National Reform Programme (NRP) over 2005-2007, but it nevertheless remains important to continue the reform process.

4. Germany has responded to the recommendations adopted by the Council. Progress has been good in consolidating public finances, mixed progress on tackling structural unemployment and limited regarding competition in services.

5. There has been some progress on the points to watch which the Council asked Germany to focus upon. Progress has been most substantial regarding childcare facilities, business start-ups and facilitating the hiring of the first employee. Germany has not moved forward sufficiently on improving public procurement procedures, improving the framework for competition in the rail sector, and on improving lifelong learning and enhancing adult vocational training.

6. Germany has made good overall progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship and energy, while there has been more limited progress regarding employment opportunities for priority categories. Germany specifies efforts it is taking to meet euro area recommendations in its Implementation Report. Measures taken include efforts to improve the quality of public finances and social security systems.

7. The NRP and the Implementation Reports have been subject to consultations with other federal ministries, the federal parliament, regional governments and social partners. However, the 2007 implementation report does not provide budgetary details on the reforms. Links between the NRP and programmes under the Structural Funds are strong with 81% of the funds in the competitiveness objective (most of

West Germany) and 71% of the funds in the convergence objective (East Germany and Lüneburg) allocated to Lisbon objectives.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The 2005-2008 NRP identified the sustainability of public finances as a key challenge. Good progress has been made since 2005 in reforming the pension system, including by promoting supplementary pensions to ensure social adequacy. The statutory retirement age will rise in steps to 67 years from 2012 onwards. The move will further enhance the long-term sustainability of public finances. An outline for reform of the long-term care system has been adopted, which introduces a periodic adjustment of expenditure. This will require raising contribution rates. Elements of a funded scheme are not planned, contrary to the announcement in the NRP.

9. The Council recommended Germany to improve the long-term sustainability of public finances and implement the health care reform. Public finances have improved markedly, from a deficit at 3.4% of GDP in 2005 towards balance in 2007. This is the result of reform implementation and the economic recovery which raised tax revenues beyond the increase in the standard VAT rate. Budgetary policy used the cyclical conditions to approach its medium-term objective under the Stability and Growth Pact. This will bring debt, currently above 60% of GDP, on a downward trend. The quality of public finances has been improved by reducing non-wage labour costs in 2007 through cutting unemployment insurance contributions, financed partly by the VAT rate increase. The effect has in part been offset by increased contribution rates to health and pension systems. The company tax reform, coming into force in 2008, will reduce statutory corporate tax rates, partly funded by a broadening of the tax base.

10. The health care reforms that entered into force between 2005 and 2007 have at least shown temporary effects on containing expenditures, whilst evidence of the effects of the 2007 reform is not yet available. These reforms give public insurers the option to offer non-standard contracts with a limited choice of service providers to the compulsorily insured. This could provide incentives for a more efficient use of medical services. Competition between health service providers may intensify, as health insurers are now free to deviate from the collectively agreed fee structure for out-patient services. The main reform measure, the financial pool (Gesundheitsfonds) to replace the insurers' autonomy in setting contribution rates, becomes operational by 2009.

11. Progress in addressing the macro-economic challenge has been good over 2005-2007. It is now important to maintain the reform momentum and secure the achieved fiscal consolidation, including by revising budgetary institutions in the ongoing second stage of the reform of the federal system. It is also important to monitor whether the health care reform can deliver the expected benefits. Overall, progress with regard to the euro area recommendations on the medium-term budgetary objective and on the quality of public finances has been good.

Micro-economic policies

12. The key micro-economic challenges identified in the NRP were: the knowledge society; market functioning and competitiveness; the business environment; and ecological innovation. Policy implementation to develop the knowledge society has been good. Since 2005, Germany has launched initiatives to help improve innovative potential particularly through improved cooperation between science, research and business and with venture capital programmes. However, the number of graduates in engineering and natural sciences and the mobility of researchers need to increase further. While the contribution of the federal level towards the 3% R&D-target is significant, regional spending and private sector co-financing has not been specified. Progress in policy implementation to counter climate change and promote renewable energy has been good. A national allocation plan for emissions trading has been adopted, a new law to increase the use of bio fuels has become effective, and the energy efficiency of buildings has been addressed.

13. Germany has made some progress since 2005 to improve market functioning and competitiveness. A significant effort has been made to improve the business environment, especially by reducing the administrative burden, for which a 25% reduction target has been set. Overall, in 2005-2007, progress in implementing the policies that address Germany's micro-economic challenges, notably those concerning knowledge society and ecological innovation, has been good.

14. The Council recommended Germany to focus on improving the framework for competition in product and services markets. There has been no recent progress on relaxing restrictive rules on regulated trades and services. On wholesale bit stream access a measure was taken in September 2006 requiring the incumbent telecommunications company to provide non-discriminatory access and to produce a standard offer for competitors. However, implementation is progressing too slowly, whilst it is important not to exempt new telecommunication markets from ex ante regulation.

15. The Council also highlighted the need to focus on: public procurement procedures; the framework for competition in the rail sector, and in gas and electricity networks; and speeding up business start-ups and the hiring the first employee. Germany has made good progress with facilitating the hiring of the first employee. It has also stepped up its efforts to reduce start-up times and costs for businesses but will not provide one-stop-shops nationwide by the end of 2007. Competition in the rail, gas and electricity sectors improved somewhat, while implementing the planned unbundling measures would further strengthen competition in the rail sector. However, fundamental elements of the existing draft law have been called into question. With respect to gas and electricity networks, Germany has implemented the Community legislation. However, high market concentration, a lack of transparency and vertical foreclosure remain problematic. The legislative process to simplify the complex public procurement procedures has not progressed in 2007, although work on a draft law is ongoing. The Commission considers this a mixed response and it is now important to step up the pace of reform.

16. Germany has partially implemented measures to deliver on the micro-economic commitments expressed in its NRP. The response to the recommendation and the euro area recommendation on strengthening competition has been limited especially

in telecommunications, liberal professions and public procurement. The process to simplify public procurement procedures has not progressed in 2007 and requires particular attention. Some points to watch have been addressed well, notably on start-ups and procedures to hire the first employee.

Employment policies

17. The key labour market challenge identified in the NRP was the adaptation to the demographic challenge. Labour market improvements over 2005-2007, and in particular the employment situation of older workers, reflect economic conditions, wage moderation, and the effects of reforms implemented to promote better incentives to take up work and prolong working life. With regard to structural unemployment, progress has been mixed. Although decreasing, the long-term unemployment rate still stood at 5.5% in 2006 (above the EU average of 3.7%) and the gap between the unemployment rate of the low-skilled and the overall unemployment rate keeps increasing.

18. The Council recommended that Germany should tackle structural unemployment by integrating the low-skilled into the labour market through better access to qualifications, pursuing the proposed tax-benefit reform, and by providing more effective employment services for the long-term unemployed and by enhancing occupational integration of young people.

19. In 2006, 31% of the budget for active labour market policies for recipients of basic income support was spent on "employment opportunities" (*Arbeitsgelegenheiten)* as compared to only 15% on qualification and training. There has been no agreement on the announced comprehensive tax benefit reform. The effectiveness of the employment services for unemployed recipients of basic income support still poses difficulties. However, reform efforts have been stepped up to improve the employment situation of young people. The National Training Pact, aiming at increasing the number of apprenticeship places has been prolonged and ambitious targets defined. A temporary programme offering on-the-job training for young people who are difficult to place has been transformed into a regular instrument of active labour market policies. Amongst unemployed recipients of basic income support, the activation rate of young people stood at 32.4% in 2006 as compared to a general activation rate of 18.4%. The positive impact of these measures has been supported by the economic upswing. Germany has thus complied with part of the recommendation.

20. The Council also highlighted the need to focus on childcare and lifelong learning. In 2007 Germany set a new national childcare target to provide places for 30% of all under-three year olds by 2013 (compared to 14% in 2006). Parents will also have a legal right to claim a childcare place. To reach the new target, a financial plan for the local authorities in charge of implementation has been adopted. This response is appropriate. In the field of lifelong learning, the government has agreed on guidelines to create incentives for employees to finance their training. No concrete steps have been taken so far on incentives for employers. The Commission considers this to be a limited response.

21. Germany has not sufficiently addressed the flexicurity concept in an integrated manner. In spite of the variety of contracts available, the labour market remains

segmented between insiders and outsiders. Support through active labour market policies is characterised by a low share of spending on training and qualifications, while the focus of the German authorities is on the provision of employment opportunities. On lifelong learning, the share of employees participating in continuous vocational training is declining. The tax-benefit system results in an increasing number of persons combining permanent work in low-paid part-time jobs with basic income support. Generally, the social partners are involved in design and implementation of labour market policies.

22. Overall, Germany has partially implemented measures to deliver on the employment policy commitments expressed in its NRP and the euro area recommendation. Structural unemployment needs to be tackled, especially by improving the labour market integration of low-skilled people. Demographic change also warrants enhancing continuous vocational training for employees.

PART III: CONCLUSIONS

23. In the light of Germany's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

24. Germany has made good progress in implementing its National Reform Programme over 2005-2007 and good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

25. The Implementation Report shows that there has been some policy response to the recommendations adopted by the Council. There has been a good response in consolidating public finances, and a more limited response regarding competition in services and on tackling structural unemployment. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

26. Among the strengths shown by the 2007 German Implementation Report are: the consolidation of public finances; the strengthening of high-class research and innovation; the progress in tackling youth unemployment; and the determined approach to increasing childcare facilities.

27. The policy areas in the German National Reform Programme where challenges need to be tackled with the highest priority: are competition in services and structural unemployment. Against this background it is recommended that Germany:

- improve the framework for competition in services, notably by continuing to relax restrictive rules in regulated trades and professions, improving public procurement procedures, without exempting new telecom markets from regulation and effectively regulating wholesale bitstream access;

- tackle structural unemployment by maintaining the path of the reforms outlined in the National Reform Programme. Focus should be placed on integrating the low

skilled into the labour market through a flexicurity approach combining better access to qualifications with the implementation of the announced comprehensive tax and –benefit reform and more effective employment services for unemployed recipients of basic income support.

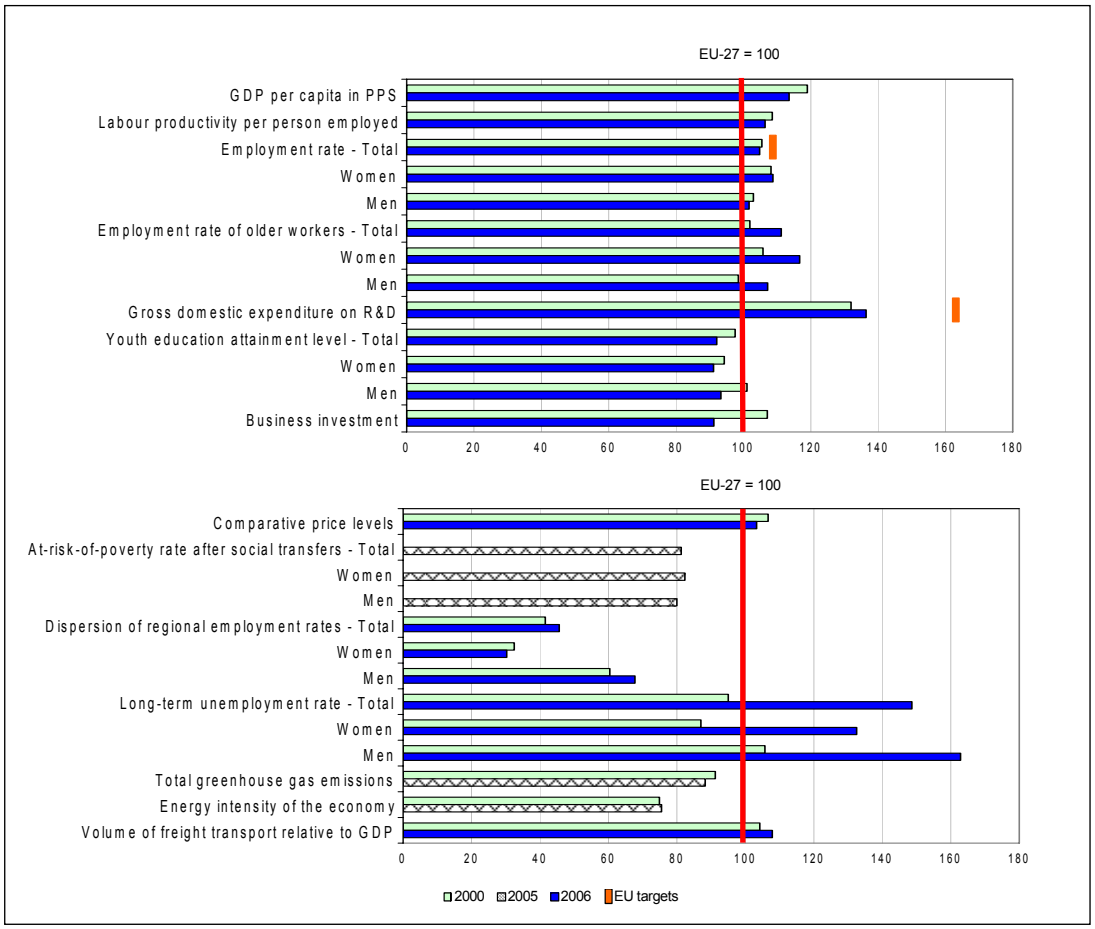
28. In addition, it will be important for Germany over the period of the National Reform Programme to focus on the following challenges: securing the long-term sustainability of public finances by firmly locking in the achieved fiscal consolidation, including in the ongoing revision of budgetary institutions in the federal system, and by carefully monitoring the impact of the health care reform to keep expenditure growth in check and strength efficiency in the health sector; improving the framework for competition in the rail sector, and in the gas and electricity networks, where competition remains insufficient due to high concentration; continue further with the establishment of one-stop-shops and the improvement of start-up times; and in the context of the planned measures to promote lifelong learning, enhance continuing vocational training.

PART IV: STATISTICAL GRAPHS AND DATA

GERMANY

		DE						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		119.0	117.1	116.1	114.6	113.6		100.0	100.0	100.0	
Labour productivity per person employed		108.6	108.5	107.5	106.7	106.4		100.0	100.0	100.0	
Employment rate	Total	65.6	65.0	65.0	66.0p	67.5p	:	62.2	63.4p	64.4p	70.0
	Women	58.1	58.9	59.2	60.6p	62.2p		53.7	56.2p	57.2p	
	Men	72.9	70.9	70.8	71.3p	72.8p		70.8	70.8p	71.6p	
Employment rate of older workers	Total	37.6	39.9	41.8	45.4p	48.4p		36.9	42.3p	43.5p	
	Women	29.0	31.6	33.0	37.5p	40.6p		27.4	33.5p	34.8p	
	Men	46.4	48.2	50.7	53.5p	56.4p		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		2.45	2.52	2.49	2.48	2.51	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	74.7	72.5	72.8	71.5b	71.6p		76.6	77.4	77.8	
	Women	74.8	73.4	74.2	72.5b	73.5p		79.3	80.1	80.7	
	Men	74.6	71.6	71.5	70.4b	69.8p		73.8	74.7	74.8	
Comparative price levels		106.6	106.1	104.7	103.8	103.3		100.0	100.0	100.0	
Business investment		19.7	16.3	16.1	16.0	16.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	10.0	:	:	13.0b	:		:	16.0e	:	
	Women	11.0	:	:	14.0b	:		:	17.0e	:	
	Men	10.0	:	:	12.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	5.4	5.9	6.0	5.6	5.2		13.0	11.9	11.4	
	Women	6.5	5.7	5.8	5.0	4.9		20.0	16.8	16.2	
	Men	5.8	6.9	7.3	7.0	6.3		9.6	9.7	9.3	
Long-term unemployment rate	Total	3.8	4.6	5.5	5.7p	5.5p		4.0	4.1p	3.7p	
	Women	4.0	4.5	5.2	5.3p	5.3p		4.6	4.5p	4.0p	
	Men	3.7	4.7	5.7	5.9p	5.7p		3.5	3.8p	3.5p	
Total greenhouse gas emissions		82.7	83.6	83.2	81.3	:		90.7	92.1	:	
Energy intensity of the economy		159.7	161.0	159.6	157.0	:		213.1	208.1	:	
Volume of freight transport relative to GDP		103.3	103.2	109.4	111.0	115.1		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Estonia

1. Estonia's economy has shown strong growth in recent years, exceeding 10% in 2005-2006 and estimated at around 8% in 2007. Growth was driven by consumption and investment, and facilitated by large-scale financing from abroad, income tax cuts and rapid wage increases. Sustained strong economic growth has, however, led to growing imbalances, evidenced by rising inflation, a tightening labour market and widened external deficits. The employment rate rose to 68.1 % in 2006, while unemployment is estimated to fall below 5% in 2007. Given the increasing labour market tightening, real wage increases have significantly exceeded productivity growth, helping to increase inflation and erode competitiveness, particularly in the low skilled-segments of the economy. Recently, a welcome slowdown in domestic demand has set in.

2. Given the strong job creation and a swift reduction in unemployment, certain sectors now face labour shortages, constraining further rapid catch-up. Continued structural reforms could help ease resource constraints and stimulate sustainable productivity-led growth. Labour market policies, including the modernisation of labour law, would contribute to higher participation in the workforce and to containing wage increases. A stronger competition policy would also contribute to limiting inflationary pressures. Further efforts to improve the regulatory framework for businesses and increase investment in R&D and innovation are necessary for strengthening competitiveness.

PART I: GENERAL ASSESSMENT

3. Overall, the 2007 Estonian Implementation Report shows very good progress on implementing the National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have slightly decelerated over the last year.

4. With regard to the issues referred to by the Council, there has been some progress on competition policy, employment policy and educational policy. Progress has been most substantial on R&D and innovation policy. Estonia has not moved forward significantly on the modernisation of labour law and the implementation of a lifelong learning strategy.

5. Last year’s Commission Annual Progress Report concluded that Estonia responded positively to the commitments made by the 2006 Spring European Council in the priority areas of knowledge, entrepreneurship, employment and energy. Since then, there has been good progress on most commitments with an end 2007 deadline.

6. Consultation and efforts to develop ownership of the NRP are quite good at the national level, although regionally this could be improved upon. Specific consultation in preparing the Implementation Report included a stakeholder seminar and web-based consultation. Estonia has an inter-ministerial working group which coordinates the Lisbon process and includes social partners and academic experts. There is a strong link between the NRP and the Structural Fund programmes, essential given that a significant proportion of the activities described in the NRP are

financed by the Structural Funds. The budgetary resources planned in the Implementation Report also include the Structural funds contribution.

7. In April 2007, the new government agreed a Coalition Programme for 2007-2011. In view of the end of the governance cycle 2005-2007, Estonia decided to update its reform programme only with measures that contribute to meeting the objectives outlined in the 2005 NRP.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. Ensuring macro-economic stability, fiscal sustainability and internal and external balance are the government's main macro-economic objectives. Raising the employment rate is seen as key to sustaining the economy's strong growth performance and to raising living standards.

9. The Implementation Report confirms a prudent fiscal policy as the key element of macro-economic stability in the framework of the currency board monetary regime pegging the kroon to the euro. Public finances have posted surpluses in recent years (3.6% of GDP in 2006). However, inflation performance has deteriorated, with a rate above 6% in 2007, and projected to rise further in 2008. Wages have recently been increasing at close to double the rate of labour productivity growth. The external deficit widened to 16% of GDP in 2006, although the 2007 deficit ratio is expected to be slightly lower. These developments should however be seen in the context of a rapid catching-up process with the EU as a whole, supported by massive financial inflows from abroad. With GDP growth rates above potential since 2005, the recent switch to targeting budget surpluses (instead of balanced budgets) was a welcome development, even though more ambitious fiscal targets would be desirable to help reduce core inflation and external imbalances in a medium-term perspective. With respect to the sustainability of public finances, continuing surpluses have allowed further reduction in the already low government debt, which stood at 4% of GDP by the end of 2006, and is expected to fall below 3% of GDP in 2007. Pension increases have recently been higher than those foreseen by legislation. A reform package adopted by parliament in November 2007 will provide for more generous pension indexation, and age and health-related expenditure is thus expected to rise.

10. The overall focus of macro-economic policies and measures proposed in the NRP on stability and long term sustainability are broadly appropriate. Nevertheless, certain elements of Estonia's fiscal policy indicate that the tax incentives (e.g. the lowering of the income tax rates) and budgetary strategy (an increase in expenditure, including in wages and pensions) may limit room for fiscal consolidation. In the near future fiscal policy may fall short of sufficiently countering inflationary pressures and of reducing external deficit in the economy, although these seem likely to be receding from the peaks of 2006-2007. Continued fiscal policy vigilance would also be justified to preserve flexibility in the case of a marked economic slowdown. Finally, efforts to facilitate labour market adjustment and ensure wage increases do not outstrip labour productivity growth are essential to limit inflation and to counter the erosion of external competitiveness.

11. In general, Estonia has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. Macro-economic stability and containing inflation now needs to be improved through adequate structural reforms and a determined fiscal policy.

Micro-economic policies

12. Estonia identified R&D and innovation as a key challenge for sustaining strong economic growth and enhancing competitiveness. Good progress has been made over the 2005-2007 period to address this key challenge.

13. The Council highlighted the need to focus on clearer prioritisation and improved cooperation for the effective use of R&D and innovation expenditure; reinforcing efforts to ensure that R&D results are translated into innovative services or products; encouraging closer cooperation between universities and enterprises; and vigorously implementing the planned proactive competition policy. The new "Knowledge-based Estonia" strategy for 2007-2013 aims at providing a long-term, prioritized and systematic development of R&D and innovation activities including the use of the structural funds. Inter-ministerial cooperation has improved, and the Strategic R&D and Innovation Coordination Committee has recently been established. Continued investment has increased R&D intensity from 0.93% of GDP in 2005 to 1.14% of GDP in 2006. Measures have been taken to strengthen competence centres facilitating the cooperation between scientists and companies. Developing human resources, including an increase in the number of scientists and engineers, remains an important challenge. In order to minimize competition-related crimes and efficiently fine cartels, the launch of a new immunity and leniency programme in 2008 is under preparation. After having previously strengthened the cooperation between the competition authority and the sectoral regulators, the government adopted a regulation in September 2007 to merge the national competition authority with these sectoral regulators.

14. During the 2005-2007 period, Estonia has taken a number of significant initiatives to improve the business environment, including the regulatory environment. Better regulation tools have been further developed and an action plan aiming at the simplification of the legal environment has been approved. However, no target for reducing administrative burdens has been set. Estonia's initiatives in the area of e-government contribute to further reducing administrative burdens on companies. Notaries now act as one-stop-shop for the establishment of new companies. The time required to start-up a company is less than a week and, via the internet, only a few hours. In order to improve access to finance for business, the Estonian Development Fund was established in December 2006. In terms of entrepreneurship education, the postponement of the new national curricula until 2009 delays the envisaged increase in attention paid to entrepreneurship in the educational system.

15. Some progress is being made on environmental issues. While the implementation of the Energy Conservation Programme aims at enhancing energy efficiency, the high energy intensity of the economy remains a challenge. The electricity market law has been amended to promote electricity production from renewable sources. In addition to the new public procurement act, general guidelines and tools have been developed to promote sustainable procurements.

16. In general, Estonia has made good progress in the micro-economic field. The points to watch in the area of competition and R&D and innovation have been partially addressed. While the priorisitation and inter-ministerial coordination of R&D and innovation policy have improved, efforts should continue to turn R&D results into innovation, to increase the number of scientists, to bridge the gap between universities and enterprises, and to further develop the new immunity and leniency programme.

Employment policies

17. The NRP identified employment as a key challenge, including increasing the employment rate, reducing structural unemployment, and improving skills through lifelong learning. Employment rates for all age groups have been increasing strongly over recent years. In 2006, employment growth was the highest in the EU, at 5.4%. The female employment rate has been increasing strongly and gender gaps in employment and unemployment rates are low and diminishing. However, a high gender pay gap is a concern for Estonia. The unemployment rate is falling, including for the most vulnerable groups. Many of the planned employment measures have been implemented. However, reducing structural unemployment and integrating inactive people and the long-term unemployed into the labour market remain important challenges for Estonia in order to increase the supply of skilled labour.

18. The Council referred in the employment area to the need to focus on the modernisation of labour laws as well as reinforcing active labour market policies and raising the skills level of the labour force through reforms in education and lifelong learning. No progress has been made regarding the modernisation of labour law announced in the NRP, limiting considerably the flexibility of the labour market and the adaptability of workers and enterprises to a changing economic environment. The Implementation Report also makes no reference to the progress in promoting flexible contractual arrangements. Several measures for increasing the quality of vocational and higher education have been taken. However, several important legislative acts, such as new curricula for basic and upper secondary schools, and new financing models for general education and for adult education have not yet been adopted. The adult participation rate in lifelong learning is low and the current system does not cover the most vulnerable groups. Several reforms in active labour market policies have been implemented. However, the share of unemployed participating in active labour market programmes continues to be very low. Therefore, more emphasis should be put on the efficiency of active labour market policy measures. The impact of the launched reform package is not clear because of a current lack of labour market monitoring and evaluation system. The Commission considers this a partial response to the challenges Estonia faces in the fields concerned.

19. Estonia does not address flexicurity in an integrated way. Nevertheless, policy development has focused on individual flexicurity-related measures. While some reforms have taken place in the social security system, in active labour market policies and lifelong learning, the measures for increasing labour market flexibility and promoting flexible forms of work still need to be developed. Social partners are partly involved in some of the flexicurity components but the involvement of social partners is generally weak and exists mainly at national level, not the sectoral or enterprise level.

20. In general, Estonia has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. The points to watch in the employment area have been addressed to some extent, although there has been no progress in modernising labour law. It is now important to step up the pace of reforms, in particular regarding increasing the flexibility of the labour market. It is also necessary to make further efforts in raising the skills level of the labour force through the implementation of lifelong learning measures and increasing the efficiency of active labour market measures.

PART III: CONCLUSIONS

21. In the light of the 2007 Estonian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

22. Estonia has been making very good progress in implementing its National Reform Programme over the 2005-2007 period. Estonia has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

23. The Implementation report shows some policy response to the areas identified by the Council as requiring attention. There has been some policy response on competition policy, active labour market policies and educational policy. The most substantial response has been on R&D and Innovation policy. Estonia has not moved significantly forward on the modernisation of labour law.

24. Among the strengths shown by the Estonian Implementation Report are: the establishment of an ambitious long-term and systematic new R&D and Innovation strategy; the measures to facilitate start-ups and financing of innovative SMEs; a strong increase in the employment rate and the measures for raising the quality of higher and vocational education.

25. The policy areas in the Estonian National Reform Programme where challenges need to be tackled with the highest priority are: the employment area where progress on the modernisation of labour law has been limited.

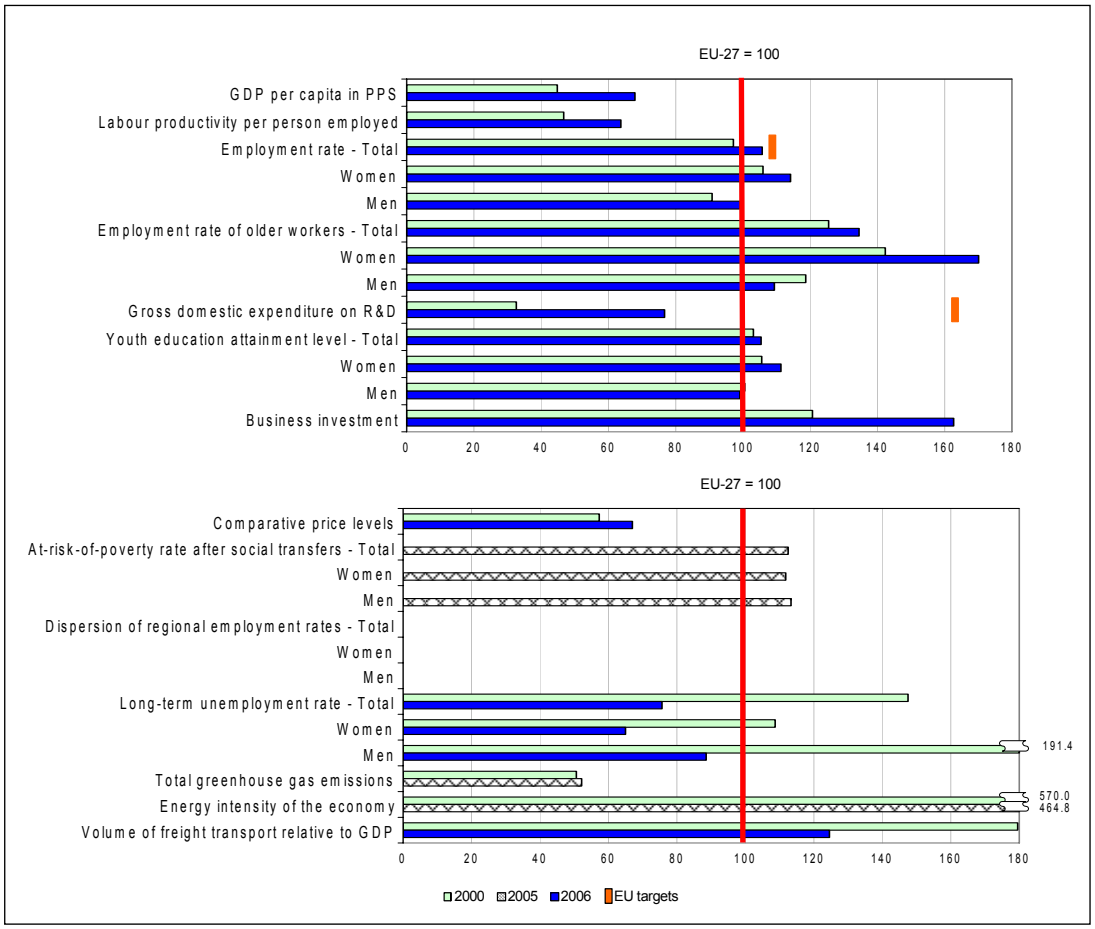
26. It will be important for Estonia over the period of the National Reform Programme to focus on the following challenges: improving macro-economic stability and containing inflation through adequate structural reforms and determined fiscal policy; reinforcing efforts to ensure that R&D results are translated into innovative services or products; encouraging closer cooperation between universities and enterprises; launching the new immunity and leniency programme and strengthening competition enforcement; reinforcing active labour market policies and increasing the supply of skilled labour by implementing a comprehensive lifelong learning strategy that responds to labour market needs; reducing labour market rigidities by urgent progress towards labour law modernisation and by promoting flexible forms of work.

PART IV: STATISTICAL GRAPHS AND DATA

ESTONIA

		EE						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		44.8	54.6	57.0	62.8	67.9		100.0	100.0	100.0	
Labour productivity per person employed		46.7	54.4	56.9	61.5	63.7		100.0	100.0	100.0	
Employment rate	Total	60.4	62.9	63.0	64.4	68.1	70.0	62.2	63.4p	64.4p	70.0
	Women	56.9	59.0	60.0	62.1	65.3		53.7	56.2p	57.2p	
	Men	64.3	67.2	66.4	67.0	71.0		70.8	70.8p	71.6p	
Employment rate of older workers	Total	46.3	52.3	52.4	56.1	58.5		36.9	42.3p	43.5p	
	Women	39.0	47.3	49.4	53.7	59.2		27.4	33.5p	34.8p	
	Men	55.9	58.9	56.4	59.3	57.5		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.61	0.77	0.86	0.93	1.41	1.9	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	79.0	81.5	80.3	82.6	82.0		76.6	77.4	77.8	
	Women	83.7	85.1	87.5	87.6	89.8		79.3	80.1	80.7	
	Men	74.2	77.9	73.2	77.6	74.1		73.8	74.7	74.8	
Comparative price levels		57.3	62.0	62.8	64.3	67.0		100.0	100.0	100.0	
Business investment		22.2	27.5	28.0	27.0	29.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	18.0	18.0	20.0b	18.0	:		:	16.0e	:	
	Women	19.0	20.0	21.0b	19.0	:		:	17.0e	:	
	Men	17.0	17.0	19.0b	17.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	5.9	4.6	5.0	4.2	2.8		4.0	4.1p	3.7p	
	Women	5.0	4.4	4.4	4.2	2.6		4.6	4.5p	4.0p	
	Men	6.7	4.8	5.6	4.2	3.1		3.5	3.8p	3.5p	
Total greenhouse gas emissions		45.9	50.1	49.2	48.0	:		90.7	92.1	:	
Energy intensity of the economy		1214.8	1179.1	1096.2	966.9	:		213.1	208.1	:	
Volume of freight transport relative to GDP		177.9	150.6	159.0	152.4	132.9		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Ireland

1. Over the period 2005-2007, Ireland experienced a continued rapid increase in real GDP per capita, bringing its level in 2006 to 143% of the EU average. Employment levels have continued rising, and labour productivity growth, though it has slowed significantly, remained well above the EU average. Over 2005 and 2006 consumer prices grew faster than in the euro area (2.4% on average annually in Ireland as against 2.2%). This divergence is forecast to widen further in 2007 (2.8% on average annually in Ireland as against 2.0%) due mainly to higher services price inflation.

2. Looking ahead, the main domestic risk comes from the housing sector which having started a steep decline from its 2006 peak may fall further and faster than expected. The worsening external environment, coupled with a real exchange rate appreciation, constitutes a significant risk for exports. As the fiscal outlook is expected to deteriorate over the medium term, a careful prioritisation of public expenditure and the promotion of reforms that strengthen higher-productivity growth, through expanding physical and human capital and reducing inflationary pressures will increase the capacity of the Irish economy to adjust to lower though more balanced growth.

PART I: GENERAL ASSESSMENT

3. Overall, the 2007 Irish Implementation Report shows very good progress on implementing the National Reform Programme (NRP) over 2005-2007. The pace of progress has remained the same over the last year.

4. No country-specific recommendations were issued for Ireland. With regard to the other areas on which the Council concluded Ireland should focus in the macro-economic, micro-economic and employment domains, there has generally been good progress. Last year's Commission Annual Progress Report concluded that Ireland had made some progress in meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been good progress on most of the commitments with an end 2007 deadline.

5. The Implementation Report does not specifically address the recommendations issued to the euro area countries, but there have been relevant developments. As Ireland's fiscal position has performed better than its medium-term objective under the Stability and Growth pact, the euro area recommendation on budgetary consolidation was not relevant for the period 2005-2007. However Ireland should strictly implement its 2007 Budget to limit the deterioration of the structural balance in 2007 and to ensure adequate room for manoeuvre against any reversal of the growth pattern.

6. Consultation and efforts to develop ownership of the NRP at the level of central and local government and with the social partners continue to be very substantial. The new generation of Irish Structural Fund programmes co-financed by the EU, with 85% of the total programme financing earmarked for Lisbon activities, effectively complement the new Irish National Development Plan in delivering the Lisbon

agenda in Ireland. The 2007-2013 strategy will focus on innovation, knowledge and entrepreneurship in the regions; competitiveness, gateways and hubs; upskilling the workforce and activation and participation of groups outside the workforce.

7. A new Irish government took office in June 2007. Ireland's 2007 Implementation Report confirms the main priorities within the NRP and aims to maintain the successful social partnership process. The Commission agrees with these priorities and welcomes the continuation of the process. A major challenge remaining is the unbalanced development between the Southern and Eastern region and the Border, Midland and Western region, especially in fields relevant for the future competitiveness of the country.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. Progress over the 2005-2007 period on the macro-economic challenges identified by Ireland, notably maintaining a stable macro-economic environment, sustainable public finances, and moderate inflation levels; prioritisation of public investment in economic and social infrastructure and other growth-enhancing expenditures, has been good. This reflects the achievement of fiscal surpluses over the period and the publication of the National Development Plan, which sets clear priorities for public investment in infrastructure. More limited progress has been made in taking concrete measures to ensure that the economy will be able to meet anticipated long-run fiscal pressures arising from population ageing.

9. The Council highlighted the need to focus on developments in the housing market and on pension reforms. In relation to the former, the Implementation Report and the recently published Pre-Budget Outlook (PBO) show that the national authorities are closely monitoring the prospects for the housing market and its implications for the broader economy. In particular the PBO (which provides an updated economic outlook for the medium term) states that *"lower output and employment in the construction sector highlight the need to find alternative sources of growth to drive the economy forward"*.

10. A green paper on pensions was published in mid-October by the Irish government, setting out the objectives of the pension system and a discussion of possible reforms. The green paper invites Social Partners and interested parties to provide their views on reform. The broad objectives of reform are: the improvement of pension coverage and access to pensions through modernisation of the pension system; ensuring the adequacy of benefits and; addressing further the financial sustainability of the pension system over the longer-term. The green paper starts from the observation that the existing system is not sustainable without adjustments to the overall policy mix and that to safeguard the pension system in the future, a combination of measures aimed at financing and reducing the size of the projected funding gap will be required. The consultation process is expected to last until summer 2008 and decisions about specific reform measures might not therefore be expected until the second half of 2008 at the earliest. The publication of the green paper is a welcome important step forward in the development of policy but falls short of identifying specific reform measures.

11. In general, Ireland has succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. In view of the risks of a greater than expected slowdown of activity in the housing sector, this point to watch remains relevant. In the pensions area, the national authorities should move rapidly after the consultation period to the identification and implementation of specific measures. This point to watch therefore also remains relevant.

Micro-economic policies

12. Over the past year Ireland has achieved good progress in implementing the micro economic policies set out in the NRP. Progress is also good over the full 2005-2007 period with regard to the implementation of policies to address the micro-economic challenges faced by Ireland, notably improving competitiveness, infrastructure, regulation and social inclusion, increasing R&D investment and efficiency, encouraging greater innovation and entrepreneurship and sustainable development.

13. The Council highlighted the need to focus on: further emission reduction measures and the setting of an intermediate target for R&D investment for 2010. The National Climate Change Strategy 2007–2012, published in April 2007, details the measures by which Ireland will meet its 2008-2012 commitment under the Kyoto Protocol, and how these measures will position Ireland for the post 2012 period. It is projected that, through existing policies, Kyoto mechanisms and carbon sinks, Irish emission levels will be slightly below the Kyoto target. With only 6.8% of electricity generated from renewable energy sources in 2005, and a modest growth in this rate, the 2010 target of 15% is still relatively far off. Investment in R&D on clean renewable energy is also low. However, the recently introduced feed-in tariff mechanism (an incentive structure that boosts the adoption of renewable energy) is expected to provide positive investment conditions and together with other policy initiatives is expected to give Ireland a good opportunity of meeting the 2010 target.

14. Ireland has made good progress towards the 2013 research investment target, but intermediate investment levels, notably for 2010, have yet to be established. Gross expenditure in R&D increased from 1.10% of GDP in 2002 to 1.32 % in 2006. Nearly 60% of overall R&D expenditure comes from the business sector. The Science, Technology and Innovation Strategy provides an adequate framework to build a world-class research base by concentrating on higher education, links between research institutions and business and increasing R&D efforts by indigenous companies. There is, however, concern about the regional balance in implementation. There are a number of noteworthy new initiatives this year including the introduction of an Innovation Vouchers system, a grant scheme for Centres for Science, Engineering and Technology and a new round of venture capital funding.

15. Under most of the SME priority areas, Ireland has performed well over the last year. The Implementation Report addresses all of the SME priorities with the exception of first employee recruitment. Nevertheless, in relative EU terms, Ireland performs well in this area. Start-up procedures are relatively fast, with most businesses generally being set up within a week, but further simplification is still possible. SME access to public procurement could also be improved, although initial steps have been taken with the May 2007 publication of a consultation document. Impact assessments are now routinely applied to ensure better regulation, alongside statute law reform, and efforts to reduce administrative burdens. Ireland has not yet set a specific target for

the reduction of administrative burdens. On ICT policy, Ireland progresses but still lags behind in some information society areas. The Knowledge Society Action Plan, expected to be in line with the EU i2010 initiative, will be crucial to stimulate further progress. Ireland has improved its performance with regard to the transposition of EU legislation. However, Ireland has an above average number of infringement procedures.

16. In general, Ireland has succeeded in implementing measures to deliver on the micro-economic commitments expressed in its NRP. There has been a good policy response to reducing emissions and the Commission considers this point to watch is no longer valid. It is now important to continue this approach and to take action. There has been good progress shown towards reaching Ireland's 2013 R&D targets but neither a target nor indicative expenditure forecasts have been given for 2010 and therefore the Commission considers this point to watch as still valid.

Employment policies

17. Ireland has sustained a strong labour market performance over the 2005-07 period, with employment rates having risen close to or above the EU employment targets, employment growth maintained, including significant inward migration, and unemployment rates which remain amongst the lowest in the EU**.** Progress over the 2005-2007 period with regard to the implementation of policies to address the key labour market challenges, notably the challenge of sustaining high employment and low unemployment and ensuring an adequate labour supply identified by Ireland in the 2005 NRP, is generally good while the challenge of ensuring a high skilled adaptable workforce, including a focus on lifelong learning, remains substantial.

18. The Council highlighted in the employment area to the need to focus on: accelerating progress in increasing labour market participation, including by establishing a comprehensive childcare infrastructure, further developing the policy framework for the labour market and social integration of migrants and placing a particular emphasis on support to older and low-skilled workers.

19. Ireland has initiated some small-scale pilot projects aimed at extending the preventive approach, which has been effective in addressing the needs of the registered unemployed, to other groups (against a background where employment rates amongst lone parents, people with disability and other inactive groups needs to increase) but there is no clear timetable for implementation. The National Childcare Investment Programme 2006-2010 continues to be rolled out while a Community Childcare Subvention Scheme to take effect from 2008 has been announced. This scheme should help to address issues of affordability of childcare for the lowest-income families but the cost of childcare generally remains comparatively high.

20. A Minister with specific responsibility for Integration Policy has been appointed and there are plans to launch a Task Force on Integration in 2008 but substantive measures in areas such as language training are yet to materialise.

21. The appointment of a Minister with responsibility for overseeing a coordinated approach to Life-Long Learning is a welcome development since this is an area where Ireland's performance lags behind many other EU member states. A National Skills Strategy to 2020, published in March 2007, sets out high-level objectives covering upskilling, second level education completion levels and progression to

third level education but the necessary detailed implementation plan for this Strategy has yet to be developed, and it remains to be seen whether the response will be sufficient to bring the level of participation in life-long learning, 7.5% in 2006, up to the EU target of 12.5%.

22. Overall, Ireland addresses flexicurity in an integrated way. Skills segmentation is a problem but is recognised by the government. The National Skills Strategy endeavours to address the significant upskilling and below EU average participation in life-long learning. Active labour market programmes are generally seen to be effective. The social partners are fully involved, with most developments in this area emerging from the consensus approach embodied in the latest Social Partnership Agreement, 'Towards 2016'.

23. In general, Ireland has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. Ireland addressed the points to watch in the employment area in some respects, but there is a need to establish clear timetables in key areas, including activation, integration and life-long learning in order to ensure that the pace of reforms is stepped up.

PART III: CONCLUSIONS

24. In the light of the 2007 Irish Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

25. Ireland has been making very good progress in implementing its National Reform Programme over the 2005-2007 period. Ireland has been showing good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

26. The Implementation Report shows a good policy response to the areas identified by the Council as requiring attention. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

27. Among the strengths of the Irish National Reform Programme and its implementation is the comprehensive and coherent national strategy. The document also highlights the usefulness of the Lisbon process through its role in focussing on the prioritisation and implementation of specific actions, and emphasising its key role in addressing the challenges and opportunities associated with globalisation.

28. It will be important for Ireland over the period of the National Reform Programme to focus on the following challenges for the future: speeding up progress in formulating concrete measures to reform pension arrangements; an intermediate target for R&D investment should be set for 2010; accelerating progress in increasing labour market participation, including by establishing a comprehensive childcare infrastructure; further developing the policy framework for the labour market and social integration of migrants and placing a particular emphasis on support to older and low-skilled workers; and developments in the housing market, affecting short and medium-term growth, should be carefully monitored.

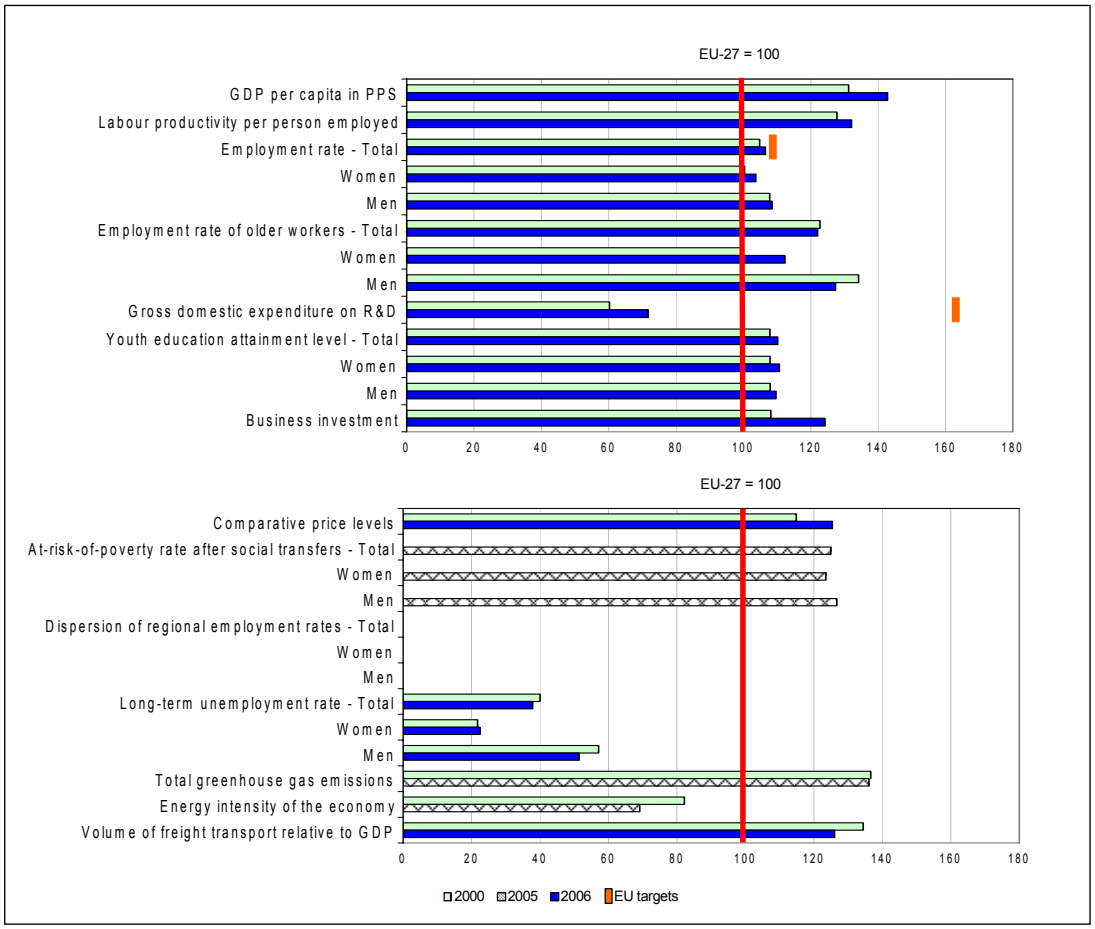
PART IV: STATISTICAL GRAPHS AND DATA

IRELAND

		IE						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		131.2	141.1	142.4	144.0	142.8		100.0	100.0	100.0	
Labour productivity per person employed		127.8	135.1	134.9	133.8	132.1		100.0	100.0	100.0	
Employment rate	Total	65.2	65.5	66.3	67.6	68.6	70.0	62.2	63.4p	64.4p	70.0
	Women	53.9	55.7	56.5	58.3	59.3		53.7	56.2p	57.2p	
	Men	76.3	75.2	75.9	76.9	77.7		70.8	70.8p	71.6p	
Employment rate of older workers	Total	45.3	49.0	49.5	51.6	53.1		36.9	42.3p	43.5p	
	Women	27.2	33.1	33.7	37.3	39.1		27.4	33.5p	34.8p	
	Men	63.2	64.6	65.0	65.7	67.0		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.12e	1.17	1.24	1.26	1.32p	*	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	82.6	85.1p	85.3p	85.8p	85.7		76.6	77.4	77.8	
	Women	85.6	88.5p	88.4p	88.9p	89.3		79.3	80.1	80.7	
	Men	79.7	81.6p	82.3p	82.6p	82.0		73.8	74.7	74.8	
Comparative price levels		114.9	126.4	125.6	124.9	125.4		100.0	100.0	100.0	
Business investment		19.9	18.5	20.0	22.6	22.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	20.0	20.0b	21.0	20.0	:		:	16.0e	:	
	Women	21.0	21.0b	23.0	21.0	:		:	17.0e	:	
	Men	19.0	19.0b	19.0	19.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	1.6	1.5	1.6	1.5	1.4		4.0	4.1p	3.7p	
	Women	1.0	1.0	1.0	0.8	0.9		4.6	4.5p	4.0p	
	Men	2.0	1.9	2.0	1.9	1.8		3.5	3.8p	3.5p	
Total greenhouse gas emissions		123.9	123.4	123.1	125.4	:		90.7	92.1	:	
Energy intensity of the economy		175.1	155.2	158.8	143.9	:		213.1	208.1	:	
Volume of freight transport relative to GDP		133.2	143.1	149.8	146.7	134.5		99.1e	105.4e	106.7e	

* National target: 2,5% (2013) of the Gross National Product (GNP)

PERFORMANCE COMPARED TO EU-27



Greece

1. Greece has experienced strong economic growth, averaging 4% in the years 2005-2007, with labour productivity growth clearly above the EU average. GDP per capita stands at 96.9% of the EU average. With job creation generally low, the employment rate (61% in 2006) remains far below the Lisbon target, particularly for women and older workers. Unemployment is decreasing (8.9% in 2006), but remains high, particularly for young people. The government deficit was reduced to 2½% of GDP in 2006 from 5.1% of GDP in 2005.

2. Greece faces high inflation pressures originating from a mixture of growth above potential and product market rigidities, while the worsening competitive position of the country creates high external imbalances. Despite labour shortages in specific sectors, unemployment remains high suggesting labour market rigidities and possible skill mismatches. Social security and pension reforms, a more efficient and transparent tax system, and the tackling of administrative malpractice could release resources which could be used to invest in human capital and active labour market policies. Efforts to transform undeclared work into formal employment would enhance the quality and sustainability of public finances and market efficiency.

PART I: GENERAL ASSESSMENT

3. Overall, the Greek 2007 Implementation Report has shown steady progress on implementing the 2005 National Reform Programme (NRP). The pace of progress in some fields appears to have accelerated slightly over the last year.

4. There has been some progress in responding to the four country-specific recommendations adopted by the Council. In the macro-economic domain, good progress has been made to consolidate public finances but more progress is needed to ensure its long-term fiscal sustainability. Progress in the micro-economic and employment areas has been partial. With regard to public administration reform, the initial steps taken are encouraging.

5. With regard to the other areas on which the Council concluded Greece should focus, as well as on the 2006 Spring European Council commitments, there has been some progress.

6. The Implementation Report does not specifically address the recommendations issued to the euro area countries, but there have been relevant developments. Greece has made good progress with budgetary consolidation, but less progress improving the quality of public finances. Additional action is necessary to strengthen competition in professional services, to promote labour mobility and improve flexibility and security in the labour market.

7. Consultation and efforts to develop ownership of the NRP by central and local governments and the social partners have been reinforced. The NRP and the 2007 Implementation Report appear to be the result of substantial dialogue between government bodies, and social partners. The Greek Parliament has also been involved. A Lisbon observatory has been set up and delivered a report in 2007. Links

between the governance of the implementation of the NRP and the programmes under the structural and cohesion funds are very strong. Earmarking of Structural Funding for Growth and Jobs objectives is being applied satisfactorily, with the Structural Funds being the driving force behind important reforms in employment and education, public administration reform, improvements to the business environment, competitiveness and regional development, and environmental protection.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. Over the 2005-2007 period, Greece has made good progress on its macro-economic challenge of fiscal consolidation. The newly elected Greek government emphasises fiscal balance and the long-term fiscal sustainability of public finances. However, more is needed to ensure the long-term fiscal sustainability of its public finances. Moreover, Greece's inflation rate and current account deficit are both amongst the highest in the euro area.

9. The Council recommended Greece to: ensure the continuation of fiscal consolidation and debt reduction and fix a timetable for the implementation of pension reform with a view to improving long-term fiscal sustainability. Fiscal consolidation began in 2004 and has made good progress - the excessive deficit procedure against Greece was abrogated in June 2007 and the government deficit has shrunk nearly 5 percentage points of GDP, to 2½% of GDP in 2006. However, use of temporary revenue measures and poor control over some items of public expenditure, particularly current primary expenditure, is a weakness. According to the Implementation Report, fiscal consolidation will continue and lead to a balanced budget by 2010. The 2008 draft budget projects that the general government deficit in 2008 will be 1.6% of GDP. Measures have been put in place to improve tax collection, intensify the fight against tax evasion and broaden the tax base. However, progress to ensure the long-term sustainability of public finances has been limited. Although Greece has declared it a high priority, the implementation of relevant reforms has been postponed. The Implementation Report stresses that the new government now has the opportunity to make good progress; public consultation and the Advisers Committee established to study the social security and pension system are expected to deliver first results and proposals before the end of 2007. The government has announced that reform of the pension system will begin by summer 2008.

10. In general, Greece has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. There has been good fiscal consolidation, but Greece still has to ensure the long-term sustainability of public finances. There has therefore been some progress meeting the country-specific recommendation on fiscal consolidation, debt reduction and pension reform for long-term fiscal sustainability. Inflationary pressures and external imbalances are a cause for concern.

Micro-economic policies

11. The 2005-2007 NRP considered the following to be key micro-economic challenges: strengthening its business environment, developing a knowledge society, environmental and sustainable development, and public administration modernisation. Progress in addressing these challenges has been mixed.

12. Energy sector reform is progressing well. The EU legislative framework has been transposed into national law and infrastructure is improving. However, the electricity incumbent has a strong market position. Transposition of the regulatory framework for electronic communications has been completed and competition in fixed telephony reinforced. Competition and lower prices have led broadband penetration to take off, facilitated by the government's Digital Strategy initiatives. The Competition Authority has been reinforced and progress made with privatisations. However, implementation of the Services Directive is slow and regulations covering professional services remain amongst the most restrictive in the EU. There are some important delayed measures, including the national land use plan.

13. Some progress has been made to set up a regulatory framework for the environment and the sustainable use of resources; however, infrastructure and enforcement of integrated waste management, waste water and biodiversity protection is needed. Strong private interest is responding to a more favourable framework and developing renewable energy sources. Climate changing emissions were already above the Kyoto target in 2005 and are growing fast. Additional measures to meet Greece's Kyoto target are needed.

14. The Council recommended Greece to modernise its public administration by building up effective regulatory, control and enforcement capacities, and ensuring an effective use of Structural Funds. A specific Structural Funds Operational Programme is now in place to assist Greece in this task. Better regulation is being improved by the gradual introduction of impact assessment, codification and simplification of legislation, as well as actions to reduce administrative burdens, for which a 25% reduction target has been set for 2013. Development of e-Government is more advanced, supported by a comprehensive Digital Strategy.

15. The Council also highlighted the need to focus on R&D, the transposition of internal market legislation and progress towards the 2006 Spring European Council SME policy targets. Actions to foster R&D and innovation depend significantly on Structural Funds financing over 2007-2013. The emphasis on innovation poles is promising but, and in spite of some encouraging signs, the predominance of family-owned SMEs and the economy's service orientation does not facilitate a rapid increase of private R&D investment. The R&D expenditure target of 1.5% of GDP has been postponed from 2010 to 2015. A bill has been submitted to parliament to improve R&D governance, but it still has to be adopted. Implementation of internal market legislation has improved remarkably, but the transposition deficit remains high. Some reform of public procurement has been achieved, but many problems remain which hamper projects financed by the Structural Funds.

16. Greece has not fully addressed the Spring 2006 European Council priority area aimed at improving the business environment. Key measures (e.g. creation of the

General Commercial Registry) have not been completed and the average business start-up time is estimated at around one month. Simplification in setting up and licensing has taken place in some sectors and a new bankruptcy code and an update of company law have been adopted. Access to finance has been improved.

17. Greece has partially succeeded in implementing measures to deliver on the micro-economic commitments expressed in its NRP. The response to the country specific recommendation on modernising public administration is in a preparatory phase. Progress regarding the promoting R&D, improving the transposition of internal market legislation, and in reaching the SME policy targets set by the Spring 2006 European Council is limited, pointing to the need to accelerate reform implementation. Moreover, additional action is necessary to strengthen competition in professional services, to protect the environment and to curb greenhouse gas emissions.

Employment policies

18. Good macro-economic performance has helped the employment rate increase to 61% in 2006 from 59.4% in 2004. Nevertheless, employment is well below EU employment targets. Unemployment, while declining, disproportionably affects the young and women. Initiatives to strengthen active labour market policies, enhance skills and promote employment are reported, but progress is mixed.

19. The Council recommended Greece to reinforce active labour market measures, fight undeclared work and speed up education and lifelong learning reforms. Current active labour policies are more focused on specific target groups and responsive to labour market needs, but efforts are needed to improve quality and coverage and transform public employment services into high quality one-stop shops for employment promotion. A 'Special Solidarity Fund' has been established to address long-term unemployment amongst older workers, but more comprehensive action is needed, including to help retain older workers in the labour market. A series of measures are planned to fight undeclared work, including reinforced controls on labour and the creation of a national committee against tax evasion. However, the magnitude of the problem requires better coordination of actions. Low wage earners appear to be taxed at a rate below the European average, but the adjusted implicit tax rate on employed labour is above the average. Tax policy aims to become more employment friendly: a recently announced tax reform package should reduce the tax burden for middle income brackets. However, the social security component of non-wage labour costs remains high. Employment protection is higher than the EU average, particularly for temporary workers. The Implementation Report refers to the establishment of a committee to study employment legislation and make proposals to ensure it is more adaptable.

20. Greece has set itself the target of allocating 5% of GDP to education by 2008, but it is not clear that expenditure on education is increasing. Policy aims to introduce ICT in schools, modernise the syllabi, and fight early school leaving. The share of early school leavers is slightly higher than the EU average. There has been progress in terms of developing legislation for higher education. On lifelong learning, a target has been set for reaching 6% of adult participation by 2015 and a dedicated agency for the promotion of continuous vocational training in enterprises will be set up. In

the Commission's opinion, the policies developed are a satisfactory response but now need to be implemented.

21. The Council also highlighted the need to implement policies to encourage women's participation in employment, and put in place a coherent active ageing strategy. Greece has taken action to promote female employability and reconcile work and family life, including targeted training and counselling measures. Nevertheless, the situation for the young and for older women continues to be difficult, suggesting more support may be needed for these groups, supported by the fact that employment and unemployment gender gaps remain significant. Further efforts are also needed to develop policies designed to help retain older workers stay in the labour market.

22. The pursuit of 'flexicurity' represents a major challenge for Greece; it has just begun to be addressed in an integrated way. The government has engaged in a broader dialogue with social partners, who approach this subject with caution. Expenditure on active labour market policies is low and decreasing. In this context the Greek authorities have set an expenditure target of 0.5% of GDP for 2015 and attention is now given to better matching labour supply with demand. Part-time work remains limited, despite recent measures to promote it in local government. The adult participation rate in life-long learning is extremely low. To address this, initial steps have been taken to implement a law linking education and training to employment. Progress so far seems modest, however, so implementation should be accelerated. Reform of the social security and pension systems to address weaknesses is the subject of public debate.

23. In general, Greece has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP and in addressing the country specific recommendations and points to watch.

PART III: CONCLUSIONS

24. In the light of the 2007 Greek Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

25. Greece has made steady progress in implementing its National Reform Programme over the period 2005-2007. Greece has shown some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

26. The Implementation Report shows there has been some policy response to the recommendations adopted by the Council. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

27. Amongst the strengths shown by the 2007 Greek Implementation Report are: good progress made to consolidate public finances, promoting female employment, implementing internal market legislation, and improving the business environment.

There are promising signs of progress to fix a timetable to implement pension reforms designed to improve long-term fiscal sustainability.

28. Policy areas in the Greek National Reform Programme where challenges need to be tackled with the highest priority are: long-term fiscal sustainability, implementation of the public administration reform agenda, the consolidation of active labour market policies, tackling high youth unemployment, tackling undeclared work and acceleration of education and life-long learning reforms. Against this background it is recommended that Greece:

- pursue fiscal consolidation and debt reduction, and proceeds rapidly with the implementation of the pension reform, with a view to improving long-term fiscal sustainability;

- implement the reform of its public administration, by building up effective regulatory, control and enforcement capacities, by modernising its human resources policy; and through effective use of the Structural Funds;

- within an integrated flexicurity approach, modernise employment protection including legislation, reduce the tax burden on labour, strengthen active labour market policies and transform undeclared work into formal employment;

- accelerate the implementation of reforms on education and lifelong learning, in order to improve quality and responsiveness to labour market needs, increase participation, and allow for a smooth transition into employment, particularly for the young.

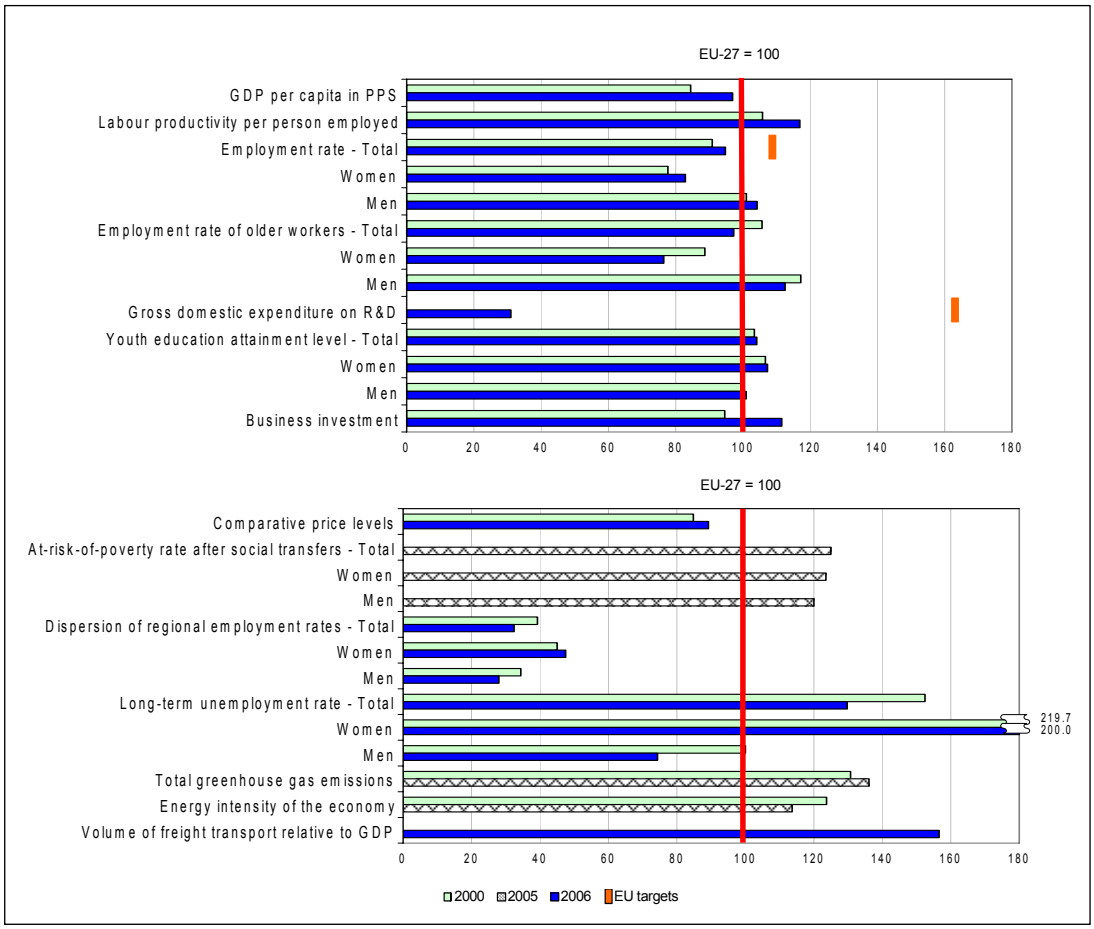
29. In addition, it will be important for Greece over the period of the National Reform Programme to focus on the following challenges: contain inflationary pressures and the current account deficit; accelerate efforts to set up a research and innovation strategy and increase investment in R&D; improve further the transposition of internal market legislation; speed up progress towards meeting the SME policy targets set by the 2006 Spring European Council; strengthen competition in the area of professional services; protect the environment by prioritising effective solid and water waste management and curb greenhouse gas emissions; encourage further female participation in employment; reduce early school leaving and put in place a coherent active ageing strategy.

PART IV: STATISTICAL GRAPHS AND DATA

GREECE

		GR						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		84.4	92.4	93.4	95.4	96.9f		100.0	100.0	100.0	
Labour productivity per person employed		105.8e	114.6e	112.8e	114.9e	116.9f		100.0	100.0	100.0	
Employment rate	Total	56.5	58.7	59.4	60.1	61.0	64.1	62.2	63.4p	64.4p	70.0
	Women	41.7	44.3	45.2	46.1	47.4		53.7	56.2p	57.2p	
	Men	71.5	73.4	73.7	74.2	74.6		70.8	70.8p	71.6p	
Employment rate of older workers	Total	39.0	41.3	39.4	41.6	42.3		36.9	42.3p	43.5p	
	Women	24.3	25.5	24.0	25.8	26.6		27.4	33.5p	34.8p	
	Men	55.2	58.7	56.4	58.8	59.2		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		:	0.58	0.55p	0.58	0.57	1.5	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	79.2	81.7	83.0	84.1	81.0p		76.6	77.4	77.8	
	Women	84.6	86.8	86.8	88.5	86.6p		79.3	80.1	80.7	
	Men	73.6	76.6	79.2	79.7	75.5p		73.8	74.7	74.8	
Comparative price levels		84.8	85.9	87.3	88.3	89.2		100.0	100.0	100.0	
Business investment		17.4	19.3	19.2	18.6	20.3f		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	20.0	21.0b	20.0	20.0	:		:	16.0e	:	
	Women	20.0	21.0b	21.0	21.0	:		:	17.0e	:	
	Men	19.0	20.0b	19.0	18.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	5.1	3.2	4.1	4.3	3.7		13.0	11.9	11.4	
	Women	9.0	6.5	8.3	8.4	7.7		20.0	16.8	16.2	
	Men	3.3	2.1	2.5	2.9	2.6		9.6	9.7	9.3	
Long-term unemployment rate	Total	6.1	5.3	5.6	5.1	4.8		4.0	4.1p	3.7p	
	Women	10.1	8.9	9.4	8.9	8.0		4.6	4.5p	4.0p	
	Men	3.5	3.0	3.0	2.6	2.6		3.5	3.8p	3.5p	
Total greenhouse gas emissions		118.6	123.6	123.9	125.4	:		90.7	92.1	:	
Energy intensity of the economy		263.6	247.8	240.6	236.5	:		213.1	208.1	:	
Volume of freight transport relative to GDP		:	108.0e	:	120.8	167.1		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Spain

1. The Spanish economy has been growing strongly at an average annual rate of 3.75% since the mid-1990s. Domestic demand has been strong, and employment growth highly dynamic, with Spain contributing almost half of the total job creation in the euro area since the mid-nineties. As a result, the unemployment rate has halved, to close to the EU average of around 8%. The employment rate has been rising steadily to 66%.

2. In parallel, a number of imbalances have emerged. The current account deficit reached 8.5% of GDP in 2006, reflecting, in part, insufficient export growth. Inflation remains high, due in part to structural factors related to the functioning of product and services markets. Inflation and low productivity growth continue to affect Spain's competitive position. In order to enhance productivity, the quantity and quality of physical, human, and knowledge capital will need to increase. Finally, strong job creation remains coupled with persistent labour market segmentation.

PART I: GENERAL ASSESSMENT

3. Overall, Spain has made good progress with implementing the 2005 National Reform Programme (NRP) over the 2005-2007 period.

4. Spain has responded to the country-specific recommendations adopted by the Council. There has been a limited response to increasing competition in the energy sector, although some progress has been made in addressing the security of supply. Progress in integrating training systems to provide a better response to labour market needs, and on modernising employment protection has been good but progress in reducing early school leaving is still insufficient.

5. With regard to the other areas on which Spain was asked to focus, there has been a some response in the macro-economic domain. The points to watch in the micro-economic and employment domains have been partially addressed. Better results are evident in raising skill levels and productivity. Despite measures put in place, progress towards the reduction of CO2 emissions may not be sufficient for Spain to meet the Kyoto target.

6. The Council concluded that Spain had adequately responded to the commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been good progress on the commitments in the priority action areas of knowledge, entrepreneurship and employment but limited progress in the area of energy.

7. Spain addresses the euro area recommendations in its latest Implementation Report. Examples include measures reported to improve the efficiency of public expenditure and measures to enhance competition in the services sector.

8. Consultation of the NRP at the level of regional and local governments and the social partners has been reinforced but ownership of the NRP remains limited. The involvement of stakeholders continues to be limited outside the employment field,

where there has been some cooperation with social partners. More information on timetables and budgetary implications of reforms would be welcome. The links between the governance of the implementation of the NRP and the programmes under the structural and cohesion funds are strong but the earmarking of structural funding for Growth and Jobs objectives needs to be reinforced particularly in Competitiveness regions. Significant support is foreseen for R&D, active labour policies, and improvement of human capital.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. Spain has made good progress over the 2005-2007 period with regard to the implementation of policies to address the macro-economic key challenges of macro-economic and budgetary stability in order to support real GDP convergence and reach the EU-25 average by 2010. In spite of some signs of deceleration, the growth rate of the Spanish economy remains above that of the euro area. Nevertheless, given the rapid increase of Spain's population, full convergence with the EU-25 in terms of per capita GDP will require additional efforts.

10. No macro-economic recommendations were issued for Spain. However, the Council referred to the need to contain inflation in the medium-term, as well as implementing the foreseen housing market measures so as to gradually reduce house price pressures in the medium-term, and pension and healthcare reforms which also impact favourably on long term fiscal sustainability.

11. There has been some progress in these areas. Measures have been designed to tackle the structural factors behind excessive inflation, namely prioritising public spending on R&D, education and infrastructure, ensuring budgetary stability, and increasing competition in certain sectors. Recent fluctuations of the inflation differential can be largely explained by exogenous factors of rather a transitory nature such as the effect associated with oil prices, which have a stronger impact on the Spanish economy than in other euro area countries. With regard to the reduction of pressure on housing prices, Spain has adopted a new law on Urban Land and implemented the Housing Plan 2005-2008 as well as approved several measures aiming at developing the rental market from the demand side. However, the current deceleration of housing prices seems to be more related to a drop in demand than to the measures implemented by the government in the rental market. Reforms have taken place to the pension system. The volume of the Social Security Reserve Fund has again been increased. The reform of the system adopted in 2006, will be implemented in January 2008, and aims at a better alignment between contributions and benefits. This has had a limited effect thus far on long-term fiscal sustainability. There has been a limited response in the area of the health care reform consisting of a reduction of spending on medicines but health care spending continues to increase at a rate well above of that of nominal GDP.

12. In general, Spain has succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. There has been limited progress in addressing the points to watch issued to Spain, with some progress on addressing the structural factors affecting the inflation differential, but more limited progress in the

other area. The Commission therefore considers that these issues merit additional focus. In addition, the increasing current account deficit is a matter for concern. With regard to the euro area recommendations in the macro-economic domain Spain's progress has been good.

Micro-economic policies

13. Progress on the implementation of measures in response to the micro-challenges identified by the Spanish NRP has continued over the last year. Good progress has been recorded in the area of R&D, business environment, and infrastructure, with more limited progress in the areas of competition, better regulation, and the environment.

14. The Council recommended Spain takes further measures to increase competition in the energy sector, notably by improving cross-border interconnection capacity to ensure security of supply. The measures planned now need to be fully implemented. However, a fundamental competition problem in the electricity market remains as the elimination of tariffs (in real terms) is not being pursued with sufficient urgency. The tariff increase in 2007 has been too modest to reflect the real cost of electricity generation and distribution, and to absorb the deficit accumulated in the regulated system. There has been good progress in enhancing the security of supply via an agreement to reinforce interconnection capacity with Portugal, but problems persist regarding interconnection capacity with France.

15. The Council also referred to the need to focus on raising competition in professional services and retail markets; improving the regulatory framework; and implementing environmental measures, in particular to reduce CO_2 emissions.

16. With regard to environmental measures, the recent national climate change strategy defines the framework for policy action to comply with the Kyoto Protocol. The significant number of planned initiatives will help contribute towards reaching the Kyoto targets but it appears further measures will also be required. On the need to raise competition in retail markets, no new information has been reported. Spain should sustain its on-going efforts to implement the Services Directive. Progress to increase competition in professional services has been limited. On better regulation, Spain has set a target for a 25% reduction in the administrative burden by 2012 and an Action Plan to facilitate this is envisaged.

17. Efforts to increase both the level and efficiency of R&D and innovation spending continue to be a strong point of the Spanish reform agenda, and in particular the improved coordination between central and regional government. All regions have R&D intensity targets for 2010. The achievement of the overall R&D target of 2% of GDP depends on whether the significant public funding effort will stimulate business spending. There are doubts concerning the return in terms of innovation output. Spain’s innovation system still needs substantial strengthening in areas like knowledge transfer between science and industry, fostering entrepreneurship, and on access to risk capital. Investment levels are increasing in the aim to develop an information society, but weak IT adoption rates persist, particularly among enterprises.

18. Spain is implementing policies to promote entrepreneurship education, to facilitate administrative processes for starting a business and to provide information on access to public procurement. Among Spain's regions the progress achieved on developing SME policies varies. Spain needs to address the high number of infringement cases and continue to decrease its transposition deficit.

19. Overall progress over the 2005-2007 period with regard to the implementation of policies to address the micro-economic challenges identified by Spain in the 2005 NRP is good. The country specific recommendations and points to watch in the micro-economic area have been only partially addressed and therefore remain valid. Progress with regard to the euro area recommendation on competition was limited.

Employment policies

20. There has been some progress over the 2005-2007 period with regard to the implementation of policies to address Spain's labour market challenges. Spain has already met its overall employment rate target of 66% three years early. Spain should now focus on attaining the EU employment rate target of 70% by 2010. While the female employment rate has risen, the employment gender gap remains one of the largest in the EU. The unemployment rate (8.5% in 2006) has fallen, and converged towards the EU27 average. The early school leaving rate has barely declined, and youth education attainment levels continue to be among the lowest in the EU.

21. The Council recommended Spain to modernise employment protection with a view to fostering flexibility and security in the labour market and counter segmentation. An agreement with the social partners in mid-2006 has helped bring down the number of fixed-term contracts by 2.6%. This is a welcome move which however will only have short-term effects. In the longer term, further measures may be needed, in particular to promote indefinite contracts and part time work.

22. The Council also recommended Spain to ensure the effective implementation of education reforms to reduce early school leaving and to integrate training systems. The new education law aims at fully integrating immigrant pupils, at reducing the rate of early school leaving, and improving some key competencies. However, the target set in the 2006 Implementation Report of almost halving the rate of early school leavers to 15% in 2010 is unlikely to be met. Legislation adopted in March 2007 to regulate the integration of occupational and vocational training systems should help raise quality and improve access to lifelong learning.

23. The Council highlighted the need for Spain to focus on: raising skill levels and productivity and integrating immigrants into the labour market; and increasing access to childcare. In spite of recent progress in productivity growth (0.8% in 2006) it remains well below the EU27 average. The number of workers participating in continuous training has increased from 10% in 2005 to 11.2% in 2006. To integrate immigrants into the labour market, Spain has a strategic plan for 2007-2010 that foresees a broad array of measures under four pillars. Measures have been announced to extend childcare services to all children aged 0-3 years which should help to bring Spain closer to meeting the EU target. However, the percentage of children under 3 years in childcare has risen only slightly (16.6%), and is well below the EU 33% target. Important regional disparities also persist in this field.

24. Spain partly addresses flexicurity in an integrated way. Some progress has been made to ensure training or job offers for all the unemployed, with activation rates increasing significantly. The social security system has been reformed by strengthening the link between contributions and benefits received, and extending the working life. Whereas there is good progress on active labour market policies and modern social security systems, implementation is still ongoing on lifelong learning legislation, and only moderate short-term effects are visible concerning contractual arrangements.

25. In general, Spain has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. Measures have been taken to address the country specific recommendations. The points to watch have been partially addressed. It is encouraging that labour market reforms have been approved in the framework of the social dialogue with a high degree of agreement of all social partners. Some progress was achieved with regard to the euro area recommendation in the employment domain.

PART III. CONCLUSIONS

26. In the light of Spain's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

27. Spain has made good progress with implementing its National Reform Programme over the 2005-2007 period. Spain has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in three of the four priority action areas.

28. The Implementation Report shows a good policy response to the recommendations adopted by the Council. With regard to the other areas on which Spain was asked to focus, there has been a limited response in the macro-economic domain. The points to watch in the micro-economic and employment domains have been partially addressed. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

29. Among the strengths shown by Spain’s 2007 Implementation Report are: a faster than targeted reduction of government debt; good progress on implementation of the R&D and innovation plan; and satisfactory progress towards the employment rate objective, in particular for female employment.

30. The policy areas in the Spanish National Reform Programme where challenges now need to be tackled with the highest priority are improving competition in electricity markets and further improvements to education and training. Against this background it is recommended that Spain:

- take further measures to increase competition in the energy sector, notably by eliminating the distorting price setting mechanisms and improving cross-border interconnection capacity to ensure security of supply;

- ensure the effective implementation of education reforms, also at regional level, to reduce early school leaving.

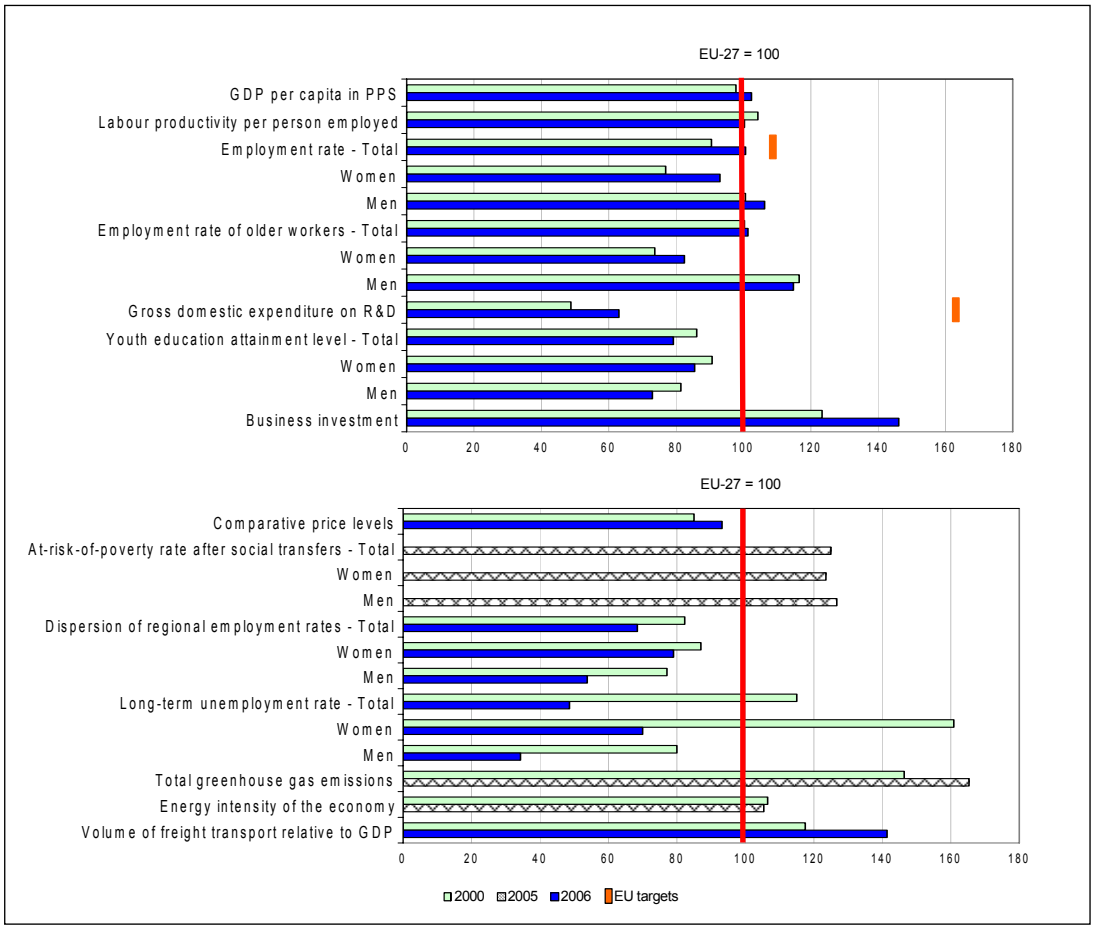
31. In addition, it will be important for Spain over the period of the National Reform Programme to focus on the following challenges: contain the current account deficit and inflationary pressures and monitor developments in the housing market; raising competition in professional services and retail markets; improving the regulatory framework; implementing environmental measures, in particular to reduce CO2 emissions; further modernise employment protection, including legislation, in order to foster flexicurity in the labour market to counter segmentation and promote the attractiveness of part-time work; raising productivity by raising skill levels and innovation; integrating immigrants into the labour market; further increase of access to childcare; and implement pension and healthcare reforms so as to improve long term fiscal sustainability.

PART IV: STATISTICAL GRAPHS AND DATA

SPAIN

		ES						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		97.8	101.4	100.9	102.5	102.4		100.0	100.0	100.0	
Labour productivity per person employed		104.3	103.7	101.5	101.3	100.3		100.0	100.0	100.0	
Employment rate	Total	56.3	59.8	61.1	63.3b	64.8	66.0	62.2	63.4p	64.4p	70.0
	Women	41.3	46.3	48.3	51.2b	53.2		53.7	56.2p	57.2p	
	Men	71.2	73.2	73.8	75.2b	76.1		70.8	70.8p	71.6p	
Employment rate of older workers	Total	37.0	40.7	41.3	43.1b	44.1		36.9	42.3p	43.5p	
	Women	20.2	23.3	24.6	27.4b	28.7		27.4	33.5p	34.8p	
	Men	54.9	59.2	58.9	59.7b	60.4		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.91	1.05	1.06	1.12	1.16p	2.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	66.0	62.2	61.2	61.8	61.6		76.6	77.4	77.8	
	Women	71.9	69.2	68.4	68.5	69.0		79.3	80.1	80.7	
	Men	60.1	55.5	54.4	55.4	54.6		73.8	74.7	74.8	
Comparative price levels		85.0	88.3	90.9	92.0	93.2		100.0	100.0	100.0	
Business investment		22.7	23.6	24.7	25.8	26.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	18.0	19.0	20.0b	20.0	:		:	16.0e	:	
	Women	19.0	20.0	21.0b	21.0	:		:	17.0e	:	
	Men	17.0	18.0	19.0b	19.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	10.7	9.0	8.7	8.3	7.8		13.0	11.9	11.4	
	Women	17.4	14.5	14.8	13.8	12.8		20.0	16.8	16.2	
	Men	7.4	6.1	5.5	5.3	5.0		9.6	9.7	9.3	
Long-term unemployment rate	Total	4.6	3.7	3.4	2.2b	1.8		4.0	4.1p	3.7p	
	Women	7.4	5.7	5.0	3.4b	2.8		4.6	4.5p	4.0p	
	Men	2.8	2.4	2.2	1.4b	1.2		3.5	3.8p	3.5p	
Total greenhouse gas emissions		132.8	141.5	146.9	152.3	:		90.7	92.1	:	
Energy intensity of the economy		227.0	219.7	222.2	219.2	:		213.1	208.1	:	
Volume of freight transport relative to GDP		116.4	135.2	149.1b	151.4	150.9		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



France

1. In 2006 GDP grew by 2.0%, lower than the 2.7% growth in the euro area. Growth is expected to be 1.9% in 2007. Growth continues to be supported by domestic demand, especially private consumption, and hampered by a negative contribution of net exports over the past five years. The employment rate (63% in 2006) remains low, particularly for the young (29.3%) and older workers (37.6). Unemployment (9.1% in 2006) has improved markedly over the year to a forecasted 8.6% but remains well above the euro area average.

2. Reforms under discussion address key challenges that France has to face in a context of an ageing population, high unemployment and a lack of competitiveness. These reforms aim at increasing potential growth and may, in the long term, improve the sustainability of public finances. However, the measures thus far adopted (including tax cuts in the summer 2007 "fiscal package") will slow down consolidation in public finances, and the envisaged structural reforms entail significant short term costs. Achieving a balanced budget has been delayed until 2012 in the case of GDP growth below 2.5%, despite France's commitment to reach this goal by 2010.

PART I: GENERAL ASSESSMENT

3. Overall, the French 2007 Implementation Report shows steady progress in implementing the National Reform Programme (NRP) over the 2005-2007 period, but more significantly some key policy orientations have been, or are in the process of being revised. Following presidential and legislative elections, France has stated its commitment to boost economic growth and job creation through structural reforms covering a wide range of areas including the labour market, pension system, social security financing, environmental sustainability, and competition in goods and services. The new French government presents a noticeably modified strategy to modernise micro-economic and labour market policies to increase growth and to reduce unemployment.

4. The response to the country-specific recommendations adopted by the Council has been limited. Progress on public finance has not been in line with the path set out in the latest Stability Programme update. Progress in opening up competition in the energy sector is faltering because of regulated tariff systems on the domestic market. The response to the need to enhance lifelong learning and modernise employment protection, has been addressed in policy announcements committing to a major reform on labour law and the vocational training system. These measures now require implementation.

5. With regard to the other areas on which France was asked to focus, an important reform has been undertaken with regard to stimulating and supporting entrepreneurship and young businesses. There has been some progress in strengthening competition in regulated trades and professions but further relaxing of restrictions is necessary. Although policies for better regulation have been enhanced, a wider use of impact assessments is needed. Measures to increase activation and

help the return to work need to be sustained in order to further increase labour supply.

6. There has been progress on some of the commitments agreed at the 2006 Spring European Council with an end 2007 deadline, in particular concerning investment in knowledge and innovation, unlocking the business potential of SMEs, and in the field of energy. The Implementation Report does not specifically address the recommendations issued to the euro area countries, but there have been relevant developments. France has improved its framework for public finances monitoring through the full implementation of the LOLF (*Loi Organique relative aux Lois de Finances*) with positive effects on the quality of public finances, while progress in terms of sustainability of public finance has been more limited. Progress in response to the euro area recommendations in the areas of competition in services and of improving flexibility and security on labour markets inter alia by promoting labour mobility is limited.

7. Consultation and efforts to develop ownership of reform at the level of local government and the social partners have been reinforced. The social partners have been invited to negotiate on sensitive labour market reforms, on which outcomes are awaited. Links between the governance and implementation of the NRP and the programmes under the structural funds are fairly strong. Earmarking of structural funding for Growth and Jobs objectives is satisfactory. However, the NRP and its Implementation Report do not provide a comprehensive overview of all announced reform measures.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The structural public deficit improved from 3.5% of GDP in 2005 to 2.5% of GDP in 2007. Both the fiscal package adopted in August 2007, largely consisting of tax reductions, and the draft Finance Act for 2008, indicate that in 2007 and 2008 the reduction with regard to the public deficit and the debt-to-GDP ratio will stall compared to the path defined in the December 2006 update of the Stability Programme.

9. The Council recommended that France should ensure the sustainability of its public finances, notably through continued budgetary consolidation and debt reduction. France has taken a number of actions in this area. A tighter set of rules for state expenditure has been established (a decrease in volume by 1% in volume in 2008), to be followed by a stabilization in volume in 2008 (but applied to a broader category of expenditure). Furthermore, France has launched a general revision of public policies based on the implementation of the LOLF, which entails annual assessments of the efficiency of public policies, ministerial reform strategies, as well as audits for modernising the State. However, the state finance rule may not be fully achieved, and the expenditure rules in the other administration sub-sectors (local government and social security) are either, limited, nonbinding or not fully implemented. In addition, the 2007 Implementation Report, while underlining that the consolidation of public finances is necessary in order to create budgetary margins for growth-supporting expenditures, envisages broad structural reforms on pensions, healthcare

financing, global taxes, and administration organisation. Some of these reforms carry short-term budgetary costs and will have a positive impact only in the medium to long term.

10. France has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. However, in 2007, the budgetary consolidation drive has slowed. The tax decreases and the measures in the draft budget imply that consolidation will not significantly progress in 2008. Achieving a balanced budget has been delayed until 2012 in the case of GDP growth below 2.5%, despite France's commitment to reach this goal by 2010.

Micro-economic policies

11. Over 2005-2007 France has made progress to address the micro-economic challenges outlined in its NRP.

12. The Council recommended that France improves the framework for competition in the gas, electricity and rail freight sectors. Despite some positive steps, the actual degree of liberalisation remains limited. Despite the full legal opening on 1st July 2007 of the domestic gas and electricity market, a regulated tariff system remains imposed by law. As a consequence real prices are below market prices, favouring incumbents, and limiting possibility for successful market entry. In the rail freight sector the market share of new operators increased from less than 1% in 2006 to between 3% and 5% in 2007, but more effective unbundling between infrastructure and operations should be vigorously pursued. Further measures to promote a greater liberalisation are not yet in place and the legal competences and administrative means of the regulator remain insufficient. Therefore the announcement of an independent railway regulator is an initial step.

13. The Council also underlined that it was important to improve regulation, to strengthen competition in the regulated trades and professions, and to encourage entrepreneurship. In the field of better regulation, France has set an administrative burden reduction target of 20% and is planning to finalize a mapping exercise in March 2008. Its codification activities are progressing well but progress on simplification remains quite slow. An explicit and comprehensive better regulation strategy is needed, in particular in view of greatly increasing the use of impact assessments and of developing more uniform consultation mechanisms.

14. Despite the relaxation of restrictions in some professions, the legal professions, especially notaries and pharmacies, remain heavily regulated, and the most serious restrictions (fixed prices and quantitative entry restrictions) are contained in state law. Some measures have recently been announced to promote competition in the retail sector. There has been a good policy response on entrepreneurship and SME policy. Many measures have been taken over the last 3 years, such as the simplification of procedures, the removal of some taxes, and financial schemes to support the creation and development of SMEs. Particularly relevant is the recent emphasis put on the encouragement of the growth of SMEs, the promotion of ICT use, the increase of financial means for small innovative companies, and measures supporting internationalisation. France has improved its performance with regard to the timely transposition of internal market legislation, but needs to reduce the high number of infringement proceedings. France should continue implementing

entrepreneurship promotion measures and to tackle more vigorously the issue of business transfer.

15. Over the past two years R&D and innovation strategies have undergone considerable reform with good progress being made. Public spending on research has increased in nominal terms since 2004. Fiscal incentives and conditions for developing public-private partnerships have been improved. Regions are also encouraged to establish their own innovation strategies. In view of the recent reforms, which give more autonomy to universities, and complement the reforms in the research domain, the role and functioning of public research organizations and better career opportunities for researchers in the private sector should be examined.

16. Industrial policy remains an important priority in the NRP with a focus on the activity of the 71 *Pôles de Compétitivité.* Measures in the ICT field have begun to yield concrete results.

17. In general, France has partially succeeded in implementing measures to deliver on micro-economic challenges and commitments expressed in the NRP. Greater efforts are needed to increase competition in the gas, electricity and rail freight sectors and thus this recommendation remains valid. France has introduced significant reforms in R&D and innovation, and has supported entrepreneurship and SMEs. Therefore this point to watch is no longer merited. However, further reforms are needed in the fields of better regulation and the regulated trades and professions.

Employment policies

18. Relatively low employment, high structural unemployment, rigid labour legislation, and labour market segmentation (with employment turnover concentrated on particular groups) have remained key challenges over the 2005-2007 period. Limited progress has been made in addressing these issues. Low skilled young people have been hit hardest by labour market segmentation, with high unemployment rates as a result. Older workers continue to retire early. Labour market policy has targeted those vulnerable in the labour market through a social cohesion programme (for example continued reductions in social security contributions on low paid work), with uneven policies to ease employment protection legislation and improve the access to and efficiency of lifelong learning. Reflecting the lag with which employment reacts to economic recovery, record unemployment has now started to come down but employment performance remains unsatisfactory. In this context, France recently announced a global labour market reform that embraces structural revision of labour law, public employment services, unemployment insurance and vocational training.

19. The Council recommended that France should modernise its employment protection and improve lifelong learning. Previously introduced reforms of labour contracts seem to have been superseded by the new government's announced global flexicurity reform which respond to the Council recommendations. In order to tackle labour market segmentation and modernise employment protection, the government has asked the social partners to consider a review of labour contracts. It has also proposed the merger of the job seekers placement and reimbursement services, in order to improve efficiency. Alongside existing measures aiming to make work pay such as the "Prime pour l'emploi" and the "Revenu de solidarité active", a revision of

the unemployment insurance system is anticipated. A shake-up of the vocational training system has been announced for 2008. This entails a review of the 2004 law on lifelong learning and the currently non-transferable individual right to training. It involves the social partners and the regions, who have gained responsibilities in the field of training, and is to remedy the fact that in spite of important investments and an individual right to training, 60% of French workers do not participate in vocational training.

20. The Council also highlighted the need for France to focus on further steps to increase labour supply. This remains relevant, given the low number of hours worked in the economy and the persistent low employment rate. France has reduced taxes on overtime work and exempted working students from income taxes. As part of the social security budget review, it is proposed to make company early retirement schemes more expensive and to phase out the exemption of job-seeking obligations for older unemployed workers. The Implementation Report acknowledges the need for sustained activation of people on benefits, and the government has established new pilot exercises.

21. Since the beginning of 2007, France has been moving towards an integrated flexicurity approach, with a number of initiatives. The weak points remain the differentiated and complex employment legislation which provides for a segmented labour market with insiders and outsiders and that expenditure on active labour market policies has been decreasing since 2000. A recent revision of the unemployment insurance system, with the aim of making work pay, has been announced. Efforts are being made to reform the lifelong leaning system in order to improve the currently non-transferable individual right to training. Social partners are now increasingly being consulted on, for example, measures to address employment legislation and transitions on the labour market.

22. In general, France has not yet succeeded reducing labour market segmentation, or achieved a more efficient and inclusive system of lifelong learning. However, the Implementation Report does announce major labour market reforms and sets 2012 targets for full employment and social inclusion. By embracing a comprehensive flexicurity approach to labour market reform, France has advanced new policy orientations that respond well to the recommendations, with reform of contractual arrangements currently under negotiation by the social partners and dialogue on a renewed vocational training system scheduled for 2008. This constitutes a promising policy response.

PART III: CONCLUSIONS

23. In the light of France's 2007 Implementation Report and the Commission's assessment of progress made in implementation of key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

24. France has made steady progress in implementing its National Reform Programme over the 2005-2007 period. France has shown some progress in fulfilling the commitment agreed by the 2006 Spring European Council in the four priority action areas.

25. The Implementation Report shows a limited policy response to the recommendations issued to France by the Council. There has been some policy response on the other areas identified in the Council conclusions as requiring attention in particular an important reform has been undertaken with regard to stimulating and supporting entrepreneurship and young businesses. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

26. Among the strengths shown by French 2007 Implementation Report are: the reform of R&D and innovation strategies, the concrete results of measures in the area of ICT, and the announced, comprehensive set of measures to improve the functioning of the labour market, including through changes in legislation.

27. The Implementation Report presents a noticeably modified strategy in which employment is to become a factor of economic policy aiming at enhanced growth. The extent to which increased competition is integrated in this new policy framework is, as yet, less clear. It is important that France strengthens its budgetary efforts in order to simultaneously implement a concerted reform strategy and further consolidates public finances. Significant or sustained further measures are needed to achieve budgetary consolidation, to increase competition in network industries and to improve labour market performance. Against this background, it is recommended that France:

- ensures the sustainability of public finances, taking into account the ageing of the population, by considerably strengthening budgetary consolidation and debt reduction, and with a view to achieving a balanced budget in 2010. The negotiation on pension systems scheduled for 2008 will have to build on the gains made following the introduction of the 2003 reform;

- improves the framework for competition in the gas, electricity and rail freight sectors;

- within an integrated flexicurity approach, improves the efficiency of lifelong learning and modernises employment protection, in order notably to combat labour market segmentation among contract types, and make it easier to switch between fixed term contracts and permanent contracts.

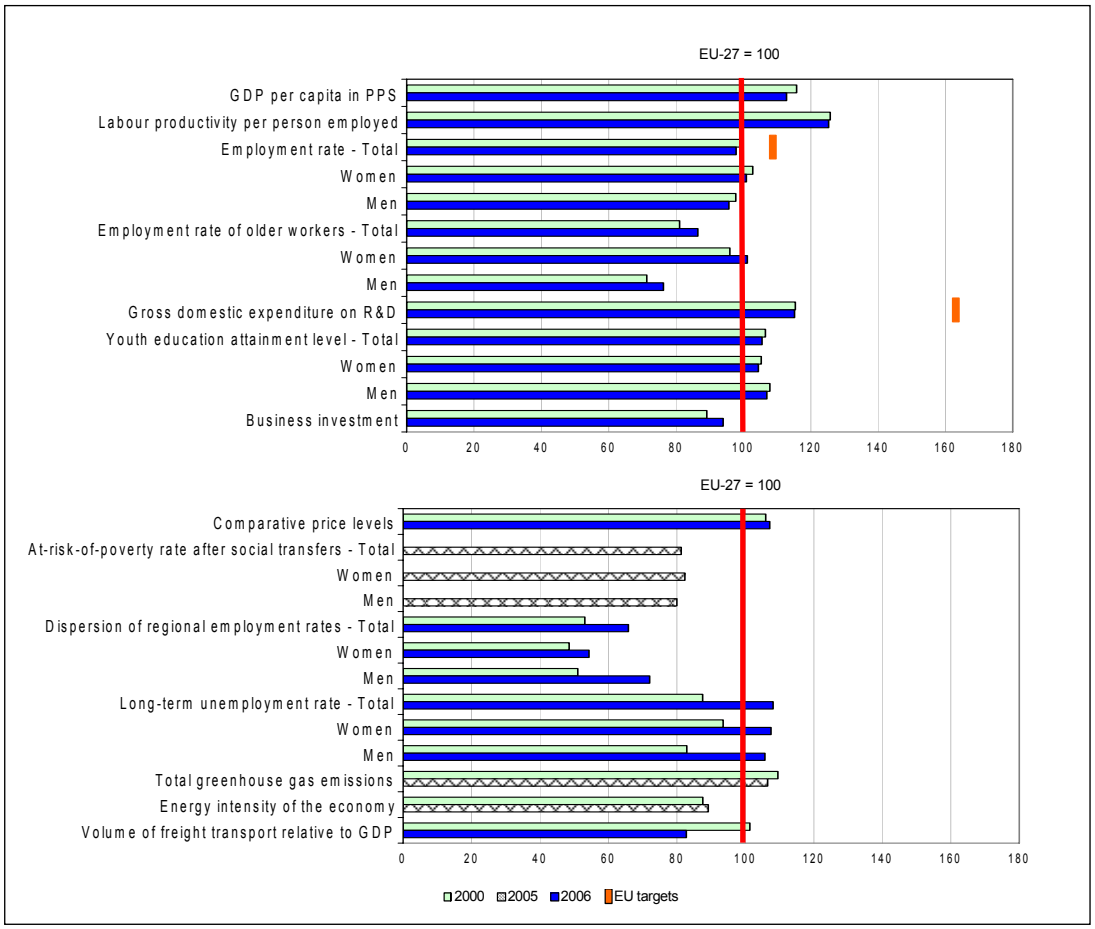
28. In addition, it will be important for France over the period of the National Reform Programme to focus on the following challenges: further strengthening competition in regulated trades and professions, further enhancing better regulation policies by including impact assessments; continuing to increase labour supply and making work pay.

PART IV: STATISTICAL GRAPHS AND DATA

FRANCE

		FR						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		115.8	112.3	112.1	114.2	112.8		100.0	100.0	100.0	
Labour productivity per person employed		125.8	121.5	122.2	125.4	125.3		100.0	100.0	100.0	
Employment rate	Total	62.1	63.3	63.1	63.1	63.0p	:	62.2	63.4p	64.4p	70.0
	Women	55.2	57.2	57.4	57.6	57.7p		53.7	56.2p	57.2p	
	Men	69.2	69.4	68.9	68.8	68.5p		70.8	70.8p	71.6p	
Employment rate of older workers	Total	29.9	36.8	37.3	37.9	37.6p		36.9	42.3p	43.5p	
	Women	26.3	32.9	33.8	35.2	35.2p		27.4	33.5p	34.8p	
	Men	33.6	40.9	41.0	40.7	40.1p		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		2.15	2.17	2.15	2.13p	2.12p	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	81.6	81.8b	81.4	82.6	82.1p		76.6	77.4	77.8	
	Women	83.5	83.3b	83.0	85.0	84.3p		79.3	80.1	80.7	
	Men	79.6	80.4b	79.7	80.1	80.0p		73.8	74.7	74.8	
Comparative price levels		105.9	110.0	110.5	107.6	107.1		100.0	100.0	100.0	
Business investment		16.4	15.8	16.2	16.5	17.1		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	16.0	12.0	13.0b	13.0	:		:	16.0e	:	
	Women	16.0	13.0	14.0b	14.0	:		:	17.0e	:	
	Men	15.0	12.0	13.0b	12.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	6.9	7.2	7.1	7.3	7.5		13.0	11.9	11.4	
	Women	9.7	8.9	8.7	9.4	8.8		20.0	16.8	16.2	
	Men	4.9	6.2	5.9	5.8	6.7		9.6	9.7	9.3	
Long-term unemployment rate	Total	3.5	3.7p	3.9p	4.0p	4.0p		4.0	4.1p	3.7p	
	Women	4.3	4.1p	4.3p	4.5p	4.3p		4.6	4.5p	4.0p	
	Men	2.9	3.4p	3.5p	3.5p	3.7p		3.5	3.8p	3.5p	
Total greenhouse gas emissions		99.3	98.6	98.6	98.1	:		90.7	92.1	:	
Energy intensity of the economy		186.6	188.5	187.0	185.5	:		213.1	208.1	:	
Volume of freight transport relative to GDP		100.4	92.9	93.2	87.9	88.3		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Italy

1. After a period of protracted slow growth, the situation of the Italian economy improved in 2006. Real GDP grew by 1.9%, the highest rate since 2000, but still below the euro area average. Prospects for 2007 appear still favourable, even though the growth momentum is losing vigour. Employment continues to rise and the unemployment rate decreased to 5.7% in June 2007. Nevertheless, the employment rate, at 58.9% in the first half of 2007, remains well below the EU average and is much lower in the South. In fact, over the last three years, the regional divide has widened.

2. Medium-term prospects for the Italian economy remain challenging under the strain of structural weaknesses feeding into low productivity growth and high public indebtedness. Reversing this requires an economic policy strategy founded on micro-economic reforms to increase the efficiency and competitiveness of domestic production and on measures aimed at raising labour market participation and employment, including by enhancing human capital. Tackling regional disparities requires particular attention. Consolidation of public finances is a necessary pre-condition for this strategy, as it helps to create more favourable conditions for investment and to make room for enhanced expenditure on knowledge, human capital and infrastructure.

PART I: GENERAL ASSESSMENT

3. Overall, the Implementation Report shows good progress on implementing the revised National Reform Programme (NRP) over the 2005-2007 period. Italy has responded to the country-specific recommendations adopted by the Council. Some progress has been made with regard to the other areas on which the Council concluded Italy should focus (R&D performance, the sustainability of healthcare, the sustainable use of resources, infrastructure, and impact assessments).

4. Last year's Commission Annual Progress Report concluded that progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas was mixed. This assessment remains valid this year. Progress is most visible in the area of unlocking the business potential. Italy specifies the efforts it is taking to meet the euro area recommendations. Although the response in the area of public finances is substantial, Italy could have done more given the favourable cyclical and budgetary developments. Some initial steps have been taken to develop an integrated flexicurity approach, and to encourage more decentralised wage bargaining.

5. Consultation and efforts to develop ownership of the NRP at the level of central and local governments and the social partners is substantial, although there is still room for improvement in co-ordinating with regions. Italy's 2007 Implementation Report confirms the main priorities within the NRP, and provides a clear overview of progress in implementing the strategy. It also correctly highlights the importance of improving the efficiency of the judicial system throughout the country, as having an across-the-board impact in terms of the competitiveness and economic context of the

country. Links between governance and monitoring of the NRP and the structural funds are strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily, with significant support to foster employability and human capital, to boost research and innovation, and fight climate change.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

6. Given the high level of public debt and the considerable pressure from an ageing population, ensuring the long-term sustainability of public finances remains a key challenge for Italy, as was highlighted in the 2005 NRP. In line with this, the Council recommended that Italy rigorously pursues fiscal consolidation in order to place the debt-to-GDP ratio on a declining path, and fully implements pension reforms with a view to improving the long-term sustainability of public finances.

7. The result of Italy's fiscal consolidation strategy over the 2006-2007 period is substantial. The general government deficit has been reduced below 3% of GDP, with the larger part of the structural correction occurring in 2006. Notwithstanding this positive result, Italy has not fully utilised the favourable cyclical and budgetary developments, missing the opportunity to further accelerate the reduction of the public debt ratio. The adjustment has been achieved through an increase in the tax burden, and thanks to measures to increase tax compliance. In the Commission's opinion, the draft 2008 Budget Law, due to be approved by Parliament by the end of 2007, implies that fiscal consolidation efforts will stall in 2008.

8. Italy is continuing its efforts to pension reform and to limit increases in age-related public expenditure in the long term. A protocol agreement with the trade unions, adopted by the government in July 2007 and confirmed by a draft law, is a further step in this direction. However, it relaxes the eligibility conditions for seniority pensions for a specific group of workers and leaves some crucial issues open (for instance the definition of the actuarial coefficients in line with increases in life expectancy). More importantly, implementation remains crucial in order to ensure long term financial sustainability.

9. The Council also referred to the need to improve the sustainability of healthcare provision, while preserving quality and accessibility. Stringent expenditure control mechanisms are to be implemented consistently as the Commission considers them a good response. However there remains a need to improve the efficiency and cost effectiveness of expenditure.

10. Italy has partially succeeded in implementing a strategy aimed at ensuring long-term fiscal sustainability, including in the area of healthcare. Given that more progress is still required, the Commission considers that the Council recommendation remains valid and stresses the importance of the euro area recommendation to make use of the favourable cyclical conditions to pursue a more ambitious budgetary consolidation. More attention should also be paid towards improving the quality of public finances by containing growth in expenditure and improving efficiency and cost-effectiveness.

Micro-economic policies

11. Italy made mixed progress over the 2005-2007 period with regard to the implementation of policies to address the micro-economic challenges identified in the 2005 NRP. Notably by extending competition, granting incentives for scientific research and technological innovation, and upgrading infrastructure and protecting the environment.

12. The Council recommended Italy to pursue the implementation of recently announced reforms aimed at increasing competition in product and service markets. Italy has taken important steps in this area and the implementation of the reforms adopted in June 2006 is progressing. A second package, introduced in January 2007 which includes a mix of competition and consumer protection measures in the areas of financial services, mobile telecommunication, retail and wholesale distributions. Significant decreases in prices have been recorded, including in the telecom and pharmaceutical sectors. Since July 2007, SMEs and households now have access to an open electricity market. A number of draft laws have been presented on energy, liberalisation of local public services, reform of competition authorities, measures for consumers and to facilitate commercial and productive activities, and on class action. These are still being discussed in parliament. These are welcome steps in the right direction, but more is needed given the scale of the competition challenge and the need to modernise Italy's industrial base. It is important that draft laws are both adopted and implemented in a timely manner, including those on energy and the liberalisation of local public services. Italy has recently significantly improved its transposition deficit of EU legislation. It is important to continue these efforts while also bringing down the number of infringement cases.

13. The Council highlighted the need to focus on: R&D, a sustainable use of resources, implementing plans to improve infrastructure, and strengthening and fully implementing the system of impact assessment for proposed regulation.

14. In the area of R&D, Italy has made some progress in implementing a number of measures. These include public-private partnerships measures at local level, a tax credit scheme to support innovation, and a streamlining of the existing support schemes. New measures are being introduced in the context of the "Industria 2015" initiative to accompany structural change of industry. An independent evaluation agency for university and research is being set up to improve the governance of the research and innovation system. However, overall research spending remains low and the Implementation Report does not indicate to what extent the measures foreseen will allow progress towards meeting the 2.5% of GDP target for R&D. Further efficiency-enhancing measures are required in the public sector, where productivity is comparably low internationally.

15. The Implementation Report sets out detailed information on priorities, budget appropriations and deadlines with regard to infrastructure projects. It is now important that Italy vigorously implements the plans. Further efforts are needed to expand broadband to rural areas.

16. In the area of the business environment, Italy has made important progress to strengthen one-stop shops and reduce the time and costs for starting an enterprise. A target has been set for cutting administrative costs by 25% by 2012. A streamlined

procedure for impact assessment is being introduced, but its scope is limited and its application across all new regulation is only expected in the medium term.

17. Italy's CO2 emissions are significantly above 1990 levels, and policies and measures implemented have so far produced only limited effects on curbing emissions. In the wider environmental field the Implementation Report details measures to improve the sustainable use of resources, notably aimed at protecting water and soil (including remediation of contaminated sites), and improving waste management.

18. Italy has partially succeeded in implementing measures to deliver on the micro-economic commitments expressed in its NRP. The recommendation on competition and the points to watch have been addressed to some extent, but the Commission considers them to remain valid.

Employment policies

19. Italy's labour market performance in terms of employment growth and reduction in unemployment continues to improve. Female participation in the labour market has increased but important gender gaps in terms of activity, employment and unemployment remain. The employment rate of older workers, and women, remain significantly lower than the EU average, affecting the adequacy of future pensions. Some progress has been registered on early school leaving and youth educational attainment levels. Regional disparities remain significant and additional efforts are required to address underlying structural weaknesses.

20. The Council recommended Italy to reduce regional disparities in employment by tackling undeclared work, increasing childcare provision and ensuring the efficient operation of the employment services throughout the country. Italy has adopted a number of measures in response. It has increased action against illegal and undeclared work, such as intensification of inspections and tighter administrative sanctions. To better reconcile work and family life, Italy has committed to improving the quality and availability of childcare services. Although employment services have been reformed, differences in the quality and efficiency of services between the south and the north persist, in particular in the way these services are tailored to individual needs. Taxes on labour have been cut for those on permanent contracts, but the impact is not yet known. The "protocol agreement on welfare" envisages some measures to promote decentralised wage bargaining, but a more comprehensive approach is needed to allow a better alignment between wage and productivity developments. The policy measures undertaken so far should help reduce regional disparities, but implementation is slow and more incisive action is needed.

21. The Council also recommended Italy to develop a comprehensive lifelong learning strategy and improve the quality and labour market relevance of education. The Implementation Report does not set out a comprehensive strategy, but progress is however being made towards the preparation of a national qualifications framework. The consolidation of reforms of the education and training system and the improvement of quality of education by filling the gap in school performance across regions remains crucial.

22. Italy has taken initial steps to address the flexicurity concept. The "Protocol agreement" on welfare reform increases the level and duration of unemployment

benefits, limits the use of fixed term contracts, and strengthens employment services. These measures are yet to be implemented and in parallel Italy needs to implement measures to increase flexibility. A lifelong learning system needs to be put in place.

23. Italy has partially succeeded in implementing its NRP commitments in the employment domain. There has been some progress in addressing undeclared work, but further efforts are needed to tackle regional disparities, including the further reform of employment services, improving the quality and labour market relevance of education, and establishing a lifelong learning system. Therefore the Commission considers the recommendation dealing with these issues to remain valid. Italy should also pay particular attention to the development of an active ageing strategy.

PART III: CONCLUSIONS

24. In the light of the 2007 Italian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

25. Italy has made good progress in implementing its National Reform Programme over the 2005-2007 period. There has been some response in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority areas.

26. The Implementation Report shows some policy response to the recommendations adopted by the Council. Given the scale of the challenge, significant further reforms are needed. There has been some policy response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

27. Amongst the strengths shown by the 2007 Italian Implementation Report are the initial steps to improve the business environment, measures to enhance competition in professional and financial services and retail distribution, recent improvements in its transposition deficit of EU legislation; and e-government actions to modernise the public sector.

28. The policy areas in the Italian National Reform Programme where challenges need to be tackled with the highest priority are: fiscal sustainability, where efforts need to be pursued and the pension reform process needs to be completed; enhanced competition in product and service markets and pursuing the full implementation of announced reforms; further fighting regional disparities in the employment; and improving education and lifelong learning. Against this background it is recommended that Italy:

- rigorously pursues fiscal consolidation, in particular by curbing growth in current primary expenditure, and completes the pension reform process with a view to improving the long-term sustainability of public finances;

- continues the progress made to enhance competition in product and services markets and vigorously pursues the implementation of announced reforms;

- improves the quality and labour market relevance of education, promotes lifelong learning, tackles undeclared work and ensures the efficient operation of employment services, within a flexicurity approach and with a view to reducing regional disparities.

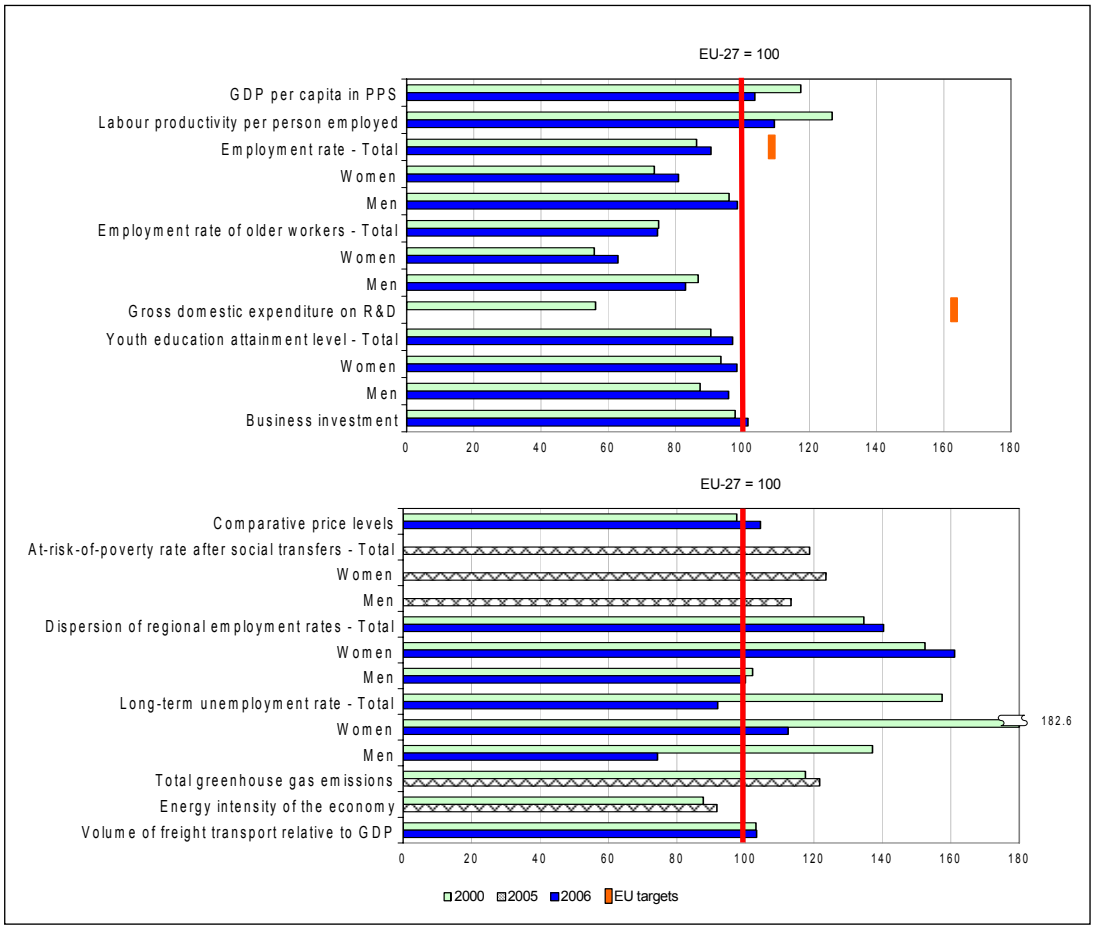
29. In addition, it will be important for Italy to focus over the period of the National Reform Programme on the following challenges: increasing R&D investment and efficiency, where despite welcome policy developments, further efforts are needed to reach the 2010 target and to enhance the efficiency of public spending; increasing efforts to meet the CO2 emission reduction targets; improving the quality of regulation by strengthening and fully implementing the system of impact assessment, notably for SMEs; implementing plans to improve infrastructure; increasing childcare provision with a view to reconciling work and family life and fostering labour market participation of women; and putting in place a consistent active ageing strategy to increase employment of older workers, and with a view to improving pension adequacy.

PART IV: STATISTICAL GRAPHS AND DATA

ITALY

		IT						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		117.4	111.2	107.6	105.4	103.7		100.0	100.0	100.0	
Labour productivity per person employed		126.7	115.4	112.6	111.4	109.5		100.0	100.0	100.0	
Employment rate	Total	53.7	56.1	57.6b	57.6	58.4	:	62.2	63.4p	64.4p	70.0
	Women	39.6	42.7	45.2b	45.3	46.3		53.7	56.2p	57.2p	
	Men	68.0	69.6	70.1b	69.9	70.5		70.8	70.8p	71.6p	
Employment rate of older workers	Total	27.7	30.3	30.5b	31.4	32.5		36.9	42.3p	43.5p	
	Women	15.3	18.5	19.6b	20.8	21.9		27.4	33.5p	34.8p	
	Men	40.9	42.8	42.2b	42.7	43.7		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.05	1.11	1.10	1.10	:	2.5	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	69.4	71.0	73.4	73.6	75.5		76.6	77.4	77.8	
	Women	74.2	75.1	78.6	78.1	79.4		79.3	80.1	80.7	
	Men	64.5	66.8	68.2	69.2	71.7		73.8	74.7	74.8	
Comparative price levels		97.5	103.6	105.2	104.4	104.4		100.0	100.0	100.0	
Business investment		18.0	17.9	18.1	18.2	18.5		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	18.0	:	19.0b	19.0	:		:	16.0e	:	
	Women	19.0	:	20.0b	21.0	:		:	17.0e	:	
	Men	18.0	:	18.0b	17.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	17.5	17.0	15.6	16.0	16.0		13.0	11.9	11.4	
	Women	30.5	29.7	25.7	26.6	26.1		20.0	16.8	16.2	
	Men	9.8	9.1	8.7	8.9	9.3		9.6	9.7	9.3	
Long-term unemployment rate	Total	6.3	4.9	4.0b	3.9	3.4		4.0	4.1p	3.7p	
	Women	8.4	6.6	5.5b	5.2	4.5		4.6	4.5p	4.0p	
	Men	4.8	3.8	2.9b	2.9	2.6		3.5	3.8p	3.5p	
Total greenhouse gas emissions		106.6	110.8	111.7	112.1	:		90.7	92.1	:	
Energy intensity of the economy		186.9	189.2	188.8	190.7	:		213.1	208.1	:	
Volume of freight transport relative to GDP		102.2	93.7	104.3	111.6	110.2e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Cyprus

1. Over the last decade, Cyprus sustained robust economic growth with an average GDP increase of about 3.75% per year, more than the EU27 average. It is estimated that in 2007, Cyprus's GDP per capita will be 93% of the EU average. In 2007 the total employment rate is estimated to have reached 70%, equalling the EU target, and the unemployment rate to have inched further down to 4.3%.

2. Cyprus is converging both in nominal and real terms with the EU. As a result, the Council decided last July in favour of Cyprus' adoption of the euro on 1 January 2008. Cyprus is a small open economy enjoying buoyant economic growth, high employment and stable prices. It also faces a long-term fiscal challenge resulting from an ageing population. Cyprus is mainly a services oriented economy. In 2006 services accounted for 77.6% of GDP and 71.0% of employment. Human capital is therefore the main economic resource. In recent years, there has been a substantial increase of foreign workers, who are mainly employed in unskilled or low-skilled occupations, accounting for 17.7% of total employment.

PART I: GENERAL ASSESSMENT

3. Overall, Cyprus has made good progress with the implementation of its National Reform Programme (NRP) over the 2005-2007 period. The NRP provided a clear and comprehensive overview of numerous specific measures and linked them well to final objectives.

4. Cyprus made some progress in addressing the Council recommendations. With a view to ensuring long-term fiscal sustainability there has been satisfactory initial progress in reforming the health care system. Progress on pension reform has been limited. A lifelong learning strategy and a reform plan of the vocational education, and training systems have been developed, but are not yet implemented.

5. With regard to the additional areas on which the Council concluded that Cyprus should focus on, there has been progress in planning alternatives to private venture capital funds. Some progress has been achieved in stimulating competition.

6. Last years' Annual Progress Report concluded that Cyprus had made good progress in meeting the specific commitments agreed at the 2006 Spring European Council in the priority areas of knowledge, entrepreneurship, employment and energy. Since then progress has remained good for instance on administration of business start ups.

7. Efforts to develop ownership of the Growth and Jobs Strategy have been strengthened. All stakeholders are involved in the consultation and implementation process. In order to increase public awareness, the government organised a number of seminars, public events, and other activities that were extensively covered in the media. The considerable efforts made by the Cypriot authorities to strengthen the relevant administrative bodies are very welcome, given that the absorption of EU Funds remains a concern, especially in the light of the considerably larger allocations for the 2007-2013 programming period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The macro-economic focus in the NRP is on fiscal consolidation and debt reduction, improvement of fiscal management, including restructuring of government expenditure and enhancing transparency. The NRP also addresses long-term sustainability of public finances, in particular through reforms in the health care and pension systems. Labour flexibility and wage moderation measures have also been launched. Fiscal consolidation has progressed well.

9. In 2006, the general government deficit fell to 1.2% of GDP from 2.4% of GDP the previous year. While wage and recruitment policy in the public sector remained restrictive, current expenditure increased, notably for social transfers. The gross government debt-to-GDP ratio continued to fall, to 65.25% of GDP from 69.25% in 2005. A further improvement is expected in 2007 when the medium-term objective is estimated to have been comfortably achieved, mainly due to better than expected revenues and despite the continuation of extra budgetary expenditure.

10. The Council recommended that Cyprus take steps to implement reforms of the pension and health care systems. On health care reform, progress was made on the implementation of the National Health Insurance System. In particular, thematic teams work with a specific time table and monitoring system, to prepare the different aspects of the system. The vetting of the law process is progressing. However, the transformation of hospitals into autonomous units does not seem to have progressed, despite government efforts. Discussions between the government and social partners on reforming the pension system have begun. The aim is to reach an agreement shortly, and adopt the reform in early 2008. However, the precise adjustments and timetable are yet to be agreed, meaning the budgetary impact is uncertain.

11. Overall, the progress made on the macro-economic reform measures outlined in the NRP is good. However, the need for action to secure the long term sustainability of public finances while ensuring adequacy in view of the population ageing remains crucial. In this respect, the recommendation remains valid while the continuation of a prudent fiscal policy and further debt reduction should be sustained.

Micro-economic policies

12. Key micro-economic challenges addressed by the NRP in 2005-2007 include promoting R&D, innovation and ICT, strengthening competition, improving the business environment, enhancing environmental sustainability, and upgrading basic infrastructure.

13. There has been some progress on R&D and innovation, and Cyprus still aims to reach 1.0% of GDP by 2010 though this would require an average annual growth rate of 23.5%. In view of the small size of most firms in Cyprus, additional measures are needed to overcome obstacles and boost the collaboration on innovation between the private sector and knowledge institutions. Fiscal measures are being studied, and new innovation networks and incubators start to engage business more in R&D. On ICT, significant progress has taken place in particular in terms of the availability of eGovernment services and digital literacy. Broadband penetration is catching up, but

take-up is still low and requires attention. Furthermore, there are delays in the implementation of a National Information Society Strategy. Additional efforts will be needed to speed up ICT uptake.

14. In the area of competition, a series of measures to strengthen the enforcement capacity of the Competition Authority and to improve competition conditions in the markets for energy, postal and telecom markets have produced first results, but it is important to maintain the pace of implementation of these measures. Cyprus is simplifying its business environment through various initiatives, but has not made much progress to date on measuring and reducing administrative burdens, or on developing a better regulation strategy. No target for a reduction in the administrative burden has been set. The 2007 National Action Plan foresees various steps to be taken in these areas, but impact assessment is only to be addressed during a second phase. It is important to ensure that equal attention is paid to improve both existing and new legislation and that these ambitious plans are carried out. Cyprus also needs to enhance its efforts to ensure timely implementation of the Services Directive. On environmental sustainability Cyprus has taken effective steps in the context of the Cyprus Strategic Plan for Reducing Green House Gas Emissions, in order to increase energy efficiency, to achieve savings in the areas of building and transport. Cyprus has set targets for the increase of renewable energy use. Cyprus plans to boost the use of public transport from the current 2% to 10 % in 2015, but implementation is still at an early stage.

15. The Council referred to the need to focus on measures to encourage venture capital investments and to improve competition in the regulated trades and professions. Cyprus has plans to develop a public venture capital fund and a loan guarantee mechanism in collaboration with the Cyprus Development Bank, which draws on the new Risk Sharing Financing Facility. This is a satisfactory policy response. On competition in professional services, Cyprus has confirmed the existence of serious regulatory restrictions on competition in the professions which are having a detrimental effect on price competition. A reform of business structure regulations and legislation is planned for lawyers, engineers and architects. The policy response has improved since 2006 but is confined to relaxing business structure restrictions. The Commission considers this a limited response to the challenges, and it is important to step up the pace of reform by doing away with much of the restrictive regulation especially on pricing.

16. Overall progress in 2005-2007 with regard to the implementation of policies to address the micro-economic challenges identified by Cyprus in the NRP is good. The micro-economic points to watch have been well covered in the area of venture capital, but less so on competition in professional services.

Employment policies

17. Over the 2005-2007 period, Cyprus has made good progress in implementing the policies set out in its NRP. Active labour market policies have helped increase employment and enabled Cyprus to close in on ambitious national employment targets. The Public employment services have been strengthened. Further initiatives are envisaged in 2008 (with European Social Fund support) to promote flexible but secure forms of employment for older workers, women, young persons, people with a disability, and migrants. The relatively high youth unemployment as compared to

total unemployment points to the need to facilitate the transition from school to work.

18. The aim to increase the labour supply is held back by the persistence of important gender imbalances across occupations and in qualifications. A national action plan on gender equality was adopted in 2007 and a preliminary draft report has put forward a number of suggested policy measures to address a gender pay gap that is substantially higher than the EU average. The Cypriot authorities have put in place an appropriate legal framework to encourage part-time work. An economic migration strategy has been established and immigration legislation amended. The main thrust of the new strategy is to discourage the inflow of unskilled non-EU nationals and attract highly skilled EU workers.

19. The Council recommended that Cyprus should enhance life long learning, and increase employment and training opportunities for young people by accelerating the reforms of the vocational, education, training and apprenticeship system. Participation of adults in lifelong learning increased in 2006 but is still short of the EU target for 2010. This increase is mainly due to the higher participation of young adults and highly skilled people. Participation rates in training of older people, the low skilled and the unemployed have stagnated. Cyprus has developed a strategic plan on educational reform, for consultation with relevant stakeholders. External evaluations of technical and vocational education programmes are now in progress, with a view to improving the curricula, and to increase their attractiveness especially to female students. An action plan for the new apprenticeship system has been finalised, and its full introduction by 2010 is foreseen. The development of a vocational qualifications certification system is advancing and a training providers' certification system is expected to become operational in 2010. A national lifelong learning strategy was approved by the Council of Ministers in November 2007. In the Commission's opinion an acceleration of these welcome policy reforms is now needed.

20. Cyprus is initiating a process to address flexicurity in an integrated way by setting up an interdepartmental committee on flexicurity within the Ministry of Labour and Social Insurance. The social partners are involved. A number of schemes are being implemented in the policy areas of contractual arrangements and active labour market policies, while the implementation of lifelong learning measures needs to be accelerated.

21. In general, Cyprus has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. The recommendation in the employment area has been addressed to a limited extent, due mainly to the delayed implementation of a comprehensive lifelong learning policy framework to further developing human capital. In addition, Cyprus needs to pay particular attention to tackling gender imbalances and reducing the high pay gap.

PART III: CONCLUSIONS

22. In the light of the 2007 Implementation Report for Cyprus and the Commission's assessment of progress made in implementing key structural reforms and based on

the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

23. Cyprus has made good progress in the implementation of its National Reform Programme over the 2005-2007 period. Cyprus had made good progress in fulfilling the specific commitments agreed at the 2006 Spring European Council in the priority areas.

24. The Implementation Report shows a good policy response to the recommendations adopted by the Council. With a view to the long term sustainability of public finances there has been a satisfactory initial response in reforming the health care system but a limited response on pension reform, enhancing lifelong learning and reforming the vocational education and training system. There has been some policy response on the additional areas identified in the Council conclusions as requiring attention.

25. Amongst the strengths of the Implementation Report is progress in the field of fiscal consolidation, in both deficit and debt reduction; a new policy to develop a comprehensive research and innovation system; and the maintenance of a good overall employment performance supported by a broad range of active labour market measures.

26. The policy areas in the Cypriot National Reform Programme where weaknesses need to be tackled with the highest priority are: addressing ageing-related expenditure; implementing a lifelong learning strategy and increasing training and labour market opportunities for young people. Against this background, it is recommended that Cyprus:

- take steps to implement reforms of the pension and health care systems and sets a timetable for their implementation with a view to improving fiscal sustainability;

- enhance life long learning, and increase employment and training opportunities for young people by implementing the reforms of the vocational, education, training and apprenticeship system.

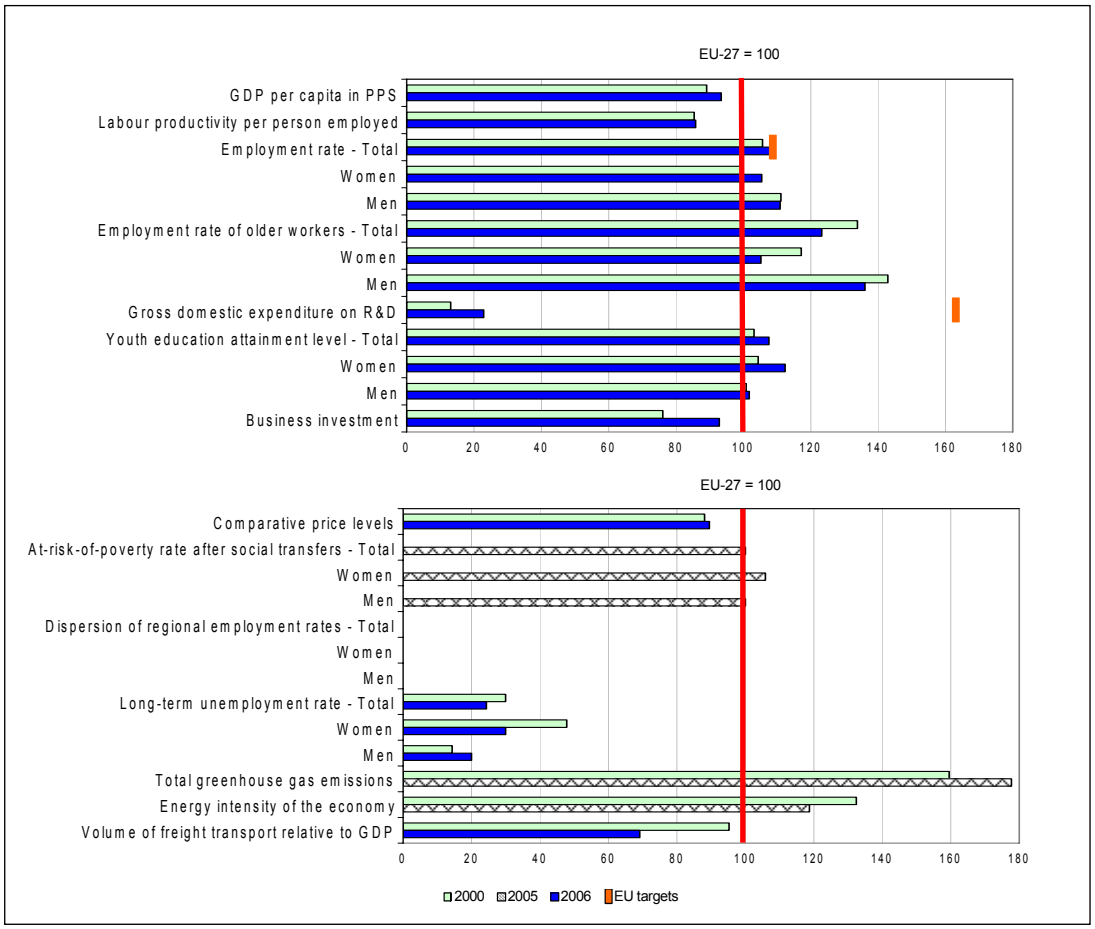
27. In addition, it will be important for Cyprus over the period of the National Reform Programme to focus on measures to: improve competition in the area of professional services; further stimulate private sector R&D; and address the very high gender pay gap.

PART IV: STATISTICAL GRAPHS AND DATA

CYPRUS

		CY						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		89.1	89.3	91.5	93.8	93.4		100.0	100.0	100.0	
Labour productivity per person employed		85.4	82.4	83.6	85.1	85.8		100.0	100.0	100.0	
Employment rate	Total	65.7	69.2	68.9	68.5	69.6	71.0	62.2	63.4p	64.4p	70.0
	Women	53.5	60.4	58.7	58.4	60.3		53.7	56.2p	57.2p	
	Men	78.7	78.8	79.8	79.2	79.4		70.8	70.8p	71.6p	
Employment rate of older workers	Total	49.4	50.4	49.9	50.6	53.6		36.9	42.3p	43.5p	
	Women	32.1	32.7	30.0	31.5	36.6		27.4	33.5p	34.8p	
	Men	67.3	68.9	70.8	70.8	71.6		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.24	0.35	0.37	0.40	0.42	1.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	79.0	79.5	77.6	80.4	83.7p		76.6	77.4	77.8	
	Women	82.8	87.0	83.8	89.1	90.7p		79.3	80.1	80.7	
	Men	74.4	71.3	70.7	71.1	76.1p		73.8	74.7	74.8	
Comparative price levels		88.1	90.9	90.6	89.1	89.5		100.0	100.0	100.0	
Business investment		14.0	14.2	14.7	16.4	16.9		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	:	15.0	:	16.0b	:		:	16.0e	:	
	Women	:	17.0	:	18.0b	:		:	17.0e	:	
	Men	:	14.0	:	15.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	1.2	1.0	1.2	1.2	0.9		4.0	4.1p	3.7p	
	Women	2.2	1.3	1.6	1.7	1.2		4.6	4.5p	4.0p	
	Men	0.5	0.7	0.9	0.8	0.7		3.5	3.8p	3.5p	
Total greenhouse gas emissions		144.7	158.4	163.4	163.7	:		90.7	92.1	:	
Energy intensity of the economy		282.3	287.9	254.3	246.9	:		213.1	208.1	:	
Volume of freight transport relative to GDP		94.4e	99.6	76.4	91.5	73.8		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Latvia

1. In the three years to 2006 Latvia's real GDP increased on average by 10.4% annually. Growth in 2007 is expected to be similar. After a slight deficit in 2006 the budget is expected to record a modest surplus in 2007 with higher surplus in prospect for 2008-2010. However, growth has primarily been driven by a credit boom in private consumption and residential investment. As the supply-side of the economy was unable to respond adequately, the external imbalance has reached very high levels. Employment is increasing rapidly (from 63.3% in 2005 to 66.3% in 2006), and unemployment shrinking (from 8.9% in 2005 to 6.8% in 2006). Labour shortages, aggravated by significant emigration, have contributed to the emergence of a wage-price spiral, with increasingly rapid wage growth outstripping productivity; inflation has risen to very high levels. From mid-2007 some limited slowdown of domestic consumption and the housing market has begun to set in, but this has been insufficient to remove the downside risks to medium-term prospects.

2. The main economic policy challenge is thus to secure macro-economic stability in the face of persistent inflationary pressures and a very large external deficit, and to transform the economy away from its dependence on low-technology, labour-intensive goods. Economic policy is confronted with the task of simultaneously stepping up fiscal consolidation in order to contain demand pressures, addressing tight labour market conditions, and fundamentally improving productivity growth.

PART I: GENERAL ASSESSMENT

3. Overall, Latvia has made some progress with the implementation of its National Reform Programme (NRP), both in the period 2005-2007 as a whole and over the last year. Reforms in general are progressing, but their pace could be stepped up.

4. There has been some progress in responding to the three country-specific recommendations adopted by the Council. On maintaining economic and budgetary sustainability, the government's anti-inflation plan adopted in March 2007 has begun to yield some results in cooling excessive demand, although much more is required to form an adequate response to this challenge. Latvia has made some progress with the implementation of research and innovation policy reforms and in efforts to increase labour supply. However, persistent labour market bottlenecks give reasons for concern and stronger efforts are needed to implement a lifelong learning strategy and improve education and training.

5. With regard to the other areas on which the Council concluded Latvia should focus, a single contact point has been established for the administrative formalities involved in hiring the first employee and sufficient progress made in promoting education in entrepreneurship. Some progress has been made as regards active labour market policies and access to childcare.

6. The Commission's 2006 Annual Progress Report concluded that Latvia had made modest progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been some progress on those

commitments with an end-2007 deadline. In the area of knowledge and innovation, Latvia has made some progress but leveraging more private investment into R&D remains a challenge. Progress has also been achieved on issues related to SMEs and entrepreneurship. A one-stop shop for starting up a company within one week has been established.

7. Consultation and efforts to develop ownership of the NRP at the level of central and local governments and social partners have continued over the past year. Discussions have been held with parliament and social partners on relevant topics and improvements in the social dialogue are foreseen. A clear internal governance structure ensures inter-ministerial coordination, but a monitoring of progress remains limited. Links between the governance of the implementation of the NRP and programmes under the Structural and Cohesion Funds are strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily. Particular attention to administrative capacity is paid in the National Strategic Reference Framework.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. Latvia's recent economic growth has been extremely high and medium-term prospects remain positive. However, booming domestic demand, labour market shortages and rapid credit growth has resulted in serious overheating pressures and threats to macroeconomic stability. Progress over 2005-2007 with regard to the implementation of policies to address the macro-economic challenges faced by Latvia has thus been limited.

9. The Council recommended Latvia to maintain economic and budgetary sustainability by pursuing a more restrictive fiscal policy. The government adopted wide ranging counter-inflationary proposals in March 2007. More ambitious fiscal targets have been set, medium-term budget planning has improved and taxation changes have helped to lessen pressures in the real estate market. However, while there are some recent signs that domestic demand is gradually slowing and the real estate market is stabilizing, the external deficit widened further in 2007 and inflation increased. This was driven primarily by overheating pressures but also factors such as energy and food costs. Wage growth in 2007 reached critical rates and urgently needs to be reduced. The breaking of the wage-price spiral, essential to curb inflation and avoid the ongoing deterioration of external competitiveness, will require strong commitment from the government and society at large. Increased competition in services, distribution and construction sectors could also help.

10. After a slight deficit in 2006 the budget is expected to record a modest surplus in 2007 with higher surpluses in prospect for 2008-2010. While this represents some progress compared with targets set earlier in 2007, the background of booming demand and risks to stability indicates that the current stance of fiscal policy remains far short of that required. A more prudent fiscal policy is needed to dampen demand pressures and to reduce the external deficit. The revenue structure could also be examined to redirect demand away from real estate, while public expenditure should aim for a strengthening of the supply side to contribute to external sustainability. To

help in this regard, the government aims to produce proposals focused on improving export competitiveness, productivity and labour supply. The authorities will need to show determination to steer the economy towards higher-productivity and more technology-intensive sectors.

11. Latvia has partially succeeded in implementing measures to fulfil the macro-economic commitments expressed in its NRP and in addressing the recommendation, which therefore remains valid.

Micro-economic policies

12. Latvia has made mixed progress with the implementation of policies to address its micro-economic challenges. There has been recent progress in the field of knowledge and innovation, whilst gradual improvements in the regulatory environment have taken place over 2005-2007. Financing in support of electricity generation from renewable energy sources has been considerably increased in 2007. The Competition Authority has raised the frequency of market surveillance in individual sectors. Creditable efforts have been made in transposing internal market legislation and in measures for administrative simplification. However, a more systematic approach to better regulation and practical implementation of the associated tools is encouraged, and a target for reducing administrative burdens should be set. Strong efforts are needed to improve the supply of online public services and their use by enterprises. The effective implementation of the "Information and Communication Technology for Quality Education" 2007-2013 should be considered a priority.

13. The Council recommended Latvia to make faster progress in the implementation of the research and innovation policy reforms in order to meet effectively the ambitious targets set out in its NRP. There have been some positive developments in this area, mainly due to the substantial increase of public investment. The link between research and education has been strengthened and the first steps have also been taken towards better linking these with industry. However, the number of private R&D actors remains small, largely due to the lack of incentives for private investment. The new market-oriented research programme is a welcome step, but a more focused approach in line with identified economic growth areas is needed. Latvia has allocated substantial amounts of Structural Fund financing for this area and successful implementation will require close monitoring to avoid crowding out private investment. R&D and innovation policies should serve the purpose of establishing favourable conditions for investment by the private sector including: appropriate infrastructure, effective protection of intellectual property rights, sufficient human resources and additional incentives for business investment. The Council's recommendation thus remains valid.

14. The Council also asked Latvia to focus on faster progress on establishing a single contact point for the administrative formalities involved in hiring the first employee and on promoting entrepreneurship education. Latvia has taken steps to establish a single contact point. An employer has to register every employee with the State Revenue Service until the fifth day of the month following a person’s recruitment. The State Revenue Service passes this information on to the State Social Insurance Agency. Latvia has also made good progress in promoting education in entrepreneurship. In addition to other measures, there is now a mandatory subject on

business basics in the curriculum of all secondary schools. The Commission considers this a good policy response.

15. In general, Latvia has partially succeeded in implementing measures to fulfil the micro-economic reform commitments set in the NRP. Despite some progress, the country-specific recommendation remains valid. There has been a good policy response to the two points to watch, and the Commission is of the opinion that these are no longer merited.

Employment policies

16. Labour market performance over the 2005-2007 period has continued to improve with good progress towards meeting national employment targets for 2010. The increase in labour supply is primarily in response to strong growth of demand, although there has also been a positive contribution of active labour market policies. However, levels of adult participation in lifelong learning have decreased, and numbers of pupils leaving school early have increased. Latvia has focused on implementing measures such as establishing a labour market forecasting system, supporting business start-ups and self-employment. Measures in place to strengthen labour market institutions and social partnership go in the right direction.

17. The Council recommended Latvia to intensify efforts to increase labour supply and productivity. Labour shortages remain a major challenge, although recent legislation on support to jobseekers will help to reach new target groups. Preventive measures such as training for the employed and self-employed and promotion of regional mobility are envisaged. Latvia has finally moved towards formulating its approach to the economic migration challenge by putting forward a policy paper on the issue. Criteria for managing short-term migration from third countries are still to be established and clear plans to introduce integration measures are lacking. Measures providing a better working environment and access to education, training and health care are important as they could help to counteract emigration. The adoption of a lifelong learning strategy needs to be followed by a plan for implementation. Plans are in place to invest in improving vocational and higher education and to boost human resources in education and science. However the responsiveness of education and training systems to labour market needs is still low.

18. The Council also asked Latvia to focus on pursuing active labour market policies and improving access to childcare. Given the decrease in European Social Fund support and the need to reach new target groups, careful monitoring is needed to ensure adequate funding and coverage. Latvia has made some progress by committing funds to enhance access to childcare. Due to efforts at local level, some improvements in the situation are already taking place. However, progress is currently too slow to make an impact and plans need to be more speedily implemented.

19. In recent years the concept of flexicurity has emerged in the Latvian policy debate, but is not yet treated in an integrated way. Social partners are involved. Envisaged measures relate to all the components and also tackle undeclared work. The focus now must be on their implementation, especially as regards facilitating regional and vocational mobility and putting in place incentives for employers and workers to participate in lifelong learning.

20. Latvia has made some progress in implementing measures to fulfil its employment policy commitments. The Commission welcomes the announced measures but the focus now must be on their effective delivery. An effective system for managing economic migration needs to be put in place and plans for implementing lifelong learning should be finalised. The country specific recommendation and the points to watch in the employment area have only been partially addressed and therefore remain valid.

PART III: CONCLUSIONS

21. In the light of Latvia's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

22. Latvia has made some progress in implementing its National Reform Programme over the 2005-2007 period and some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

23. The Implementation Report shows that there has been some progress in responding to the recommendations adopted by the Council. There has been a mixed response to the additional areas identified by the 2007 Spring European Council as requiring attention.

24. Among the strengths shown by the Implementation Report are: the first positive steps in the field of knowledge and innovation; the progress achieved on certain SME and entrepreneurship issues; the strengthened role of the Competition Authority in market surveillance; and further measures to promote energy efficiency and the use of renewable energy resources. Latvia has also implemented a set of measures that have successfully supported labour market performance.

25. The policy areas in the Latvian National Reform Programme where weaknesses need to be tackled with the highest priority are: more concrete measures to secure macroeconomic stability in the face of overheating pressures; further development of the R&D strategy to improve prioritisation and increase private sector involvement; and stronger measures to increase labour supply and strengthen the skills of the labour force. Against this background, it is recommended that Latvia:

- pursue a more restrictive fiscal policy, with a careful prioritisation of expenditures and wage developments that are in line with productivity, in order to contribute to correcting overheating pressures and reducing the risk of macroeconomic instability;

- make faster progress in the implementation of the research and innovation policy reforms, in order to meet the ambitious targets set. This concerns especially policies to stimulate partnerships between research and education institutions and businesses;

- within an integrated flexicurity approach, intensifies efforts to increase labour supply and productivity by improving regional mobility and, enhancing the

responsiveness of education and training systems to labour market needs, by putting in place a lifelong learning system and pursuing active labour market policies.

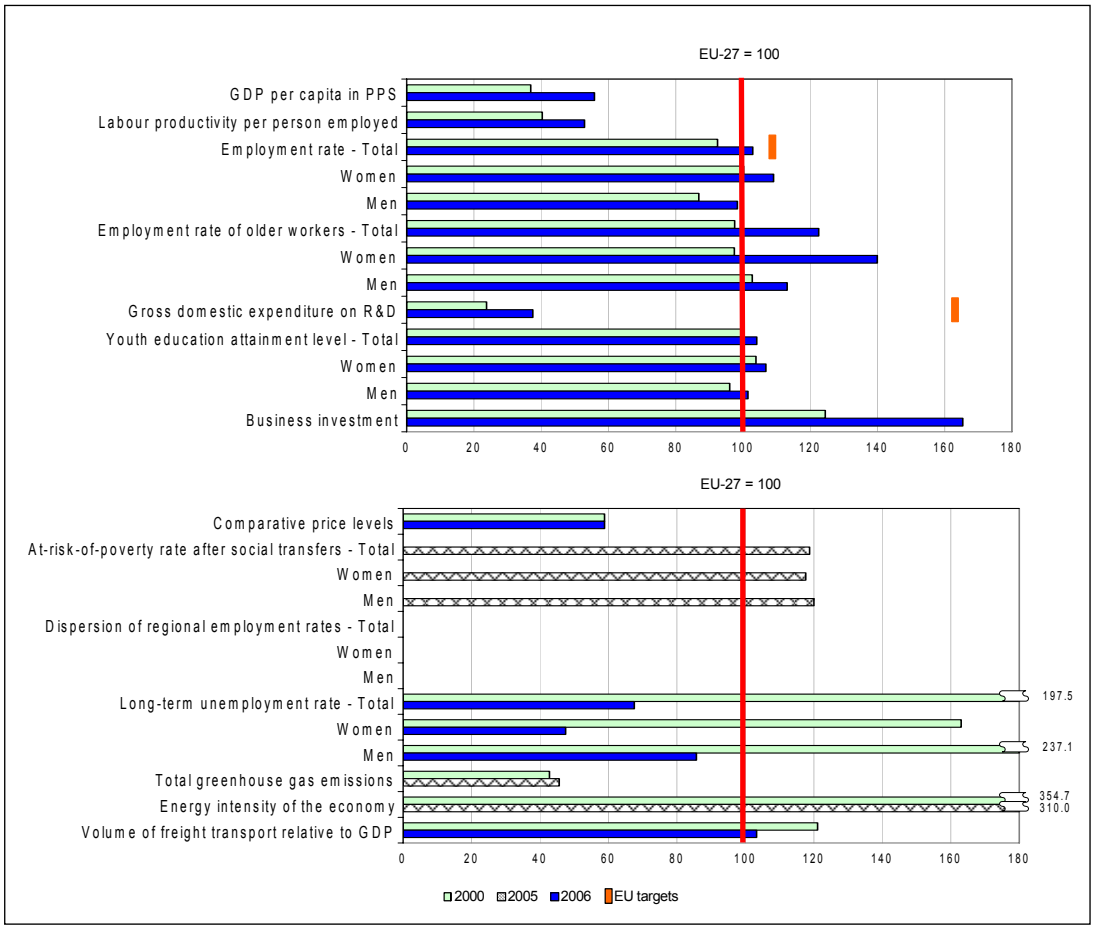
26. In addition, it will be important for Latvia over the period of the National Reform Programme to focus on: improving further the regulatory environment, notably by means of an explicit better regulation policy; and improving access to childcare.

PART IV: STATISTICAL GRAPHS AND DATA

LATVIA

		LV						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		36.9	43.5	45.5	50.2	55.8		100.0	100.0	100.0	
Labour productivity per person employed		40.3	44.2	45.5	49.4	52.9		100.0	100.0	100.0	
Employment rate	Total	57.5	61.8	62.3	63.3	66.3	67.0	62.2	63.4p	64.4p	70.0
	Women	53.8	57.9	58.5	59.3	62.4		53.7	56.2p	57.2p	
	Men	61.5	66.1	66.4	67.6	70.4		70.8	70.8p	71.6p	
Employment rate of older workers	Total	36.0	44.1	47.9	49.5	53.3		36.9	42.3p	43.5p	
	Women	26.7	38.8	41.9	45.3	48.7		27.4	33.5p	34.8p	
	Men	48.4	51.3	55.8	55.2	59.5		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.44	0.38	0.42	0.56	0.69	1.5	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	76.5	75.4	79.5	79.9	81.0		76.6	77.4	77.8	
	Women	82.4	80.9	85.1	85.2	86.2		79.3	80.1	80.7	
	Men	70.9	70.1	74.2	74.7	75.9		73.8	74.7	74.8	
Comparative price levels		58.8	54.4	55.5	56.3	58.8		100.0	100.0	100.0	
Business investment		22.9	22.0	24.4	27.2	30.1		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	16.0	:	:	19.0b	:		:	16.0e	:	
	Women	16.0	:	:	20.0b	:		:	17.0e	:	
	Men	17.0	:	:	18.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	7.9	4.4	4.6	4.1	2.5		4.0	4.1p	3.7p	
	Women	7.5	4.4	4.3	3.7	1.9		4.6	4.5p	4.0p	
	Men	8.3	4.3	4.8	4.4	3.0		3.5	3.8p	3.5p	
Total greenhouse gas emissions		38.8	41.7	41.4	42.0	:		90.7	92.1	:	
Energy intensity of the economy		756.0	725.1	692.3	644.8	:		213.1	208.1	:	
Volume of freight transport relative to GDP		120.0	133.1	128.6	126.0	110.2		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Lithuania

1. Lithuania's economic growth has continued to be very strong. In 2004-2006 real GDP increased on average by 7.6%, and it is forecast to be higher at 8½% in 2007. GDP per capita is an estimated 61% of the EU average in 2007. The employment rate has been rising (63.6% in 2006) and unemployment falling (5.6% in 2006, and estimated at 4.2% in 2007). Growth has mostly been driven by private consumption and construction. Rapid credit expansion, income tax cuts and wage increases in excess of productivity growth have boosted household demand, including for housing. The supply side is struggling to match demand, and labour market constraints have become evident. Excess demand has resulted in mounting imbalances: the current account deficit is forecast to be 13.9% of GDP and inflation around 5½% in 2007.

2. The main economic policy challenge for Lithuania is to preserve macroeconomic stability: containing inflationary pressures, the large external deficit and the credit growth. Strengthening the supply side of the economy would help stabilising imbalances while maintaining robust growth. Tightened labour markets, demonstrated by skills gaps, wage pressure, and increased labour shortages should be addressed by containing wage increases, mobilising labour reserves, increasing flexibility, and improving education and training.

PART I: GENERAL ASSESSMENT

3. Overall, Lithuania has made good progress in implementing its 2005 National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have slowed down over the last year.

4. There has been some progress in responding to the recommendation issued by the Council on strengthening research and innovation. There has been a limited response to the recommendation on increasing the supply of skilled labour, but Lithuania is committed to implementing relevant measures in the near future.

5. With regard to other areas on which the Council concluded Lithuania should focus, there has been a very good response on environmental protection, a good response on facilitating business start-ups, and a limited response in the other areas.

6. Last year's Commission Annual Progress Report concluded that Lithuania had made moderate progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas. Since then, progress has been good in unlocking business potential but limited in other areas.

7. Lithuania has continued efforts to increase the visibility of the NRP and the Lisbon strategy, supported by the creation of a Lisbon internet portal. An inter-ministerial commission ensures coordination of the NRP within the government. A special framework has been set up for stakeholder consultation on the NRP, which can be considered as good practice. The Implementation Report covers all relevant areas highlighted as challenges, but would have benefited from more of a focus on the country specific recommendations and points to watch. Links between the NRP and

the structural and cohesion funds are strong, with substantial support earmarked for R&D, innovation and information society as well as for the improvement of transport networks.

8. Lithuania's 2007 Implementation Report confirms the main priorities within the NRP as: sustaining rapid economic growth, a stable macroeconomic environment and seeking full-fledged membership in the EMU; promoting the competitiveness of Lithuanian enterprises; promoting employment and investment in human capital.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. Progress over 2005-2007 with regard to the implementation of policies to address the macro-economic challenges faced by Lithuania, is limited and stronger efforts to achieve macro-economic stability are needed.

10. In the face of mounting macro-economic imbalances, the Medium-term Price Stability Strategy and the Law on Fiscal Discipline were adopted in 2007. The latter aims at strengthening the multi-annual expenditure framework and providing a firm commitment to fiscal restraint, however, the law does not as such introduce a binding medium-term budgetary framework. Nevertheless, a more active role should be played by the government to contain overheating. Although strong growth has boosted tax revenue, the government still runs a small budget deficit and fiscal policy does not take advantage of the good economic climate and remains expansionary. Moreover, the target to reduce the deficit from 0.9% of GDP in 2007 to a balanced budget in 2009 could be difficult to achieve in the light of planned tax reforms, including reductions in personal income tax, and the abolition of the temporary social tax on corporate profits, and expenditure increases due to the ongoing pension reform. Fiscal policy should play a stronger role in mitigating the risks from strong demand by stepping up fiscal consolidation in general and by scaling back tax incentives, particularly those for real estate.

11. In spring 2007, the Council invited Lithuania to focus on containing inflationary pressures. Inflation was 3.8% in 2006 and is expected to rise to 5.5% in 2007. It seems unlikely to decline quickly without more effective policy action. A wage-price spiral risks adding further to overheating. Further price increases stem from food, the harmonisation of indirect taxes, and increases in regulated prices such as heating, gas and electricity. The 2007 Medium-term Price Stability Strategy would benefit from being more concrete. Stronger commitment by the government and social partners is needed to ensure that wage growth is better aligned with productivity gains.

12. Lithuania was also invited to focus on increasing foreign direct investment (FDI). Despite some increase, Lithuania's progress in creating a more attractive environment for foreign investment has been limited. The investment promotion programme, which the Lithuanian authorities intend to implement in 2008, contains a wide range of measures to attract FDI. In the Commission's opinion, it is vital to ensure that this programme is coherent and rapidly implemented.

13. Lithuania has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. Improving macro-economic stability and containing inflation remain major challenges. A more determined fiscal policy aimed at containing inflationary pressures and to signal the need for more realistic growth expectations is warranted.

Micro-economic policies

14. Lithuania has made some progress over 2005-2007 in implementing policies to address its micro-economic challenges. The policy response to e-government policy is adequate and now needs to be sustained and set alongside a comprehensive strategy. More emphasis needs to be placed on the implementation of all the foreseen ICT measures. There has been limited progress in finalising the Better Regulation Programme, as implementation of the policy measures to improve the regulatory framework, and in particular measures to reduce the administrative burden, is still pending. Measures related to legislative simplification seem to have been discarded and no specific target for reducing administrative burdens has been set. When designing new legislation, Lithuania needs to increase the use of impact assessments and consultation tools.

15. The Council recommended Lithuania to strengthen its R&D system to reach its ambitious target for overall investment in R&D. Despite the considerable increase in public R&D expenditure over recent years, the R&D share of GDP has remained virtually stagnant due to a rapid GDP growth, and private R&D intensity has remained at a very low level (0.2% of GDP). Major efforts are thus needed to progress towards the target of 2% of GDP by 2010, particularly in order to achieve the 1% target from private sources.

16. In 2007 political parties signed an agreement on the principles of research and higher education reform. The reform should develop R&D capacity of the public sector, improve conditions for business R&D, and facilitate knowledge transfer between public and private R&D, thus help to raise the efficiency of public R&D investment. Lithuania should now urgently move to implementation by creating the two agencies to administer funds competitively, and develop stronger cooperation between science and business in the Integrated Research, Study and Innovation Centres. It should adopt the law enhancing conditions for creating spin-offs from research institutions and monitoring programmes to prevent brain drain, and make PhD studies and researchers careers more attractive. Due account should also be taken of traditional and low-tech sectors which are important in the Lithuanian economy, but where growth potential is hampered by low levels of innovation. Innovation support services should therefore ensure that these sectors are appropriately targeted.

17. The Council invited Lithuania to focus on environmental protection and facilitating business start-ups. Lithuania is implementing a series of measures to address issues of climate change, green public procurement, sustainable energy use and drinking water resources. This represents a very good policy response. On business start-ups, Lithuania has now established a one-stop-shop, shortened the time needed to start-up a company to 6 days, lowered the cost of starting a private limited company, and established one contact point for the recruitment of the first employee. This represents a good response.

18. Lithuania has partially responded to the recommendation on implementing measures to deliver on its research and innovation commitments. Further implementation of the outlined R&D reform is needed. Good progress was made on environmental protection and business start-ups and these points to watch are no longer merited. However, more focus is needed on efforts to finalise and implement the Better Regulation Programme.

Employment policies

19. Lithuania has made some progress in 2005-2007 regarding policies to address its labour market challenges. Important policy measures include the approval of the laws on Employment Support and Vocational Training. However, preparations to increase the statutory retirement age and the introduction of compulsory pre-school education are still pending. Health care reform needs more impetus to improve access to services and to ensure its financial sustainability.

20. The Council recommended Lithuania to increase the supply of skilled labour. Lithuania has conducted a study on the reasons for labour force emigration and launched information campaigns on working and living conditions in Lithuania. There has been no progress in promoting internal labour mobility but the government is committed to prepare and implement relevant measures in 2007-2008. Participation in lifelong learning remains very low (4.9% in LT, 9.6% in the EU). A number of European Social Fund co-financed projects are on-going and a study on the training needs for older workers has been launched. The Lifelong Learning Strategy is to be revised by the end of 2007. These policy measures and pace of their implementation represent a limited response, and it is important to speed up the implementation of the plans. Furthermore, substantial efforts are needed to ensure that the skills and qualifications provided by the education and training systems are of sufficient quality and relevance for the labour market.

21. The Council also invited Lithuania to focus on improving youth employability, expanding entrepreneurship education, increasing the availability of childcare, and strengthening occupational health and safety. The Law on Vocational Training adopted in 2007 sets the basis for the national qualification system and apprenticeships. This is a limited policy response and it is important to reform higher education and promote flexible working arrangements for young people. The adoption and implementation of the National Youth Entrepreneurship Programme should be speeded up to promote entrepreneurship.

22. On childcare, Lithuania has established a number of pre-school education groups and drafted a Compulsory Pre-school Education Programme, which still needs to be approved and implemented. The Commission considers this a limited response. To improve occupational health and safety, the 2007 Law on Health and Safety at Work was extended with provisions governing the prevention of accidents at work and occupational disease, and by specifying that the liability for the creation of a safe and healthy work environment lies with employers. This is a welcome step but tackling the issue requires an integrated policy response based on a thorough analysis of the situation and covering the increase of the availability and capacity of occupational physicians.

23. There is no integrated flexicurity approach in Lithuania, although a number of flexicurity-related measures have been taken. The involvement of social partners is increasing. Active labour market policy has been improved and work is ongoing to prepare the basis for flexible contractual arrangements. More effort is needed to raise the participation in lifelong learning.

24. Lithuania has partially succeeded in implementing measures to deliver on the NRP employment policy commitments. The recommendation and points to watch have been addressed to a limited extent and therefore remain valid.

PART III: CONCLUSIONS

25. In the light of the 2007 Lithuania's Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

26. Lithuania has made good progress in implementing its National Reform Programme over 2005-2007. Lithuania has also been showing some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

27. The Implementation Report shows a limited policy response to the recommendations adopted by the Council. There has been some policy response on the additional areas identified by the Council as requiring attention.

28. Among the strengths shown by the 2007 Lithuania's Implementation Report are: approval of priority areas for R&D development and adoption of the Vocational Training Law.

29. The policy areas in the Lithuanian National Reform Programme where challenges need to be tackled with the highest priority are implementing measures: increasing and improving the efficiency of investment in R&D and support for innovation; to increase internal mobility of labour, promote adult participation in lifelong learning, especially among older workers, and reform the education and training systems to ensure quality and labour market relevance. Against this background it is recommended that Lithuania:

- accelerates the implementation of the structural reform of its R&D and innovation system so as to raise the efficiency of public spending and create conditions favourable to increased private investments in this area, including for innovation in traditional and low-tech sectors;

- intensifies efforts to increase the supply of skilled labour, with a special focus on the participation of older workers by: improving the regional mobility, reforming the education and training systems to ensure their quality and relevance to the labour market needs and implementing the revised lifelong learning strategy.

30. In addition, it will be important for Lithuania to focus over the period of the National Reform Programme on the following challenges: improving macro-economic

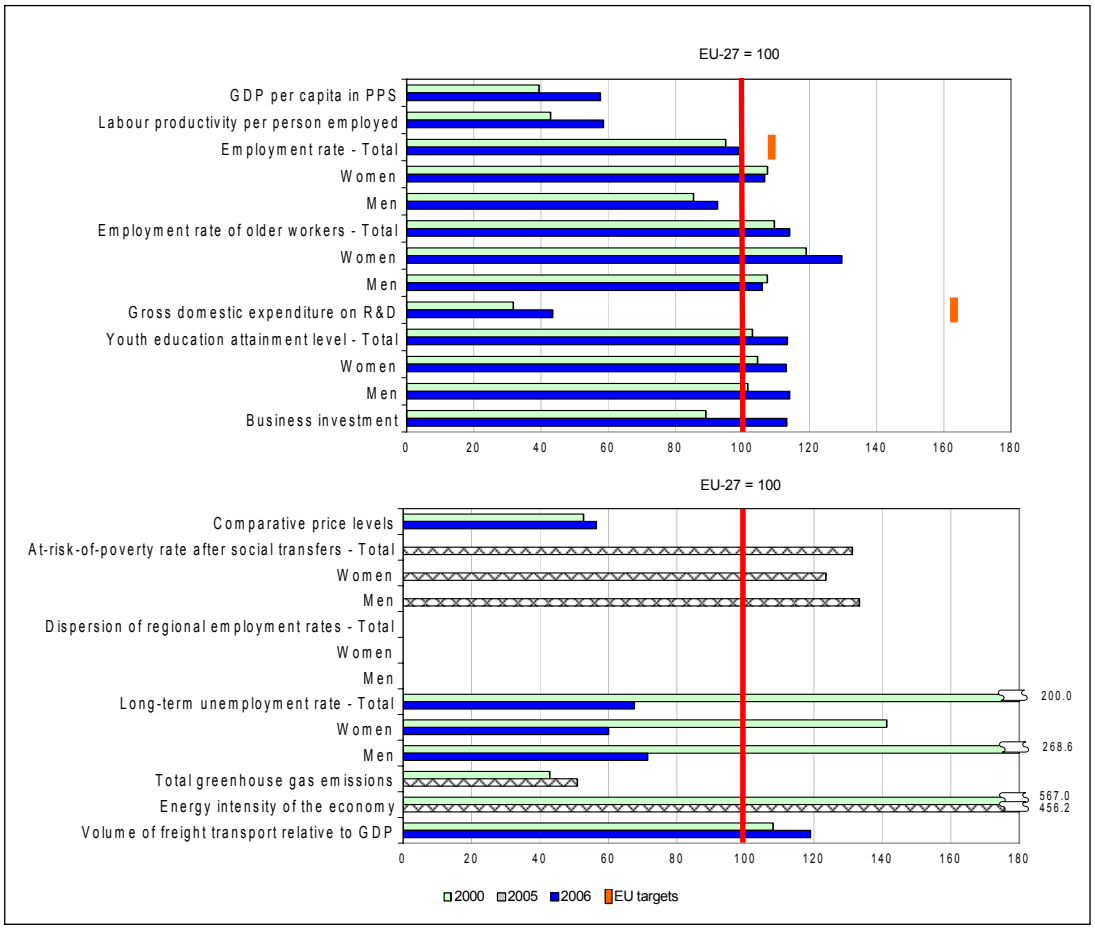
stability and containing inflation; increasing foreign direct investment; improving the efficiency of regulatory environment with particular focus on legislative simplification; improving youth employability; expanding entrepreneurship education; increasing the availability of childcare; and strengthening occupational health and safety.

PART IV: STATISTICAL GRAPHS AND DATA

LITHUANIA

		LT						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		39.4	49.2	51.1	53.8	57.7		100.0	100.0	100.0	
Labour productivity per person employed		42.9	51.8	53.7	55.2	58.6		100.0	100.0	100.0	
Employment rate	Total	59.1	61.1	61.2	62.6	63.6	68.8	62.2	63.4p	64.4p	70.0
	Women	57.7	58.4	57.8	59.4	61.0		53.7	56.2p	57.2p	
	Men	60.5	64.0	64.7	66.1	66.3		70.8	70.8p	71.6p	
Employment rate of older workers	Total	40.4	44.7	47.1	49.2	49.6		36.9	42.3p	43.5p	
	Women	32.6	36.7	39.3	41.7	45.1		27.4	33.5p	34.8p	
	Men	50.6	55.3	57.6	59.1	55.7		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.59	0.67	0.76	0.76	0.80	2.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	78.9	84.2	85.0	87.8	88.2		76.6	77.4	77.8	
	Women	82.9	87.9	88.5	91.8	91.2		79.3	80.1	80.7	
	Men	75.0	80.6	81.5	83.9	85.3		73.8	74.7	74.8	
Comparative price levels		52.7	52.3	53.1	54.6	56.4		100.0	100.0	100.0	
Business investment		16.4	18.2	18.9	19.4	20.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	17.0	:	:	21.0b	:		:	16.0e	:	
	Women	17.0	:	:	21.0b	:		:	17.0e	:	
	Men	17.0	:	:	20.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	8.0	6.0	5.8	4.3	2.5		4.0	4.1p	3.7p	
	Women	6.5	6.0	6.2	4.5	2.4		4.6	4.5p	4.0p	
	Men	9.4	6.0	5.5	4.2	2.5		3.5	3.8p	3.5p	
Total greenhouse gas emissions		38.9	41.7	43.8	46.9	:		90.7	92.1	:	
Energy intensity of the economy		1208.4	1194.8	1086.2	949.1	:		213.1	208.1	:	
Volume of freight transport relative to GDP		107.1	116.9	113.7	124.9	127.0e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Luxembourg

1. Since the end of the 2001-2003 slowdown, Luxembourg has experienced another period of growth well above the EU average. Real GDP growth reached 6.1% in 2006 but decelerated to about 5% in 2007. While in 2006 it was mostly driven by foreign trade, in 2007 the contribution of domestic demand became more important. Although likely to remain above the EU average, GDP growth should continue to slow down to about 4.5% in 2008 and 2009.

2. Despite high growth and low unemployment, Luxembourg needs to continue to prepare for future challenges. The longer-term growth potential could be affected by the deterioration of competitiveness induced by a relatively rapid increase of wage costs. The employment rate of the resident population remains below the EU average, and it is particularly low among older workers. Youth unemployment also remains a problem. Micro-economic challenges persist in the areas of start-up procedures, the transposition of EU legislation, and certain competition issues.

PART I: GENERAL ASSESSMENT

3. Overall, the Implementation Report shows very good progress in implementing the National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have accelerated slightly over the last year.

4. No country specific recommendations were addressed to Luxembourg. With regard to the areas on which the Council concluded that Luxembourg should focus, there has generally been some progress, the notable exceptions being the employment of older workers and further reform of early retirement systems, as well as some measures for improving the economic environment.

5. Last year's Commission Annual Progress Report concluded that Luxembourg had made very good progress in meeting the specific commitments agreed at the 2006 Spring European Council, but that additional measures were necessary for facilitating the recruitment of the first employee and speeding up the establishment of new businesses. Since then, there has been some progress on most of the commitments with an end 2007 deadline. Luxembourg describes efforts it is taking to address the euro area recommendations in its latest Implementation Report.

6. Consultation and efforts to develop ownership of the NRP within government and the social partners continue to be very substantial. Social partners were involved in drafting the 2007 Implementation Report. The regular publication of the "Observatoire de la Compétitivité" helps increase the visibility of the Lisbon Process. Links between the governance and implementation of the NRP and the programmes under the structural funds are fairly strong. The earmarking of structural funding for Lisbon priorities is being applied satisfactorily with 82% of ERDF and 100% of ESF budgets devoted to achieving these objectives. The ESF input focuses on increased labour supply by ensuring adequate skills for people at work and better integration of disadvantaged groups. The ERDF contribution emphasises support for innovation, R&D and entrepreneurship.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The main macro-economic challenges identified for Luxembourg in the coming years were the deterioration in public finance as well as the risks of accelerating inflation and worsening competitiveness. It now appears that the deterioration in government finances, though substantial, was more limited than at first suggested. Revised data indicates that the deficit already peaked in 2004 at 1.2% of GDP and fell to only 0.1% of GDP in 2005 (rather than the 2.3% of GDP that was suggested by initial estimates. In 2006, government finance recorded a surplus of 0.7% of GDP, which is likely to have widened to about 1.25% in 2007. Wage increases seem to have been strong in 2006 and 2007 (around 4.5%) despite the partial de-indexation agreed in April 2006.

8. Further reforms are needed to ensure the long-term viability of the pension system. Luxembourg faces an aging population, and the employment growth observed since the early 1980s will inevitably be matched in the future by a comparable increase in the number of pensioners. Despite this, little has been done to reform the pensions system and no significant progress was recorded in 2007.

9. There has been good progress over the 2005-2007 period with regard to the short-term macro-economic challenges facing Luxembourg, although this improvement is probably for a part due to favourable incidental factors. There has been little progress in ensuring the long-term sustainability of the pension system.

Micro-economic policies

10. Implementation of micro-economic policies over 2005-2007 focussed on integrating the economy into the European and international context, creating an attractive economic environment, and complying with the principles of sustainable development. Good progress has been made on the integration of the economy, especially in the field of rail and electronic infrastructure. To foster an attractive economic environment, an extensive simplification policy focuses on business needs and includes ex ante checks for administrative burdens. However, a target for reducing the administrative burden should be set and some informal consultations embedded in formal policy.

11. Luxembourg promotes ICT take up, addresses digital security issues and enhances the supply of e-Government services. The public research budget has significantly increased and is to double from 2005 to 2009. Whilst reaching the 3% expenditure target is important, the focus on efficient governance is appropriate to increase absorption capacity. Public-private collaboration needs to be strengthened, especially to increase relatively low levels of research investment by SMEs. Luxembourg has undertaken a number of measures in a wide range of areas to promote sustainable development, and is committed to a Kyoto target of a 28% reduction in greenhouse gases. However, reporting on progress towards the Kyoto goals should be improved, and meeting the target will require implementing additional measures.

12. The Council concluded that in order to render the economic environment more attractive Luxembourg should focus on: greater support for competitive markets, for

the transposition of EU directives and for SMEs. A recent legislative proposal aims at merging and reinforcing the competition authorities and widening their mandate. Despite this the authorities remain clearly understaffed, and widening their mandate. Despite the high importance of the professional services' sector in Luxemburg the level of competition remains low in a international context. Luxembourg should therefore take clear steps to increase competition in this sector.

13. The transposition deficit of EU legislation remains high, though the situation has improved significantly since 2005. Luxembourg should consolidate the procedures introduced in 2006 and set a deadline for achieving the 1% target agreed by the Council. Key directives awaiting transposition include those on public procurement, the enforcement of intellectual property rights, and the Financial Services Transparency Directive.

14. Entrepreneurship education needs to become more routine in secondary schools. Luxembourg already set up one-stop shops for businesses. However, further improvements should be made in order to remove lengthy and often expensive procedures for setting up an enterprise and recruiting the first employee.

15. In general, Luxembourg has succeeded in implementing measures to deliver on the micro-economic commitments expressed in its NRP, although a number of challenges remain. The point to watch in the area of fostering an attractive economic environment has been addressed to some extent. More efforts are needed to facilitate start-up procedures, including the recruitment of the first employee, to speed up the transposition of EU directives, and to strengthen market competition, in particular in the professional services sector. The Commission considers this a mixed policy response to the challenges Luxemburg faces for improving the economic environment.

Employment policies

16. Recent structural reforms launched by the government and the social partners focus on measures for retaining people in employment, flexible contractual arrangements, activation policies for young people and reducing numbers leaving school early. The employment of women has improved since 2003, facilitated by an expansion of childcare facilities. However, more initiatives are needed to increase the employment rate of older workers and to tackle unemployment amongst the young.

17. The Council referred to the need to focus on: raising the employment rate of older workers and further reform early-retirement systems: to reduce school drop-out rates and remove artificial barriers between different types of education; and to closely monitor the impact of recent measures on youth unemployment. There has been little policy response to support active ageing, and no progress in changing culture towards longer working lives, improving incentives to remain in work and discouraging early retirement. However, the recent law on vocational training may have a positive impact on the employment rate of older workers. Increasing the employment rate of older workers is also closely linked to the modernisation of social protection systems and their financial sustainability.

18. A broad set of measures to improve education and training and lifelong learning have been approved in order to fight worsening trends in early school leaving and the

completion of upper secondary education, with recent legislation including new measures to assist early school leavers to re-enter education and vocational training. A further law reorganizes vocational training and helps to support young people in the transition from school to work. Steps have been taken to improve the recognition and validation of qualifications and competences, and enrich training opportunities. However, as implementation is still in its initial phase, it remains to be seen whether these reforms will be sufficient.

19. Luxembourg is taking appropriate measures to improve activation and professional guidance, especially for young people. The introduction of a personal mentor will help re-integrate the young unemployed into the labour market and improve their employability. However, as implementation has only just begun, it remains important to closely monitor the impact of the new measures.

20. Overall, Luxembourg has a balanced approach towards flexicurity and is taking steps towards addressing it in an integrated way. Recently social partners have reached a consensus on the introduction of a single status for private sector employees, which should increase labour market flexibility. Recent reforms of active labour market policies concentrate on the rapid insertion of young people, and a new law aims to anticipate restructuring and support career transition. Life long learning considerably improved in 2007 and a right to individualized training will take effect on 1st January 2008. However, there is no visible progress on the continued adaptation of the social security system.

21. In general, Luxembourg has succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. The points to watch in the employment area have been addressed, with the notable exception of active ageing. Although progress is evident, implementation is now the key and therefore the Commission considers these points to watch as remaining valid.

PART III: CONCLUSIONS

22. In the light of the Luxembourg 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

23. Luxemburg has made very good progress in implementing its National Reform Programme over the 2005-2007 period. Luxembourg has shown some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

24. The Implementation Report shows a mixed policy response to the areas identified by the Council as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

25. Among the strengths shown by the Luxembourg's 2007 Implementation Report are: investments to integrate the economy into the international context, efforts to develop an extensive simplification policy focussed on business needs, the

development of childcare infrastructures, reform of professional training, and the introduction of new forms of employment.

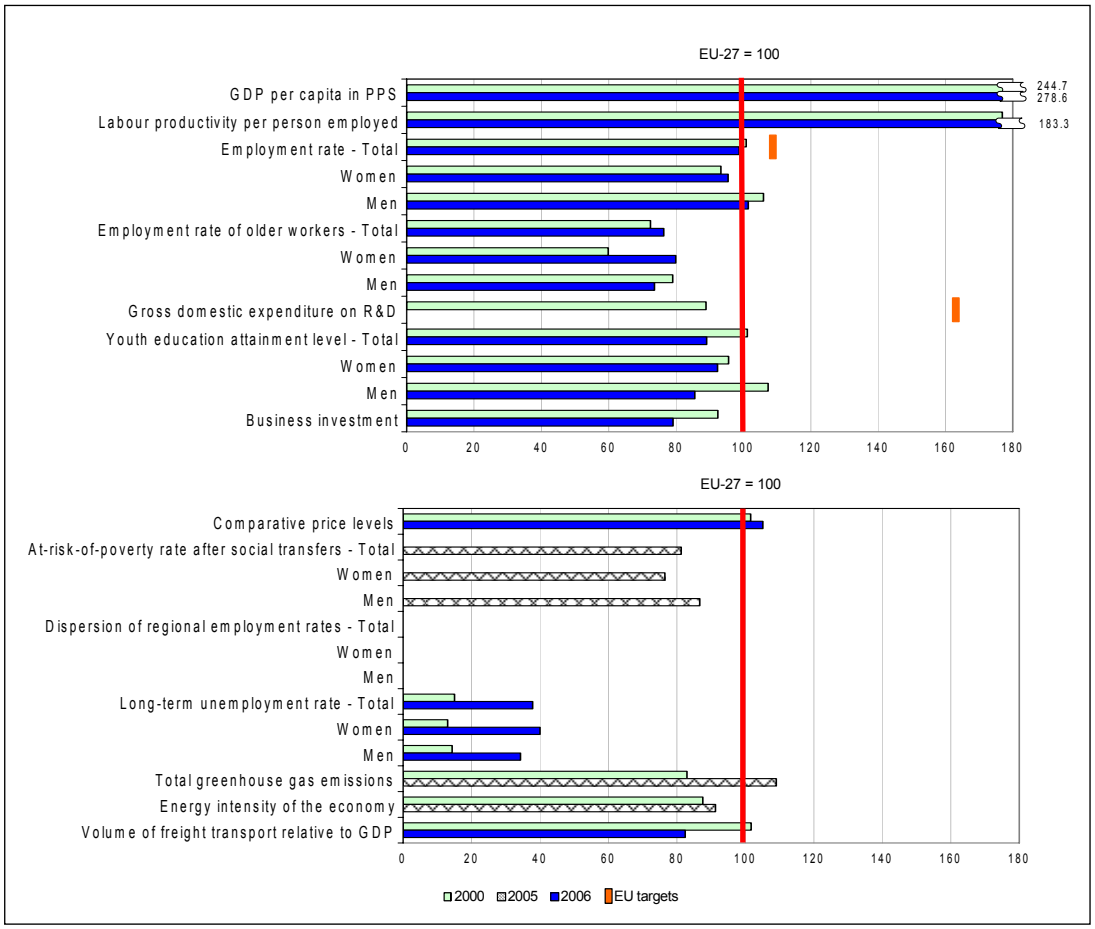
26. It will be important for Luxembourg over the period of the National Reform Programme to focus on the following challenges: accelerate the implementation of measures aimed at increasing the employment rate of older workers, in particular through reform to discourage early retirement; take further measures to reduce the number of early school leavers, and to remove the artificial barriers between different types of education; closely monitoring the impact of recently adopted measures to reduce unemployment amongst the young; and in order to deliver a more attractive economic environment, greater support is needed to deliver competitive markets, improve the transposition of EU legislation, and support SMEs.

PART IV: STATISTICAL GRAPHS AND DATA

LUXEMBOURG

		LU						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		244.7	247.7	252.7	263.0	278.6		100.0	100.0	100.0	
Labour productivity per person employed		176.9	166.4	168.9	174.4	183.3		100.0	100.0	100.0	
Employment rate	Total	62.7	62.2	62.5	63.6	63.6	:	62.2	63.4p	64.4p	70.0
	Women	50.1	50.9	51.9	53.7	54.6		53.7	56.2p	57.2p	
	Men	75.0	73.3	72.8	73.3	72.6		70.8	70.8p	71.6p	
Employment rate of older workers	Total	26.7	30.3	30.4	31.7	33.2		36.9	42.3p	43.5p	
	Women	16.4	20.6	22.2	24.9	27.8		27.4	33.5p	34.8p	
	Men	37.2	39.7	38.3	38.3	38.7		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.65	1.66	1.63	1.57p	:	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	77.5	72.7b	72.5	71.1	69.3		76.6	77.4	77.8	
	Women	75.8	75.6b	73.4	75.8	74.5		79.3	80.1	80.7	
	Men	79.2	69.7b	71.6	66.6	64.0		73.8	74.7	74.8	
Comparative price levels		101.5	103.2	105.1	104.6	105.1		100.0	100.0	100.0	
Business investment		17.0	17.0	16.5	15.5	14.4		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	12.0	11.0b	12.0	13.0	:		:	16.0e	:	
	Women	12.0	12.0b	12.0	13.0	:		:	17.0e	:	
	Men	12.0	11.0b	12.0	13.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	0.6	0.9	1.1	1.2	1.4		4.0	4.1p	3.7p	
	Women	0.6	0.9	1.4	1.2	1.6		4.6	4.5p	4.0p	
	Men	0.5	0.9	0.8	1.2	1.2		3.5	3.8p	3.5p	
Total greenhouse gas emissions		75.2	88.6	100.8	100.4	:		90.7	92.1	:	
Energy intensity of the economy		186.6	181.8	193.5	189.9	:		213.1	208.1	:	
Volume of freight transport relative to GDP		100.8	111.8	107.2	92.4	87.9e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Hungary

1. Economic growth started to slow down in 2006. GDP is projected to expand by 2% in 2007, down from 3.9% in 2006. The growth profile reflects to a large extent the correction of the unsustainable path of fiscal policy over the last few years. Employment and participation rates are still far below average EU levels, despite slightly improving to 57.3% and 62% respectively in 2006. After rising to 9.2% of GDP in 2006, the budget deficit is expected to fall below 6.5% of GDP in 2007, and the increase in the debt-to-GDP ratio is projected to slow down.

2. The overriding priority for Hungary is to continue its fiscal consolidation programme underpinned by sound structural reforms, and a comprehensive reform of fiscal governance. Progress in fiscal consolidation will underpin an expected return to a robust growth path. At the same time, long-term sustainability of public finances, which is at high risk, should be ensured. Institutional and regulatory measures to improve the functioning of labour markets, and the micro-economic environment should also be implemented, but without jeopardising fiscal consolidation.

PART I: GENERAL ASSESSMENT

3. Overall, the 2007 Hungarian Implementation Report shows limited progress on implementing the revised National Reform Programme (NRP) over 2005-2007. Hungary is making strong efforts and the pace of progress has accelerated over the last year.

4. There has been some progress on responding to the four country-specific recommendations addressed to Hungary by the Council. The fiscal consolidation programme is likely to result in a better-than-targeted budgetary outturn in 2007. However, the deficit is still high and the medium-term public finance situation remains fragile. Further incentives to work and to remain in the labour market have been introduced and good progress has been made towards the establishment of the integrated employment and social services system. As Hungary's priority is on fiscal consolidation, progress has been limited in relation to education, training and active labour market policies.

5. With regard to the other areas on which the Council concluded that Hungary should focus, progress has been most substantial on developing a coherent strategy for R&D, innovation and ICT and transforming undeclared work into formal employment.

6. Last year's Annual Progress Report concluded that Hungary had made limited progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. There has again been limited progress on most of the commitments with an end-2007 deadline.

7. Government and ownership of the NRP seems somewhat strengthened. The report was discussed by Parliament and stakeholders before submission. Although clear timetables were presented for the reform steps, systematic information on the

budgetary impacts of the adopted and planned measures is missing. The operational programmes co-financed by the structural and cohesion funds play a key role in the implementation of the NRP and their common governance is ensured. However, the earmarking of structural funding for Growth and Jobs objectives could be stronger.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The NRP identified reducing the fiscal deficit and improving the sustainability of public finances as key macro-economic challenges. Progress in this respect over 2005-2007 is mixed. After years of loose fiscal policy which had induced serious macroeconomic imbalances, the re-elected government started a major fiscal consolidation and reform programme in the second half of 2006. The first results are starting to bear fruit but further progress is needed. Wage developments and the evolution of non-wage labour costs should also be continuously monitored as there is a need to improve wage responsiveness to economic changes.

9. The Council recommended Hungary to address the government deficit and public debt ratio; and to improve long-term fiscal sustainability and economic efficiency. Wide-ranging tax increases and expenditure control measures, including budgetary freezes until the end of 2008 limited the deficit in 2006 to 9.2% of GDP, still very high but almost 1% of GDP less than targeted. Hungary is likely to outperform its 2007 target of 6.8% of GDP by about half a percentage point. However, this reduction could have been around one percentage point if no additional spending measures had been taken. The debt-to-GDP ratio is expected to stabilise at around 66% in 2007-2008. An important blueprint for the comprehensive reform of public finances was adopted in 2007, introducing fiscal rules and institutional changes. The implementation of these proposals is however, dependant on related constitutional amendments being passed. A reinforcement of the budgetary framework has just begun, essential, given that the budget deficit, although declining, remains the highest in the EU.

10. Following the adoption of laws in 2006 to reform the public administration, health care, pension and education systems, the Government has implemented measures in these areas in 2007. Significant spending cuts in price subsidies were achieved, in particular for pharmaceuticals and gas. Moreover, the public administration and hospital systems have been further streamlined, although follow-up steps, such as the improvement of outpatient care, are still missing. Thanks to a series of financial incentives, the provision of joint services at local government level has also been substantially strengthened. On pension reform, in addition to the revision of disability pension schemes in 2007, several other steps have been adopted which will impact on the long-term pension costs. These include a lower starting level for new pensions, actuarially fair pension calculation and stricter eligibility regulation in early retirement. The expert group set up by government will further review the reform of the key parameters (indexation, retirement age). Overall, the sustainability of Hungarian public finances remains at high risk, given the expected rise in long-term age-related expenditures. Further actions are needed in all areas, also in view of ensuring social adequacy.

11. Hungary has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. Following the lack of fiscal discipline in the past, the recent policy responses have been fairly strong. However, the public finance situation remains fragile. Hungary needs to maintain the momentum with fiscal adjustment and structural reforms and therefore the recommendations remain valid.

Micro-economic policies

12. The revised NRP of 2006 identified R&D and innovation, business environment, competition, infrastructure development, and energy policy and environment as key micro-economic challenges. In its conclusions, the Council also referred to reducing and redirecting state aids; develop a more coherent strategy for R&D, innovation and ICT; and further reduction of the administrative burden on enterprises.

13. Concerns remain about the absence of concrete measures to reduce state aid and redirect funds towards horizontal objectives, and in particular whether the phasing-out of aid will suffice. On R&D and innovation, the recently adopted strategy is welcome but further progress is needed. Following previous reforms, the adoption of the science, technology and innovation strategy, which seeks to co-ordinate public and private R&D and innovation, and to stimulate the creation and utilisation of knowledge, represents a significant step. However, reaching 1.4% of GDP (changed from 1.8%) for total R&D expenditures by 2010 depends on the availability of resources and the efficient implementation of a recently adopted action plan. Concerns remain about how to integrate the Academy of Science in the research and innovation system and how to improve the links between research and business. In addition to simplifying the legal framework for e-business, ICT initiatives focus on infrastructure development and increasing ICT use. This heads in the right direction, but implementation should be accelerated. Faster progress can now be expected as EU structural funds will increasingly be used. Obstacles continue to hinder entrepreneurial activities and the targets set in the 2006 Spring European Council conclusions were only partially achieved.

14. Better regulation policies focus on simplification and on reducing the administrative burden, but no specific target has been set for the later. Preparatory work for improving impact assessments is being carried out but implementation remains inadequate. There has however been a significant shortening of the setting-up time for businesses, and, as of 2008, the electronic registration of a company should require less than one hour. Newly adopted measures to improve access to finance for enterprises should benefit SMEs. However, only limited progress can be seen in promoting education in entrepreneurship and the establishment of a single contact point for recruiting the first employee.

15. The opening of the rail freight market has been delayed and the development of the Coherent Transport Development Strategy needs to be accelerated given the composition of infrastructure spending and the dispute over the feasibility of rail infrastructure financing via access charges. Hungary should continue its efforts to ensure timely and full implementation of the Services Directive.

16. Regarding environment and energy, new legislation to promote green electricity is a welcome step. Hungary has also announced a National Climate Change Strategy, but

concrete measures have still to be devised. The liberalisation of network industries is on course. However, since the ownership of electricity transmission networks reverted to the previous owner in 2006, there is some concern about the effective separation of infrastructure and operations.

17. Overall, despite encouraging signs in some areas, the progress over 2005-2007 is mixed with regard to policies addressing the challenges set out in the NRP. Hungary needs to maintain the pace and scope of microeconomic reforms if it is to achieve the growth and job creation necessary to underpin rapid economic improvements. The points to watch in the micro-economic area therefore remain valid.

Employment policies

18. In 2006, the revised NRP set the priorities of: strengthening the role of active labour market policies; targeted support for the employment of disadvantaged people; promoting lifelong learning; and improving the quality, effectiveness and efficiency of education.

19. The Council recommended a focus on: improving active labour market policies and incentives to work, integrating the employment and social services system, and reforming education and training, to improve skills and the responsiveness to labour market needs.

20. Active labour market policies increasingly aim at enhancing job-search activity and improving employability, with measures targeted on the most disadvantaged groups. The scope and effectiveness of these policies needs to be improved. A number of incentives to work and to remain on the labour market have been introduced, including recent measures reforming the social benefit system. Further reforms to reduce early retirement and revise the system of disability benefits are also welcome. Given the very low rate of return to employment of women after childbirth, further measures are required to reconcile work and family life, including the extension of childcare provision and reforming lengthy parental leaves. The integration of employment and social services is in progress and the public employment service has coordinated rehabilitation services since 2007.

21. The integration of schools, and restrictions on them in the selection of students, together with the introduction of new national curricula focusing on key competencies, are among recent measures to reduce school segregation and to provide pupils with skills which better respond to labour market needs. Higher education quotas in natural sciences, IT and technology were also increased to ensure the provision of a sufficient number of graduates in these fields. Despite these welcome steps, the existence of a clear strategy to achieve systemic changes to improve the quality, openness and efficiency of education and training is not evident.

22. The Council also highlighted the need to focus on improving the labour market situation of the disadvantaged; tackling undeclared work; reducing regional disparities in employment; and implementing the lifelong learning strategy. Although a number of measures were launched to improve the labour market situation of disadvantaged groups, the result of these measures remains to be seen. In certain areas progress is limited. Besides helping career-starters, older workers and women, further efforts are required to improve the employment chances of the low skilled,

people with disabilities, and the Roma. Strong coherent measures, focused on incentives and sanctions have led to visible progress in reducing undeclared work. However, given the gravity of the problem, it is important to continue this approach. There has been no visible progress in reducing persistent regional disparities in employment. A coherent policy approach to tackle this challenge, including the low mobility of the labour force is still missing. The implementation of the lifelong learning strategy, although it has started, remains a considerable challenge, requiring stronger coordination and monitoring.

23. Hungary has started to address flexicurity in an integrated way. Strengthening active labour market policies, the modernisation of social security systems and combating undeclared work have been given particular attention. Increasing participation in lifelong learning is a challenge. The government, with the involvement of the social partners, aims at a comprehensive revision of the Labour Code to reflect the diversity of employment forms and ensure adaptability.

24. Despite clear improvements in certain areas, there has been partial progress over 2005-2007 with regard to the implementation of policies to address the labour market challenges. The policy response to the recommendations and points to watch has also been partial. It is important to deepen and step up the pace of reforms, in particular in education and training.

PART III: CONCLUSIONS

25. In the light of the 2007 Hungarian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

26. Hungary has made limited progress in implementing its National Reform Programme over 2005-2007. Hungary has shown limited progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

27. The Implementation Report shows a mixed policy response to the recommendations adopted at the Council. There has been some policy response on the additional areas identified in the Council conclusions as requiring more attention.

28. Among the strengths shown by the 2007 Implementation Report are: strong improvements on fiscal consolidation, the adoption of various structural reform steps, the shortening of the setting-up time for businesses and the efforts to reduce administrative costs, the introduction of further incentives to work and to remain on the labour market and the transformation of undeclared work into formal employment.

29. The policy areas in the Hungarian National Reform Programme where challenges need to be tackled with the highest priority are: correcting the excessive deficit as planned, further improving the sustainability of public finances, improving the labour market situation of disadvantaged groups, reducing persistent regional disparities in employment and reforming the education and training systems. Against this background, it is recommended that Hungary:

- continues to implement the necessary measures to ensure a durable reduction of the government deficit and of the public debt ratio, with increased reliance on the expenditure side, including through the establishment of more thorough and comprehensive expenditure rules;

- continues to reform the public administration, health care, pension and education systems with a view to ensuring long-term fiscal sustainability and improving economic efficiency. This should include steps to further limit early retirement, reduce the number of new recipients of disability pensions and further restructure health care;

- reinforces active labour market policies to improve the labour market situation of disadvantaged groups; and reduces persistent regional disparities in employment;

- ensures access to high quality education and training for all, upgrade skill levels, and increases responsiveness of education and training systems to labour market needs.

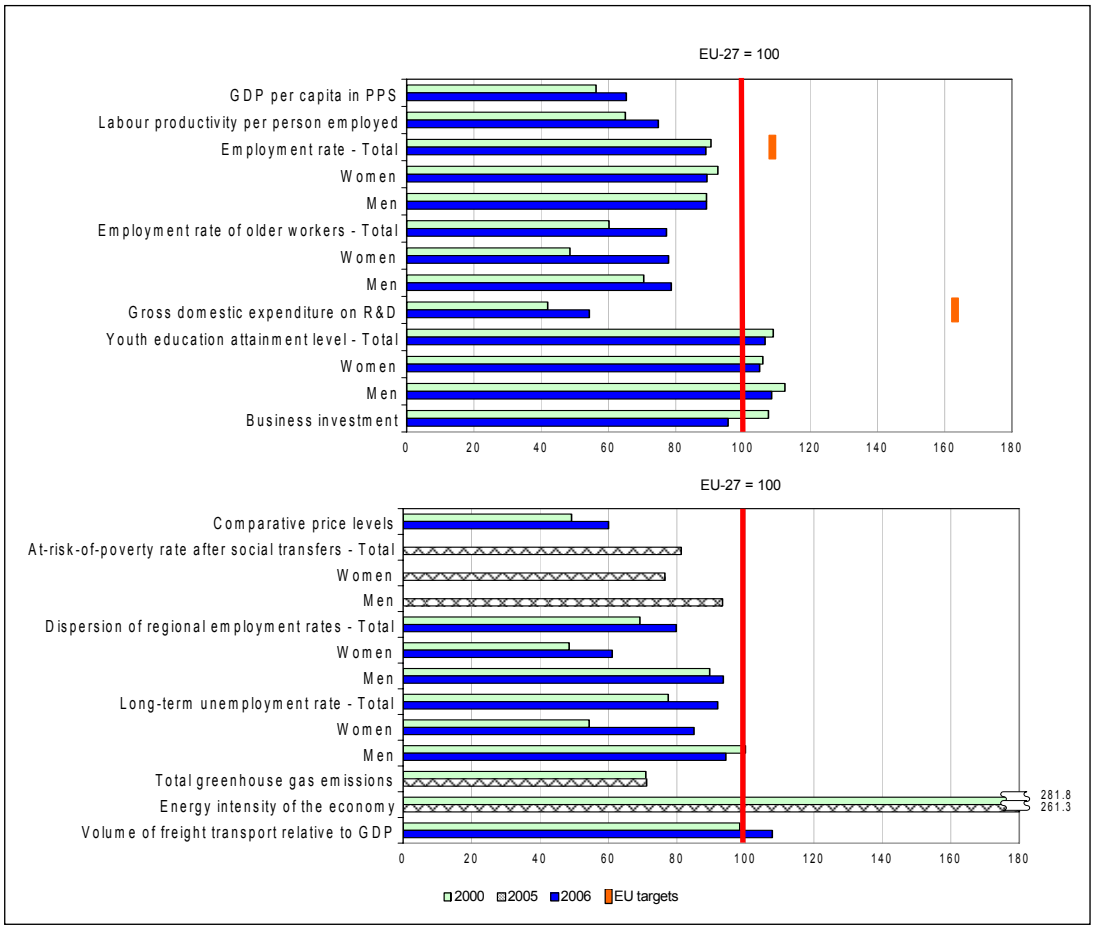
30. In addition, it will be important for Hungary over the period of the National Reform Programme to focus on the following challenges for the future: further reforming the public research system, increasing the effectiveness of public R&D expenditure and improving linkages between public and private R&D; reducing and redirecting state aids; improving the regulatory environment through further reducing administrative burden and legislative simplification; introducing further incentives to work and to remain in the labour market; ensuring better reconciliation of work and private life; completing the establishment of the integrated employment and social services system; transforming undeclared work into formal employment; and implementing the lifelong learning strategy.

PART IV: STATISTICAL GRAPHS AND DATA

HUNGARY

		HU						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		56.3	63.6	63.9	64.8	65.3		100.0	100.0	100.0	
Labour productivity per person employed		65.0	71.7	72.7	73.9	74.8		100.0	100.0	100.0	
Employment rate	Total	56.3	57.0	56.8	56.9	57.3	58.7	62.2	63.4p	64.4p	70.0
	Women	49.7	50.9	50.7	51.0	51.1		53.7	56.2p	57.2p	
	Men	63.1	63.5	63.1	63.1	63.8		70.8	70.8p	71.6p	
Employment rate of older workers	Total	22.2	28.9	31.1	33.0	33.6		36.9	42.3p	43.5p	
	Women	13.3	21.8	25.0	26.7	27.1		27.4	33.5p	34.8p	
	Men	33.2	37.8	38.4	40.6	41.4		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.78	0.93	0.88	0.94	1.00	1.8	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	83.5	84.7b	83.5	83.4	82.9		76.6	77.4	77.8	
	Women	84.0	86.1b	84.9	84.9	84.7		79.3	80.1	80.7	
	Men	83.0	83.4b	82.0	81.9	81.2		73.8	74.7	74.8	
Comparative price levels		49.2	58.2	61.6	63.2	60.0		100.0	100.0	100.0	
Business investment		19.8	18.6	18.9	18.8	17.4		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	11.0	12.0	:	13.0b	:		:	16.0e	:	
	Women	12.0	12.0	:	13.0b	:		:	17.0e	:	
	Men	11.0	12.0	:	14.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	9.0	8.5	9.4	9.9	9.1		13.0	11.9	11.4	
	Women	9.7	9.2	10.6	10.8	9.9		20.0	16.8	16.2	
	Men	8.6	8.1	8.6	9.4	8.7		9.6	9.7	9.3	
Long-term unemployment rate	Total	3.1	2.4	2.7	3.2	3.4		4.0	4.1p	3.7p	
	Women	2.5	2.3	2.6	3.2	3.4		4.6	4.5p	4.0p	
	Men	3.5	2.5	2.8	3.3	3.3		3.5	3.8p	3.5p	
Total greenhouse gas emissions		64.3	66.8	64.7	65.5	:		90.7	92.1	:	
Energy intensity of the economy		600.5	566.6	533.6	543.6	:		213.1	208.1	:	
Volume of freight transport relative to GDP		97.5	85.1	91.5	102.1	115.1		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Malta

1. Following a slowdown in the early 2000's, Malta's economic growth has recovered since 2004, with GDP growth reaching 3.2% in 2006. The turnaround was mainly driven by domestic demand. In relation to the EU-27 average, labour productivity has been declining in recent years but stabilised in 2006. GDP per capita amounted to 75.5% of the EU-27 average in 2006. Malta's employment rate (54.8% in 2006) remains well below the Lisbon target, particularly for women and older workers. The general government deficit has been reduced to 2.5% of GDP in 2006 from 3.1% in 2005 and Malta's general government debt declined from 72.7% of GDP in 2004 to 64.7% in 2006.

2. The structural weaknesses of Malta's economy necessitate a continuing reform policy to bolster competitiveness and exploit long-term growth potential. The continued implementation of structural expenditure reforms would contribute to sounder public finances in the medium-term and help release more public funds for growth-enhancing spending such as R&D and innovation. The continuation of efforts to reform health care as well as to pursue the further review of the benefit system could improve the long-term sustainability of public finances, and simultaneously facilitate moves into regular employment. Growth and employment are expected to benefit from the implementation of recent initiatives as well as from reducing and redirecting state aid towards horizontal objectives and strengthening competition.

PART I: GENERAL ASSESSMENT

3. The Maltese 2005-2008 National Reform Programme (NRP) identified the sustainability of public finances, competitiveness, the environment, employment and education and training as key challenges. In addition, the Commission focussed on competition, the quality of the regulatory system, and making work more attractive.

4. Overall, the Implementation Report shows good progress on implementing the NRP over 2005-2007 in many key areas. Malta has followed a steady reform policy over the period. The most prominent result of this policy is the Council decision in favour of Malta's adoption of the euro on 1st January 2008.

5. However, Malta has shown only limited progress in addressing the recommendations adopted by the Council to reinforce the competition authority and to attract more people into the labour market.

6. The Council also concluded that Malta should focus on health care reform, speeding up progress on improving and simplifying the regulatory environment, measuring R&D expenditure more accurately, introducing systematic impact assessment, connecting Malta to Europe's energy network, raising educational attainment and increasing the employment rate of older workers. The response in these areas has also been limited.

7. Last year's Commission Annual Progress Report concluded that Malta was partly responding to the commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since

then Malta has made some further progress, on better regulation, ICT and innovation. However, more concrete steps are needed to meet all commitments in the area of improving competition.

8. The governance of the NRP has been very good, involving all relevant ministries and an extensive consultation with stakeholders. The links between the NRP and the Structural Funds' programmes are good: 45% of the total NSRF budget is earmarked for implementing the Lisbon strategy (up from 20% in the previous programming period). This limited share of funds devoted to improving competitiveness, in comparison to other Member States, stems from plans for strong investment in environmental infrastructures to ensure the environmental sustainability of tourism. Cohesion Policy funding will amount to 2.4% of GDP in the 2007-2013 period.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. Malta made good progress over 2005-2007 in addressing the macro-economic challenge of restoring the fiscal balance. The fiscal consolidation process, initiated in 2004, has shown good progress. Although some part of this progress has been because of one-off measures, budgetary adjustment has been achieved mostly through expenditure restraint. The general government deficit declined to 2.5% of GDP in 2006, and the debt-to-GDP ratio followed a downward trend. As a result, the Council decided to abrogate the Excessive Deficit Procedure, paving the way for Malta's adoption of the euro on 1st January 2008. The Implementation Report underlines the Maltese government's continued commitment towards further fiscal consolidation through public expenditure restraint.

10. There has been some progress in the area of long-term sustainability of public finances. The main provisions of the new pension system, which came in force in January 2007, include a progressive increase in the retirement age, a longer reference period used for the calculation of pensions and a change in the indexation of pensions.

11. During 2005-2007 some progress was achieved in re-directing public expenditure towards growth-enhancing spending. In particular, increased attention has been devoted to upgrading Malta's human capital. However, the reallocation of additional public funds towards innovation, research, and development was less ambitious. Such a restructuring could support the achievement of the objective to attract high-technology investment and bolster Malta's competitiveness and growth potential.

12. The Council referred to the need to implement and reinforce delayed measures in healthcare reform. The financial sustainability of the healthcare system depends on reversing past spending trends. New legislation, announced in the NRP, that would separate the regulation and delivery of the healthcare system, has not been fully implemented. The Maltese authorities have put in place the required administrative steps for implementation. Moreover, the authorities regard the full implementation of these measures essential to improve the public healthcare system's financial management and control systems and ensure value for money and the efficient use of resources.

13. In general, Malta is making good progress in improving public finances and some progress in re-directing public expenditure towards growth-enhancing spending. Malta is making limited progress in addressing the financial sustainability of the healthcare system and therefore the Commission considers that the point to watch in this area remains valid.

Micro-economic policies

14. Competitiveness and the environment were identified as key micro-economic challenges in the Maltese NRP. These challenges include the business environment and better regulation, R&D, innovation and ICT, tourism, infrastructure and competition. Malta has, overall, made good progress over 2005-2007 through better regulation initiatives, a broad-based approach to strengthen R&D, ICT, and some steps towards liberalisation.

15. The Council recommended that Malta should strengthen competition, notably by reinforcing the Competition Authority, liberalising professional services and reducing and redirecting state aids. The Maltese authorities are developing measures to strengthen the enforcement capabilities of the competition authority and to amend the Competition Act but these measures are yet to be implemented. Consultation and dialogue with regard to professional services is still ongoing but has not yet resulted in reform measures. Malta needs to enhance its efforts to ensure a timely implementation of the Services Directive. The level of state aids (2.25% of GDP in 2006) and the share of sectoral aid (93%) in Malta are still the highest in the EU. Malta needs to progress in this area given that there has also has been an increase of infringement cases. Malta should improve the quality of the transposition of internal market legislation.

16. The Council also asked Malta to focus on impact assessment and simplification. Malta shows strong political support for the better regulation agenda and is making progress in improving the regulatory environment. All of the public sector is now involved in the Simplification Action Plan and Malta has appointed a better regulation co-ordinator in every ministry. Malta could do more to enhance the regulatory framework by continuing ongoing simplification, making a systematic use of impact assessments, and ensuring a transparent better regulation strategy. Regarding the reduction of the administrative burden, Malta has planned several measures for 2008 and 2009. However, no specific target has yet been set. Malta also reports on the introduction of one stop shops for business start-ups but it appears that they are not yet fully operational.

17. The Council highlighted the need of measuring R&D expenditure more accurately. The Implementation Report reaffirms Malta's commitment to an R&D intensity target of 0.75% for 2010. The level of public investment in R&D has increased to 0.20% of GDP in 2006. Steps have also been taken to increase the number of researchers, through funds for postgraduate studies, by facilitating access to Malta for researchers from other countries, and by promoting the attractiveness of science to students. Selected government entities will implement Research and Innovation programmes and spend at least 0.25% of their budgets for 2008 on this. Links between industry and academia are being encouraged. However, the report does not inform on developments in private sector R&D, a sector which accounts for almost 65% of the R&D expenditure.

18. The Council also asked Malta to look into the issue of connecting Malta to Europe's energy network. As a response, Malta is currently seeking advice on the feasibility of this. This would improve the functioning of the energy market, and reduce the current complete dependency on imported oil. Additional steps could include an increased emphasis on energy efficiency and on renewable energy.

19. Malta considers ICT as crucial for the modernisation of its economy and has made significant progress in the past three years. Policy attention mainly focuses on e-Government, e-Inclusion and ICT take-up and enhancing employment in the sector by promoting ICT skills and competencies. There have been strong advances in the online availability of public services but more attention needs to focus on ICT usage, both of e-services and of broadband. The recent National ICT Strategy for 2008-2010 is expected to stimulate further progress in the area, alongside the SmartCity project. Malta reports increases in tourism due, in part from a growing importance of cruise ships and low cost airlines, and on strategic initiatives to develop this sector further. It highlights that ensuring environmental sustainability is a precondition for a successful tourism strategy which remains a challenge for the future.

20. Overall, Malta has made good progress in implementing measures to tackle its micro-economic key challenges. However, more could be done to stimulate competition, including further reducing state aid and redirecting it towards horizontal objectives. Therefore, the Commission considers the country-specific recommendation in this area to remain valid. Given the limited progress with regard to the points to watch on the regulatory environment, simplification, impact assessment, one stop shops for business start-ups, and on the diversification of energy sources, the Commission considers them to remain valid.

Employment policies

21. The Council recommended Malta to increase efforts to attract more people into the labour market and addressed also the low employment rate of older workers, educational attainment and reducing early school leaving. There has been some progress in 2005-2007 with regard to employment and education performance. The overall employment rate increased slightly, reaching 54.8% in 2006, alongside a female employment rate of 34.9%, which is still the lowest in the EU. Malta's target of a 40% female employment rate by 2010 seems some way off. The employment among older workers remains a problem (30% in 2006 and decreasing), and is especially problematic for older women (only 11.2%). Malta has the lowest secondary school attainment levels and the highest numbers of early school leavers in the EU.

22. Malta is implementing fiscal measures to attract more people, in particular women, into the labour market. These measures include a revision of income tax bands, tax credits for women returning to work, fiscal support for part-time workers, and recognition of people working in family business. Other initiatives aim at an increased use of childcare services and the provision of training. To increase the effectiveness it seems that the implementation of some measures could be extended. In addition, more could be done to improve the match between labour supply and demand and the Implementation Report does not set out any changes to the benefit system. Efforts to tackle undeclared work and to reduce social benefit fraud have

begun to show some positive results. However, their impact on the labour market is not yet clear.

23. Efforts are also in place to improve the education system, in particular by improving infrastructure and the quality of teaching, the implementation of compulsory education system, and the extension of post-secondary and tertiary education courses. Offers of post-secondary and tertiary education courses have increased, with particular attention given to scientific and IT subjects. The government strategy to reduce the numbers of students leaving school early does not appear to target specific groups at risk. It appears that continued reform of education and training systems is necessary to raise the qualification level of the population, to reduce early school leaving, and to increase the number of students staying on in further and higher education.

24. The recent pension reform is an important initiative aiming at an increase of the average retirement age. There are no foreseen measures to increase employment opportunities for older workers to complement the increase in the retirement age. Isolated redeployment schemes that assist the long term unemployed and people over 40 to re-enter the labour market are present but these are not part of a comprehensive approach to active ageing.

25. Malta is not yet addressing flexicurity in an integrated way, although it is implementing some policies under its different components. Some progress has been achieved on fostering part-time work, and on active labour market policies. The government is taking different initiatives to improve lifelong learning but a coherent strategy has not been implemented. This is important to avoid increasing differences in the skills level of the labour force and to prevent unemployment among unskilled young people.

26. Malta has made some progress in implementing measures to deliver on its employment and education challenges. While access to education and training improved, and the social protection system has been modernised, progress was limited on the revision of the benefit system and on employment for older workers. Efforts to tackle undeclared work are promising, but measures to make work pay, especially for women, are limited. Therefore, the Commission considers that the country-specific recommendation remains valid. The Commission also confirms the importance for Malta to focus on raising educational attainment and reducing early school leaving as well as increasing the employment rate of older workers.

PART III: CONCLUSIONS

27. In the light of the 2007 Maltese Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

28. Malta has made good progress in the implementation of its National Reform Programme over the 2005-2007 period. Malta has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

29. The Implementation Report shows a limited policy response to recommendations adopted by the Council. There has also been a limited policy response to the additional areas identified by the Council as requiring attention.

30. Among the strengths of the Maltese National Reform Programme and its implementation are its governance and the progress achieved in fiscal consolidation as well as progress in strengthening the business environment, liberalising certain markets (e.g. ports), reforming education and increasing ICT use.

31. The policy areas in the National Reform Programme where weaknesses need to be tackled with the highest priority are competition policy and persistent labour market problems. Against this background, it is recommended that Malta:

- strengthens competition, notably by reducing state aids and redirecting them towards horizontal objectives as well as by reinforcing the competition authority and by further steps in opening up professional services;

- steps up efforts to attract more people into the labour market, particularly women and older workers; maintain efforts to tackle undeclared work and take further action on the benefit system to make declared work more attractive.

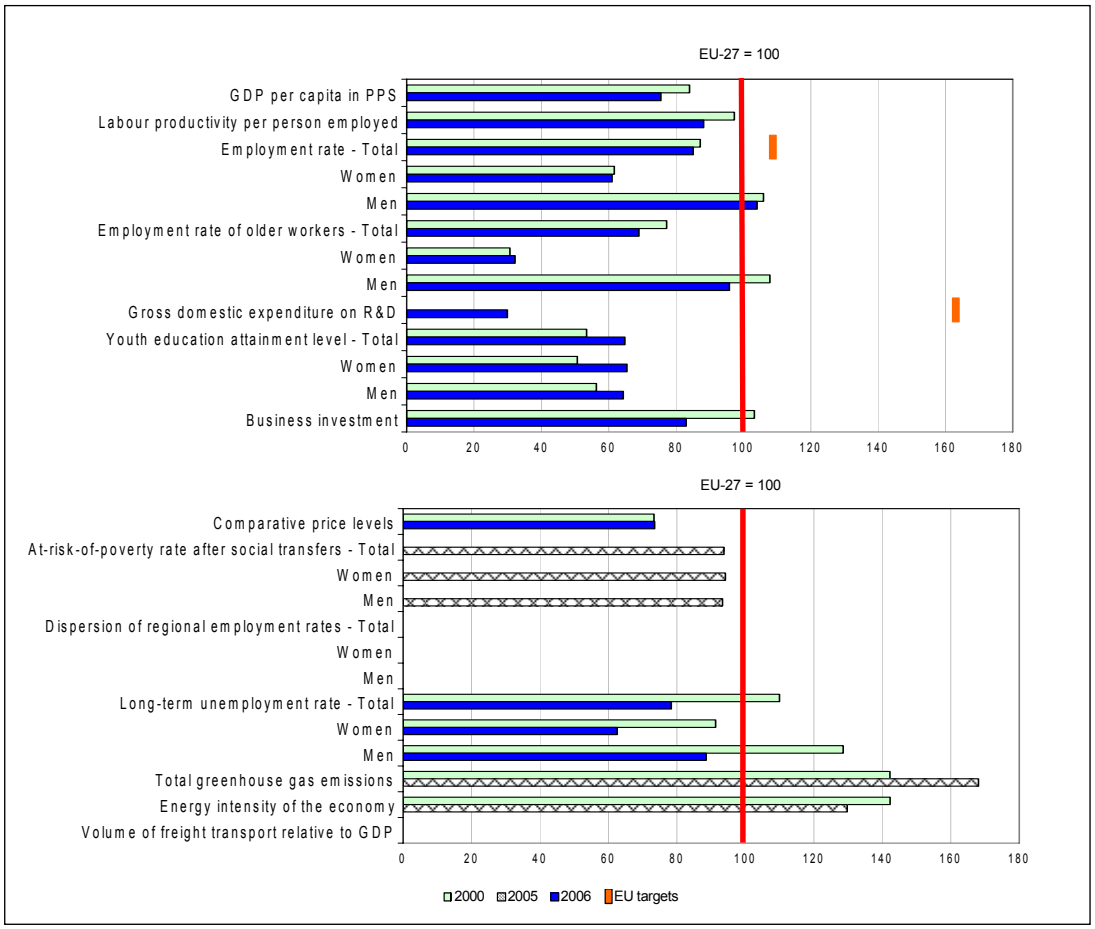
32. In addition, it will be important for Malta over the period of the National Reform Programme to focus on: continue implementing and reinforcing measures on health care reform; further improving the regulatory environment by continuing simplifying legislation, by introducing systematic impact assessments and effective one stop shops for business start-ups; diversifying its energy sources, including enhancing energy efficiency and renewable energy and connecting Malta to Europe's energy networks; continuing efforts to raise educational attainment and reduce early school leaving.

PART IV: STATISTICAL GRAPHS AND DATA

MALTA

		MT						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		84.0	78.7	75.9	75.9	75.5		100.0	100.0	100.0	
Labour productivity per person employed		97.3	90.2	88.4	87.9	88.2		100.0	100.0	100.0	
Employment rate	Total	54.2	54.2	54.0	53.9	54.8	57.0	62.2	63.4p	64.4p	70.0
	Women	33.1	33.6	32.7	33.7	34.9		53.7	56.2p	57.2p	
	Men	75.0	74.5	75.1	73.8	74.5		70.8	70.8p	71.6p	
Employment rate of older workers	Total	28.5	32.5	31.5	30.8	30.0		36.9	42.3p	43.5p	
	Women	8.4	13.0	11.5	12.4	11.2		27.4	33.5p	34.8p	
	Men	50.8	53.8	53.4	50.8	50.4		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		:	0.26	0.54	0.54	0.55p	0.75	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	40.9	45.1b	51.0	53.7	50.4		76.6	77.4	77.8	
	Women	40.2	48.8b	52.4	57.0	52.8		79.3	80.1	80.7	
	Men	41.6	41.3b	49.8	50.5	48.1		73.8	74.7	74.8	
Comparative price levels		73.3	72.0	72.8	72.8	73.5		100.0	100.0	100.0	
Business investment		19.0	14.9	15.4	14.6	15.1		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	15.0	:	:	15.0b	:		:	16.0e	:	
	Women	15.0	:	:	16.0b	:		:	17.0e	:	
	Men	15.0	:	:	14.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	4.4	3.2	3.4	3.4	2.9		4.0	4.1p	3.7p	
	Women	4.2	2.4	3.0	3.2	2.5		4.6	4.5p	4.0p	
	Men	4.5	3.4	3.7	3.4	3.1		3.5	3.8p	3.5p	
Total greenhouse gas emissions		129.0	140.0	145.9	154.8	:		90.7	92.1	:	
Energy intensity of the economy		303.2	284.2	261.0	269.9	:		213.1	208.1	:	
Volume of freight transport relative to GDP		:	:	:	:	:		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



The Netherlands

1. After a slow start of the economic recovery in both 2004 and 2005, economic growth gathered pace in 2006. GDP growth was 3% in 2006 supported by both exports and domestic sources. In line with the early stage of the economic upturn, private investment growth was strong, growing by 7% in real terms. GDP per capita stands at 125% of the EU average in 2006. Buoyant economic growth has led to high labour demand, which has been met by a reduction of unemployment to a rate of slightly above 3% in 2007, and an increase in the overall employment rate. Nevertheless, the average number of hours worked per person is relatively low in comparison to other Member States, partly because of the relatively high share of part-time employment.

2. Implementation of the 2008 budget will restore a positive budgetary position. However, further measures are needed to increase long-term fiscal sustainability, including by raising labour market participation and the number of hours worked. The largest potential of labour supply lies with women, disadvantaged groups and older workers. Growth can also be further enhanced by promoting innovation and the knowledge intensity of the economy.

PART I: GENERAL ASSESSMENT

3. The 2007 Implementation Report, presented by the new Dutch government, shows significant progress in implementing the 2005 National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have slowed down over the last year. In the report renewed ambitions in the area of sustainability and energy are announced. There has been some progress in responding to the country specific recommendation adopted in 2007 in the area of labour supply.

4. The Council concluded that special attention should be given to raising the overall number of hours worked in the economy and raising private R&D expenditure. Progress on these issues has been limited, although many policy measures are being implemented. Last year's Commission Annual Progress Report concluded that the Netherlands had not fully met commitments agreed at the 2006 Spring European Council in the priority action area of unlocking of business potential. Since then, there has been good progress on most of the commitments in the priority action areas with an end 2007 deadline. The Netherlands specifies efforts it is taking to meet euro area recommendations in its latest Implementation Report. It foresees a significant improvement of the headline government deficit and it has strengthened active labour market policies.

5. Consultation and efforts to develop ownership of the NRP at the level of central and local governments and the social partners continue to be substantial. The Implementation Report provides the budgetary information for planned and implemented reform policies. Links between the governance of the implementation of the NRP and the programmes under the Structural Funds are fairly strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily with almost the entire ESF-budget and 63% of the ERDF-budget devoted to these goals.

6. The 2007 Implementation Report confirms the main priorities within the NRP as: improving labour supply; achieving faster growth in labour productivity, in particular by strengthening R&D, innovation and education; and improving price competitiveness, in particular by containing labour costs. The Implementation Report also underlines the importance of a sustainable living environment. The Commission agrees with these priorities.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The Implementation Report reiterates the challenges in the macro-economic domain: promoting a stable macro-economic environment and well-functioning markets as well as attaining a sustainable budgetary position. In 2007, corporate taxes were lowered and legislation for the monitoring of proper conduct of pension funds has been implemented.

8. The Netherlands has committed itself to a structural budget surplus of 1% of GDP in 2011, which will help improve the sustainability of public finances. From a surplus of 1% of GDP in 2006, the structural balance worsened markedly in 2007, to a small deficit of 0.2% of GDP. For 2008 a surplus of 0.5% of GDP is projected. The long-term fiscal position benefits somewhat from planned measures to further increase labour participation, such as tax incentives and measures that aim to simplify the combination of work and care. However, more should be done to ensure sustainable public finances in the long term. The Implementation Report indicates that in recent years, wages have been in line with macro-economic conditions. However, given the labour market shortages in some sectors and the fact that no agreements with social partners are currently foreseen, stronger than expected wage increases in the coming years may affect competitiveness. Further increases in household indebtedness may have an effect on medium-term growth prospects.

9. In conclusion, the Netherlands is progressing in implementing measures to deliver on the macro-economic commitments expressed in its NRP. However, strong growth and a tightening labour market are expected to exert upward pressure on wages. In response to the euro area recommendation, progress is more limited in the area of fiscal consolidation.

Micro-economic policies

10. Improving labour productivity growth by boosting innovation and R&D remains one of the key challenges for the Dutch economy. The Commission welcomes the policy objective of the new government to strengthen the innovative capacity in order to better address societal challenges. The Council referred to the need to focus on: measures to increase private sector R&D expenditure and further action to create a single administration point for the recruitment of the first employee.

11. To improve its R&D and innovation performance, the Netherlands is implementing new measures that in particular promote excellence in higher education and research, facilitate innovative start-ups, and stimulate innovation in SMEs and key sectors. Other measures include the identification and development of innovative clusters

("hot spots"), increasing the number of highly educated people, and to attract foreign knowledge workers. The public contribution to the 3% R&D target remains significant. To promote private R&D expenditure, the Netherlands is strengthening a number of existing policy measures (such as the innovation vouchers scheme and the WSBO fiscal incentives scheme), launching a comprehensive SME strategy, setting up new innovation programmes driven by societal demand (such as water management, sustainable energy, eco-efficient innovations, and health care), and committing to increased accessibility and transparency of policy measures. Generally, the Netherlands is advancing well with the implementation of these measures although there is limited progress on increasing the involvement of the public research base and the level of foreign R&D investment is still relatively low. This needs to be addressed. Given that private R&D has remained stagnant over recent years and that the 3% R&D target for 2010 is very challenging, it will be essential to continue coordination at the highest political level of the R&D and innovation policies which are implemented by many different bodies.

12. The Netherlands has achieved good progress in implementing measures to improve the business environment and to strengthen competition, e.g. by unbundling energy companies. The new government has set ambitious targets with a package of accompanying measures within the "Clean and Green" working programme to counter climate change and to promote renewable energy. Good progress has been made in facilitating the recruitment of the first employee. The number of procedures has decreased considerably, and in most cases the tax authorities are the single point of contact. The Netherlands has made some progress towards the establishment of one-stop-shops for setting up a new business but nation-wide implementation has been delayed, although efforts are announced for the next two years. Lastly, good progress has been made in promoting entrepreneurship education. Although entrepreneurship education is not part of the standard curriculum, a promising programme has begun with implementation on a voluntary basis at all levels of education. Increasingly, the road network in the Netherlands suffers from heavy congestion. To avoid a further worsening of road congestion in the near future, the timely implementation of a comprehensive strategy, including road pricing, appears necessary.

13. As one of the frontrunners in the area of better regulation, the Netherlands aims to build upon the reduction of 20% in administrative costs imposed on business already achieved with an additional net 25% reduced aimed at by 2011. This will be accompanied by a series of monitoring tools to verify if the reduction is noticeable to companies. Although the focus on administrative burden is very positive, the 2007 Implementation Report would have benefited from more specific details on simplification and consultation. The Consumer Authority charged with informing consumers about their rights and obligations started its work in 2007.

14. In general, the Netherlands has made good progress in implementing measures to deliver on the micro-economic commitments expressed in its NRP. The points to watch in the area of business climate and entrepreneurship education have been addressed and good progress has been achieved. These points to watch are therefore not maintained. Progress in the area of private R&D expenditure remains moderate and therefore the Commission considers that the point to watch on this issue remains relevant. In response to the euro area recommendations, good progress has been

made to strengthen competition and to promote the full integration of financial markets.

Employment policies

15. Implementation of labour market policies in the 2005-2007 period focused on reforming benefit schemes, discouraging early retirement, improving childcare provisions and lowering its costs and increasing funding to tackle early school leaving. These policies together with existing labour market institutions have contributed to higher overall employment rates and very low unemployment rates. Progress has been more limited with regard to increasing the number of hours worked by part-time workers and increasing employment rates for disadvantaged groups. Thus, progress over the 2005-2007 period with regard to the implementation of policies to improve labour supply identified by the Dutch 2005 NRP, is mixed.

16. The Council concluded that the Netherlands must take further measures to improve labour supply, notably of older workers, women and disadvantaged groups. In addition, the Netherlands was also asked to focus on raising overall hours worked in the economy. In its response, the Netherlands has set a new overall employment target of 80% for 2016 (in 2006 73%) and announced new policies orientations. These include an action plan to reduce unemployment of older workers and a new tax on pensions - to be progressively introduced from 2011- in case of retirement before the statutory retirement age of 65. In addition, extra funding for improving quality childcare has been announced. New tax incentives directed at women, representing approximately 75% of unused labour potential in the Netherlands, aim at increasing their participation and number of hours worked. Although in the short term the impact of individualising the general tax credit (to be introduced in 2009) will be modest given the long transition period (15 years), it is a step in the right direction. Widening its narrow scope and significantly reducing the marginal tax on second incomes would, however, contribute to removing barriers for increasing the number of hours worked.

17. The Project “Everyone Participates” aims at, amongst others, providing guidance for 200 thousand people at the lower end of the labour market to work by 2011, in particular to foster the long-term (re)-integration of disadvantaged groups which remains a challenge. Lowering the age limit for reassessing disability benefit recipients may have reduced labour supply. Measures to tackle language learning and school drop-out rates have been planned to increase the employment rate of young immigrants. This will be complemented by a strategy for tackling discrimination and a new Integration Plan. The need for an integrated approach to the challenges has been emphasized with the appointment of a Minister for Youth and Family. The national target for reducing early school leaving to 8% has been postponed to 2012.

18. The Implementation Report refers to flexicurity and supports an integrated approach. While until recently the focus has been on reforms increasing back-to-work incentives within the social security system, emphasis is now on improving lifelong learning systems. Active labour market policies are developed and implementation need to further focus on disadvantaged groups. To maintain the current strong performance in terms of employment rates and unemployment of the Dutch labour market, continued efforts to further strengthen flexicurity policies are necessary, for

example by decisions on employment protection legislation. A Committee will be installed to look at all policy options to further increase labour participation.

19. In general, the Netherlands progressed in implementing measures to deliver on the employment policy commitments expressed in its NRP. Many employment measures are announced in the Implementation Report. Because the measures, although positive, remain modest for tackling the challenges ahead and implementation is still in its early stages, the Commission considers the recommendation on labour supply to remain relevant.

PART III: CONCLUSIONS

20. In the light of the 2007 Dutch Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

21. The Netherlands has made significant progress in implementing its National Reform Programme over the 2005-2007 period. The Netherlands has shown a good response to fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

22. The Implementation Report shows some policy response to the recommendation adopted by the Council. There has been a limited policy response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

23. Among the strengths of the National Reform Programme and its implementation are: the efforts to reduce administrative burden and to improve the business climate; the ambitious plans in the area of energy and climate change; and incentives to improve childcare provision.

24. The policy area in the Dutch National Reform Programme where challenges need to be tackled with the highest priority is in improving labour supply. Against this background it is recommended that the Netherlands:

- take further measures to improve labour supply of women, older workers and disadvantaged groups with a view to raising overall hours worked in the economy.

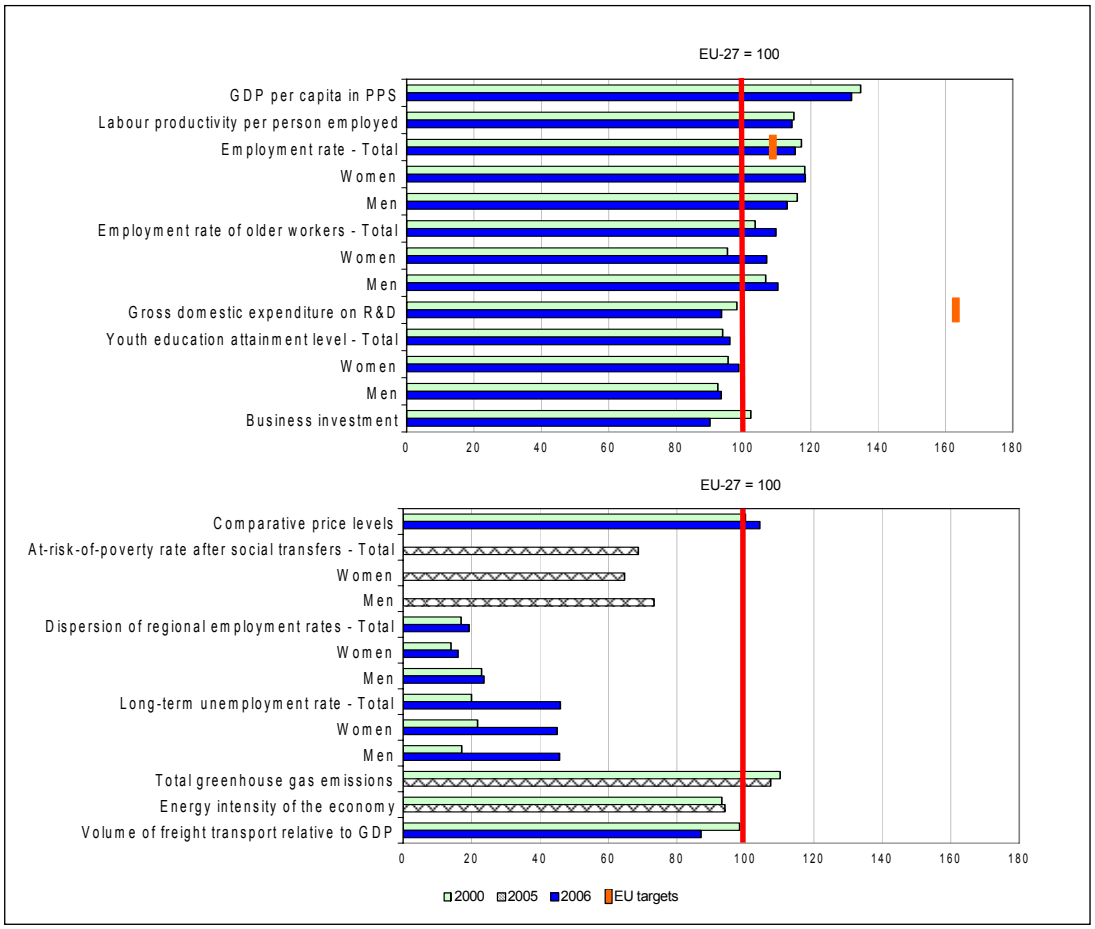
25. In addition, it will be important for the Netherlands over the period of the National Reform Programme to focus on the following challenges: stepping up efforts aimed at increasing private sector R&D expenditure by avoiding fragmented policy governance structures and putting in place a coherent strategy for R&D and innovation which addresses the interaction between private R&D and public research as well as foreign R&D investment.

PART IV: STATISTICAL GRAPHS AND DATA

NETHERLANDS

		NL						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		134.8	129.9	130.3	131.9	132.1		100.0	100.0	100.0	
Labour productivity per person employed		115.0	110.7	112.7	114.7	114.4		100.0	100.0	100.0	
Employment rate	Total	72.9	73.6	73.1	73.2	74.3	:	62.2	63.4p	64.4p	70.0
	Women	63.5	66.0	65.8	66.4	67.7		53.7	56.2p	57.2p	
	Men	82.1	81.1	80.2	79.9	80.9		70.8	70.8p	71.6p	
Employment rate of older workers	Total	38.2	44.3	45.2	46.1	47.7		36.9	42.3p	43.5p	
	Women	26.1	31.8	33.4	35.2	37.2		27.4	33.5p	34.8p	
	Men	50.2	56.7	56.9	56.9	58.0		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.82	1.76	1.78p	1.73p	1.72p	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	71.9	75.0	75.0	75.6	74.7		76.6	77.4	77.8	
	Women	75.7	78.0	78.9	79.9	79.6		79.3	80.1	80.7	
	Men	68.2	72.0	71.2	71.4	69.9		73.8	74.7	74.8	
Comparative price levels		100.0	107.8	106.0	104.6	104.2		100.0	100.0	100.0	
Business investment		18.8	15.9	15.6	15.7	16.4		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	11.0p	12.0p	:	11.0b	:		:	16.0e	:	
	Women	11.0p	12.0p	:	11.0b	:		:	17.0e	:	
	Men	10.0p	12.0p	:	11.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	2.2	2.3	2.3	2.0	2.2		13.0	11.9	11.4	
	Women	2.8	3.2	2.8	2.6	2.6		20.0	16.8	16.2	
	Men	2.2	2.0	2.1	2.1	2.2		9.6	9.7	9.3	
Long-term unemployment rate	Total	0.8	1.0	1.6	1.9	1.7		4.0	4.1p	3.7p	
	Women	1.0	1.1	1.6	1.9	1.8		4.6	4.5p	4.0p	
	Men	0.6	1.0	1.5	1.9	1.6		3.5	3.8p	3.5p	
Total greenhouse gas emissions		99.9	101.1	101.8	98.9	:		90.7	92.1	:	
Energy intensity of the economy		198.5	202.2	202.0	195.6	:		213.1	208.1	:	
Volume of freight transport relative to GDP		97.4	93.7	102.4	101.0	92.9e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Austria

1. Austrian GDP is expected to grow at 3.3% in 2007, exceeding the growth in the euro area by about 0.5 percentage point, as was the case during 2005-2006. The main contributions to growth came from net exports and gross fixed capital investment; private consumption was more moderate. The unemployment rate has declined since 2005 and is expected to stabilize just above 4% in 2007. At 70.2% in 2006, the overall employment rate is relatively high, but the employment rate for older workers (35.5%) still remains well below the EU average (43.5%), even though it increased considerably over the past year.

2. Austria's strong economic performance has been bolstered by its generally consistent and mutually reinforcing mix of policies. There are a small number of shortcomings whose removal could further strengthen its growth potential. In particular, more could be done to better use labour resources, notably older workers, and to improve the integration of vulnerable young people. Sustainable growth will also depend on stronger fiscal consolidation.

PART I: GENERAL ASSESSMENT

3. Overall, Austria has made significant progress in implementing its 2005 National Reform Programme (NRP) over the 2005-2007 period. However, the Council country-specific recommendation concerning older workers and vulnerable youth has only been addressed to some extent. With regard to other areas on which the Council concluded Austria should focus, namely competition in services and emission reduction, there has been some progress. Austria has not moved adequately towards achieving a balanced budget in 2008. Progress in strengthening the entrepreneurial culture and tackling gender segregation in the labour market is limited.

4. Last year's Commission Annual Progress Report concluded that, overall, Austria had given an adequate response to the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Austria is close to fulfilling the commitments with an end 2007 deadline.

5. The Implementation Report specifically addresses the recommendations issued to the euro area countries. Austria has delivered well regarding the flexicurity recommendation. Some steps have been taken to improve the quality of public finances and competition, whereas progress in budgetary consolidation is less substantial.

6. Consultation and efforts to develop ownership of the NRP continue to be substantial. Responsibility for national co-ordination is at ministerial level. A wide range of stakeholders are consulted, including parliament, the social partners, regions, municipalities and economic research institutes. Progress is monitored by an Austrian research institute. Links between the governance of the implementation of the NRP and the programmes under the structural and cohesion funds are strong, with an earmarking of above 90% of structural funding for Growth and Jobs objectives, among the highest in the EU.

7. Following the formation of a new government at the beginning of the year, Austria's 2007 Implementation Report places a new emphasis on the social system while confirming the main priorities within the 2005 NRP. Financial resources have been increased for R&D and innovation, infrastructure and education. A new focus on 'decent work' complements the aim of full employment. The Commission broadly agrees with these priorities.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. Thanks to the recent reform of the pension system, the risk to the long-term sustainability of Austria's public finances is considered relatively low. However, in order to further improve the situation, the authorities committed themselves in the 2005 NRP to some expenditure cuts. These were to come mainly from general expenditure restraint, and the continued reform of the public administration and health care, but they did not materialize to the expected degree. Progress over the 2005-2007 period, in terms of enhancing the sustainability of public finances has therefore been limited.

9. The Council highlighted the need to focus on achieving a balanced budget in 2008. The budget deficit is projected to decline from 1.4% of GDP in 2006 to 0.8% of GDP in 2007. However, in the March 2007 update of the Stability Programme, achieving a balanced budget was postponed until 2009/2010. In its Opinion on the update, the Council invited Austria, after achieving a lower-than-targeted deficit in 2006, to further exploit good economic conditions, strengthen adjustment in 2008, and continue fiscal consolidation thereafter. In its response, Austria has spelt out in the updated NRP a series of measures (public administration and health care reform) contributing to the consolidation of public finances. More detailed information on the budgetary impact of these measures would be welcome. The long-awaited introduction of the medium-term budgetary framework, initially planned for 1 January 2007, was finally adopted by Parliament in December 2007. It is expected to significantly enhance the predictability of the budgetary process from 2009 on

10. In the opinion of the Commission Austria has made limited progress in responding to the point to watch on achieving a balanced budget in 2008, and on the two macro-economic euro area recommendations. Steps have been taken towards improving the quality of public finances by increasing R&D and education spending, and reforming administration, but full use has not been made of the favourable cyclical conditions to approach its medium-term objective.

Micro-economic policies

11. Austria has taken further steps to strengthen innovation capacity and improve the framework conditions for business. R&D expenditure continues to increase, and is expected to reach 2.5% of GDP in 2007, well above the EU average. Besides support for technology development, increased funding aims to develop human resources. However, Austria faces a challenge to meet the demand for science and engineering graduates. Austria remains highly ranked on many indicators of innovation, with the notable exception of venture capital availability. It has introduced a number of

schemes targeting SMEs, including the promotion of collaboration with research organisations, and measures to improve protection and exploitation of intellectual property rights. Innovation policy also focuses on the demand side, with the release in July 2007 of a guideline on public procurement to encourage innovation.

12. In terms of improving the business environment, numerous schemes are now in place, with a strong focus on SMEs. Austria remains committed to reducing the administrative costs incurred by enterprises by 25% by 2010. There are now one-stop-shops for setting up a new company, although these are not yet available country-wide.

13. Infrastructure plays a key role in securing Austria's attractiveness as a business location. The implementation of the information society i2010 initiative has made excellent progress since 2006 and Austria is the first Member State to have achieved full online availability of e-government services. The targets for broadband availability have been met in most regions. Additional resources are being allocated to transport infrastructure, and important projects brought forward to relieve bottlenecks. Priority is being given to improving road and rail connections to the new Member States.

14. The Council referred to the need for Austria to focus on increasing competition in services, strengthening the entrepreneurial culture, and identifying further emission reduction policies and measures. Austria has taken steps to increase shop opening times, and is exploring further measures to increase competition in the electricity and gas markets. In the area of professional services, some reforms have been implemented: entry regulation for architects has been relaxed and recommended fees for accountants, auditors, tax advisors and architects have been removed. However, a number of significant restrictions still remain, in particular in the notary and pharmacy professions, and in legal services.

15. Surveys indicate that the overall entrepreneurial mindset of young people in Austria is low. Entrepreneurship education forms part of the curriculum in some schools, but not all, and this is often at the technical level. The promotion of entrepreneurial skills has been the focus of a number of targeted initiatives. This goes some way towards addressing the challenges Austria faces in this field but a more comprehensive and substantial initiative, particularly targeting entrepreneurial attitudes, remains to be developed.

16. Austria has introduced a number of policy measures directly aimed at reducing CO2 emissions. These include the 2007 revision of the 2002 climate strategy, the creation of a climate and energy fund, the continued implementation of a green electricity act, a climate protection initiative (Klima:aktiv), and the national energy efficiency action plan. In addition, measures such as improving railway infrastructure, and increasing lorry tolls and fuel tax should lead to reduced emissions. Austria continues to be well placed in terms of both the use and export of environmental technologies, and these have contributed to economic growth and job creation. However, thorough implementation of all existing and announced measures is needed because most recent projections indicate that Austria will not meet the Kyoto target with existing policies, including Kyoto mechanisms and carbon sinks.

17. In general, Austria has succeeded in implementing measures to deliver on the micro-economic commitments in its NRP, notably R&D and innovation, infrastructure and the business environment. In the Commission's opinion, there has been a limited response to the points to watch, and euro area recommendation, and they therefore remain valid.

Employment policies

18. Due to good economic developments and the successful overall implementation of employment policies, positive results in labour market performance were achieved over the 2005-2007 period. Active labour market policy was strengthened and the public employment service (AMS) made substantial efforts to integrate groups at the margins of the labour market, although the effectiveness of some measures could be further enhanced. Rising youth unemployment has been tackled effectively through a range of important measures. A newly designed programme to prevent a skilled labour shortage includes more training courses for skilled workers. The recently extended Universities of Applied Sciences have helped increasing the relatively low rate of graduates from tertiary education.

19. The Council recommended Austria to improve incentives for older workers to continue working and enhance the conditions for the education of the vulnerable youth. Active ageing has been supported by a number of measures including awareness raising campaigns, vocational skills development and company-based training, supported by the European Social Fund. However, more emphasis should be placed on encouraging enterprises to adapt working conditions to the needs of older workers, including schemes aimed at preventing health problems. As a result of pension reforms and several tax benefit measures, the actual retirement age has substantially increased. However, the recent reduction of discount rates for early retirement applicable during a long transition period gives the wrong signal. Furthermore, the take-up of early retirement on disability grounds has been increasing. The support of young people with a migrant background through German language acquisition, and the planned introduction of a compulsory year of kindergarten for migrant children are positive steps, but a more comprehensive strategy, including reform of the education system in order to remove early selection, is needed.

20. The Council also referred to the need to focus on tackling the gender segregation of the labour market, including by improving the availability of childcare. Austria has now reformed the childcare benefit scheme, which favours a faster reintegration into the labour market. Childcare facilities have not been significantly expanded thus far, but some additional funding will be made available as of January 2008. A sufficiently ambitious national target has not been set. The new minimum wage will benefit women in particular but it will not be sufficient to substantially reduce the gender pay gap. Austria's policy response in this area has thus been limited.

21. Austria's approach to flexicurity combines considerable flexibility in contractual arrangements with appropriate social benefits, accompanied by active labour market measures and strong reliance on social partnership. A number of measures to enhance flexibility but also increase security have recently been implemented. These include the introduction of more flexible working times, stricter eligibility rules for unemployment benefits, enhanced training leave, improved social protection for

atypically and self-employed people, and an obligation for temporary work agencies to pay contributions for further training of their employees. Moreover, a modernized legal definition of an employee is currently in preparation. More efforts are needed to improve the skills and employability of older workers and the least qualified section of the workforce.

22. Austria has generally succeeded in implementing measures to deliver on the employment policy commitments in its NRP and on the euro area recommendation on flexicurity. The country specific recommendation and point to watch in the employment area have been addressed to some extent and therefore remain valid.

PART III: CONCLUSIONS

23. In the light of the 2007 Austrian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

24. Austria has made significant progress in implementing its National Reform Programme over the 2005-2007 period. Austria has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

25. The Implementation Report shows a limited policy response to the employment recommendation adopted by the Council. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

26. Among the strengths shown by the 2007 Austrian Implementation Report are: good practices to boost innovation, such as the innovation voucher; increased budgets for R&D in line with the 3% target; the creation of a climate and energy fund; the successful implementation and further development of its flexicurity model.

27. The policy areas in the Austrian National Reform Programme where challenges need to be tackled with the highest priority are: increasing labour supply of older workers and improving the skills and employability of disadvantaged young people. Against this background it is recommended that Austria:

- further improve incentives for older workers to continue working by implementing a comprehensive strategy including enhanced job-related training, adaptation of working conditions and tightening the conditions for early retirement; and improve education outcomes for vulnerable youth.

28. In addition, it will be important for Austria to focus over the period of the National Reform Programme on the following challenges: strengthening the fiscal adjustment in order to achieve a balanced budget before 2010; increasing competition in services, in particular in professional services; strengthening entrepreneurship education; identifying further emission reduction policies and measures; tackling the

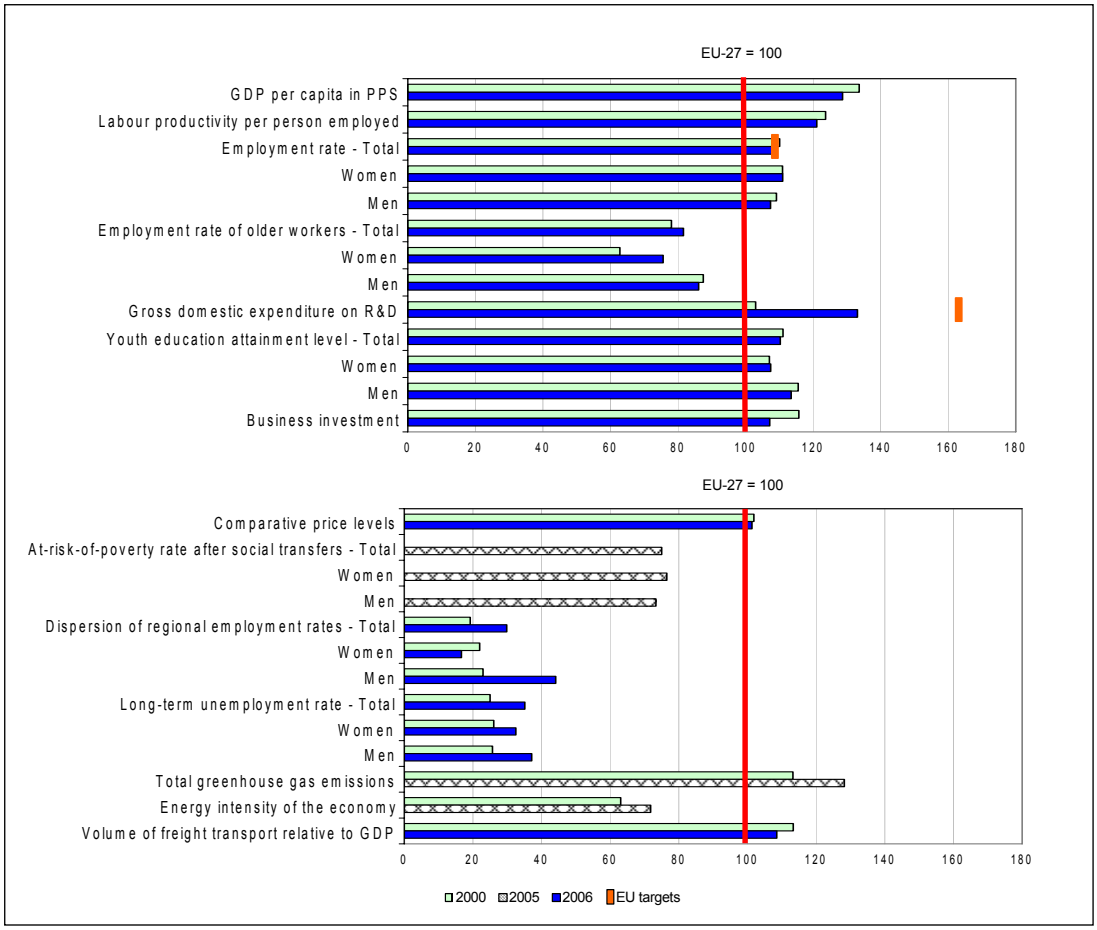
gender segregation of the labour market, including by further improving the availability of childcare.

PART IV: STATISTICAL GRAPHS AND DATA

AUSTRIA

		AT						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		133.7	129.0	128.8	128.6	128.7		100.0	100.0	100.0	
Labour productivity per person employed		123.7	120.0	120.2	119.9	121.1		100.0	100.0	100.0	
Employment rate	Total	68.5	68.9	67.8b	68.6	70.2	:	62.2	63.4p	64.4p	70.0
	Women	59.6	61.6	60.7b	62.0	63.5		53.7	56.2p	57.2p	
	Men	77.3	76.4	74.9b	75.4	76.9		70.8	70.8p	71.6p	
Employment rate of older workers	Total	28.8	30.3	28.8b	31.8	35.5		36.9	42.3p	43.5p	
	Women	17.2	20.8	19.3b	22.9	26.3		27.4	33.5p	34.8p	
	Men	41.2	40.4	38.9b	41.3	45.3		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.91e	2.23	2.22	2.41	2.45	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	85.1	84.2	85.8	85.9	85.8		76.6	77.4	77.8	
	Women	84.9	83.4	86.5	87.3	86.7		79.3	80.1	80.7	
	Men	85.3	85.1	85.1	84.6	84.9		73.8	74.7	74.8	
Comparative price levels		101.9	103.3	103.1	101.9	101.3		100.0	100.0	100.0	
Business investment		21.3	20.1	19.6	19.2	19.5		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	12.0	13.0b	13.0	12.0	:		:	16.0e	:	
	Women	14.0	14.0b	14.0	13.0	:		:	17.0e	:	
	Men	9.0	12.0b	11.0	11.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	2.5	3.0	3.5	4.1	3.4		13.0	11.9	11.4	
	Women	4.4	3.8	3.2	3.4	2.7		20.0	16.8	16.2	
	Men	2.2	3.6	3.9	4.9	4.1		9.6	9.7	9.3	
Long-term unemployment rate	Total	1.0	1.1	1.3b	1.3	1.3		4.0	4.1p	3.7p	
	Women	1.2	1.1	1.4b	1.4	1.3		4.6	4.5p	4.0p	
	Men	0.9	1.1	1.3b	1.2	1.3		3.5	3.8p	3.5p	
Total greenhouse gas emissions		102.7	117.7	115.5	118.1	:		90.7	92.1	:	
Energy intensity of the economy		134.4	149.0	147.1	149.3	:		213.1	208.1	:	
Volume of freight transport relative to GDP		112.3	118.2	117.5b	112.2	115.8		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Poland

1. Over the 2005-2007 period, the Polish economy expanded at an annual rate of 5.4%. In 2007, GDP per capita is expected to reach 55% of the EU average. Growth has been driven primarily by domestic demand, in particular by investment and private consumption. The government deficit has been reduced from 4.3% of GDP in 2005 to 3.8% of GDP in 2006, and is expected to reach 2.7% of GDP in 2007. Labour market conditions have improved markedly, with the unemployment rate projected to be less than 10% in 2007 compared with 17.7% in 2005. Nevertheless, serious labour market problems persist, including the lowest employment rate in the EU (estimated at 54% in 2007), and a falling activity rate (62.3%).

2. Poland's growth and jobs performance is constrained by a number of interconnected structural problems, including the low level of labour utilisation, slow progress in economic restructuring, underinvestment, and imbalances in public finances. Removing disincentives to work and shifting the expenditure from the social benefits system towards growth enhancing measures could contribute to a stronger performance of the labour market, and improve the sustainability of public finances.

PART I: GENERAL ASSESSMENT

3. Overall, the 2007 Polish Implementation Report shows limited progress in implementing the National Reform Programme (NRP) over 2005-2007. The pace of progress appears to have accelerated slightly over the last year and the new Polish government should ensure continued implementation.

4. There has been some progress in response to the four country-specific recommendations adopted by the Council. Progress has been insufficient on fiscal consolidation and control over expenditure, improving the competition in network industries, boosting R&D, increasing employment of older workers and increasing participation in lifelong learning. Although further steps are required, initial progress has been made on decreasing the tax burden on labour, reforming employment services and reinforcing active labour market policy.

5. With regard to the other areas on which the Council concluded Poland should focus, there has been some progress on reducing and redirecting state aids, ensuring an effective framework for competition in the financial sector and improving environmental protection. There has been good progress on linking the cohesion policy instruments with the NRP measures and setting a more realistic target for investment in R&D. Insufficient progress has been made in upgrading transport infrastructure, continuing the process of the liberalisation of energy markets and speeding-up the business registration process.

6. Last year's Commission Annual Progress Report concluded that Poland had made limited progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been limited progress on most of the commitments with an end 2007 deadline.

7. Consultation and efforts to develop ownership of the NRP at the level of central and local governments and with Parliament, and the social partners have been reinforced. In order to increase public awareness, the government organised a number of seminars and public events. Links between the governance of the NRP and the cohesion policy programmes are strong. The earmarking of the structural funding for the Growth and Jobs objectives amounts to 64% of the available funds.

8. The Commission, recognising the formation of a new government, would stress the importance of tackling the structural weaknesses outlined in the country specific recommendations and points to watch the Council issued to Poland.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. The NRP identified the consolidation and better management of public finances as the key challenge in the macro-economic area. Poland has planned a range of measures to address this challenge, but their implementation has been abandoned due to the parliamentary election. The improvement in the fiscal balance is mainly the result of strong growth yielding windfall tax revenues, data revisions, lower-than-planned expenditure and also budgetary discipline.

10. The Council recommended that Poland should pursue actions to continue fiscal consolidation and supplement the nominal state budget deficit "anchor" (a deficit ceiling) with further mechanisms to enhance control over expenditure. While fiscal consolidation has proceeded, Poland has not taken any steps to introduce an expenditure rule. Furthermore, a range of planned actions, such as uniform operational principles in the pension and retirement benefit systems for defining benefit levels, a new public finance act, the introduction of "bridge pensions" (temporary pensions for people working in difficult conditions), the creation of a network of hospitals, and defining a "basket" of guaranteed healthcare services have not been implemented.

11. In general, Poland has not implemented measures to deliver on the macro-economic commitments expressed in its NRP, despite the government's broad approach towards making public finance more sustainable. In the opinion of the Commission, the announced policy measures to address challenges facing Poland were promising and necessary, but since none of them has been fully implemented, the recommendation remains valid.

Micro-economic policies

12. The NRP identified four micro-economic challenges: developing entrepreneurship; increased innovation by companies; upgrading and developing infrastructure; and ensuring a competitive environment in networks sectors. Developing entrepreneurship has been well addressed, but further efforts on business registration and on overcoming delays in the implementation of the better regulation programme are still necessary and there is no specific target for reducing administrative burdens.

13. The Council recommended Poland to improve the framework for competition in network industries, pursue the reform of the public research sector to boost R&D and innovation and improve the framework for private sector R&D to maximise the benefits from foreign direct investment. The Council also asked Poland to set a firm and realistic R&D target for 2010 and to continue the liberalisation of energy markets.

14. Poland has opened the electricity and gas markets to all customers and implemented the relevant directives. Further actions are devoted to restructuring or increasing security of supply. However, Poland is facing a large numbers of infringement procedures related to EU legislation in the electricity, gas and telecommunications sectors.

15. The reform of public sector R&D, with its focus on a limited number of large projects and on the best performing institutions, is welcome. However, progress is mainly limited to adoption of legislation. A new, more realistic R&D target of 0.92% of the GDP by 2010 has been adopted. To increase Poland's innovation potential, a number of measures are foreseen in the document "Increasing innovation over the 2007-2013", but its implementation is awaited. Targeted tax breaks will help address a lack of business innovation, together with pilot projects on clusters and technology start-ups. Reform of public procurement rules could stimulate innovative products and services. Alongside this, a comprehensive strategy for attracting foreign direct investment in medium and high-tech industries is needed. In the quest to generate innovation, some progress is visible, but the key now is to implement and continuously evaluate these measures.

16. The Council highlighted a number of areas in the micro-economic domain on which Poland needs to focus. An environment protection policy strategy for 2007-2010 has been adopted and a number of actions developed to address the issue. This approach needs to be maintained in order to meet the accession commitments and apply the environmental *acquis* (e.g. NATURA 2000). The upgrading of infrastructure has focused on planning and institutional issues, with the rapid implementation now a priority. A new transport strategy for 2007-2020, has been approved, but the investment plans within this strategy now need implementing. The effective use of structural funds to support these plans is particularly important, alongside the use of public private partnerships, and a continued simplification of the investment procedures.

17. State aids are being monitored better and more are devoted towards horizontal goals, and this trend needs to continue. Transposition of financial sector legislation has improved, although some important pieces of legislation are still missing. New regulatory institutions have been established. Their independence needs to be assured. The transposition deficit of internal market legislation has doubled over recent times and contains a high number of related infringements, now demanding urgent action. A prompt and well co-ordinated implementation of ICT plans will help the establishment of a one-stop shop for business registration and other delayed e-government projects. The link between the NRP and the use of structural funds has been strengthened and it is now important to continue this trend during implementation.

18. In general, Poland has partially succeeded in implementing measures to deliver on the micro-economic commitments expressed in its NRP. The policy measures to address the country specific recommendations may not prove sufficient and therefore in the opinion of the Commission they remain valid. The Commission considers that there has been some response to the points to watch for Poland but they remain valid and it is now important to step up the pace of reform.

Employment policies

19. The NRP identified two employment challenges: creating and sustaining jobs and reducing unemployment; and improving the adaptability of workers and enterprises. Labour market performance has continued to improve, with good progress towards meeting national employment targets for 2010, and a rapid fall in the unemployment rate. However, given the increase in the poverty rate (from 17% in 2003 to 21% in 2005), now the highest in the EU, Poland faces the challenge of placing more emphasis on early prevention programmes and on building an inclusive labour market for people at risk of poverty and social exclusion.

20. The Council recommended that Poland should introduce a range of reforms in order to improve the functioning of the labour market. New legislative acts have been enacted to improve the operation of public employment services, and legislative amendments have been introduced to offer every unemployed person a job-counselling within 7 or 30 days (depending on the unemployment benefit rights). Alongside this, new programmes have been launched to support the integration of disadvantaged groups. Poland has cut the non-wage labour costs by lowering the disability pension premium paid by the employer (from 13% to 6%) and the employee (from 6.5% to 4.5%). This should have a positive effect on the attractiveness of employment of low-skilled workers.

21. Poland has the lowest employment rate for older workers and one of the lowest average exit ages from the labour force in the EU. Tackling this requires a comprehensive active ageing strategy, with strong incentives to work longer, better access to training, and incentives for employers to recruit. This needs to be backed-up by a revision of the early retirement and disability benefits system to make-work pay and shift resources from passive to active labour market policies. Increasing the extremely low level of childcare provision would help to increase one of the lowest female employment rates in the EU. The implementation of a lifelong learning strategy has again been delayed, and there are still problems with the quality of training programmes and their relevance to labour market needs.

22. Poland partly addresses flexicurity in an integrated way. The Labour Code has been amended to encourage flexible forms of work organisation. Expenditure on active labour market policy has increased, but needs to be complemented by better-targeted programmes that prevent long-term unemployment. Participation in lifelong learning is one of the lowest in the EU, and too little is invested in the vocational training of workers. The reform of the social security system, offering various forms of early withdrawal from the labour market, has not been brought forward. Social partners are partly involved in some of the flexicurity components.

23. In general, Poland has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. The country specific

recommendation has been addressed to some extent with measures going in the right direction, but that may not prove sufficient considering challenges Poland is facing. The Commission therefore considers that this recommendation remains valid.

PART III: CONCLUSIONS

24. In the light of the 2007 Poland's Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

25. Poland has made limited progress in implementing its National Reform Programme over the 2005-2007 period and has shown limited progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

26. The Implementation Report shows a mixed policy response to the recommendations adopted by the Council. There has been some policy response on the additional areas identified in the Council conclusions as requiring attention.

27. Among the strengths shown by the 2007 Poland's Implementation report are: the attention paid to developing entrepreneurship; initial steps to bring down the tax burden on labour; the priority and funding allocated to active labour market measures; and the strong linkage of the National Reform Programme priorities with EU funding.

28. The policy areas in the Polish National Reform Programme where challenges need to be tackled with the highest priority are: a stronger commitment to address the sustainability of the public finances; vigorous actions to improve regulation and to promote opening of markets in network industries; rapid implementation of the R&D reforms; further measures to address the low employment rate of older workers; better focusing of active labour market policy on the most vulnerable groups; and putting in place the lifelong learning strategy. Against this background Poland is recommended to:

- strengthen the fiscal consolidation and supplement the nominal state budget deficit "anchor" (deficit ceiling) with further mechanisms to enhance control over expenditure;

- improve the framework for competition in network industries, including through a review of the role of regulators, and vigorously continue the process of the liberalisation of energy markets;

- pursue the reform of the public research sector with a view to R&D and innovation being boosted, and implementing the framework for private sector R&D, thereby maximising the benefits from foreign direct investment;

- with a view to developing an integrated flexicurity approach, increase the level and efficiency of active labour market policy, notably for older persons and groups vulnerable to poverty, review benefit systems to improve the incentive to

work, put in place the lifelong learning strategy, and modernise education and training systems in view of labour market needs.

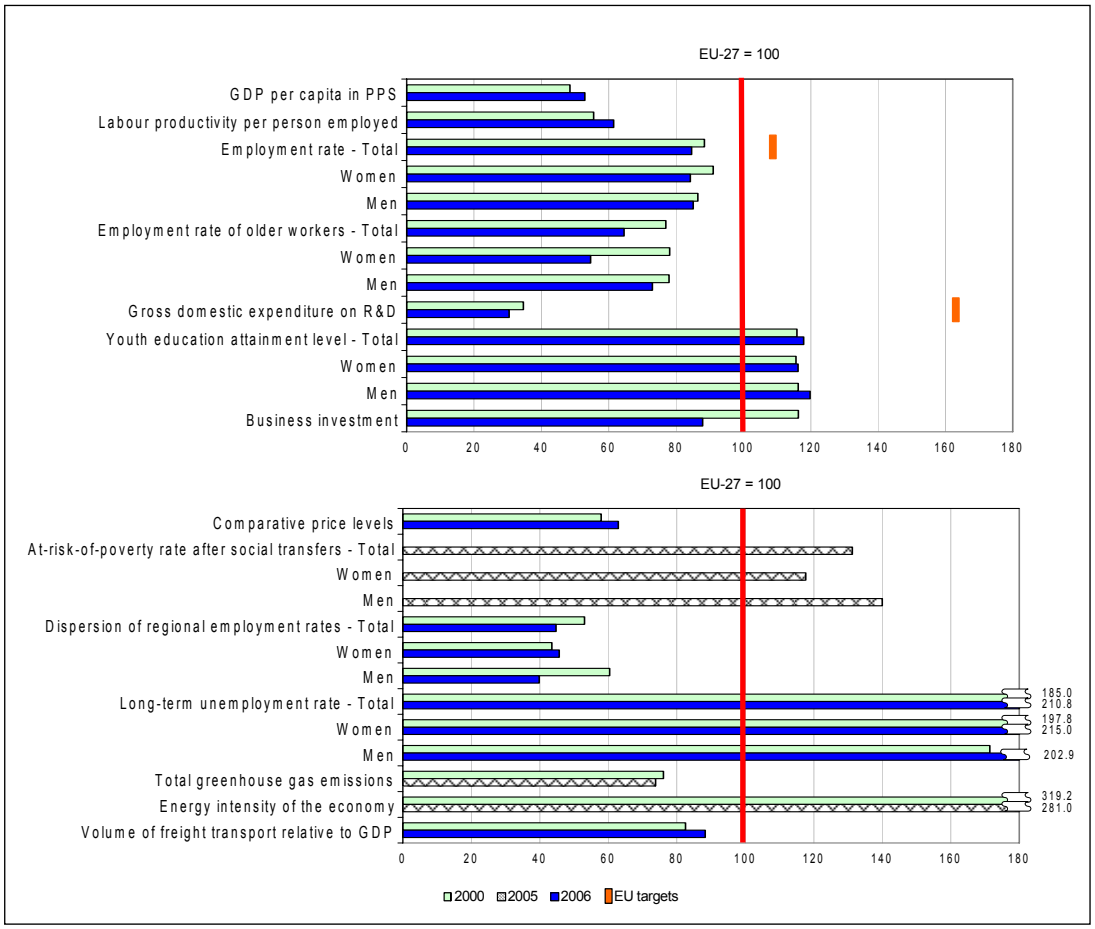
29. In addition, it will be important for Poland over the period of the National Reform Programme to focus on the following challenges: upgrading transport infrastructure; speeding-up the business registration process; ensuring timely implementation of the e-government programmes; improve the transposition of internal market legislation; and increasing the provision of childcare facilities.

PART IV: STATISTICAL GRAPHS AND DATA

POLAND

		PL						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		48.5	49.1	50.8	51.0	52.9		100.0	100.0	100.0	
Labour productivity per person employed		55.5e	59.9e	61.4e	60.4e	61.5e		100.0	100.0	100.0	
Employment rate	Total	55.0	51.2	51.7	52.8	54.5	:	62.2	63.4p	64.4p	70.0
	Women	48.9	46.0	46.2	46.8	48.2		53.7	56.2p	57.2p	
	Men	61.2	56.5	57.2	58.9	60.9		70.8	70.8p	71.6p	
Employment rate of older workers	Total	28.4	26.9	26.2	27.2	28.1		36.9	42.3p	43.5p	
	Women	21.4	19.8	19.4	19.7	19.0		27.4	33.5p	34.8p	
	Men	36.7	35.2	34.1	35.9	38.4		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.64	0.54	0.56	0.57	0.56	1.65 (2008)	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	88.8	90.3	90.9	91.1	91.7		76.6	77.4	77.8	
	Women	91.7	92.8	93.1	93.3	93.8		79.3	80.1	80.7	
	Men	85.8	87.9	88.7	88.9	89.6		73.8	74.7	74.8	
Comparative price levels		57.9	54.4	53.2	61.7	62.9		100.0	100.0	100.0	
Business investment		21.4	14.9	14.7	14.8	16.0		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	16.0	:	:	21.0b	:		:	16.0e	:	
	Women	16.0	:	:	20.0b	:		:	17.0e	:	
	Men	16.0	:	:	21.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	6.9	7.2	6.4	5.6	5.1		13.0	11.9	11.4	
	Women	8.7	8.7	7.6	7.0	7.4		20.0	16.8	16.2	
	Men	5.8	6.4	6.0	5.1	3.7		9.6	9.7	9.3	
Long-term unemployment rate	Total	7.4	11.0	10.3	10.2	7.8		4.0	4.1p	3.7p	
	Women	9.1	11.7	11.0	11.4	8.6		4.6	4.5p	4.0p	
	Men	6.0	10.3	9.6	9.3	7.1		3.5	3.8p	3.5p	
Total greenhouse gas emissions		69.0	68.4	67.6	68.0	:		90.7	92.1	:	
Energy intensity of the economy		680.2	623.1	596.4	584.7	:		213.1	208.1	:	
Volume of freight transport relative to GDP		81.8	81.7	88.4b	89.0	94.2		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Portugal

1. In 2007, the Portuguese economy GDP grew at an estimated rate of 1.8% compared with 1.3% in 2006. In the face of slow economic growth, the unemployment rate has been rising from 4% in 2001 to 8% in 2007. The employment rate has remained close to 68%, above the EU average. Portugal still has a current account deficit of close to 9% of GDP, reflecting insufficient external competitiveness. Nevertheless, exports showed strong growth (8.9% in 2006 and 6.7% in 2007). Developments on public finances are more positive, with a falling general government deficit, which is estimated at 3% of GDP in 2007 compared with 6.1% of GDP in 2005. It is expected to decline further in 2008.

2. Whereas the recent economic growth has been led by the external sector, which is sound in view of the large external imbalances, the competitive position of the economy remains fragile. Domestic demand has remained weak. However, given the prospects of sounder public finances and ongoing structural reforms, economic performance should recover gradually, albeit at a moderate pace. Furthermore, economic growth has been hampered by weaknesses of a more structural nature. Productivity is low, due mainly to low levels of human capital as a result of deficiencies in the educational and training system. It would benefit from stronger competition in some markets.

PART I: GENERAL ASSESSMENT

3. Overall, the 2007 Portuguese Implementation Report shows good progress with the implementation of the National Reform Programme (NRP) over the 2005-2007 period. The pace of progress has remained the same over the last year.

4. There has been good progress responding to the country specific recommendations adopted by the Council. Further steps have been taken towards a sustainable reduction of the government deficit, to reform public administration and pension systems, and to restructure the public sector. Progress has been less evident on redirecting public spending towards growth enhancing activities. There has been some progress in reforming educational and vocational training systems and in modernising employment legislation and countering labour market segmentation.

5. There has been some progress with regard to the other areas upon which the Council concluded that Portugal should focus. Measures have been taken to foster competition in energy and financial services markets, although problems remain. The measures to reduce green house gas emissions are not likely to be sufficient for Portugal to meet its Kyoto target. Portugal has not progressed in transposing EU legislation into national law. Some of the factors undermining social cohesion were addressed, but levels of persistent poverty and disparities in income distribution remain the highest in EU.

6. Last year's Commission Annual Progress Report concluded that Portugal had made generally good progress regarding the commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been good progress on the

commitments in most of the priority action areas. Portugal describes efforts it is taking to address the euro area recommendations in its latest Implementation Report. However, it is unlikely to reach its medium-term objective by 2009.

7. Political ownership over the Lisbon strategy and the NRP is very strong. The Lisbon coordinator reports directly to the Prime Minister, is in charge of the Technological Plan, and is actively involved in the coordination of Structural Funds. The implementation of the NRP is closely monitored through an active network involving all relevant government departments. The Implementation Report is discussed in parliament, and with social partners and other stakeholders prior to adoption. With over 200 public events at national and regional level, much has been done to raise public awareness of the Lisbon Strategy. The links between the implementation of the NRP and the programmes under the structural funds have been reinforced with the approval of the new National Strategy Reference Framework for 2007-2013. The earmarking of structural funding for the Growth and Jobs objectives is satisfactory (82% of the Portuguese structural funds 2007-2013).

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The NRP considered Portugal's commitment to fiscal consolidation as a key macro-economic driver. A target to reduce the general government deficit to below 3% of GDP has been set for 2008. After a second consecutive year of impressive progress the deficit has been reduced from 6.1% of GDP in 2005, to 3.9% in 2006, and an estimate 3% in 2007. This is the result of both revenue increase and expenditure restraint. On the basis of current policies, the continuation of this downward path over the near future seems plausible. The upward trend in the government debt ratio in terms of GDP seems to have halted. Overall, good progress has been achieved in correcting fiscal imbalances in the period covered by the NRP.

9. The reform of public administration, one key instrument for controlling government spending and raising its efficiency, has been progressing well. Reforms cover the restructuring of central administration services and the streamlining of administrative procedures and internal procedures. The implementation of these reforms has been facilitated by a wider use of ICT. In 2007, the approval of new legislation and further implementation of these measures continued at a sustained pace. Many important implementation steps lie ahead, but progress has so far been good.

10. Portugal has generally made good progress in correcting public finance imbalances in a sustained way, for example, on rationalising the education and health services networks. This has been supported by public sector wage and employment restraint. The tightening of eligibility requirements for unemployment benefits is keeping expenditure growth under control and new rules for the indexation of social payments should help in keeping expenditure growth under control. Public finances have also benefited from buoyant tax revenue growth.

11. Major pension reforms were adopted in 2007 to tackle the long-term costs of an ageing population. These build on four main measures: the inclusion of a "sustainability factor"; automatically adjusting outlays for new pensioners to the

evolution of life expectancy; a new indexation rule for pensions as a function of growth and consumer price inflation; additional penalties for early retirement and a relative bonus for work beyond retirement age; and a different rule for pension calculation accounting for contributions over the entire career. Additional steps were taken to bring the rules for government employees in line with those in the private sector. This should significantly contribute towards improving the sustainability of spending on pensions.

12. Portugal has made good progress in addressing the macro-economic challenges set out in its NRP. Most progress has been made in correcting fiscal imbalances and on public administration reform, with less progress on redirecting public spending towards growth enhancing activities. The current account deficit remains high. The Commission therefore considers the recommendation as remaining valid and adds a new point to watch on external imbalances.

Micro-economic policies

13. In the micro-economic domain the Council referred to the need for Portugal to focus on: ensuring that the promising Technological Plan is fully implemented, consolidating the linkages between research and industry, and strengthening the involvement of the private sector; as well as ensuring effective competition in energy and financial services markets; reducing emissions; and reducing the deficit in transposing EU legislation into national law.

14. Portugal has strengthened its science, technology and innovation measures on the basis of the "Technological Plan" but the implicit national R&D target of 1.8% of GDP by 2010 will be a challenge to achieve. Signs of improvement are visible: the public budget for science and technology for 2008 has reached 1% of GDP and monthly figures for the technological balance of payments showed systematic surpluses. A number of measures have been taken to strengthen inputs into knowledge production, especially human resources in public and private sectors, increased networking and internationalisation. The continued implementation of the Technological Plan, alongside further initiatives to stimulate the linkages between research, higher education and industry, and to foster private R&D, is now essential to ensure enough absorption capacity.

15. Problems remain in competition in energy and financial services markets. Access to the electricity market remains difficult for new entrants, partly due to regulated tariffs, with the liberalised (non-regulated tariff) electricity supply representing a very modest share of the market. Some promising steps have been either announced or implemented, but progress will take time. In the financial services market, despite some earlier positive developments in the credit cards market, more steps are needed to address concerns raised by the Commission's sector inquiry. The transposition rate of the Financial Services Action Plan directives has improved but is not yet complete. Portugal has recently improved its transposition deficit of EU legislation, however it is still much above the interim target and still has a high number of infringement cases. It has yet to implement some of the directives in the fields of public procurement and intellectual property rights, and prepare for the implementation of the services directive on time.

16. Portugal set new policy goals on renewable energy sources in 2007. Several measures have been taken to achieve the 2010 target of 45% of electricity produced from renewable sources and some important initiatives have been taken to improve energy efficiency. The most recent projections indicate that Portugal will reach the Kyoto targets coupling existing policies, Kyoto mechanisms, carbon sinks and additional measures.

17. Portugal shows considerable progress in terms of improving the business environment. The SIMPLEX programme has improved e-Government and helped generate administrative simplification across a wide spectrum of business activities. Portugal has a good record in e-Government and is amongst the front-runners in the provision of public services to enterprises and citizens, but lags behind in several aspects of ICT take-up. In particular, more is needed to stimulate take-up among households and enterprises, even though broadband penetration in households doubled from December 2005 to December 2007, 98% of large enterprises and 90% of medium enterprises have broadband connections. A range of initiatives to facilitate access to capital for SMEs have been implemented. Plans to teach entrepreneurship education in secondary schools have yet to be implemented. Despite some progress, the implementation of policies to ensure better regulation is limited in areas like impact assessment and stakeholder consultation, there is no specific target for reducing administrative burdens, and a comprehensive approach is still required.

18. Portugal has been implementing measures to address the micro-economic challenges set out in its NRP. There has been a response to strengthening and implementing measures in science, technology and innovation, and in developing the business environment. Despite some progress in the areas of competition in energy and financial markets, and in addressing energy-related environmental challenges, problems remain. The transposition of EU legislation remains a problem. Therefore the Commission considers the points to watch as remaining valid.

Employment policies

19. The NRP identified five keys priorities in the employment area: enhancing education and qualifications, job creation, managing restructuring, promoting flexibility and security, and modernising social security. All of planned measures have now been implemented, complemented by new measures. Overall there has been some progress in implementation of policies.

20. The Council recommended Portugal to implement measures to strongly improve the education attainment levels of the young, and develop a vocational training system that is relevant to labour market needs and based on a "National Qualifications Framework". Reforms at all levels of the education system are strengthening educational and vocational training and improving relevance to labour market needs. In particular, the "Novas Oportunidades" initiative is a significant response aimed at reducing school drop-outs and increasing qualifications. A 7% reduction in the number of drop-outs from secondary education is recorded. However, Portugal still has a high number of early school leavers (36.3% in 2006) and low youth education attainment (49.6%), both demanding further action. The policy response to these challenges needs to generate improvements in the overall quality and efficiency of

the education and training system, in order to ensure better educational achievements and an enhanced employability of the population.

21. The Council also recommended Portugal to modernise employment protection, including legislation to foster flexibility and security to reduce the high levels of labour market segmentation. Portugal has taken action to pursue the modernisation of employment protection with an independent working group set up to evaluate the existing legal framework. Its final report will be published by late 2007, and a revision of the Labour Code is expected in 2008. Further steps are needed to deliver an effective reduction of labour market segmentation.

22. The Council also referred to the need to focus on factors undermining social cohesion. Priority has been given to upgrading qualification levels and enlarging social infrastructures for childcare and elderly. Vulnerable groups, especially the disabled and immigrants, are targeted for specific policy measures. It is important to strengthen the links with the National Action Plan for Inclusion, as well as with macro and micro economic policies.

23. Portugal partially follows an integrated approach on flexicurity. A number of measures have been taken to stimulate life long learning, especially through the "Novas Oportunidades" and a proposal to reform active labour market policies was presented in June 2007. Measures were also adopted to promote the modernisation of social protection and unemployment benefit systems. Further efforts are needed in particular concerning employment protection legislation. Social partners are involved and have been consulted on the major reforms taking place.

24. Portugal has succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. There has been a good policy response to the recommendations and point to watch in the employment area. However, important challenges remain, including a sustained improvement in educational achievements and an integrated approach on flexicurity, with special focus on reducing labour market segmentation. The Commission therefore considers the recommendation and points to watch in this area remaining valid.

PART III: CONCLUSIONS

25. In the light of the 2007 Portuguese Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

26. Portugal has made good progress in implementing its National Reform Programme over the 2005-2007 period. Portugal has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

27. The Implementation Report shows a good policy response to the recommendations issued by the Council. There has also been some policy response on the additional areas identified by the Council conclusions as requiring attention. The

Implementation Report also specifically addresses the recommendations issued to the euro area countries.

28. Some of the strengths shown by the 2007 Portuguese Implementation Report are: the progress achieved in correcting fiscal imbalances and promoting sustainable reforms of the public administration, on pension and health-care reform, progress on unlocking business potential and the implementation of the Technological Plan.

29. The policy areas in Portugal's National Reform Programme where challenges need to be tackled with the highest priority are: consolidating public finances, whilst improving its quality and sustainability, and gearing public spending towards raising Portugal's growth potential; improving the efficiency of the educational system notably by improving attainment levels and reducing early school leaving; modernising employment protection to curb the segmentation of the labour market. Against this background it is recommended that Portugal:

- in the context of the on-going correction of fiscal imbalances and public administration reform, redirect public spending towards uses more supportive to potential economic growth, while maintaining firm expenditure control overall;

- further implement measures to strongly improve the efficiency of the educational system notably by improving attainment levels of the young, fighting early school leaving and developing a vocational training system that is relevant to the labour market needs and based on the National Qualifications Framework;

- continue efforts to modernise employment protection, including legislation to reduce the high levels of labour market segmentation, within the flexicurity approach.

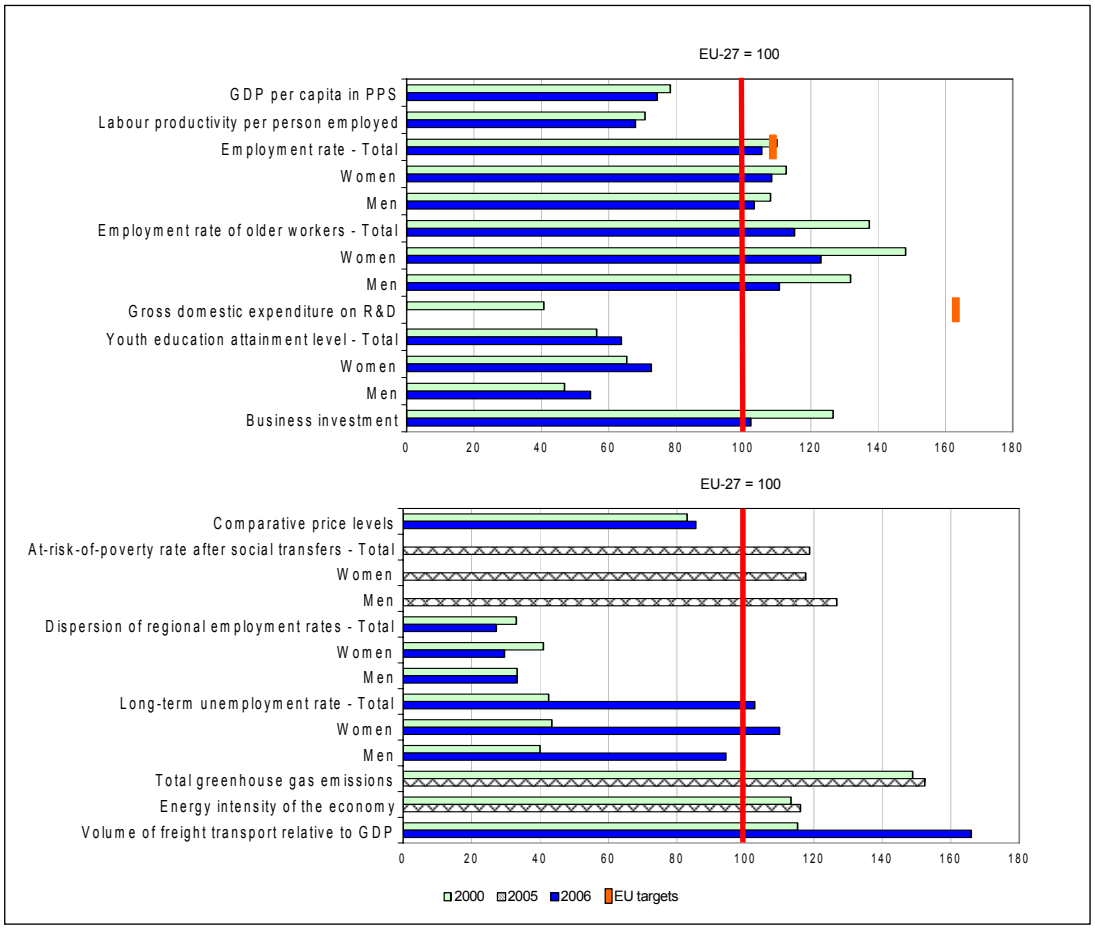
30. In addition, it will be important for Portugal over the period of the National Reform Programme to focus on the following challenges for the future: narrowing its current account deficit in a sustained way; pursuing the implementation of the Technological Plan, consolidating the linkages between research, higher education and industry, and involving the private sector further; ensuring effective competition, notably in energy and financial services markets; further implement a better regulation programme and in particular strengthen the impact assessment system; reducing the deficit in transposing EU legislation into national law; devising and implementing the measures needed to reduce green house gas emissions; and continuing to address factors undermining social cohesion.

PART IV: STATISTICAL GRAPHS AND DATA

PORTUGAL

		PT						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		78.3	77.0b	75.2	75.4	74.4f		100.0	100.0	100.0	
Labour productivity per person employed		70.8	69.8f	67.3f	68.1f	67.9f		100.0	100.0	100.0	
Employment rate	Total	68.4	68.1	67.8	67.5	67.9	70.0	62.2	63.4p	64.4p	70.0
	Women	60.5	61.4	61.7	61.7	62.0		53.7	56.2p	57.2p	
	Men	76.5	75.0	74.2	73.4	73.9		70.8	70.8p	71.6p	
Employment rate of older workers	Total	50.7	51.6	50.3	50.5	50.1		36.9	42.3p	43.5p	
	Women	40.6	42.4	42.5	43.7	42.8		27.4	33.5p	34.8p	
	Men	62.1	62.1	59.1	58.1	58.2		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.76e	0.74	0.77	0.81	:	1.8	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	43.2	47.9	49.6	49.0	49.6		76.6	77.4	77.8	
	Women	51.8	55.5	58.7	57.5	58.6		79.3	80.1	80.7	
	Men	34.6	40.4	40.8	40.8	40.8		73.8	74.7	74.8	
Comparative price levels		83.0	86.0	86.7	85.0	85.5		100.0	100.0	100.0	
Business investment		23.3	19.8	19.5	18.7	18.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	21.0	19.0p	20.0b	19.0	:		:	16.0e	:	
	Women	22.0	:	22.0b	20.0	:		:	17.0e	:	
	Men	19.0	:	19.0b	19.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	4.3	3.9	3.5	3.3	3.1		13.0	11.9	11.4	
	Women	8.2	6.3	5.9	5.6	4.8		20.0	16.8	16.2	
	Men	3.2	3.2	3.2	3.1	3.1		9.6	9.7	9.3	
Long-term unemployment rate	Total	1.7	2.2	2.9	3.7	3.8		4.0	4.1p	3.7p	
	Women	2.0	2.7	3.4	4.2	4.4		4.6	4.5p	4.0p	
	Men	1.4	1.8	2.6	3.2	3.3		3.5	3.8p	3.5p	
Total greenhouse gas emissions		135.0	136.1	138.9	140.4	:		90.7	92.1	:	
Energy intensity of the economy		241.5	234.7	238.0	241.4	:		213.1	208.1	:	
Volume of freight transport relative to GDP		114.2	113.7	163.7b	171.2	177.1e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Romania

1. Romania has experienced strong economic growth averaging 6.4% annually from 2003 to 2006, and it is expected to be 6% in 2007 and 5.9% in 2008. Growth has been driven largely by foreign investment and fast growing domestic demand, creating a widening current account deficit (13.3% of GDP in the last 12 months to August 2007) and rising inflation. GDP per capita is low, about 38% of the EU-average in 2006. Unemployment was 7.3% in 2006 and is expected to decrease to 7.1% in 2007. The employment rate (58.8%) is far below both the Lisbon target of 70% and the current EU average. Romanian youth unemployment is over 20%, amongst the EU's highest.

2. Romania joined the European Union on 1st January 2007. Its strongly performing economy is showing clear signs of overheating with a very high and growing external account deficit, growing labour shortages in spite of a significant share of untapped labour, strong wage growth and rapid increases in household borrowing; these have, in turn, fuelled inflationary pressures. The challenge for Romania is to tackle these macro-economic vulnerabilities urgently whilst speeding up structural reforms to strengthen its competitiveness and, with its low-cost advantages gradually eroding, move the economy towards more innovative and higher value activities.

PART I: GENERAL ASSESSMENT

3. The Romanian National Reform Programme (NRP), submitted at the end of July 2007, identifies 6 key challenges which need to be tackled to lay the foundations for the successful implementation of further reforms: improving the quality and management of government expenditure in the context of prudent macroeconomic policies; improving the functioning of markets; further improving the business environment; increasing employment and activity rates on the labour market; sustainable management of resources; and an overarching challenge of improving administrative capacity. The Commission fully agrees with this analysis of the main priorities and Romania's proposed approach to sequence its reforms.

4. The NRP's ultimate aim - to catch up with the rest of the EU by growing robustly and increasing its employment rate - appears realistic; however, a high degree of political focus, continuity and determination will be required to implement the reforms necessary. Success will require the different political actors - the national parliament and stakeholders – to rally behind an ambitious structural reform agenda for which the NRP is a good basis. The NRP should be further developed so that it presents a truly strategic vision; one that explains sufficiently how the reforms in various areas are integrated and what possible synergies they have; and that includes sufficient detail about time-tables, budgetary implications and monitoring and evaluation procedures to assess the feasibility of the proposed policy responses.

5. In spite of some progress achieved so far, Romania's economic and social development is still hampered by weak public administration. Reinforcement of administrative capacity is particularly urgent in budget planning and execution, enforcement of competition rules, supervisory and regulatory authorities (particularly

in network industries and financial markets), modernising public employment services and ensuring a coherent judiciary system. The NRP recognises that administrative capacity must be strengthened both at national and local level, but proposes few concrete actions. Corruption still affects the business environment and access to and quality of public services, so this is also an issue that needs significant improvement. Progress on these aspects is monitored through the Commission's co-operation and verification mechanism.

6. The NRP foresees several measures to meet the 2006 Spring European Council conclusions in the priority action areas of knowledge, entrepreneurship, employment and energy. However, greater effort is needed to ensure adequate simplification of the business environment. There is little information provided on making it easier to recruit the first employee or measures for the young unemployed.

7. Efforts to build political ownership during the NRP's formulation have been substantial; a national Lisbon coordinator has been appointed and the Prime Minister's Office has been closely involved. Consultation of stakeholders, particularly parliament, the social partners and local authorities, needs to be strengthened. Monitoring needs more effort, particularly by improving inter-ministerial coordination.

8. Romania is eligible for €19.67 billion of funding from the Structural and Cohesion Funds in the period 2007-2013. Links between NRP priorities and structural and cohesion fund programmes are strong. Of the total programme allocation, 56% is earmarked for Lisbon objectives. While some steps have been taken to strengthen administrative capacity, more efforts are needed, particularly at local level, to ensure their effective use and absorption.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. Romanian fiscal policy is not yet sufficiently predictable; frequent budgetary amendments during the year result in expenditure increases and shifts of some investment expenditures to current spending. The NRP identifies improvements to the quality and management of government expenditure as the key macro-economic priority so as to ensure productive investments in a prudent macro-economic framework and enhance the credibility of its fiscal policy. The Commission fully agrees with this focus.

10. According to the NRP, budgetary policy will be oriented towards maintaining macroeconomic stability and disinflation. Introduction of a medium-term expenditure framework and (partial) programme-based budgeting is an important step in the right direction; to produce its full impact, it should be generalised across all departments. Efforts should be stepped up to effectively implement such instruments and ensure they bear fruit. This would help the restructuring of, expenditure to improve the quality of public finances, where more progress is needed.

11. The NRP foresees the budget deficit improving to 2% of GDP in 2009-2010. If achieved, that would tighten the rather loose pro-cyclical fiscal policy conducted

since 2006, helping contain the widening current account deficit that poses an increasing risk to macro-economic stability. However, the NRP does not make sufficiently clear how the budget deficit will be sustainably reduced, particularly given pressures arising from demographic developments. For instance, pension and health care reforms underway are described, but their long-term impact on the sustainability of public finances is not examined. Still, pension reform has helped increase the statutory retirement age; however, further steps will be needed in this area.

12. Tightening labour market and skills shortages, in no small part due to large outward migration, have contributed to private sector wages increasing much faster than productivity growth. At the same time, the public sector wage bill has risen by some 30% on average over 2006-2007. This fuels inflation and means higher public expenditure, which threaten to erode Romania's competitiveness rapidly. This makes it all the more urgent to implement ambitious structural reforms in the micro-economic and employment areas to tap into new more durable sources of growth and promote more innovation.

13. Overall, the NRP broadly addresses Romania's key macro-economic challenges. But while the NRP shows good intentions, the credibility and effectiveness of the approach largely depends on the authorities' ability to improve budget planning and execution as well as restructure the composition of public spending towards growth potential enhancing investments. Further measures will also be needed to ensure the long-term sustainability of public finances; these include increasing the number of people in work contributing to social security, gradually raising the retirement age and further reforming health care and pension systems.

Micro-economic policies

14. Romania's NRP identifies increasing economic competitiveness, improving the business environment and the sustainable use of renewable resources as its key micro-economic challenges. The Commission subscribes to these priorities.

15. The NRP sets out in general terms a range of initiatives, most of which will draw on structural funds investments, to improve transport, telecommunications and energy infrastructure; however, the anticipated results sometimes seem overstated. In any event, different departments and levels of government will need to coordinate closely to achieve maximum benefits. Opening up network markets and the services sector, as presented in the NRP, will increase competition. However, the detail provided is insufficient to assess its likely impact, particularly in electricity and telecommunications where the staffing and independence of the regulator remains a concern. Total state aid (as a percentage of GDP) is much higher than the EU average, and Romania should continue to reduce and reorient its state-aid towards horizontal objectives, such as innovation.

16. Onerous regulation, long delays in obtaining authorisations and legal insecurity are serious obstacles to growth and innovation, particularly for SMEs. Whilst the NRP proposes some positive measures to improve the business environment, such as e-government applications and the introduction of impact assessments on some new measures, as well as some simplification of legislation, it shies away from tackling deeper problems. Given Romania's starting position, the NRP could have been much

more ambitious, particularly with regard to reducing administrative burdens and cutting red tape. Romania should enhance its efforts to ensure a timely implementation of the Services Directive and use this opportunity to streamline its authorisation and licensing systems.

17. Key factors constraining Romania's innovation capacity include a very fragmented research activity (with many institutions producing low-quality outputs), weak links between business and research institutions, and a low R&D content in foreign direct investment. The NRP foresees a significant increase of public spending in R&D from 0.19% of GDP in 2005 and 0.5% in 2007 to 1% by 2010; budgetary plans reflect this increase up to 2008. The NRP sets an overall R&D target of 3% of GDP by 2015. In order to achieve this objective and avoid absorption problems, Romania should do more to increase the number of researchers, strengthen management capacity and set up intermediary funding bodies.

18. Implementation of a new National Research, Development and Innovation Strategy for 2007-2013 is underway. This foresees a broad range of measures to stimulate excellence and co-operation, technology transfer and investments in human resources and provides for a wide use of competition-based funding. The latter, fully implemented, could accelerate the much-needed consolidation of Romanian research institutions. However, the overall policy response could benefit from a clearer identification of strengths, and more targeted use of public funding, including structural funds, to leverage greater private sector R&D investments. To facilitate the move towards a knowledge-based society, inefficiencies in Romania's education system need to be tackled. The NRP fully recognises the importance of spreading the use of ICT, but says little how this could be done.

19. Sustainable resource use is high on Romania's reform agenda. Some measures are foreseen to increase energy efficiency by 2.5 to 3% annually during the period of the NRP. More should be done; the high energy-intensity of the economy (six times above the EU average) and fast rising energy costs are increasingly undermining competitiveness and social cohesion. For example, more structural funds could be devoted to energy-efficiency. The NRP emphasises the importance of the environment in its own right, but also to tourism, whose importance for the economy is growing.

20. The effects of Romania's micro-economic policies are unclear given the absence of details on concrete measures, time-tables and budgetary impacts. The proposed steps to improve the regulatory environment and cut red tape are insufficient to address the challenges

Employment policies

21. The Romanian economy is facing increased labour shortages, due to fast growth and large outward migration. Nonetheless, employment rates remain low and under-employment high so that there is, in principle, still a large source of untapped labour. Against this backdrop, the Romanian NRP focuses on attracting and retaining more people in employment, by addressing the high level of non-wage labour costs, making contractual arrangements more flexible, developing vocational education and training and increasing the capacity of public employment services. The Commission subscribes to this.

22. Agricultural activities represent nearly one third of total employment, but contribute less than 10% of GDP. Policies are needed to modernise agricultural production and help (re-)integrate subsistence farmers into other sectors of economic activity. More resolute steps are needed to reduce the very large number of inactive people, especially the long-term unemployed, youth and vulnerable groups. Some measures are proposed to integrate Roma into employment and education, but it remains a major challenge.

23. The NRP recognises that education and labour market needs are relatively weakly linked. Early school leaving is a serious problem; policy should focus more on the students most likely to leave school early due to their social or geographical background. The NRP refers to draft legislation for both pre-university and university education and to ongoing efforts to increase education quality, but it is not clear when measures will be taken, nor whether they will be sufficient to tackle the problems.

24. The NRP sets an ambitious target for increasing adult participation in training which, at 1.5%, is the EU's lowest. This should be achieved by implementing a national qualification framework and increasing investment in continuing vocational training, including with European Social Fund support. Social partners should be more closely involved in the design and implementation of training, so that efforts target sectors where skill deficits are most pressing.

25. Efforts to increase participation in lifelong learning are not combined with measures to modernise social security systems and employment legislation or reinforce active labour market policies within an integrated flexicurity approach. Further action is envisaged to improve contractual arrangements, but more resolute steps are needed to strengthen the link between contributions and benefits and enforcement capacity, if the significant share of undeclared work is to be addressed properly. The effectiveness and geographical scope of public employment services needs further improvement, particularly at regional and local levels. Romania has proposed measures in all four policy areas, but a wide discussion on flexicurity between policy makers and social partners is still needed.

26. Overall, some initial steps have been taken on specific aspects of employment policy, but there is as yet no coherent overall approach or sustained integration of education and employment policies. Stronger action is required to improve the employment prospects of vulnerable groups, especially Roma, youth and older workers, by upgrading the skills of the current and future workforce, by strengthening incentives to work and by tackling undeclared work. Extending active life and reducing early retirement should contribute to both the adequacy and long-term sustainability of the pension system and increase the labour supply.

PART III: CONCLUSIONS

27. In the light of Romania’s 2007 Implementation Report and the Commission's assessment of the National Reform Programme and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

28. Overall, the National Reform Programme focuses on the right challenges. However, in some critical areas, such as strengthening administrative capacity and improving the business environment, the programme lacks ambition. In other areas, information about the content of measures, their timelines and budgetary support is sometimes lacking which makes it difficult to assess whether measures will bring solutions to the problems and challenges identified.

29. The programme's strengths include initiatives aimed at implementing a medium-term expenditure framework, reducing non-wage labour costs and reforming research structures.

30. The policy areas in the Romanian National Reform Programme where weaknesses need to be tackled with the highest priority are: strengthening administrative capacity, addressing overheating and improving budget planning and the quality of expenditure; cutting red tape and activating labour supply and raising skill levels. Against this background, it is recommended that Romania:

- urgently strengthen administrative capacity at both central and local levels of government by building up effective regulatory, control and enforcement capacity;

- avoid pro-cyclical fiscal policy to contain the growing current account deficit and inflationary pressures, keep wage developments in line with productivity growth and improve budget planning and execution as well as the quality of public finances by reviewing the composition of public spending and by reducing and redirecting state aid to horizontal objectives;

- take rapid measures to reduce substantially administrative procedures and delays to obtain authorisations as part of a coherent better regulation policy in order to improve the business environment, which will also help in the fight against corruption;

- implement an integrated approach to increasing employment, activity rates and productivity levels, especially by accelerating reforms of the education system to respond better to labour market needs, by reducing early school leaving, by significantly increasing adult participation in education and training; and by transforming subsistence/semi-subsistence farming into sustainable employment.

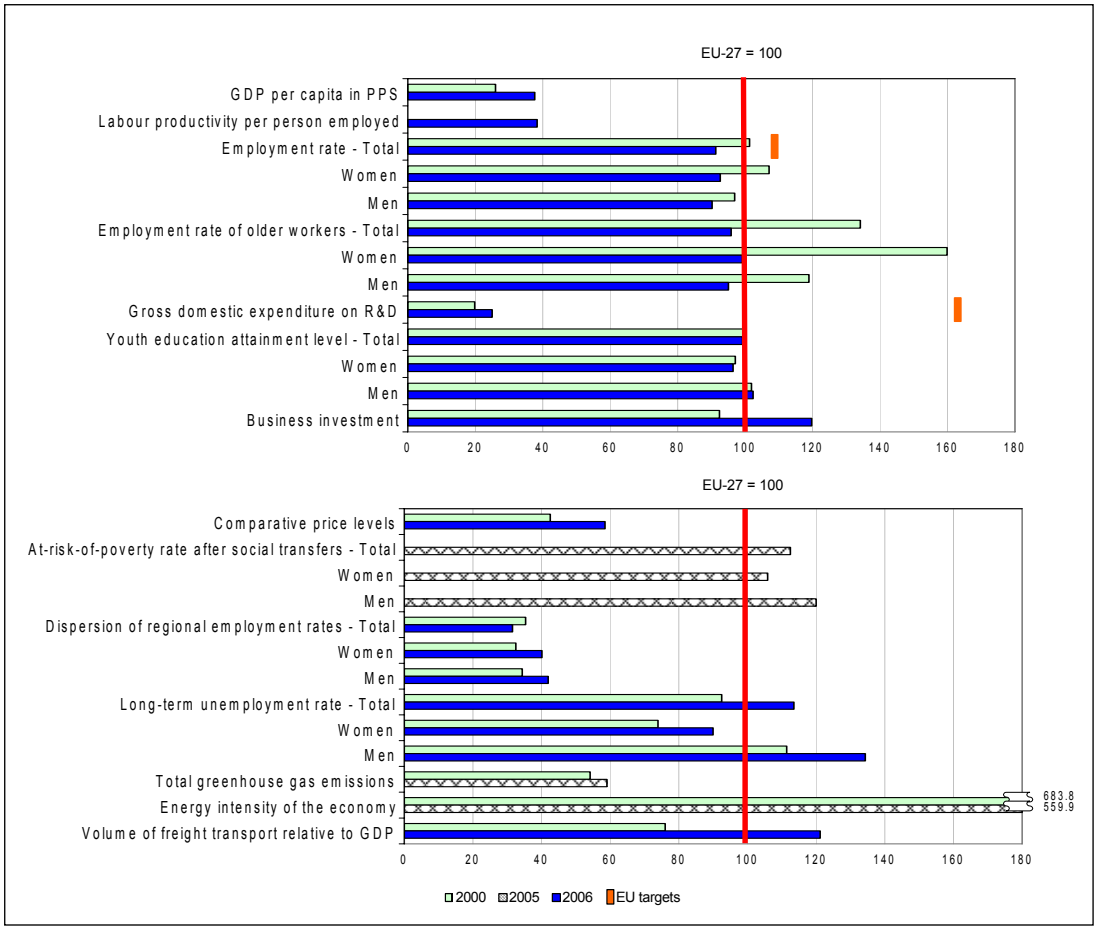
31. In addition it will be important for Romania over the period of the National Reform Programme to focus on: taking further measures to ensure the long-term sustainability of public finances, in particular with regard to potential risks in terms of adequacy and sustainability of pensions; reinforcing measures to tackle fragmentation of the research base whilst ensuring that planned increases in public research funding yield effective returns by vigorously implementing the national R&D and innovation strategy and by regularly monitoring its results; pursuing a more integrated approach to infrastructure development and roll-out of ICT; intensifying efforts to tackle undeclared work; improving the effectiveness and geographical scope of public employment services, particularly to assist vulnerable groups.

PART IV: STATISTICAL GRAPHS AND DATA

ROMANIA

		RO						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		26.0	31.5	33.6	34.4	37.6f		100.0	100.0	100.0	
Labour productivity per person employed		:	32.1	34.7	35.6f	38.3f		100.0	100.0	100.0	
Employment rate	Total	63.0	57.6	57.7	57.6	58.8	63.0	62.2	63.4p	64.4p	70.0
	Women	57.5	51.5	52.1	51.5	53.0		53.7	56.2p	57.2p	
	Men	68.6	63.8	63.4	63.7	64.6		70.8	70.8p	71.6p	
Employment rate of older workers	Total	49.5	38.1	36.9	39.4	41.7		36.9	42.3p	43.5p	
	Women	43.8	33.3	31.4	33.1	34.5		27.4	33.5p	34.8p	
	Men	56.0	43.5	43.1	46.7	50.0		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.37	0.39	0.39	0.41	0.46	1.8	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	76.1	75.0	75.3	76.0	77.2		76.6	77.4	77.8	
	Women	77.0	75.7	76.1	76.8	77.8		79.3	80.1	80.7	
	Men	75.2	74.3	74.6	75.2	76.6		73.8	74.7	74.8	
Comparative price levels		42.5	43.4	44.3	55.5	58.5		100.0	100.0	100.0	
Business investment		17.0	18.2	18.9	19.3	21.8		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	17.0	17.0	18.0	18.0	:		:	16.0e	:	
	Women	18.0	18.0	18.0	18.0	:		:	17.0e	:	
	Men	17.0	17.0	18.0	18.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	4.6	3.5	4.9	4.5	3.6		13.0	11.9	11.4	
	Women	6.5	6.1	7.7	8.2	6.5		20.0	16.8	16.2	
	Men	3.3	2.6	3.1	2.8	3.9		9.6	9.7	9.3	
Long-term unemployment rate	Total	3.7	4.3	4.8	4.0	4.2		4.0	4.1p	3.7p	
	Women	3.4	4.1	3.8	3.4	3.6		4.6	4.5p	4.0p	
	Men	3.9	4.6	5.5	4.6	4.7		3.5	3.8p	3.5p	
Total greenhouse gas emissions		49.1	55.8	56.7	54.4	:		90.7	92.1	:	
Energy intensity of the economy		1457.2	1353.7	1226.9	1164.9	:		213.1	208.1	:	
Volume of freight transport relative to GDP		75.3	95.6	104.3b	131.1	129.3		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Slovenia

1. The Slovenian economy has shown strong growth performance over the entire last decade, most notably during the 2005-2007 period when GDP increased at an average annual rate of above 5%. In 2006, GDP growth reached a high at 5.7%, while GDP per capita in purchasing power standard reached 89% of the EU-27 average, with domestic demand as the main growth driver. Inflation was at 2.5% in 2006, but has increased markedly in 2007, with the average rate forecast to reach the highest rate in the euro area at 3.5%. Unemployment stood at 6% in 2006 and it is continuing to decline. However, structural challenges in the labour market persist and a gender gap in employment is increasing.

2. On 1 January 2007, Slovenia was the first new Member State to join the euro area, thus achieving one of the key objectives of its economic policy. Euro area membership reinforces the need for fiscal consolidation and for removing structural rigidities in the labour and product markets. Improvements in these areas will help Slovenia absorb country-specific shocks and strengthen the adjustment capacity of its economy. In this context, the challenges to the long-term fiscal sustainability related to population ageing remain highly relevant. Containing national inflationary pressures in the euro area is also essential to ensure competitiveness and sustained growth.

PART I: GENERAL ASSESSMENT

3. Overall, the 2007 Slovenian Implementation Report shows good progress in implementing the National Reform Programme (NRP) over the 2005-2007 period.

4. Slovenia has addressed the two country specific recommendations adopted by the Council to some extent. However, efforts need to be substantially increased with regard to the reform of the pension system and promotion of active ageing, as well as enhancement of employment services.

5. With regard to the other issues in the micro-economic and employment domains, on which the Council concluded Slovenia should focus on, some progress has been recorded. However, reforms need to be strengthened, especially in some of the micro areas.

6. Last year's Annual Progress Report concluded that Slovenia had made rather limited progress on meeting the commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been some progress in some areas, such as shortening start-up times for businesses.

7. The Implementation Report does not specifically address the recommendations issued to the euro area countries. Nevertheless, relevant developments include an ongoing comprehensive tax reform which has improved the quality of public finances, although challenges remain to be tackled. Slovenia has not taken sufficient advantage of the favourable cyclical conditions to make more rapid progress towards the medium-term objective, in line with the Stability and Growth Pact. The structural

budget deficit is projected to remain unchanged in 2007, despite the good economic times. Moreover, there continues to be a lack of competition, especially in the utilities sector. The financial system remains small and inefficient, with a limited degree of openness. Steps have been taken in the labour market to introduce the flexicurity system, but more needs to be done.

8. Consultation and efforts to develop ownership of the NRP at the central and regional level have been enhanced and the involvement of social partners is substantial. The responsibility for national co-ordination is at ministerial level. There is a high level of parliamentary involvement. There is also a strong public debate on the reforms in the media. However, the monitoring process needs some improvement. Slovenia took a progressive approach towards the programming of its cohesion policy spending for the 2007-2013 period. Its National Strategic Reference Framework indicatively allocates more than 60% of the structural and cohesion funds for Lisbon objectives.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. In the 2005-2007 period, there has been good progress on some of the commitments made in the NRP. Slovenia has successfully adopted the euro, thus achieving one of the primary goals set out in the NRP. A major tax reform has reduced the fiscal burden on labour and capital, while improving the quality of public revenues. Slovenia is on track to achieve the envisaged reduction in the expenditure-to-GDP ratio, due to lower expenditure on social transfers and interest payments, as well as lower cost of government operations. However, progress in other areas has been less satisfactory. The rigidity of the budget remains a concern, especially since the high share of non-discretionary spending commitments leaves little scope for shifting expenditure towards growth enhancing activities. The recent Collective Agreement for Public Sector wages poses some risks to both fiscal consolidation and price stability. Membership in the euro area indeed points to the continued need for Slovenia to place considerable emphasis on price stability as an important contribution to a growth friendly environment.

10. The Council recommended that Slovenia should continue reforming its pension system and promote active ageing, in order to increase the employment rate of older workers and improve long-term sustainability. The employment rate of older workers at 32.6% (2006) is still low compared to the euro area average, but shows an increasing trend due to various support measures, including incentives for private sector employers and the gradual increase of the retirement age stipulated by the 1999 pension reform. However, the government backtracked on the sustainability-oriented pension indexation element of the reform in 2005. No new measures have been introduced in 2007 in response to the recommendation, even though the expected increase in the age-related expenditure threatens the long-term sustainability of public finances. An active ageing strategy is still under preparation.

11. In general, Slovenia has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. However, progress is limited regarding the country specific recommendation.

Micro-economic policies

12. Slovenia has made some progress over the 2005-2007 period in tackling the micro-economic challenges identified in its NRP. It has been successful in exploiting the positive business climate in Europe: exports grew by 25% between August 2006 and August 2007. However, it has been less successful in attracting foreign direct investment. While there are delays in the privatisation process, particularly in the banking and insurance sectors, the privatisation of the second largest bank is currently underway. The issue of competition has often been raised in public debate, following the unexpectedly high price increases in the food retail sector, retail banking, tourism (restaurant services) and utilities (communal services). Regulation of the network industries has brought about good results, particularly in the telecommunication sector, which saw many new entrants and decreasing prices. Liberalisation of the energy sector has started on time in mid-2007. Better regulation remains high on the political agenda. Good progress has been made in cutting the administrative burden, and a 25% target has been set for some priority fields. However, Slovenia has not yet established a comprehensive framework for impact assessment.

13. The Council referred to the need to focus on: setting realistic targets for R&D investment; improving competition, notably in professional services, and strengthening the Competition Protection Office; promoting environmental technologies and energy efficiency; and shortening business start-up times and reducing the related costs. Slovenia has set an ambitious goal of reaching 3% of GDP in R&D investment by 2010. Nevertheless, public sector investment has been lagging behind the growing investment by the private sector. Thus, the aggregate R&D investment has remained stable at approximately 1.5% of GDP for the last five years, highlighting the lack of appropriate R&D strategy with a clear allocation of tasks amongst the responsible institutions. The Implementation Report indicates that some deregulation is underway in the professional services: notaries, pharmacists and architects are under review. However, the responsibility for action lies solely with a single ministry without any coordination with the relevant actors (e.g. professional bodies etc.). The effectiveness of the Competition Protection Office has been improved with the adoption of a new law that gives it powers to impose fines. The Implementation Report recognises that the implementation of measures on energy efficiency, renewable energy sources, cleaner fuels and curbing of CO_2 emissions have been insufficient. Without additional measures Slovenia is unlikely to meet its Kyoto targets. As regards business environment, a one-stop-shop electronic registration system has significantly reduced the costs and time needed for self-employed persons to start business activities. In early 2008, the system will be extended to enable setting up a private limited company in four days. This has been accompanied by a business-friendly tax reform, a tax break for R&D activities, venture capital investments by local firms, and improved access to finance for early-stage SMEs. Further measures need to be taken on entrepreneurship education, the "Think Small First" principle and the one-stop shop for recruiting the first employee.

14. In general, Slovenia has partially succeeded in implementing measures to deliver on the micro-economic commitments expressed in its NRP. The point to watch on business environment has been addressed satisfactorily. However, the points to watch on appropriate R&D investment strategy and energy efficiency, in particular

with regard to CO_2 emissions, have been addressed only in a limited manner. The Commission welcomes the improvements to the effectiveness of the Competition Protection Office, but considers the progress on deregulating professional services as limited.

Employment policies

15. In 2005-2007, Slovenia has launched most of the major employment reforms set out in the NRP. Activation policies helping people into employment have been enhanced and conditions for receiving social benefits have been tightened. A consensus on revised contractual arrangements has recently been reached with the social partners to improve labour market flexibility. Nevertheless, the reforms in relation to flexicurity fell short of what was announced in 2005. New legislation and funding are intended to complement the reforms in the education system and to improve its link with the economy. Although the employment rate of older workers has somewhat increased, the Pensions and Disability Act has not been amended to promote active ageing, which remains a fundamental challenge. Progress with the implementation of policies that address the labour market challenges identified in the 2005 NRP is, therefore, mixed.

16. The Council recommended that Slovenia should enhance its employment services to support the move towards more flexible contractual arrangements and increased conditionality of benefits, giving high priority to early stages of unemployment. Cooperation between public and private labour market institutions is being enhanced, helping to improve the efficiency of the job-brokering service. However, in spite of modernisation and additional training, the employment service of Slovenia still faces capacity constraints, making it difficult to deliver an effective, personalised service. Therefore, improvements to the effectiveness of the service should continue, especially in relation to persons with low employment prospects.

17. The Council also referred to the need to strengthen the link between the education system and the labour market, to reduce segmentation and better integrate young people into the labour market. The NRP set an ambitious goal that by 2008 every young person with a university or higher level of education should find employment within six months after their studies. The Implementation Report is not explicit on whether this target is met. Nonetheless, the overall goal is being pursued through active labour market policy measures and a promotion campaign on education areas that offer better employment opportunities. A new law on scholarships has been adopted and additional funding provided, in order to increase the number of scholarship recipients and to ensure a better link with the labour market needs. The reforms of vocational and higher education are continuing. The Commission considers this an appropriate response to the challenges Slovenia faces. Further efforts should pursue the same line of action, whilst increasing the supply of higher education programmes should not compromise their quality.

18. Slovenia has demonstrated its intention to develop a flexicurity system, but further efforts are necessary to achieve an appropriate combination of labour market flexibility and employment security. The social security system is relatively effective and efforts have been made to strengthen the implementation of active labour market policies. Lifelong learning has improved remarkably. The respective amendments to the Labour Relations Act were negotiated with the social partners who are fully

involved in the reform process. However, the amendments do not go far enough in terms of increased flexibility for those in permanent employment, rather increasing flexibility for the outsiders. In addition, there has been no progress in integrating "student work" into the mainstream labour market. Therefore, there is a risk that segmentation will persist, mainly affecting young people. The new tripartite Social Agreement 2007-2009 is an important basis for further measures.

19. In general, Slovenia has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. The country specific recommendation and points to watch have been addressed to some extent.

PART III: CONCLUSIONS

20. In the light of the 2007 Slovenian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

21. Slovenia has made good progress in implementing its National Reform Programme over the 2005-2007 period. Slovenia has also been showing some progress in fulfilling the commitments agreed by the 2006 Spring European Council.

22. The Implementation Report shows some policy response to the recommendations issues by the Council. There has also been some policy response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

23. Among the strengths shown by the 2007 Implementation Report are: the involvement of social partners in drafting all major labour market reforms; efforts to strengthen the link between education and scholarship systems and the economy; the shortening of business start-up times and the reduction of administrative burden. Slovenia's entry into the euro area is the central achievement in the macro field.

24. The policy areas in the National Reform Programme where challenges need to be tackled with the highest priority are: further pension reform and effective implementation of the active ageing strategy; and a more flexible labour market combined with a more effective personalised approach in the implementation of active labour market policies. Against this background it is recommended that Slovenia:

- take further steps to strengthen the reform of the pension system and promote active ageing, with a view to increasing the employment rate of older workers and improving long-term sustainability;

- within an integrated flexicurity approach, promotes more flexible contractual arrangements and improves the effectiveness of employment services, particularly in relation to persons with low employment prospects, in order to counter labour market segmentation mainly affecting young people.

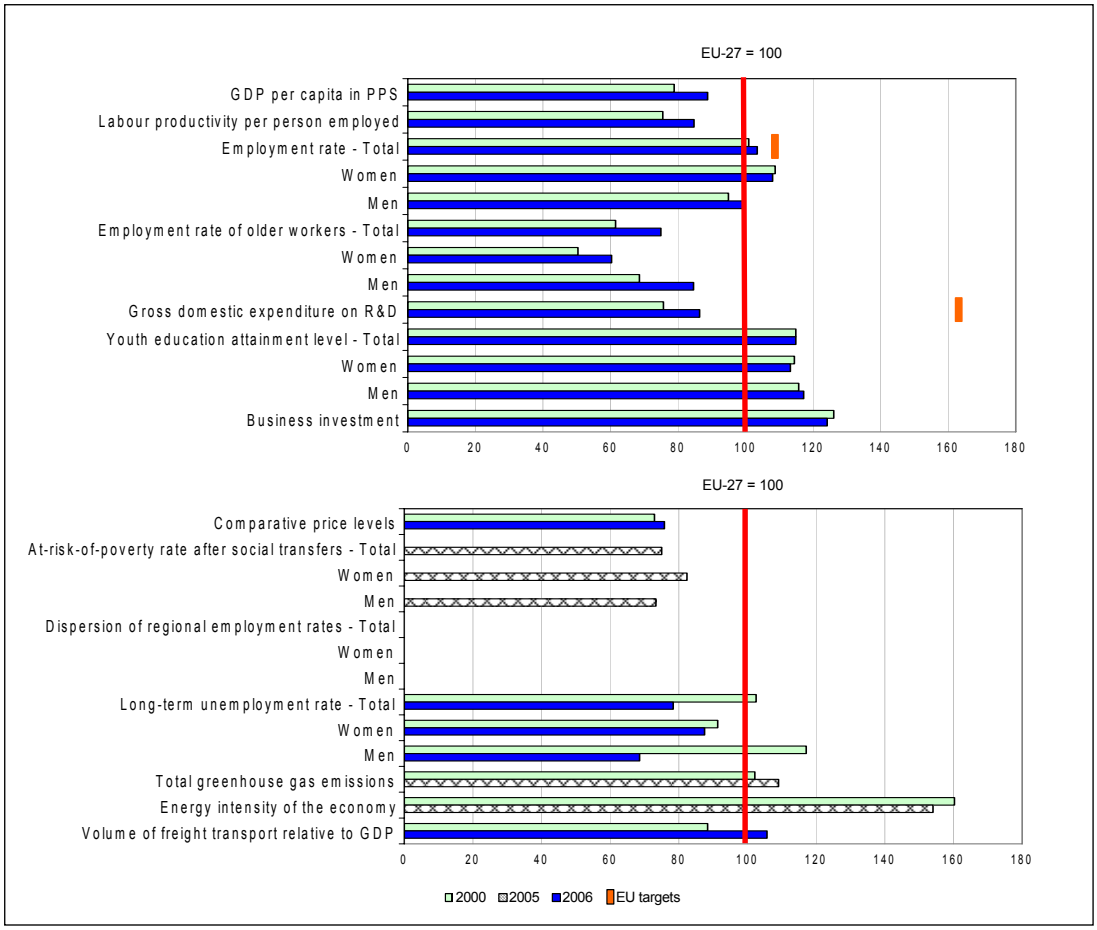
25. In addition, it will be important for Slovenia to focus over the period of the National Reform Programme on the following challenges: develop an effective research and innovation strategy and ensure its effective implementation; also with a view to containing inflation, improve competition in the services sector, with particular emphasis on retail, financial services, utilities and professional services; improve implementation of energy efficiency measures, particularly with regard to CO_2 emissions and unfulfilled Kyoto targets; implement the ambitious plans to strengthen the link between the education system and the labour market.

PART IV: STATISTICAL GRAPHS AND DATA

SLOVENIA

		SI						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		78.9	82.5	85.0	86.6	88.8		100.0	100.0	100.0	
Labour productivity per person employed		75.5	77.9	80.3	82.3	84.7		100.0	100.0	100.0	
Employment rate	Total	62.8	62.6	65.3	66.0	66.6	67.0 (2008)	62.2	63.4p	64.4p	70.0
	Women	58.4	57.6	60.5	61.3	61.8		53.7	56.2p	57.2p	
	Men	67.2	67.4	70.0	70.4	71.1		70.8	70.8p	71.6p	
Employment rate of older workers	Total	22.7	23.5	29.0	30.7	32.6		36.9	42.3p	43.5p	
	Women	13.8	14.6	17.8	18.5	21.0		27.4	33.5p	34.8p	
	Men	32.3	33.2	40.9	43.1	44.5		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.41	1.29	1.42	1.46	1.59	3.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	88.0	90.8	90.5	90.5	89.4		76.6	77.4	77.8	
	Women	90.8	94.0	94.1	93.2	91.4		79.3	80.1	80.7	
	Men	85.4	87.7	87.1	88.0	87.7		73.8	74.7	74.8	
Comparative price levels		72.9	76.2	75.4	75.6	75.8		100.0	100.0	100.0	
Business investment		23.2	20.8	22.0	22.2	22.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	11.0	10.0	:	12.0b	:		:	16.0e	:	
	Women	12.0	11.0	:	14.0b	:		:	17.0e	:	
	Men	11.0	9.0	:	11.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	-	-	-	-	-	-	13.0	11.9	11.4	
	Women	-	-	-	-	-	-	20.0	16.8	16.2	
	Men	-	-	-	-	-	-	9.6	9.7	9.3	
Long-term unemployment rate	Total	4.1	3.5	3.2	3.1	2.9		4.0	4.1p	3.7p	
	Women	4.2	3.6	3.4	3.3	3.5		4.6	4.5p	4.0p	
	Men	4.1	3.4	3.1	2.9	2.4		3.5	3.8p	3.5p	
Total greenhouse gas emissions		92.6	96.8	98.4	100.4	:		90.7	92.1	:	
Energy intensity of the economy		341.7	341.1	324.7	320.5	:		213.1	208.1	:	
Volume of freight transport relative to GDP		87.6e	86.5	97.5	110.0	112.8		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Slovakia

1. Real GDP growth, driven by both domestic and external demand is expected to remain high at 8.7% in 2007, up from 8.5% in 2006. Employment increased to 59.4% in 2006 compared with 57.4% a year earlier, with increases across all groups and ages, but particularly for older workers (which has increased from 30.3% in 2005 to 33.1% in 2006). However, this is still below the EU average. Unemployment has also fallen rapidly from 16.3% in 2005 to 13.4% in 2006. It is projected to fall further to 11.2% in 2007. However this remains considerably above the EU average. Thanks mainly to lower increases in regulated prices in the energy sector at the beginning of 2007 and the impact of exchange rate appreciation, inflation is expected to decrease from 4.3% in 2006 to below 2% in 2007. The government deficit is foreseen to fall below 3% of GDP in 2007 and to around 2.3% in 2008.

2. Large-scale reforms of social, labour market and health care policies implemented in recent years have helped accelerate GDP and employment growth. However, large regional differences persist and the unemployment rate remains one of the highest in the EU. Despite one of the highest productivity growth rates in the EU, Slovakia continues to lag behind the EU average GDP per capita, due mainly to lower labour productivity and low labour resource utilisation.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) was revised slightly in 2006 by the new government, but the key challenges remain: information society; R&D and innovation; business environment; education and employment. Overall, the 2007 Slovak Implementation Report shows some progress on implementing the NRP over the period 2005-2007. The pace of progress appears to have remained the same as last year.

4. Slovakia has made some progress in responding to the country specific recommendations adopted by the Council. Expenditure on R&D and education has not increased sufficiently and, notwithstanding the adoption of some strategy documents, the R&D sector still lacks a coherent reform connecting research institutions and business. A life long learning strategy has been adopted, but more is needed to improve participation by adults and marginalised groups in education and training. Revision of labour market policies has not yet addressed the very high long term unemployment, including the soaring share of low skilled people.

5. The Council also concluded that Slovakia should focus on a range of further issues. There has been some progress on developing a legislative framework to address the gender pay gap, although further efforts are needed to improve its enforcement. However, Slovakia has not moved forward significantly on ICT take-up, broadband infrastructure, improving the better regulation system and developing an active ageing strategy.

6. Last year's Commission Annual Progress Report concluded that Slovakia made mixed progress meeting the commitments made at the 2006 Spring European Council in the priority actions areas of knowledge, entrepreneurship, employment

and energy. In the past year, there has been limited progress on a few of the commitments with a 2007 deadline. Entrepreneurship education and the Think Small First principle have not yet been addressed. Further efforts are also needed to implement one stop shops and support the young unemployed.

7. The NRP and subsequent Implementation Reports have been prepared under the auspices of the Government Office and the Ministry of Finance, in cooperation with other stakeholders. An intensified reporting mechanism and a set of indicators were put in place in 2007 to improve monitoring and overall policy co-ordination. New mechanisms are applied to national and structural fund allocations to support Lisbon objectives. Links between the governance of NRP implementation and the programmes under the structural and cohesion funds are fairly strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. To achieve long-term sustainability of public finances by 2010, Slovakia committed itself to reduce the headline general government deficit to below 3% of GDP in 2007 and the structural deficit to below 1% of GDP by 2010.

9. The government adopted an expansionary fiscal stance in 2006 which, together with non-discretionary deficit-increasing factors (an increase in pension reform costs from 0.8% of GDP in 2005 to 1.2% in 2006), increased the general government deficit from 2.8% of GDP in 2005 to 3.7% in 2006. Nevertheless, the policy measures implemented by the government are foreseen to decrease the deficit below 3% of GDP in 2007 and to around 2.3% in 2008. As a result some progress has been made over the period 2005-2007 to meet fiscal targets set in the 2005 NRP.

10. The Council recommended that Slovakia should reallocate expenditure towards R&D and education. The Slovak authorities clarified their 2010 target for R&D investments between public (0.8% of GDP) and private expenditure (1%). Planned increases in resources devoted to education in the 2007 and the 2008 budgets have lagged behind expected nominal GDP growth. The share of public expenditure as a percent of GDP assigned to universities and the Slovak Academy of Sciences is also projected to decline in 2007 and 2008. Hence, in the Commission's opinion, there has been limited policy response in this area.

11. In general, Slovakia has partially succeeded in implementing measures to deliver on the macro-economic commitments expressed in its NRP. The country-specific recommendation in the macro-economic area has been addressed only to a limited extent and therefore remains valid.

Micro-economic policies

12. Over the period 2005-2007, progress with the implementation of key challenges identified by Slovakia in its 2005 NRP, notably on the business environment, R&D

and innovation, and information society has been mixed. There has been limited progress over the past year.

13. The Council recommended that Slovakia should complete the preparation of a coherent national R&D and innovation strategy, with strong interconnections between research institutions and businesses. During 2007, the Slovak government has adopted a number of strategy documents for R&D and innovation for the period 2007-2013. However, they do not tackle the need for reform of the public research system. A coherent R&D and innovation strategy with adequate human resources and finance for its operational structures should be implemented.

14. The Council also referred to the need for continued efforts on ICT policies, especially on broadband infrastructures and improvements in the Better Regulation system. Despite some advances in e-Government and digital literacy, Slovakia's development of an Information society still lags behind. The roadmap for public administration electronic services has faltered and the electronic signature is yet to be adopted. Additional targeted measures are needed to further ICT take-up and broadband deployment.

15. Limited progress characterises better regulation efforts to improve the business environment. Consolidation of various impact assessment methodologies is foreseen, but no implementing structures have been designed yet. The Action Plan for Reducing Administrative Burdens sets a 25% reduction target for administrative burdens, but does not provide general principles for good regulation and effective coordination. Furthermore, while efforts have been made to implement one-stop-shops for setting up a new business for sole traders, many steps remain to be taken to extend the system to registered companies. The current reform of the education and training system should be used to introduce entrepreneurship education into the curricula for secondary and higher education. Slovakia remains very successful at transposing EU internal market legislation into national law.

16. Despite identifying the energy industry as a new priority in its revised NRP, Slovakia still needs to develop competition in the power supply market. The main hindrance remains the dominance of the incumbent companies with negative price effects for consumers. Slovakia has temporarily decided to mitigate these effects using comprehensive price regulation. However, together with the decreasing independence of the Regulatory Office for Network Industries, this policy mix might prevent the development of competition in these sectors.

17. Slovakia has introduced a number of climate protection, energy efficiency, and adopted a "Strategy for greater use of renewable energy sources in Slovakia". Its energy intensity has declined consistently since 2001, but remains about four times above the EU-27 average. Strengthening the Ministry of Economy's horizontal role in monitoring energy efficiency and implementing the Energy Efficiency Concept, along with its Energy Efficiency Action Plan, would further improve efficiency and help achieve the target set for electricity production from renewable sources by 2010.

18. Slovakia has partially succeeded in implementing measures to deliver on the micro-economic commitments in its NRP. The country specific recommendation on Slovakia's R&D strategy has been address to some extent by the adoption of a number of strategy documents, but these now need to be implemented. The point to

watch of ICT polices has been addressed to some extent, however there has been only a limited response to the need to improve the better regulation system.

Employment policies

19. Economic growth and extensive labour market reform triggered employment growth in 2005-2007. Despite this several concerns emerged, including high rates of long-term unemployment (10.2% compared with the EU average of 3.7%) that coincide with a shortage of skilled workers, a low employability of certain social groups, and a decrease in youth employment.

20. The Council recommended that Slovakia develop a comprehensive approach to tackling long-term unemployment, notably by developing targeted active labour market policies for the most vulnerable groups. Several steps have been taken to address this problem including revised active labour market policy measures that better target disadvantaged jobseekers, the preparation of a new legislative framework for employment policy, and a plan to introduce in-work benefits. However, long-term unemployment, which includes a very high proportion of the low skilled and the Roma minority, remains extremely high, and thus a stronger policy response is merited.

21. The Council also recommended that Slovakia adopt a lifelong learning strategy and complete reform of its education and training system. The lifelong learning strategy was adopted in 2007. Its implementation is now the key challenge given the skills mismatch that persists and that adult participation in lifelong learning remains critically low. However, the adoption of the Educational Act for primary and secondary education has been postponed. In higher education, the core legislative framework has been revised, but raising the quality of higher education and reinforcing links between education, research and business remain key challenges. The inclusion of marginalised Roma communities into education and training, despite some successful initiatives, also continues to be a high priority.

22. The Council also referred to the need to address the gender pay gap and develop an active ageing strategy to increase employment of older workers. Despite a reinforced legal definition of equal remuneration and a ban on gender discrimination, the gender pay gap still remains very high (22%). In addition, the gender gap in both employment and unemployment has significantly increased over recent years. The recently adopted strategy for reconciling work with family life has not sufficiently increased female employability, or access to flexible work organisations. Employment of older people has increased, mainly due to the progressively rising retirement age and incentives to remain in employment. These measures should be complemented by an active approach creating favourable labour market conditions for this age group which would include labour legislation, active labour market policies, increase training provision, and health care. The Commission considers this a limited policy response to these challenges and further action is necessary to improve the employment situation of women and older workers.

23. Slovakia has not built an integrated model of flexicurity, but a number of flexicurity-related measures have been introduced. The last revision of the Labour Code introduced new forms of work organisation, while tightening the contractual arrangements with increased employees' protection. Implementing the new lifelong

learning strategy should increase the very low participation rate in education and training. In spite of active labour market policies for disadvantaged jobseekers, their employability remains low and they are unable to fill the emerging shortage of skilled workers. The social partners' involvement in policy-making has slightly improved, notably consultation of trade unions.

24. In general, Slovakia has partially succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. The country specific recommendations and points to watch have been addressed to some extent, but further initiatives and implementation of adopted strategies is now required. The Commission therefore considers the recommendation and the points to watch remaining valid.

PART III: CONCLUSIONS

25. In the light of the 2007 Slovak Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

26. Slovakia has made some progress in implementing its National Reform Programme over the period 2005-2007. There has been a limited response in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority areas.

27. The Implementation Report shows a mixed policy response to the recommendations adopted by the Council. Further reforms are necessary to increase R&D and education expenditure, implement strategies in the micro-economic area, to tackle long-term unemployment and to complete education and training reform. There has been a mixed response on the additional areas identified in the Council conclusions as requiring attention.

28. Among the strengths shown by the 2007 Slovak Implementation Report are: the foreseen reduction of the public finance deficit to below 3% of GDP in 2007; the adoption of a number of strategy documents in the area of R&D and innovation, energy efficiency and renewably energy; the partial implementation of a one-stop-shop for start-up companies; the revision of employment legislation; the adoption of the lifelong learning strategy; and efforts to revise active labour market policies to better comply with labour market developments.

29. The policy areas in the Slovak National Reform Programme where challenges need to be tackled with highest priority are: increasing expenditure to education, R&D and innovation, improving the regulatory environment, tackling long-term unemployment, completing the reform of the education and training system and raising its quality in line with labour market needs. Against this background, it is recommended that Slovakia:

- reallocate resources to education, R&D and innovation, and duly implement a coherent R&D and innovation strategy with a particular focus on the institutional reform of the public research sector and substantial improvement of business-research cooperation;

- improve the regulatory environment, notably by implementing a comprehensive better regulation strategy covering both impact assessment and simplification of existing legislation;

- within an integrated flexicurity approach, ensures implementation of the lifelong learning strategy addressing the needs of the labour market, completes the reforms of primary, secondary and tertiary education to improve qualification and skill levels, and enhance access to employment, notably for the long-term unemployed and vulnerable groups.

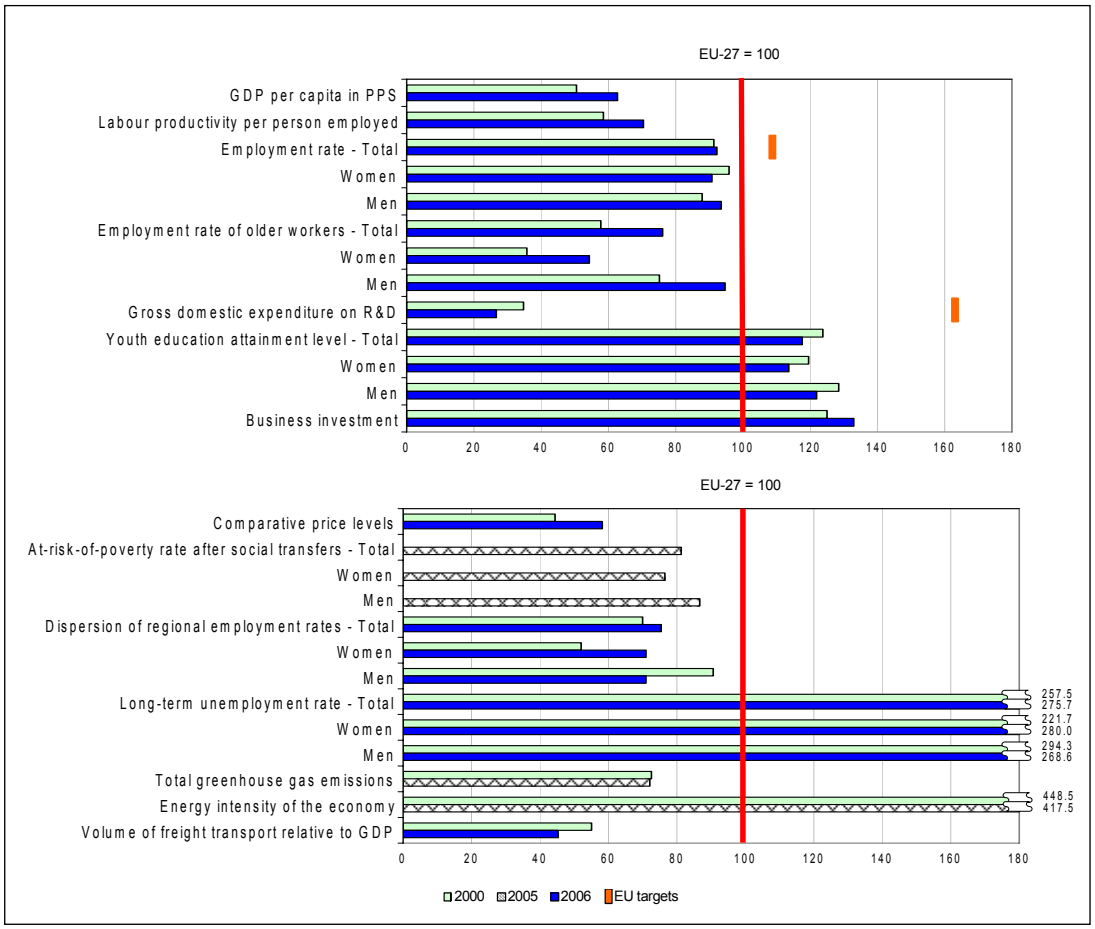
30. In addition, it will be important for Slovakia over the period of the National Reform Programme to focus on: further developing ICT policies, especially for broadband infrastructure; full implementation of one-stop shops for start-up companies; introducing entrepreneurship education; increasing competition in power supply; addressing the gender gap in pay and employment; developing an active ageing strategy; and creating job opportunities for young people.

PART IV: STATISTICAL GRAPHS AND DATA

SLOVAKIA

		SK						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		50.5	55.2	56.7	59.8	62.7		100.0	100.0	100.0	
Labour productivity per person employed		58.5	62.7	64.7	67.8	70.4		100.0	100.0	100.0	
Employment rate	Total	56.8	57.7	57.0	57.7	59.4	:	62.2	63.4p	64.4p	70.0
	Women	51.5	52.2	50.9	50.9	51.9		53.7	56.2p	57.2p	
	Men	62.2	63.3	63.2	64.6	67.0		70.8	70.8p	71.6p	
Employment rate of older workers	Total	21.3	24.6	26.8	30.3	33.1		36.9	42.3p	43.5p	
	Women	9.8	11.2	12.6	15.6	18.9		27.4	33.5p	34.8p	
	Men	35.4	41.0	43.8	47.8	49.8		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		0.65	0.58	0.51	0.51	0.49	0.8	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	94.8	94.1	91.7	91.8	91.5		76.6	77.4	77.8	
	Women	94.8	94.5	92.0	92.6	91.7		79.3	80.1	80.7	
	Men	94.8	93.7	91.3	91.0	91.2		73.8	74.7	74.8	
Comparative price levels		44.4	50.7	54.9	55.8	58.2		100.0	100.0	100.0	
Business investment		23.0	22.4	21.7	24.7	24.2		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	:	:	:	13.0b	:		:	16.0e	:	
	Women	:	:	:	13.0b	:		:	17.0e	:	
	Men	:	:	:	13.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	9.1	7.6	9.0	9.8	8.6		13.0	11.9	11.4	
	Women	10.4	9.0	10.5	11.7	11.5		20.0	16.8	16.2	
	Men	8.7	6.7	8.1	8.5	6.6		9.6	9.7	9.3	
Long-term unemployment rate	Total	10.3	11.4	11.8	11.7	10.2		4.0	4.1p	3.7p	
	Women	10.2	11.7	12.4	12.3	11.2		4.6	4.5p	4.0p	
	Men	10.3	11.3	11.3	11.2	9.4		3.5	3.8p	3.5p	
Total greenhouse gas emissions		65.8	68.0	67.5	66.4	:		90.7	92.1	:	
Energy intensity of the economy		955.9	929.6	910.2	868.6	:		213.1	208.1	:	
Volume of freight transport relative to GDP		54.6	48.8	48.6	52.0e	48.3		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Finland

1. Over recent years, the Finnish economy has enjoyed an extended upswing. GDP growth peaked at 5% in 2006, and will decelerate only moderately in 2007. Growth has remained broad-based, with a strong contribution from foreign demand. Employment has grown at an annual rate of 2% over 2006-2007. Unemployment declined rapidly to 7.7% in 2006 and should decline by a further percentage point in 2007. Nevertheless, the unemployment rate is still at only the euro area average.

2. Notwithstanding the relatively high unemployment rate, there are increasing labour shortages in many sectors, which points to structural labour market weaknesses. Stepping up the government's current labour market response and maintaining on-going improvements to the business environment could improve the situation. Moreover, such improvements could counterbalance the effects on the sustainability of public finances of a declining working age population.

PART I: GENERAL ASSESSMENT

3. The 2007 Implementation Report shows that Finland is in general making very good progress on implementing its National Reform Programme (NRP) over the 2005-2007 period. Progress is steady in most areas.

4. The Council concluded that Finland should focus on implementing reforms to improve competition and productivity in some service sectors, simplify recruitment procedures for businesses, encourage local wage bargaining systems, and address labour market bottlenecks to tackle high structural unemployment, especially unemployment of low skilled workers, including young people. Finland has good progress on simplifying recruitment procedures and local wage bargaining. Some progress has been achieved in the area of competition and service sector productivity. Only limited progress has been made to tackle continuing bottlenecks in the labour market and persistently high structural unemployment.

5. In last year’s Annual Progress Report, the Commission concluded that Finland had generally responded well to the commitments agreed at the 2006 Spring European Council in the priority areas of knowledge, entrepreneurship, employment and energy. Since then, this good progress has been maintained.

6. The Implementation Report specifically addresses the recommendations issued to the euro area countries, although further progress is necessary with regard to competition and the balance between flexibility and security on labour markets.

7. A new government took office in spring 2007. The 2007 Implementation Report confirms the main priorities within the NRP and builds on exploiting policy complementarities. The Finnish government also announced several new policy measures. Consultation between government officials and a wide range of stakeholders and representatives of NGOs is extensive. An integrated approach is further strengthened by the concentration of some important policy areas within the planned new Ministry of Labour and Industry. The new generation of Finnish Structural Fund programmes shows strong commitment to the Lisbon agenda, with some 88% of total programme financing earmarked for activities supporting the

competitiveness of regions and the creation of growth and jobs, well above the 75% minimum requirement set by the Commission. The Finnish Structural Fund strategy for 2007-2013 is largely consistent with the priorities identified in the NRP.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. The overarching policy goal identified in the NRP is to ensure the sustainability of public finances in the face of demographic change. Despite Finland's very strong overall macro-economic performance, this will be a main key challenge in the medium and long term. Key priorities to tackle it are the control of public expenditure, ensuring the capacity to fund welfare services and improving public sector productivity.

9. The new government has revised the system of central government spending ceilings; the main principles of medium term expenditure planning remain intact, but various adjustments to the spending ceilings system imply some increased flexibility. Central government spending limits will remain a crucial tool for containing government expenditure.

10. Reforms to boost public sector productivity and the quality of its service provision are progressing well - horizontal central government functions (administrative affairs, human resources, IT, etc.) are being consolidated. Central government intends to reinforce its productivity programme with new measures to be decided in connection with its spring 2008 spending limits decision. Reform efforts targeting local governments continue; the Act on Restructuring Municipalities and Services entered into force in early 2007. While the bulk of the anticipated positive effects will only be visible in the medium to long term, some progress in municipal mergers and improved service provision structures is already visible.

11. The phasing in of pension reform is advancing according to initial plans and targets. The principal aim is to defer retirement by around 3 years in the long run, and clear progress has been made, helped by pension reform incentives and the economy's cyclical upswing. Legislative changes to the investment and management of employment pension funds entered into force at the beginning of 2007; these allow such funds to increase their investments in stocks, which should increase investment returns.

12. Finland has in general made very good progress over the 2005-2007 period in implementing the specific macro-economic measures outlined in its NRP. The measures should help secure the long-term sustainability of public finances and address long-term challenges due to population ageing. Finland has used the present cyclical upswing in the economy to further strengthen its public finances, in line with the first euro-area recommendation.

Micro-economic policies

13. Finland's national innovation system is a role model for a technology-driven economic reform programme. Finland spends 3.5% of GDP on R&D investment. However, given R&D investment is stagnating, it will be challenging to increase this

figure to the 4% objective in 2011 (2010 in last year's Implementation Report). Public R&D dropped slightly below 1% of GDP in 2007 (partly due to the increase in GDP). New knowledge needs to find its way into practical applications more often. Some sectoral reform programmes have been implemented, including reform of the public research sector, modernisation of the university sector, establishment of strategic centres of excellence in science, technology and innovation, as well as the creation of clusters of centres of expertise. In 2007, the new government launched the preparation of a new National Innovation Strategy and the setting up of a new Ministry for coordinating innovation policy. This should result in a pioneering model for a broad based innovation policy, beyond the traditional science and technology domain, which will engage all organisations to promote innovation in a co-ordinated, mutually reinforcing way.

14. The increasing number of businesses is encouraging, and the business environment is favourable for start-ups. However, the limited growth of existing SMEs is a concern. The government intends to increase the availability of venture capital in cooperation with pension institutions. While the administrative burden is already low, further improvements could be achieved by committing to a specific target, as agreed at the Council. In order to further limit bureaucracy related to entrepreneurship, the government is encouraged to swiftly adopt and implement its national action plan for better regulation and the new impact assessment guidelines. Finland is among the leading information society countries in Europe. Over the past three years, it has met its main objectives in terms of ICT infrastructure (e.g. on the use of broadband). The public administration productivity programme foresees the provision of 100 million euros to overhaul the core IT system so as to improve the quality of services and make better use of ICT through central and local governments.

15. Finland is projected not to meet its Kyoto emissions target unless additional policies and measures are implemented. These policies are under preparation, but Finland is encouraged to give special consideration to climate change to ensure that these policies are implemented as soon as possible. The Finnish economy is highly energy-intensive, and climate, environmental and energy policies may affect competitiveness. A timely announcement of policies is therefore necessary to give the economy time to adjust to the new commitments, though it should be noted that the required measures may create new market opportunities.

16. The Council referred to the need to focus on implementing reforms to improve competition and productivity in services. While productivity is higher in many services than previously thought, and competition has become fiercer, service sector prices still exceed the EU average by about 30%, and productivity differences across different services are substantial. While sector-specific regulations impeding competition are largely dismantled, some regulations remain in certain services, for example covering pharmacies and shop opening hours. Competition enforcement has been strengthened throughout the period. However, the effective implementation of competition policies is sometimes hindered by the length of court proceedings. New legislation which came into force in June 2007 should promote competitive tendering in public procurement. The access of SMEs to public tenders is an important issue in Finland, as the share of SMEs in government procurement is one of the lowest in the EU (around 31% of the number of contracts and only 8% of the value). Finland has been performing well in terms of less and better state aid (excluding aid to

agriculture which remains high). After an initial increase Finland has managed to reduce its transposition deficit and is approaching the 1% target.

17. The Council also referred to the need for Finland to focus on simplifying recruitment procedures for businesses, including through specific measures regarding the recruitment of the first employee. Several improvements have been made, including progress towards a virtual one-stop-shop for hiring employees. As part of the new government programme a similar procedure should be introduced to create new companies. In addition, the government is considering subsidising businesses the hiring of the first employee, which could support firm growth. The Commission therefore considers that Finland has responded appropriately to this issue.

18. Finland has made good progress with the implementation of measures responding to its micro-economic key challenges and has sufficiently addressed the point to watch covering recruitment procedures. However, while competition and productivity in services is improving, welfare gains in terms of lower price levels are still largely unexploited, and continued action remains necessary. A sustainable growth strategy will require some bold policy interventions, putting to the test the economy's capacity to adjust. Timely actions would limit these adjustment costs.

Employment policies

19. Finland achieved the 70% employment rate target in 2007, and female employment has increased to 67.3%, one of the highest in the EU. The growth in female participation is partly explained by increased part-time work. Further improvements can be made if gender pay gaps are addressed; the unadjusted pay gap between men and women is about 20%. The pension reform aiming at extending working life has increased the employment rate of older people. The unemployment rate remains relatively high with persisting structural unemployment, while recruitment problems are growing. Progress over the 2005-2007 period with regard to the functioning of the labour market is mixed and still requires a strong policy response.

20. The Council referred to the need to encourage local wage bargaining systems and address bottlenecks in the labour market, with a particular view to increasing the low participation of youth and tackling high structural unemployment. There has been an increase in local level wage bargaining and the Commission therefore considers that Finland has made an appropriate response to the challenge of setting the right framework for wage bargaining to reflect regional productivity differences and labour market challenges. It is important to continue this approach.

21. Labour supply shortages are a major risk to future economic growth. Some economic sectors already have acute recruitment problems; one third of employers have difficulties finding staff with appropriate skills. So far, there has been limited progress in solving structural unemployment, although the reform of employment services has improved the activation of long term unemployed. The immigration policy introduced in 2006 has not yet boosted international mobility, but the authorities indicate that the issue is being addressed at the political level with the nomination of a minister for migration. Further measures to promote work-based immigration are expected. Early school drop out is being tackled. Efficient measures are still needed to attract people outside the labour market into employment.

22. Finland addresses flexicurity in an integrated way, with measures being implemented across the four components of flexicurity. The social partners are fully involved in policy level programmes. A high level tripartite working group was established in 2007 to reconsider flexibility and security in the Finnish labour market. Lifelong learning has been promoted through workplace development programmes. The comprehensive social security reform initiated in 2007 is welcomed in order to thoroughly review the incentives to work. Legislative reform is being introduced on fixed term employment and attention should be paid to the particularly high number of fixed-term contracts for women. A system has been in force for a year helping employees facing redundancy to find new jobs.

23. In general, Finland has shown good progress meeting most of the NRP's employment policy commitments and has sufficiently addressed the point to watch regarding local wage bargaining. Persistent labour market bottlenecks, however, are an ongoing concern. In light of the growing inefficiency in matching job vacancies to the unemployed, the Commission considers that Finland has made only a limited response to the challenges it faces in addressing its labour market bottlenecks. It is important to increase the pace of reform in order to improve the balance of labour supply and demand.

PART III: CONCLUSIONS

24. In light of the 2007 Implementation Report for Finland and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

25. Finland has made very good progress in implementing its National Reform Programme over the 2005-2007 period. Good progress has been shown in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

26. The Implementation Report shows some policy response on the additional areas identified by the Council as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

27. Among the strengths of the 2007 Implementation Report are the ongoing reforms to further improve the functioning of the national innovation system and the observed increase in the employment rate of older workers.

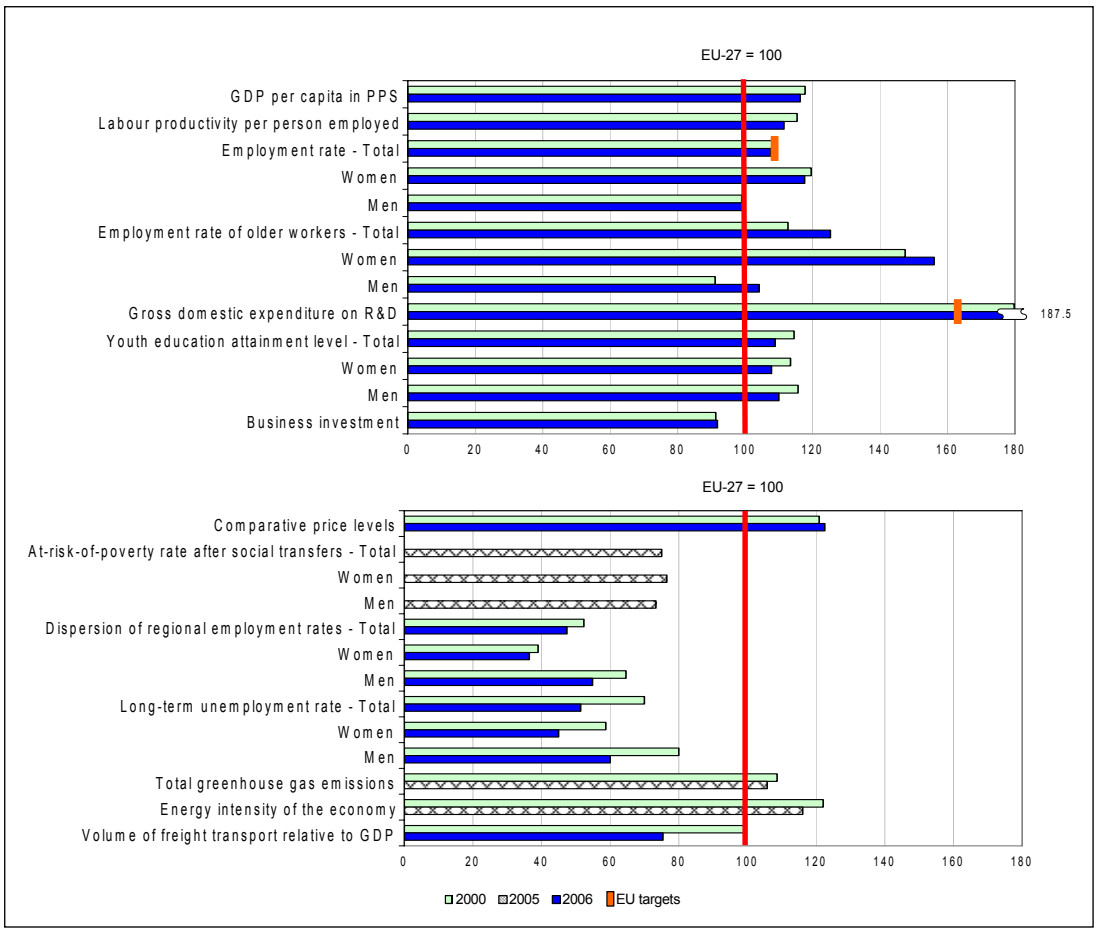
28. It will be important for Finland over the period of the National Reform Programme to focus on the following challenges: continue reforms to improve competition and productivity in services, and create the necessary leverage to reduce high price levels; implement announced measures to reach its Kyoto target; continue reforms to address bottlenecks in the labour market, with a particular view to tackling high structural unemployment, especially unemployment of low skilled workers, including young people, and taking into account the contribution economic migration can make.

PART IV: STATISTICAL GRAPHS AND DATA

FINLAND

		FI						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		117.8	113.5	115.9	114.5	116.3		100.0	100.0	100.0	
Labour productivity per person employed		115.4	109.3	111.8	109.8	111.5		100.0	100.0	100.0	
Employment rate	Total	67.2	67.7	67.6	68.4	69.3	75.0 (2011)	62.2	63.4p	64.4p	70.0
	Women	64.2	65.7	65.6	66.5	67.3		53.7	56.2p	57.2p	
	Men	70.1	69.7	69.7	70.3	71.4		70.8	70.8p	71.6p	
Employment rate of older workers	Total	41.6	49.6	50.9	52.7	54.5		36.9	42.3p	43.5p	
	Women	40.4	48.3	50.4	52.7	54.3		27.4	33.5p	34.8p	
	Men	42.9	51.0	51.4	52.8	54.8		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		3.34	3.43	3.45	3.48	3.45	4.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	87.7	85.3	84.5	83.4	84.7		76.6	77.4	77.8	
	Women	90.0	87.6	87.0	85.7	87.0		79.3	80.1	80.7	
	Men	85.4	83.0	81.9	81.0	82.3		73.8	74.7	74.8	
Comparative price levels		120.9	126.6	123.8	123.5	122.5		100.0	100.0	100.0	
Business investment		16.8	15.2	15.3	16.3	16.7		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	11.0	11.0	11.0b	12.0	:		:	16.0e	:	
	Women	13.0	12.0	11.0b	13.0	:		:	17.0e	:	
	Men	9.0	11.0	10.0b	11.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	6.8	6.1	5.5	5.5	5.4		13.0	11.9	11.4	
	Women	7.8	6.7	6.2	6.1	5.9		20.0	16.8	16.2	
	Men	6.2	5.7	5.2	5.1	5.1		9.6	9.7	9.3	
Long-term unemployment rate	Total	2.8	2.3	2.1	2.2	1.9		4.0	4.1p	3.7p	
	Women	2.7	2.0	2.0	1.9	1.8		4.6	4.5p	4.0p	
	Men	2.8	2.6	2.3	2.4	2.1		3.5	3.8p	3.5p	
Total greenhouse gas emissions		98.5	119.9	114.1	97.4	:		90.7	92.1	:	
Energy intensity of the economy		260.1	280.1	268.9	241.5	:		213.1	208.1	:	
Volume of freight transport relative to GDP		98.7	90.5	90.3	86.0	80.4e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



Sweden

1. Over the period 2005-2007, the Swedish economy has been experiencing strong and broad-based economic growth, averaging 3½% a year. External demand has been an important driving force, but owing to the recent deceleration of global economic activity, export growth has entered a weaker phase. Domestic demand remains buoyant, supported by robust consumption growth and booming investment. Employment rates are high, and there have recently been strong increases for all age groups, especially young people, while unemployment has fallen to below 6%.

2. The strong domestic economy is partly a result of various policy measures taken by the government, including lower taxes on labour and other labour market measures that have contributed to strong employment growth, a marked reduction of unemployment and rising household disposable income. This has provided an impulse to private consumption growth, part of which is still to materialise.

PART I: GENERAL ASSESSMENT

3. Overall, the Swedish 2007 Implementation Report has shown very good progress in implementing the updated National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have accelerated significantly over the last year.

4. No country specific recommendations were addressed to Sweden, but it was concluded that special attention should be paid to increasing competition, improving the impact assessment system, taking a more coherent approach to better regulation, and strengthening the strategy to increase labour supply and hours worked. There has been a good response with regard to better regulation and on impact assessment, and on measures aimed at increasing labour supply and hours worked. However, Sweden has not moved forward sufficiently on increasing competition.

5. Last year's Annual Progress Report concluded that Sweden had made good progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been very good progress on most of the commitments with an end 2007 deadline.

6. Consultation and efforts to develop ownership of the NRP continue to be substantial. The political visibility of the Strategy for Growth and Jobs has increased, following the assignment of responsibility at ministerial level. The Implementation Report presents a thorough coverage of all the guidelines and addresses the challenges highlighted in last year's assessment. Consultation with the social partners, civil society and young people has been thorough. Efforts to include local authorities have been further stepped up, with the creation of a national forum, for political dialogue between national and regional level, to consider regional development issues and implementation of the Lisbon Strategy. Links between the implementation of the NRP and the programmes under the Structural Funds are fairly strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily (ERDF 79.5% and for ESF 96% of funds). The ESF priorities focus on

increased labour supply by ensuring adequate skills for people at work and better integration of disadvantaged groups. The ERDF emphasises support for R&D, innovation, entrepreneurship and risk capital.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. Sweden is coping well with the key macro-economic challenges of maintaining sound public finances and safeguarding fiscal sustainability. The general government budget has recorded successive surpluses well above 2% of GDP a year, contributing to a further consolidation of public finances. In 2007, the government has further enhanced the rules-based budgetary framework supporting the overall strategy, notably by clarifying and improving the credibility of the objectives on which it is based. The implementation of a range of labour market reforms as well as improvements in tax and benefit systems have contributed to increasing employment growth and to lower unemployment. Increased employment and high resource utilisation has, however, contributed to higher wage agreements. Wage growth is set to exceed the rate implied by recent productivity trends over the next few years. The inflation rate has remained low, though it is gradually rising.

8. Progress over 2005-2007 with regard to the implementation of macro-economic policies identified by Sweden in the NRP, notably the challenge of sound fiscal policies and safeguarding fiscal sustainability, and of increased labour supply, employment and number of hours worked, is good.

Micro-economic policies

9. Sweden confirms the micro-economic challenges notably as regards creating a better environment for entrepreneurship and SMEs, strengthening the linkage between academic R&D and industry, and encouraging the sustainable use of resources.

10. R&D expenditure as a share of GDP was 3.82% in 2006. More public funds have been allocated to R&D since 2005 and additional resources for research and postgraduate education are planned over 2007-2009. There is scope for stronger emphasis on the role of SMEs in the R&D and innovation system, notably by focusing on research-driven and innovative firms, and by encouraging links with larger firms and universities. Efforts to promote cooperation between public and private actors should continue. Fiscal efforts have been made to promote entrepreneurship in the service sector, especially in the welfare sector, but private undertakings still face having to compete on unequal terms with public authorities. Appropriate improvements have been introduced to simplify the regulatory and fiscal framework for small entrepreneurs. However, SMEs' participation in public procurement is still hindered by the extensive use of large framework contracts.

11. Sweden is likely to comfortably achieve its Kyoto target for a reduction of carbon emissions and the move towards a sustainable economy has been a high priority for Sweden over the last three years. The government plans to spend SEK 1 billion to combat climate change over 2008-2010. In 2007 the government presented a

programme to further develop environmental technology capacity with significant financing for 2007 and 2008.

12. The Council referred to the need for Sweden to rapidly implement planned improvements to the impact assessment system and to take a more coherent approach to better regulation. In June 2007, the Swedish government presented a first phase of a solid and encompassing action plan for regulatory simplification, including general guidelines and significant number of measures aimed at alleviating the administrative burdens. The widespread introduction of e-government throughout the public administration, since 2005, may help achieve the ambitious administrative burden reduction target of 25% by 2010. The government is committed to adopting an ordinance on impact assessments and to dedicating additional human resources to better regulation, notably by creating a regulatory council in charge of ensuring the quality of impact assessment.

13. The Council also underlined that Sweden should take further regulatory measures to increase competition, notably in services. Several initiatives set out in the Implementation Report head in the right direction. In the public procurement area, the merger of the Public Procurement Board with the Competition Authority is a positive step, but the transposition of the EU legislation should be completed without further delay, and the recommendations of the Competition Authority in this area implemented. Planned measures regarding competition between public and private undertakings should be adopted. It remains to be seen whether the foreseen revision of the Competition Act will sufficiently improve competition law enforcement, notably by strengthening the Competition Authority's powers and mechanisms to deter competition infringements.

14. In general, progress over the 2005-2007 period with regard to the implementation of policies to address the micro-economic challenges faced by Sweden is good. The Commission considers there has been a good response to the challenges Sweden faces in ensuring better regulation. It is now important to continue this approach in 2008 and 2009. The point to watch in the competition area has been partially addressed and it is important to step up the pace of reform.

Employment policies

15. The government continues to place emphasis on increasing labour supply and employment, and on reducing the number of people outside the labour force. Employment rates are high across all groups, with the overall rate standing at 73.1%. Unemployment has recently fallen to below 6%. Labour supply has started to grow after the decreases over the last few years, with signs of enhanced integration of groups previously outside the labour market. Young people account for half of the recent expansion in employment, but despite this youth unemployment remains high, at over 18%. In addition employment rate gaps between foreign-born and native people are still a concern at more than 14 percentage points, and there are still 551 000 people on disability pension (about 9% of the working age population). Recent reforms focus on increasing incentives to work, reforming active labour market policy and the education system. Progress over 2005-2007 with regard to addressing the challenge faced by Sweden to increase labour supply is good.

16. The Council referred to the need to strengthen the strategy to increase labour supply and hours worked, including through the implementation of proposals to increase incentives to work, as well as stronger measures to increase the employment rate of immigrants and young people, and to reintegrate people on sickness-related schemes.

17. Sweden has introduced a number of measures that address work incentives, in particular subsidised jobs in the private sector (lower social contributions), an in-work tax credit and stricter controls of the social security systems. The reform packages for young people and immigrants focus on incentives to work and other targeted measures. For young people intensified counselling is followed by further training or work experience, more resources are given to the public employment services for job matching, and the cost of social contributions for employers have been halved when employing young people. This should all help the integration process. The planned reforms of the education system (improved quality, up-dating of teachers' skills, modernising upper secondary schools, and a new apprenticeship programme) should help reduce early school drop-outs.

18. To better integrate immigrants in the labour market, subsidised jobs combined with language courses are now being implemented. Alongside this, the validation of qualifications from outside Sweden, and supplementary university courses for people with a foreign training in law, teaching, and public administration are being introduced. Municipalities now receive financial compensation if they provide jobs for refugees. The recent reform to reintegrate people on sickness-related schemes includes measures for rehabilitation, restrictions of the sickness insurance system and large reductions of the social contributions. For disabled persons, about 3000 new jobs will be created through wage subsidies and sheltered work. There are a number of new measures planned for 2008, for example a reinforced in-work tax credit.

19. Overall, Sweden has a balanced approach towards flexicurity and addresses it in an integrated way. The government has facilitated the use of fixed-term contracts which should work as a stepping stone into the labour market. Recent reforms of the unemployment and sickness insurance systems imply restrictions, but they still provide adequate income security. Active labour market policy has been reformed focusing on improved matching and reforming the National Labour Administration. Measures devoted to lifelong learning concentrate on the initial education system and less on adult education. The social partners are fully involved in most of the flexicurity components.

20. In general, Sweden has succeeded in implementing measures to deliver on the employment policy commitments expressed in its NRP. The points to watch in the employment area have been well addressed and it is now important to focus on implementation and impact evaluation. Important challenges remain, in particular with regard to the high youth unemployment, the high employment gap between immigrants and native Swedes, and the high number of people on disability pension.

PART III: CONCLUSIONS

21. In the light of Sweden's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on

the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

22. Sweden has made very good progress in implementing its National Reform Programme over the 2005-2007 period. Sweden has also shown very good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

23. The Implementation Report shows a good policy response to the areas identified by the Council as requiring attention.

24. Among the strengths shown by the 2007 Sweden's Implementation Report are: the action plan for regulatory simplification and the commitment to improve the impact assessment system; the progress with increasing labour supply and reducing unemployment; the sustainable use of energy; and the progress made on increasing public investment in R&D.

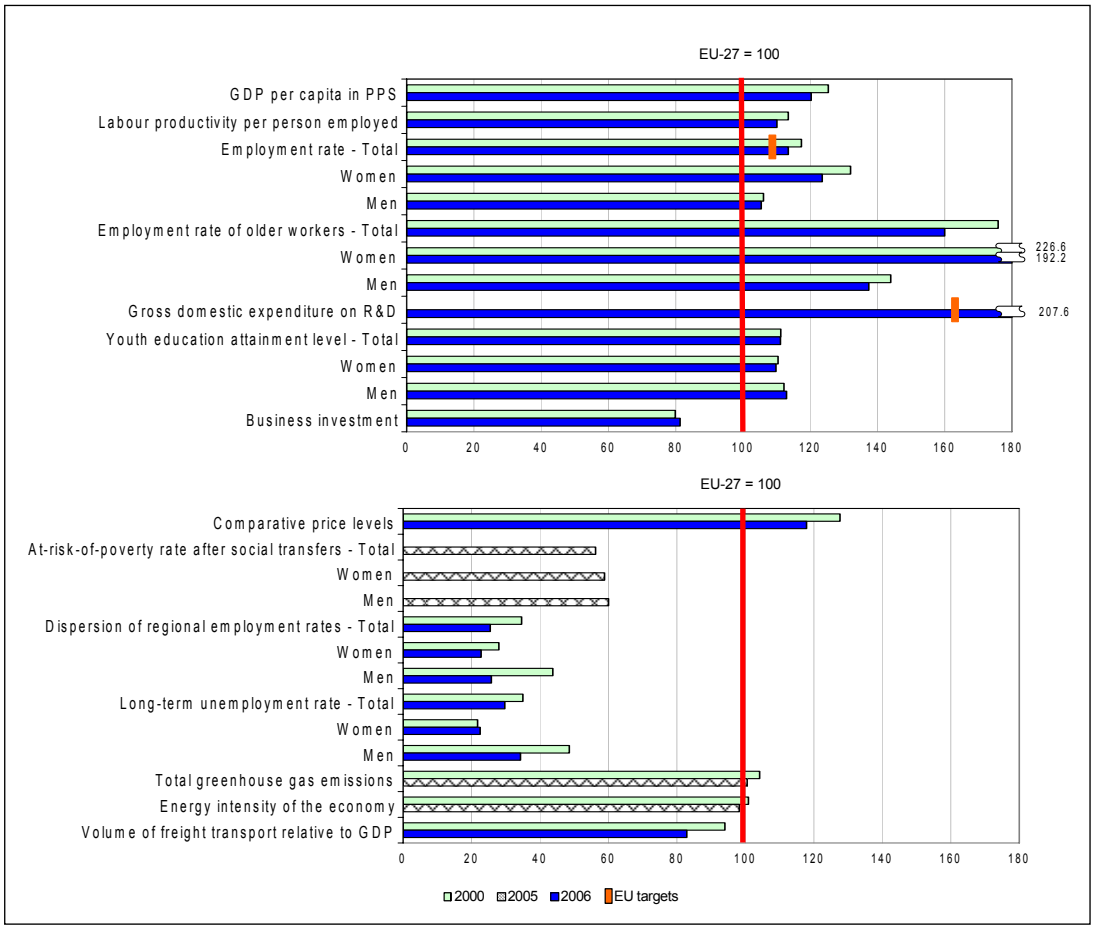
25. It will be important for Sweden to take further regulatory measures to increase competition, notably in services; and to focus on the implementation and impact evaluation of recent reforms to increase work incentives, to tackle youth unemployment, to raise the employment rate of immigrants and to reintegrate people on sickness-related schemes.

PART IV: STATISTICAL GRAPHS AND DATA

SWEDEN

		SE						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		125.4	120.5	120.4	119.1	120.3		100.0	100.0	100.0	
Labour productivity per person employed		113.5	108.3	109.6	109.0	110.1		100.0	100.0	100.0	
Employment rate	Total	73.0	72.9	72.1	72.5b	73.1	:	62.2	63.4p	64.4p	70.0
	Women	70.9	71.5	70.5	70.4b	70.7		53.7	56.2p	57.2p	
	Men	75.1	74.2	73.6	74.4b	75.5		70.8	70.8p	71.6p	
Employment rate of older workers	Total	64.9	68.6	69.1	69.4b	69.6		36.9	42.3p	43.5p	
	Women	62.1	66.3	67.0	66.7b	66.9		27.4	33.5p	34.8p	
	Men	67.8	70.8	71.2	72.0b	72.3		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		:	3.95	3.71	3.89	3.82	4.0	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	85.2	85.8	86.0	87.5	86.5		76.6	77.4	77.8	
	Women	87.6	87.2	87.2	88.7	88.6		79.3	80.1	80.7	
	Men	82.8	84.3	84.8	86.4	84.5		73.8	74.7	74.8	
Comparative price levels		127.6	123.5	121.8	118.5	117.9		100.0	100.0	100.0	
Business investment		14.7	12.9	13.2	14.2	14.8		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	:	:	11.0b	9.0	:		:	16.0e	:	
	Women	:	:	12.0b	10.0	:		:	17.0e	:	
	Men	:	:	10.0b	9.0	:		:	15.0e	:	
Dispersion of regional employment rates	Total	4.5	4.3	4.4	3.0	2.9		13.0	11.9	11.4	
	Women	5.6	4.8	4.3	3.5	3.7		20.0	16.8	16.2	
	Men	4.2	4.1	4.8	2.8	2.4		9.6	9.7	9.3	
Long-term unemployment rate	Total	1.4	1.0	1.2	1.4b	1.1		4.0	4.1p	3.7p	
	Women	1.0	0.8	1.0	1.2b	0.9		4.6	4.5p	4.0p	
	Men	1.7	1.2	1.4	1.5b	1.2		3.5	3.8p	3.5p	
Total greenhouse gas emissions		94.5	97.9	96.4	92.6	:		90.7	92.1	:	
Energy intensity of the economy		215.0	217.1	214.7	204.3	:		213.1	208.1	:	
Volume of freight transport relative to GDP		93.2	90.6	88.6	89.7	88.4e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27



United Kingdom

1. Real GDP growth in the UK is expected to reach 3.1% in 2007. Robust output growth the last two years has been driven by domestic demand, accompanied by a sizeable external imbalance. The general government deficit narrowed to 2.6% of GDP in financial year 2006/2007 from 3.2% of GDP in the previous year. The employment rate (71.5% in 2006) is above the EU target. Labour supply has been growing, partly owing to immigration and increased participation from female and older workers. The unemployment rate has remained stable at around 5.3% in 2007.

2. Labour, capital and product markets are very flexible but, despite steady growth and good employment performance and some narrowing of the productivity gap with other Member States, the UK still faces a productivity challenge. While the UK has focussed on the development of policies to improve skills, R&D intensity, better regulation and the competition regime, further improvements are still needed to support future productivity growth. The planned reform of the pensions system should result in both improving the adequacy of retirement income and increasing incentives for participation in the labour market.

PART I: GENERAL ASSESSMENT

3. Overall, the UK's 2007 Implementation Report shows significant progress in implementing the National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have accelerated slightly over the last year.

4. There has been good progress in response to the country specific recommendation that the UK should increase basic and intermediate skills in order to raise productivity and further improve employment prospects for the most disadvantaged. However, it will be some time before the new skills package is fully implemented.

5. With regard to the other areas for the UK to concentrate upon: there has been good progress on the implementation of the pension reform; and on improved access to childcare. In R&D and innovation policy some progress has been made. Concerning increasing the supply of housing, some measures have been taken, but it is too early to judge whether these will be effective.

6. Last year's Annual Progress Report concluded that the UK had made good progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas of knowledge, entrepreneurship, employment and energy. Since then, there has been further good progress on all of the commitments.

7. Consultation and efforts to develop ownership of the NRP at the level of central and local governments and amongst the social partners continue to be good. The devolved administrations in Scotland, Wales and Northern Ireland were involved in preparing the Implementation Report concerning their own policy responsibilities. There has also been consultation on many individual policy elements. Specific consultation in preparing the Implementation Report has included a stakeholder seminar and web-based consultation.

8. Governance links between the implementation of the NRP and the programmes under the structural and cohesion funds are strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily. The overall objectives for future Structural Funds Programmes are strengthening the drivers of regional productivity and employment, responding to the increasing pace of economic change and the expanding reach of global markets, and improving the sustainability of communities and the environment.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

9. The UK's NRP identified macro-economic stability and long-term fiscal sustainability as the government's overall macro-economic priorities. Over the programme period inflation has been contained; some pronounced increases in early 2007 have subsequently been reversed. The 2007 Comprehensive Spending Review has set departmental spending allocations for the three financial years beginning in April 2008, with total public spending increasing by 2.1% per year on average in real terms. Although the government deficit is foreseen to remain close to the reference value of 3% of GDP in the financial years 2007/2008 and 2008/2009, the Implementation Report does not highlight the need for ensuring fiscal consolidation. It focuses mainly on the quality of public finances, pension reform and housing supply. Progress over the 2005-2007 period with regard to the implementation of policies to address the macro-economic challenges faced by the UK is thus mixed.

10. The Council referred to the importance for the UK of ensuring that the current proposals on pension reform were effectively implemented. The government's plans, partly already enacted by Parliament, involve increasing the value and coverage of the state-pension by linking pension payments to average earnings from 2012 (subject to affordability), and increasing the state pension age in line with average life expectancy. Moreover private pension saving will be encouraged through the introduction of automatic enrolment of employees into a work placed pensions, mandatory employer contributions, and a new scheme of personal accounts. The impact will only be fully evident in the long term.

11. The Council also referred to the importance for the UK of progressively increasing housing supply to reduce house price pressures in the medium-term. The government released a Housing Green Paper in July 2007 setting a target of building 240,000 new additional homes per year in England by 2016 (2 million new homes in total) – about 30% higher than would be generated by recent construction rates – and a 50% increase in social housing supply by 2010/2011. The 2007 Pre-Budget Report and the Comprehensive Spending Review announced an increase in spending on housing in the period 2007/2008 to 2010/2011. Whilst some measures have already been implemented, further measures have been announced, such as the government's plan for a new Housing and Planning Delivery Grant to reward those councils who are achieving a high level of housing supply. These policies are steps in the right direction , but most of the reforms are still in the early stages of implementation so the actual impacts will clearly take much longer to judge.

12. In general, the UK has partially succeeded in implementing measures to achieve the macro-economic objectives expressed in its NRP. The Commission considers the measures taken to reform the pension system to be a very good response, addressing the adequacy of retirement income, while limiting the risks to the sustainability of public finances. However, the fiscal position needs improving and further consolidation in the medium term is required.

Micro-economic policies

13. The UK NRP identified promoting R&D and innovation and building an enterprising and flexible business sector as key micro-economic challenges. Progress has been made on R&D and innovation, notably by ensuring the sustainability of the public research base, promoting technology transfer, stimulating private R&D investment through a strengthening of the R&D tax credit, and the setting up of the Technology Strategy Board, at arm's length from government. The UK continues to provide a business-friendly regulatory environment and competition regime. Progress has also been made in moving towards creating one-stop-shops for business start-ups and support services, as well as in improving SMEs' access to public procurement contracts. Strengths in entrepreneurship training and in improving regulation for small businesses have been reinforced, and the UK is committed to reduce administrative burdens by 25%. On energy policy, the UK is already advanced in energy market opening. The White Paper on energy policy published in May 2007 set out a strategy for tackling climate change and ensuring energy security. Consultations are currently taking place on aspects of this policy.

14. The Council referred to the need to focus on: implementing its science and innovation strategy, in the context of which an intermediate R&D target for 2010 should be set and measures should be taken to further strengthen investment incentives and to increase private sector engagement. The government aims to implement the recommendations of the recent Sainsbury review. This will result in a more active engagement in stimulating R&D and innovation activity, including a leadership role and increased funding for the Technology Strategy Board, explicit knowledge transfer targets for the Research Councils, and increased efficiency and coordination of public R&D spending. However, the foreseen increases in government spending on R&D (including substantial Structural Fund financing) and forecasts for private spending are insufficient to advance towards the UK's 2014 R&D intensity target. Therefore raising private R&D investment and innovation further continues to be an important challenge for the UK in an increasing knowledge based economy. The UK should capitalise upon the strength of its services sector by developing further policies for stimulating R&D and innovation and improving skills in this sector, including assessing the challenges and existing policy framework as part of the overall monitoring arrangements for the science and innovation framework.

15. The Commission considers there has been some response to the challenge the UK faces in the micro-economic field. It is now important to implement the recommendations from the recent Sainsbury review of science and innovation policy, ensuring a greater focus on increasing R&D and innovation, especially in services.

Employment policies

16. The NRP identified two major employment-related challenges: raising the skill levels in the workforce and increasing employment opportunities, by removing barriers for people from groups characterised by low employment rates. Progress has been made on both fronts. Over the period 2005-2007, employment has increased, although the employment rate has changed little since the population has also grown. Inactivity rates have generally fallen. Employment gaps for women, lone parents, older workers and ethnic minorities have narrowed but have widened for those without qualifications. Progress over the period 2005-2007, with regard to the implementation of policies to address the labour market challenges in the NRP is good.

17. The Council recommended the UK to increase basic and intermediate skills in order to raise productivity and further improve employment prospects for the most disadvantaged. In July 2007, the government presented plans to implement the Leitch Report's recommendations on skills in England, with the devolved administrations also having welcomed the report. This was accompanied by a green paper setting out the next steps in welfare reform. The reforms on skills are designed to make training more demand-led. To stimulate demand the government has launched a "Skills Pledge" by which employers make a public commitment to provide training opportunities for their workers with low level qualifications while the programme to subsidise this training is expanded. There will be institutional changes that give employers a greater role: including the creation of a Commission for Employment and Skills. One task for this new Commission will be to advise the government on the strategy needed to increase employment an skills rates, as well as assessing progress.
Some new measures are already being implemented; others are to be implemented over the next three years or so. The steps taken so far show a substantial new impetus to reach the targets set. The success depends upon a greater commitment by employers to training and their acceptance of the new qualifications framework being developed. The moves to give a greater role for the private sector in the delivery of services for the unemployed will have to ensure a balance between giving incentives for greater innovation and ensuring that the complex needs of the more disadvantaged are met.

18. The Council also referred to the need to further improve access to childcare. The measures in the Childcare Act 2006 introduce a duty on local government to ensure that sufficient childcare is available especially for parents on low incomes or with disabled children came into force in April 2007. Progress in implementing England's ten year childcare strategy is on course, including the creation of children centres, out-of-school childcare places, a free weekly entitlement to 15 hours of pre-school provision for 3 and 4 year olds by 2010, and rights for parents to time off work, and statistics are beginning to show the impact of the measures taken. However, there is some way to go to reach the government's targets, and some concerns remain over affordability and the choice available to parents.

19. The UK addresses the aspects of flexicurity in a broadly integrated way. Active labour market programmes could do more for sustainable employment by giving more attention to promoting retention and progression, and a better integration of

employment and skills services would enhance learning opportunities and career progression. The social partners are not directly involved in the preparation of reforms but are routinely consulted.

20. In general, the UK has made good progress in implementing measures to deliver on the employment policy commitments in its NRP and in addressing the country specific recommendation and the point to watch. On skills and on improving the employment prospects of people from disadvantaged groups, the government has set out a comprehensive and well-balanced strategy, and has begun to implement measures that signal the new impetus given to policy in this area. However, it will be some time before the whole package is implemented and measurable results are available.

PART III: CONCLUSIONS

21. In the light of the UK's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

22. The UK has made significant progress in implementing its National Reform Programme over 2005-2007. The UK has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

23. The Implementation Report shows a good policy response to the recommendation issued by the Council. There has also been a good policy response on the additional areas identified in the Council conclusions as requiring attention.

24. Among the strengths shown by the 2007 UK Implementation Report are: the plans to provide an integrated approach to employment and skills, moves towards the creation of a business-friendly regulatory environment, and the forward-looking plans on energy policy.

25. The policy areas in the UK National Reform Programme where challenges need to be tackled with the highest priority are improving skills levels to increase productivity and reduce disadvantage in the labour market. Against this background it is recommended that the UK:

- implement recent plans to substantially improve skill-levels and establish an integrated approach to employment and skills in order to improve productivity and increase opportunities for the disadvantaged.

26. In addition, it will be important for the UK to focus on the following challenges for the future: progressively increase housing supply in order to meet medium term demand pressures; ensure progress towards the UK's R&D intensity target through full implementation of the recent review of R&D and innovation policy, particularly taking fuller account of the specific needs of the services sector.

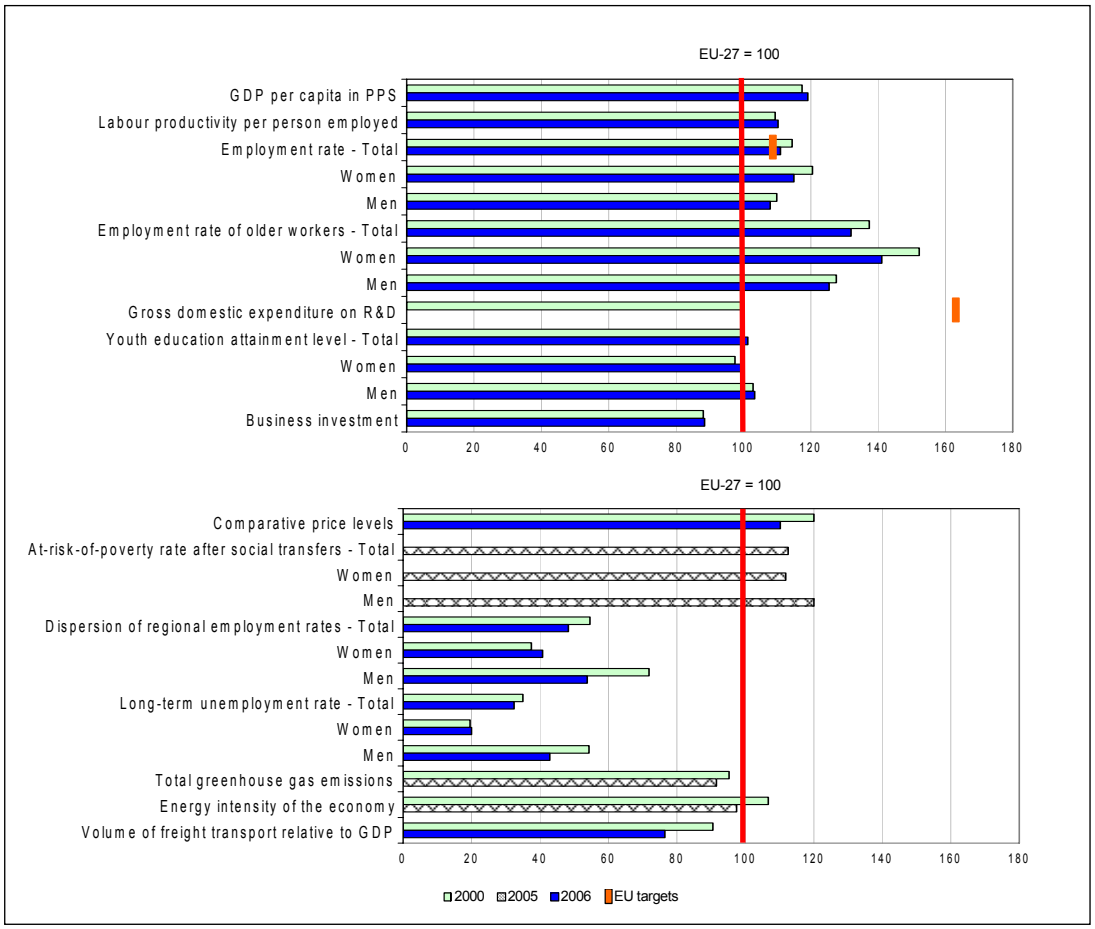
PART IV: STATISTICAL GRAPHS AND DATA

UNITED KINGDOM

		UK						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		117.4	120.0	121.8	119.6	119.1		100.0	100.0	100.0	
Labour productivity per person employed		109.4	110.3	111.7	109.8	110.3		100.0	100.0	100.0	
Employment rate	Total	71.2	71.5	71.6	71.7	71.5	*	62.2	63.4p	64.4p	70.0
	Women	64.7	65.3	65.6	65.9	65.8		53.7	56.2p	57.2p	
	Men	77.8	77.7	77.8	77.6	77.3		70.8	70.8p	71.6p	
Employment rate of older workers	Total	50.7	55.4	56.2	56.9	57.4		36.9	42.3p	43.5p	
	Women	41.7	46.3	47.0	48.1	49.1		27.4	33.5p	34.8p	
	Men	60.1	64.8	65.7	66.0	66.0		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.85	1.78	1.72	1.76	:	2.5 (2014)	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	76.6	78.7	77.0	78.2	78.8		76.6	77.4	77.8	
	Women	77.3	78.9	78.0	78.9	80.3		79.3	80.1	80.7	
	Men	75.9	78.4	76.0	77.4	77.3		73.8	74.7	74.8	
Comparative price levels		120.0	107.8	107.9	109.2	110.2		100.0	100.0	100.0	
Business investment		16.2	15.1	15.3	16.5	16.1		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	19b	18.0	:	18.0b	:		:	16.0e	:	
	Women	21b	19.0	:	19.0b	:		:	17.0e	:	
	Men	16b	17.0	:	18.0b	:		:	15.0e	:	
Dispersion of regional employment rates	Total	7.1	6.1	5.9	5.7	5.5		13.0	11.9	11.4	
	Women	7.5	6.7	6.5	6.4	6.6		20.0	16.8	16.2	
	Men	6.9	5.8	5.7	5.6	5.0		9.6	9.7	9.3	
Long-term unemployment rate	Total	1.4	1.1	1.0	1.0	1.2		4.0	4.1p	3.7p	
	Women	0.9	0.7	0.6	0.7	0.8		4.6	4.5p	4.0p	
	Men	1.9	1.4	1.2	1.3	1.5		3.5	3.8p	3.5p	
Total greenhouse gas emissions		86.4	85.0	84.7	84.3	:		90.7	92.1	:	
Energy intensity of the economy		227.3	212.1	206.0	202.6	:		213.1	208.1	:	
Volume of freight transport relative to GDP		89.7	84.5	83.9e	82.1e	81.6e		99.1e	105.4e	106.7e	

* National target: 80% following the national definition

PERFORMANCE COMPARED TO EU-27



Euro Area Member States

1. The economic performance of the euro area has improved since the Lisbon Strategy was renewed in 2005. GDP growth rebounded to 2.8% in 2006 and is forecast to decelerate slightly to 2.6% in 2007. The estimated potential growth rate of GDP has increased by some ¼ percentage points since 2005 to some 2¼ % in 2007. Employment increased by 4.3 million between 2005 and 2007, whilst the rate of unemployment declined from 8.9% in 2005 to 7.3% in 2007. The recent output growth has had a particularly strong positive effect on employment and part of the acceleration of labour productivity growth might be more than just cyclical in nature. Interdependence of the euro area economies is large with annual intra-area trade at 20% of euro area GDP.

2. The fiscal and monetary developments in the euro area have contributed to stability while supporting the economic recovery. With deficits and debt levels going down to more sustainable levels, overall fiscal performance has made significant steps to confront the ageing challenge. The implementation of structural reforms has improved fundamentals and increased the resilience of the economy. Inflation in the euro area Member States has been contained despite increasing energy prices and food prices. Such favourable outcome could be attained at interest rates that are low in a historical perspective, which should be conducive to continued capital formation.

3. The number of euro area Member States is growing. While in 2007 Slovenia adopted membership of the Economic and Monetary Union (EMU), 2008 will see Malta and Cyprus join. This brings the total euro area membership to a level of about 320 million people and fifteen Member States.

PART I: GENERAL ASSESSMENT

4. The euro area Member States have engaged in substantive structural reforms to tackle their economic, social and environmental challenges, although some have responded more robustly to some challenges than others. To stimulate Member States, the Council adopted country specific recommendations in the macro-economic, micro-economic and employment domain.

5. Stability oriented macro-economic policies foster favourable growth conditions and, especially relevant in the current juncture, are key to reduce uncertainty. Although important for all EU Member States, structural reforms are especially relevant for the economies in the euro area. Primarily aimed at creating more growth and jobs, structural reforms also enhance integration and the adaptability of euro area economies and synchronise its business cycles. Against the background of changing global economic conditions, well-functioning labour, product and service markets and more investment in skills are particularly important because they facilitate the reallocation of resources. Better integrated economies and the single currency stimulate competition, intra-EU trade in the internal market, promote innovation, and give consumers better value for money. Moreover, regional differences in demand can more easily be met through increased supply from elsewhere in the euro area, thus avoiding price pressures. In the absence of the exchange-rate instrument for

individual Member States, flexible labour markets and healthy government budgets are key to preventing strong downward (recession) and upward (overheating) fluctuations in growth. More synchronised business cycles will make it possible to have a monetary policy better geared to the needs of the EMU as a whole and Member States individually.

6. By tackling the euro area's common challenges in a coordinated manner, the benefits will be more substantial given the important spillovers across Member States. The Council therefore recommended that the euro area Member States aim at more ambitious budgetary consolidation, improving the quality of public finances, improving competition, especially in (financial) services and better balancing flexibility and security in labour markets. Evidently, there are differences across Member States in the degree of relevance of these recommendations. The Commission (in its October 2007 communication to the Informal European Council and the Council, highlighted the importance of effective policy co-ordination, especially in the context of the Eurogroup, and where appropriate in international fora.

7. In addressing the call for more effective policy coordination in the euro area, a positive development has been that the Eurogroup stepped up its analysis and monitoring of structural reforms. Over the last year, it held discussions on all the issues highlighted by the euro area recommendations, enabling Ministers to be better informed about the strategies, choices and challenges outstanding in the individual Member States and for the euro area as a whole, and to foster consensus on the importance of policies that improve adjustment in the euro area. A further notable development is that ten participating Member States (AT, BE, DE, ES, FI, IT, LU, NL, PT, SI) included details on their response to the euro area recommendations in their Implementation Reports. Although both developments are steps in the right direction, there is more scope for effective policy co-ordination.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

8. Macro-economic stability and sound fiscal policies enhance growth, create leeway to withstand adverse cyclical conditions, and help maintain price stability and low interest rates. The budget deficit in the euro area has come down from 2.5 % of GDP in 2005 to a forecast 0.8 % in 2007. Gross debt has declined from over 70% of GDP in 2005 to an expected 66.5 % in 2007. This has supported the monetary policy objective of maintaining price stability and, together with the implemented pension reforms, contributed to the sustainability of public finances, thereby helping tackle the budgetary consequences of ageing populations. Wage growth has remained contained in the period 2005-2007, despite tightening labour markets and a considerable fall in unemployment. Due to sound domestic fundamentals, the euro area economy was in a relatively good position to weather the continued rise in oil and commodity prices, and the turmoil in the financial markets that began during the summer of 2007. However, looking forward, the effect of the changed international economic climate, notably concerning financial markets, is likely to take its toll. The impact is likely to be differentiated, as shown by a correction already underway in Member States which experienced a housing boom in the recent past.

9. In their response to the recommendation to pursue ambitious budgetary consolidation, the euro area Member States committed, in April 2007, to implement their 2007 budgets as planned, avoiding expenditure overruns, and using unexpected extra revenue for deficit and debt reduction. They also committed to carefully designing fiscal policy plans for 2008 so as to accelerate adjustment towards the medium-term objective for Member States which had not reached it and for those which have reached it to avoid feeding macro-economic imbalances overall. Against this background, recent information suggests that budget balances would improve by 0.7 percentage points of GDP in the euro area in 2007. Structural balances in the euro area (i.e. government budgets adjusted for cyclical factors and one-off and temporary measures) are expected to improve by almost ½ a percentage point of GDP in 2007, a results of improved underlying balances in ten euro area Member States. Although a significant improvement of the headline government deficit is foreseen for some Member States (AT, EL, NL, PT), overall fiscal consolidation for the euro area is forecast to stall in 2008 and 2009. Most euro area Member States which have not yet achieved their medium term objective (AT, EL, FR, IT, PT, SI), are unlikely to reach it by 2009.

10. The recommendation to improve the quality of public finances refers to the role of public expenditures, revenues, and the institutional framework, in boosting potential growth and in helping adjustment to changing economic circumstances. A shift of public expenditure from consumption to productive investment (such as R&D, education, and skills) could contribute to this goal. These issues are of particular importance in the euro area because both the share of public expenditure to GDP, and levels of labour taxation are relatively high. In the context of a high share of expenditure on social protection in many euro area Member States, the observed differences in the effectiveness of social spending, suggests a considerable scope for efficiency gains. In their Implementation Reports, some Member States (e.g. DE, ES, FI) reported on measures aimed at improving the composition and size of public expenditure, including the flexibility to free up resources. Important revenue side measures announced by Member States (AT, DE, FI, SI) concern the reduction of, distortions arising from the tax system, and of compliance and administrative costs. The improvement of institutional elements has been on the agenda in some Member States (DE, ES, FR). There is a consensus that the methodology for analysing and measuring the quality of public finances needs to be developed further. To this end, more effort is required in the provision of detailed data on the composition of public spending and revenues.

11. In general, the euro area has succeeded in fostering stability and creating conditions more conducive to growth. The recommendations in the macro-economic area have been addressed to some extent. Achieving the goal of sustainable public finances relies on continuing budgetary consolidation where medium term objectives are not met yet. Moreover, the quality of public finances can be further improved, along with policy co-ordination, through an enhanced exchange of best practice.

Micro-economic policies

12. A well functioning internal market is important to ensure competition, productivity growth and lower prices. It also improves the capability of euro area economies to adjust to changes in the external environment, and increased competitive pressures from third Member States. It appears that the continued efforts to improve the

functioning of the internal market and the introduction of the euro have both boosted trade, foreign direct investment, and cross-border mergers within the euro area. Euro area Member States would benefit from further product and service market reform that remove obstacles to cross-border trade in services and knowledge diffusion, tackle the low expenditures of R&D, and the lack of business dynamism and competition in network industries. Further financial integration and stronger competition in the financial retail service would also be helpful in this respect.

13. The Council recommended euro area Member States to enact measures that lead to more competition, especially in services, and to step up the integration of financial markets and competition in retail financial services. A full and timely implementation of the Service Directive by December 2009 is essential for the well functioning of the internal market. Uneven progress in this area restricts the full economic potential of the services sector from being exploited. Costly, given that this sector accounts for 70% of euro area GDP. Progress at national level to implement further actions to enhance competition in services is visible in a limited number of euro area Member States. In network services only a limited number of significant measures have been carried out in the rail (NL), telecom (EL, SI, FI) and energy (NL) sectors. Measures have been taken (ES, IT) or are expected (FR) in the retail sector. Last year's Annual Progress Report assessed that competition in professional services was insufficient in nine euro area Member States. Despite measures taken in some of these Member States (BE, ES, FI, IT, NL), the situation has not significantly improved.

14. Progress on financial integration has been notable at the EU level. The European parliament has adopted the proposal for the Payment Services Directive, with the Commission proposing two further directives. Implementation of the Financial Services Action Plan at the Member State level is close to completion, but several Member States have yet to transpose both the Transparency Directive and the Markets in Financial Instruments Directive. Legislative measures have mainly focussed on the integration of wholesale markets, with the European retail banking markets remaining significantly more fragmented. While the existing financial surveillance mechanisms have been effective in addressing the financial turmoil in the summer of 2007, there is a need to further develop financial stability arrangements, including common principles for cross-border financial crisis management.

15. In general, the euro area Member States have partially succeeded in implementing measures to improve competition in services. Euro area Member States have also taken measures to accelerate financial integration. The Commission considers that these policy measures are going in the right direction, but fall short of leading to integrated and competitive service markets with a visibly higher degree of price flexibility and stronger productivity growth. The recommendation in the micro-economic area has been addressed at least in part, although the benefits from policy co-ordination have not yet been exploited.

Employment policies

16. There are indications that the employment growth recorded over the last years is resulting from structural reforms undertaken in the past, especially from reforms that targeted increasing labour supply and making work pay. However, the evidence of

wage rigidities and persistently high unemployment among some social groups suggest that labour market structures are not yet sufficiently flexible and adaptable, in particular since the mobility of labour across borders, regions and occupations is low in the euro area.

17. Euro area Member States have addressed the recommendation to improve flexibility and security in labour markets. As a result, wage bargaining systems in some Member States are gradually moving in the direction of more wage and working time flexibility and differentiation, while achieving aggregate price stability and competitiveness through enhanced bargaining coordination. For example, signs of more decentralised wage bargaining have emerged in some Member States (AT, ES, FI, IT), more differentiated agreements were observed in other Member States (PT, SI), and in IE an anti-inflation group has been established. Some Member States (e.g. AT, FI, IE, NL) have progressed towards an integrated flexicurity approach, with others taking steps towards this (FR, IT, SI). There has reform across the four flexicurity components. On contractual arrangements, progress is seen in AT and LU; there is an increasing adoption of lifelong learning strategies, but effective implementation remains limited, active labour market policies have been strengthened (e.g. AT, BE) and social security systems improved (e.g. BE, DE). Labour mobility has been the focus of EU initiatives (the Recommendation on "European Qualifications Framework" and the European Job Mobility Action Plan). However, with some exceptions (e.g. AT, BE, FI, IT), there has been limited progress on cross-border mobility.

18. In general, the euro area Member States have partially succeeded in implementing measures to review the wage setting mechanisms and to improve the financial incentives for labour market participation. In the Commission's opinion, these are useful steps in the right direction. It is necessary to spread the results achieved in some Member States and areas to others. The concept of flexicurity has not yet been used to design a comprehensive policy strategy. Overall, the euro area Member States have partly complied with the recommendation, but further areas need reform, and Member States that have not yet taken measures should do so. Stronger policy co-ordination, in particular through common learning from successful previous reforms, could stimulate much needed further reform.

PART III: CONCLUSIONS

19. In the light of the 2007 Implementation Reports of the euro area Member States, and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:

20. Based on their Implementation Reports, the euro area Member States have been making some progress in implementing policy measures that improve the functioning of the euro area.

21. Significant further reforms are necessary to fulfil the micro-economic and employment recommendations. The progress recorded in 2007 concerning the macro-economic area needs to be sustained.

22. Among the strengths shown by the 2007 Implementation Reports of the euro area Member States are: budgetary adjustment in 2007, the implementation of legislation to foster financial market integration, and wage bargaining systems more conducive to wage flexibility in some Member States.

23. The policy areas in the euro area where challenges now need to be tackled with the highest priority are: the sustainability of public finances and their contribution to growth; competition in product and service markets, especially in services, financial integration and competition in financial retail services, in order to facilitate adjustment and more flexible prices; adequate wage developments at the aggregate, sector, regional and occupational level; flexicurity in labour markets; and more labour mobility in order to foster labour market adjustment.

24. Against this background it is recommended that the euro area Member States together with their country specific recommendations:

- pursue budgetary consolidation towards their medium-term objectives in line with the Stability and Growth Pact, hence striving to achieve an annual structural adjustment of at least 0.5% of GDP as a benchmark;

- improve the quality of public finances by reviewing public expenditures and taxation, with the intention to enhance productivity and innovation, thereby contributing to economic growth and fiscal sustainability;

- effectively implement measures that improve competition, especially in services, and step up measures that promote the full integration of financial markets and the competition in retail financial services, whilst strengthening stability and supervisory arrangements;

- improve flexibility and security on labour markets inter alia by implementing "flexicurity" strategies, better aligning wage and productivity developments, and enacting measures to promote labour mobility across borders and between occupations.

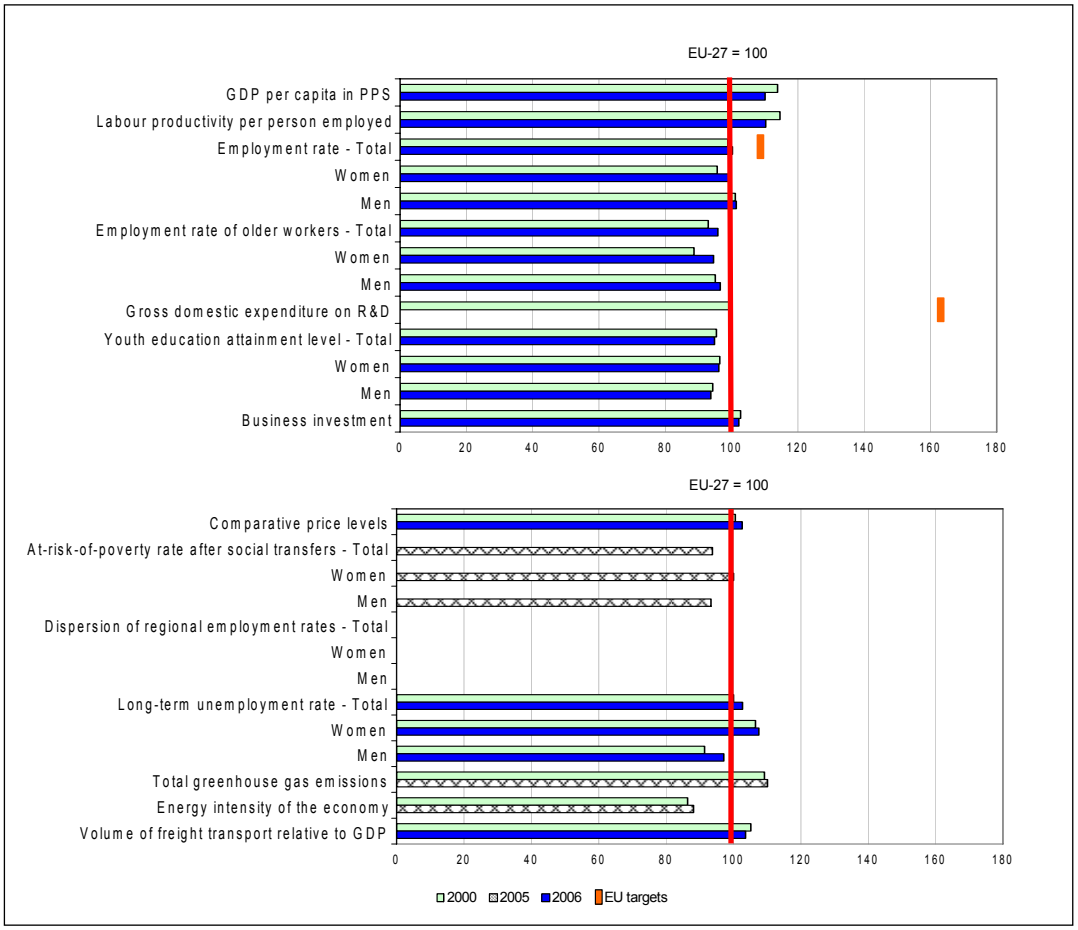
25. For the future it will also be important for euro area to further strengthen governance to maximise policy synergies, which are stronger in a monetary union, and enhance political ownership of reforms. The Eurogroup's April 2007 Berlin orientations on public finances are a welcome step in this regard and a similar approach should be extended to other fields. A strengthening of the euro's representation in international financial institutions and fora would be in line with its potential as a pole of stability and growth in the global economy.

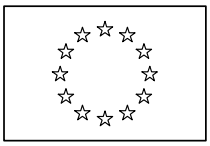
PART IV: STATISTICAL GRAPHS AND DATA

EURO AREA

		EURO AREA						EU27			
		2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS		113.9	111.9	110.9	110.9	110.1		100.0	100.0	100.0	
Labour productivity per person employed		114.6	111.5	110.6	110.8	110.3		100.0	100.0	100.0	
Employment rate	Total	61.5	62.6	63.0	63.7p	64.6p	:	62.2	63.4p	64.4p	70.0
	Women	51.4	53.6	54.5	55.6p	56.7p		53.7	56.2p	57.2p	
	Men	71.6	71.5	71.5	71.8p	72.6p		70.8	70.8p	71.6p	
Employment rate of older workers	Total	34.3	37.8	38.6	40.4p	41.7p		36.9	42.3p	43.5p	
	Women	24.3	27.9	29.0	31.5p	32.9p		27.4	33.5p	34.8p	
	Men	44.8	48.1	48.5	49.7p	50.8p		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D		1.85e	:	:	:	:	:	1.86e	1.84e	1.84e	3.0
Youth education attainment level	Total	73.1	73.1	73.5	73.6	73.8		76.6	77.4	77.8	
	Women	76.5	76.3	77.2	77.2	77.6		79.3	80.1	80.7	
	Men	69.6	69.8	69.9	70.1	70.1		73.8	74.7	74.8	
Comparative price levels		100.5	103.5	103.7	102.7	102.6		100.0	100.0	100.0	
Business investment		18.9	17.6	17.8	18.1	18.6		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers	Total	:	:	:	15.0e	:		:	16.0e	:	
	Women	:	:	:	17.0e	:		:	17.0e	:	
	Men	:	:	:	14.0e	:		:	15.0e	:	
Dispersion of regional employment rates	Total	:	:	:	:	:		13.0	11.9	11.4	
	Women	:	:	:	:	:		20.0	16.8	16.2	
	Men	:	:	:	:	:		9.6	9.7	9.3	
Long-term unemployment rate	Total	4.0	3.9	4.1	4.0p	3.8p		4.0	4.1p	3.7p	
	Women	4.9	4.5	4.7	4.5p	4.3p		4.6	4.5p	4.0p	
	Men	3.2	3.4	3.6	3.5p	3.4p		3.5	3.8p	3.5p	
Total greenhouse gas emissions		99.0	101.7	102.1	101.4	:		90.7	92.1	:	
Energy intensity of the economy		184.2	186.7	185.7	183.4	:		213.1	208.1	:	
Volume of freight transport relative to GDP		104.2e	102.8e	109.3be	109.7e	110.5e		99.1e	105.4e	106.7e	

PERFORMANCE COMPARED TO EU-27





COMMISSION OF THE EUROPEAN COMMUNITIES

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PART III

COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN COUNCIL

Strategic report on the renewed Lisbon strategy for growth and jobs: launching the new cycle (2008-2010)

Companion document

TABLE OF CONTENTS

I. Macro-economic part 5

Summary and conclusions 5

1. Economic performance during the 1st Lisbon cycle (2005-07) and prospects for the 2nd cycle (2008-10) 7

2. Assessing progress with reforms that contribute to macroeconomic stability 14

II. Micro-economic part 27

Summary and conclusions 27

1. Economic effects of microeconomic reforms 29

2. Three years in the new reform agenda: an assessment of progress by policy area 30

3. Implementing priorities for action 48

III. The Commission Draft of the Joint Employment Report 2007/8 51

Summary and conclusions 51

1. Progress in achieving the objectives of the European Employment Strategy 52

2. Implementing priorities for action 55

IV. THE GENERAL APPROACH USED BY THE EUROPEAN COMMISSION TO ASSESS PROGRESS WITH STRUCTURAL REFORMS 63

V. THE EUROPEAN GROWTH INITIATIVE 65

1. The improved framework for investment – Preliminary results 66

2. The Growth Initiative within the Lisbon Strategy for Growth and Jobs 68

INTRODUCTION

In March 2005, the Lisbon strategy was re-launched placing growth and jobs at the top of European political priorities. This focus stemmed from the recognition that economic growth in Europe had been disappointing relative to the most dynamic economies in the world, and that the Union faced major challenges in coping with globalisation and ageing populations. Euro area countries faced the additional challenge of improving the capacity of their economies to adjust to economic shocks in the absence of national monetary or exchange rate policies.

The re-launched Lisbon strategy provides a comprehensive framework for reform efforts to raise growth and jobs potential, encompassing measures which promote macroeconomic stability, increase labour utilisation and enhance labour productivity: The Lisbon strategy places considerable emphasis innovation and promoting a knowledge-based economy, through policies which enhance market entry and flexibility, plus higher investment in education, training and R&D.

The end of the revised strategy's first-three year cycle is an appropriate moment to draw some conclusions about how well it is succeeding. Europe's economic situation has improved considerably since the Lisbon Strategy was re-launched in 2005, although recent months have witnessed growing downside risks. Average annual real GDP growth since 2005 has been 2.6%. Growth has been increasingly driven by domestic demand, leaving Europe better placed to cope with adverse external shocks. Budget deficits have been reduced from 2.5% of GDP in 2005 to a forecasted 1.1% in 2007, whilst public debt has declined from 62.7% in 2005 to just below 60% in 2007. Almost 6.5 million extra jobs have been created in EU27 in the last two years, with 5 million more projected to be created by 2009. Unemployment is expected to fall below 7%, the lowest level since the mid-80s. For the first time in a decade, robust employment increases have gone hand in hand with robust productivity growth. In some Member States, improving growth conditions have been accompanied by a gradual build-up of imbalances with signs of overheating, as witnessed by large current account deficits, a loss of competitiveness, increasing household indebtedness and rapidly increasing house prices.

The business environment has benefited from a series of structural reforms. The EU's better regulation agenda is gradually being put into place, although many Member States still need to implement the necessary instruments, including impact assessments and methods to measure and reduce administrative burdens. It is now much easier and cheaper to start a business in almost all Member States. Europe, as a whole, however does not yet have a dynamic, entrepreneurial culture. Too often, efforts to improve the business environment are made in a piecemeal way as opposed to being part of an integrated approach geared towards the growth of SMEs. Whilst Member States have set targets committing themselves to significantly increasing R&D investments which would help the EU approach its 3% of GDP target by 2010, the evidence does not yet reflect this ambition. The EU has made the first steps towards transforming itself into a low carbon society. There is progress in meeting the overall EU Kyoto target and at the Spring 2007 European Council the EU committed itself to ambitious targets for greenhouse gas reduction and increasing the share of renewable energies by 2020.

In some countries, unfortunately, reform seems to be slowing down. However, it is imperative that reforms continue. Most Member States still lag behind leading economies, for example in labour utilisation and labour productivity, and the challenges of globalisation and population

ageing will continue into the next decades. Moreover, structural reforms will not only help enhance growth and jobs potential over the medium-run, they also play an essential role helping economies adjust and cope with the shocks and pressures that sparked the recent financial turmoil and heightened economic uncertainty.

A crucial question on the threshold of a new three-year Lisbon cycle is what part structural reforms played in the improved economic performance. Commission analysis has found evidence of structural improvement in the functioning of labour markets. In particular, sustained increases in the employment rates of women and older workers seem partially due to previously enacted policy reforms. The trend decline in productivity growth that entrenched itself in the early 1990s seems to have halted in recent years; since mid-2005, labour productivity growth has accelerated.

This Companion Document accompanies the Strategic report on the renewed Lisbon strategy for growth and jobs: launching the new three-year-cycle. It aims at providing further detail on the underlying rationale for carrying out coordinated policy reforms. It also takes stock of the main developments in policy reform since the re-launch of the Lisbon strategy in 2005.

The paper is divided in five sections. The first, second, and third sections take stock of the main progress, in terms of policy reforms, in the macroeconomic, microeconomic and employment pillars of the Lisbon strategy. The fourth section outlines the Commission's methodology in assessing structural reforms and the Implementation Reports. The fifth provides a mid-term evaluation of the European Growth Initiative.

I. MACRO-ECONOMIC PART

Summary and conclusions

Overall, over the period 2005-2007, there has been some progress with macro economic reforms, although the pace has slowed in the last 12 months.

Consolidation of public finances has advanced, though it remains a challenge in several Member States. The nominal EU27 budget deficit was 2.5 % of GDP in 2005 and it is forecast to drop to 1.1 % in 2007. This mainly reflects reduced government expenditures (as a share of GDP), although revenues (as a share of GDP) have increased. At the start of 2006, twelve countries were in excessive deficit, but only six by end-2007. However, fiscal adjustment seems to have slowed somewhat in the last year; the opportunity to use relatively strong growth conditions to reduce structural deficits by the 0.5% of GDP benchmark in the Stability and Growth Pact (applicable to euro area and ERM II countries) has not been fully taken in all Member States. Indeed, most countries still have some way to go to achieve medium-term budgetary positions that would allow the budget to fully play its stabilising role.

Stability-oriented policies have made some positive contributions. Headline inflation in the EU27 has hovered just above 2% over the last 3 years and is expected to remain at this level. However, in some Member States, improving economic growth has been coupled with a gradual build-up of imbalances with large current account deficits and signs of overheating: poor competitiveness developments, increasing household indebtedness and rising house prices. There is therefore a strong case for macro-economic policies to restrain demand in several Member States as well as further reforms to improve adjustment capacity to shocks and the functioning of the supply side of the economy.

The significant challenge in most countries of keeping intact the long-term sustainability of public finances and the urgency takeoff taking additional measures has increased. At the same time, better budgetary positions and several important pension and health care reforms in some countries have improved the situation in the last few years. The EU27 debt/GDP ratio has declined, from 63 % of GDP in 2005 to just below 60 % in 2007. Pressing ahead with ambitious reform plans and avoiding damaging policy reversals is important**.**

A primary EU policy objective is to bring more of the working age population into work. Policies need to support wages developing in line with productivity so as to achieve high employment and contain inflation. In the aggregate, wage moderation has continued to support price stability over the period 2005-2007, including the last 12 months, despite a tightening labour market and the closing of output gaps. However, the situation varies across countries. Within countries, across sectors and regions only partial progress has been made to make wage dispersion reflect productivity differentials.

It is important to continue with policies that improve incentives to become employed. Several Member States have indeed taken measures to improve incentives to work, from reforms in the benefit system (both levels of benefits and availability criteria) to labour taxation. However, less has been done to relax employment protection legislation. While many countries have taken measures that go in the right direction, the overall impact is relatively limited in many cases and thus there is a need to further pursue such strategies along the

principles of flexicurity. A challenge is how to lower labour taxes without endangering fiscal consolidation.

This part of the annex focuses on the Integrated Guidelines package that addresses policies to ensure a stable and sustainable macroeconomic environment. A first section takes a closer look at economic developments during the three years of the 1st Lisbon cycle (2005 to 2008). It examines whether the economic upturn is cyclical (transitory) or structural (potentially due to the positive impact of past structural reforms) in nature. It also considers the reform agenda facing the EU for the next three year cycle (2008-2010) in the face of challenges resulting from globalisation and ageing populations, as well as the urgent need to address climate change. A second part of the annex reviews progress with structural reforms in several key macroeconomic domains, with a particular emphasis placed on reform efforts over the past year.

1. ECONOMIC PERFORMANCE DURING THE 1ST LISBON CYCLE (2005-07) AND PROSPECTS FOR THE 2ND CYCLE (2008-10)

Economic performance has improved since 2005

Economic performances have improved considerably since the re-launch of the Lisbon Strategy in 2005. Economic growth was 3.0% in the EU27 in 2006 compared with 1.8% in 2005, and is forecast to remain at 2.9% and 2.4% in 2007 and 2008. Thirteen million jobs have been created since 2000, and more than half of that after 2005, and unemployment has fallen steeply from 8.6% to 6.9% over the 2005-2007 period. An especially welcome development is that for the first time since 1997, job creation and productivity improvements have occurred simultaneously[1]. As a result of the improved growth performance, the Commission estimates the output gap is merely -0.1 p.p. % in 2007 compared with 1 p.p. negative gap in 2005. Moreover, the gap in GDP per capita with the US has closed slightly, from 65.4% of the US-level for EU-27 and 72.1% in the euro area in 2005 to 67.1% and 73.5% respectively in 2007. Although it is difficult to disentangle the impact of cyclical and structural factors on growth, it is an encouraging sign that the Commission's calculations suggest that potential GDP growth, i.e. net of cyclical factors, has improved from 2.3% in 2005 to 2.5% in 2007 for the EU-27, and from 2.0 to 2.2% for the euro area. The three Baltic states, Slovakia, Slovenia and the Czech Republic have experienced an especially rapid convergence. The recovery has also spread to EU15 countries, most remarkably to Germany, which seems to have overcome its role as growth laggard in the EU.

In addition to higher growth rates, the composition of growth has become more favourable to domestic drivers over time, which bodes well for increased resilience to adverse external factors. As shown in Table 1, the contribution to growth of fixed capital investment had been particularly weak in the first half of the decade. Since 2005, it has strengthened, returning to growth rates comparable to the ones observed in the late 1990s which raise hopes that firms' higher investment, through the diffusion of technological progress, translates into higher productivity growth. Though private consumption contributed less to growth in 2005-2007 than in the late 1990s, an upward shift in the contribution of private consumption spending is now clearly evident from the data on consumer expenditures as well as from the recovery in consumer confidence underpinned by the declining rates of unemployment. Moreover, as can be seen from a more detailed breakdown of the growth performance (Graph 1) productivity gains accounted for more than half of the average economic growth recorded in EU27 2005-2007, with labour inputs accounting for the remaining part. Labour inputs benefited from net migration, and to a lower extent an increasing native population, while the rise in participation rates, especially of women and older workers, was partly offset by the decline in average hours worked per person employed and the decline in youth participation. As regards

[1] A recent Commission publication entitled Moving Europe's productivity frontier reviews different explanations of the trade-off between productivity and employment growth and provides an empirical assessment of the size of this trade-off and of how it has been changing over time, see the EU Economy 2007 Review: http://ec.europa.eu/economy_finance/publications/european_economy/2007/the_eu_economy_review2007_en.htm

labour productivity, technical progress appears to have been a stronger driving force than capital accumulation and rise of labour initial education. Compared to the 2000-2004 period a key difference is the positive contribution to growth from the reduction in unemployment rates, which should be partly attributed to the cyclical recovery.

Due to sound economic fundaments, most Member States are in a good position to withstand the strains from the financial turbulence witnessed in summer 2007. According to the autumn 2007 forecast of the European Commission[2], growth in the EU-27 is predicted to be 2.9% in 2007 and 2.4% in 2008. For a few Member States (LV, LT, EE), however, accumulated macroeconomic imbalances such as high inflation, large current account deficits and excess housing price increases bear important risks in the current juncture. Also in BG and RO, external deficits are large and inflation high. In other countries such as EL, ES and PT deteriorating economic growth is likely to jeopardise the sustainability of competitiveness, foreign debt or households' indebtedness. Such countries need to closely survey financial stability and, in case of a further widening of the external deficit, vigorous structural reforms to restore cost competitiveness.

Table 1. Economic developments 2000-2009, key figures, EU27

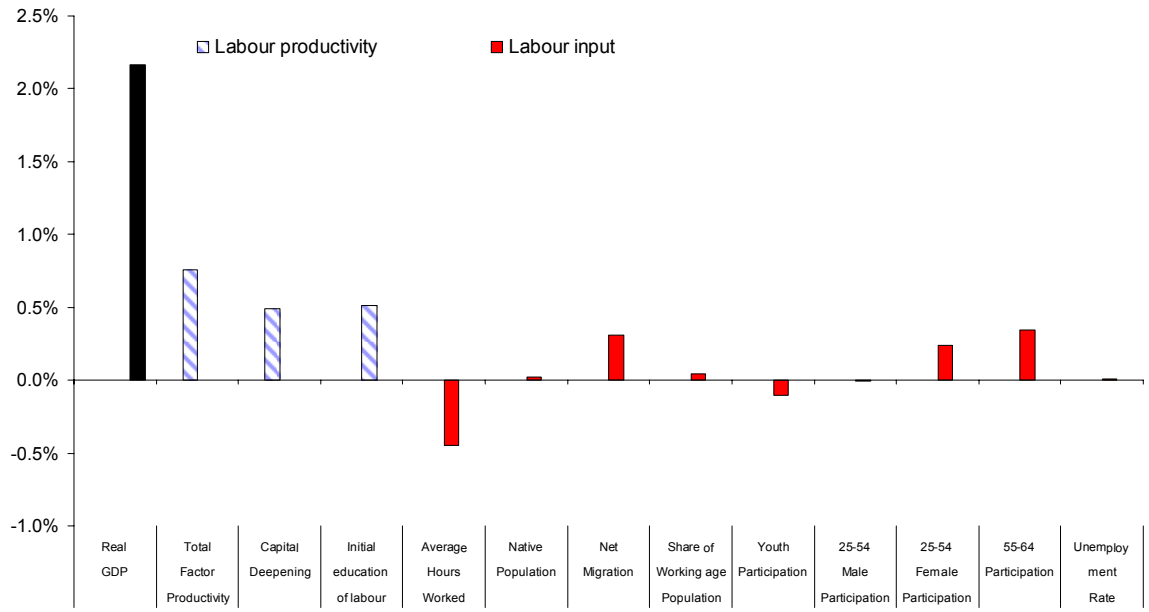
	2000-04	2005-2007	2007	2008-09
GDP growth	2.2	2.6	2.9	2.4
Consumption growth	2.2	2.0	2.2	2.2
Investment growth	1.6	4.8	5.6	3.4
Employment growth	0.9	1.4	1.6	1.0
Unemployment rate (% labour force)	8.8	8.1	7.1	6.7
Inflation rate	2.7	2.3	2.3	2.3
Government balance (% of GDP)	-1.8	-1.7	-1.1	-1.1
Government debt (% of GDP)	61.5	61.4	59.7	57.8
Current Account (% of GDP)	0.0	-0.6	-0.8	-0.9

Source: Commission Autumn Forecast

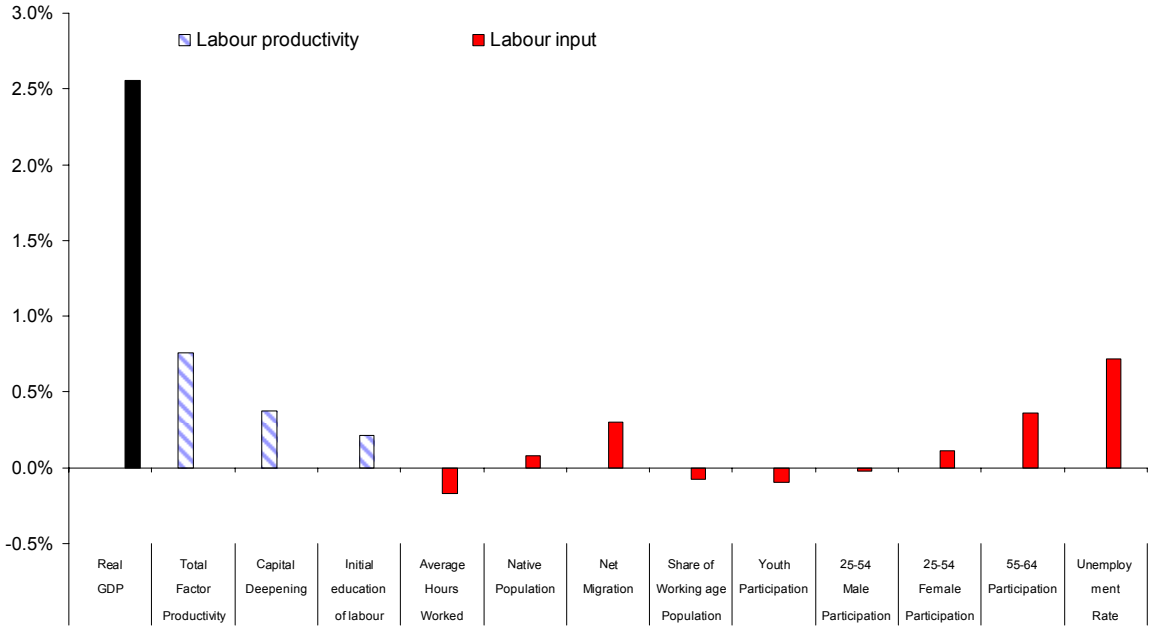
[2] See the 2007 Autumn Economic Forecast of the European Commission, http://ec.europa.eu/economy_finance/publications/european_economy/forecasts_en.htm

Graph 1. Real GDP growth and its components in EU27, 2000-2004 and 2005-2007

EU-27 , 2000-2004



EU-27 , 2005-2007

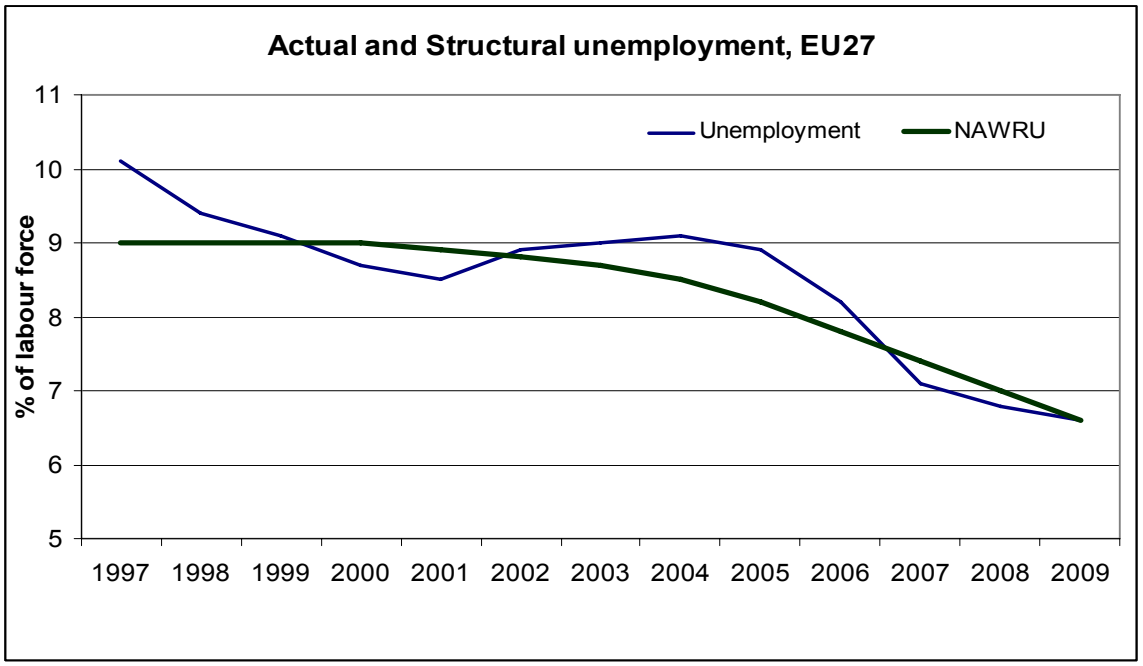


Are past reforms starting to pay dividends?

One of most important questions as the EU enters a new three-year Lisbon cycle is whether the improved economic performance is in part due to the effects of structural

reforms. Establishing a causal link between the progresses made in the Lisbon agenda and economic performance is not straightforward. This is because the observed changes in economic variables can be due to several factors, some of which are beyond the direct or immediate influence of government policies, e.g. the economic cycle, globalisation, technological developments and demographic changes. Also, analysis suggests that reforms need a considerable time before their benefits become visible in growth numbers, and thus relevant reforms may pre-date the revision of the Lisbon strategy. Moreover, it is difficult to establish the extent the new Lisbon governance structures have contributed to overcome reform resistance in individual Member States, as many reforms have a clear domestic rationale and governments may have undertaken them independently of co-ordination efforts at EU level.

Graph 2: Employment and labour productivity growth, actual and structural, 1997-2009



Notwithstanding the caveats mentioned above, analysis by the Commission suggests that, there is a structural component linked to past structural reforms enacted by EU Member States and in a number of policy areas there are a visible EU level dimension which is expressed through common targets and actions.

There is evidence of structural improvement in the functioning of labour markets[3]. As regards labour utilisation, employment grew by more than 1% each year since 2005, leading to almost 6.5 million new jobs in the EU by 2007. Although sustained efforts will be required to bring the employment rate of 70% by 2010 closer, female employment rates have increased from 54% in 2000 to 56% in 2005 to about 58%[4] in 2007, and the Lisbon employment target of 60% is within reach. There has also been a substantive increase in the employment rates of older workers (aged 55 to 64) from 37% in 2000 to 42% in 2005 and 44%[4] in 2007. Moreover, the effective retirement age has increase by 1 year between 2001 and 2005, which is welcome reversal of long standing historical trends. Analysis suggests that part of this is due to lagged effects of pension reforms: preliminary econometric estimates[5] suggest that the participation rates of older workers (55-64) increased by about 1.5 percentage point after 5 years that a pension reform has been enacted.

Employment has not increased on average in the group of low-skilled workers, with the employment rate being around 55% over the 2000-2006 period. Given the fact that this labour market segment performs rather badly in comparison to other skill groups (employment rates of medium- and highly-skilled workers stand at around 73% and 84% respectively) many Member States have nevertheless focused their policies in this direction. In particular, there has been a general trend towards reducing the tax burden for low skilled workers. As a result, there has been a drop in the total tax wedge (including social security contributions by employees and employers) for the low-skilled workers of almost 4 percent over the period 2000 to 2006[6].

Further evidence of ongoing structural improvements in the functioning of labour markets emerges from an analysis of unemployment rates. The rate of unemployment declined from 8.7% in 2005 to 6.9 % in 2007. This is in stark contrast to previous economic cycles when unemployment rates increased sharply and took a long time to decline: it not only contributes to economic growth, but is equally important for equity and welfare considerations as having a job is the single most important factor in avoiding poverty and social exclusion. When only cyclical forces are at work, the reduction in unemployment typically leaves a clear trace in higher wage growth. In the current upturn, wage growth has hardly accelerated, implying also reduction in the structural rate of unemployment. Structural unemployment, captured as the non-accelerating wage rate of unemployment, NAWRU, is estimated to have been reduced from 8.2% in 2005 to 7.4% in 2007. Similar calculations suggest that the reforms between 2001 and 2006 that aimed at increasing the employability of marginally attached people increased employment rates by 0.8 percentage points one year after the reforms were enacted.

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3 For an encompassing description on EU labour market and wage developments See report "Labour market and wage development in 2006", European Economy no.4, 2007, http://ec.europa.eu/economy_finance/publications/european_economy/labour_mkt_wage2007_en.htm

4 2007 estimate based on the average of data for the first two quarters.

5 Arpaia, A.F. Pierini and P. Braila "Tracking labour market reforms in the European union using the LABREF database" paper presented at the IZA-Fondazione Rodolfo Debenedetti Workshop "Measurement of Labour Market Institutions".

6 Based on EuroStat data on single earner without children (EU27 minus CY, EE, MT, LV, SI, BG, RO) and OECD Working paper (2004-5) on 2004 distribution on family types and earning levels for selected countries.

Positively, since mid-2005 productivity growth in the EU has picked up. Labour productivity growth is estimated at 1.4% in EU-27 in 2007, slightly lower than the 1.5% in 2006 but better than the 1.0% recorded in 2005. An additional positive feature of this is that in 2006, rising employment took place in an environment of accelerating productivity growth: this was the first time since 1997 that both employment and labour productivity accelerated in tandem. Indeed, a central policy goal of the Lisbon strategy is higher structural labour productivity growth given the need to close the gap in the productivity performance vis-à-vis the USA that emerged since mid 1990s. For now, however, it is early to assess whether the welcome acceleration in productivity growth is not only due to cyclical factors, but also linked to structural improvements. .

Aggregated data suggest that the trend decline in productivity growth, which has become entrenched since the early 1990s, has come to a halt in the last years. While statistical tests broadly confirm the bottoming out of the decline in trend productivity growth at the start of this decade, evidence of a turning point beyond that date indicating a recent pick-up in trend productivity growth remain weak.

The challenges for the 2nd Lisbon cycle, 2008-10

The Lisbon strategy is now entering a new three year cycle to cover the period 2008 to 2010. Notwithstanding the progress made since 2005, the diagnosis of the underlying structural challenges facing the Union as regards growth and jobs remains valid. As illustrated in Graph 4, large income per-capita gaps remain across countries. In 2007, based on the Commission Autumn forecast figures, the average per capita GDP of the EU27 was 10% below that of EU15 (and 33% below that of the US). For EU15 and euro area countries, the gap is mainly due to lower labour utilisation (i.e. the numbers of hours worked in the economy), whereas lower labour productivity (measured in terms of output per hour) is the main explanatory factor for Member States which joined in 2004 and 2007. The final column in Graph 3 indicates that over the 2005-2007 period, EU10 countries in particular have further narrowed the income gap benefiting from the process of real convergence. However, progress has been mixed, with some larger euro area countries doing less well.

These challenges may indeed become even more pertinent in the coming years as short- and long-term pressures become more explicit. In the short term, based on the Commission autumn forecast, the outlook for 2008-2009 indicates (see Table 1) a slow-down in growth albeit moderate, towards potential rates at around 2.5% per year. The projected slowdown mainly finds its roots in a slower forecasted pace of investment growth, while employment growth is also forecasted to decelerate (even though unemployment rates will continue to decline somewhat). In the longer term, pressures both from demographics and increased international competition are set to strengthen:

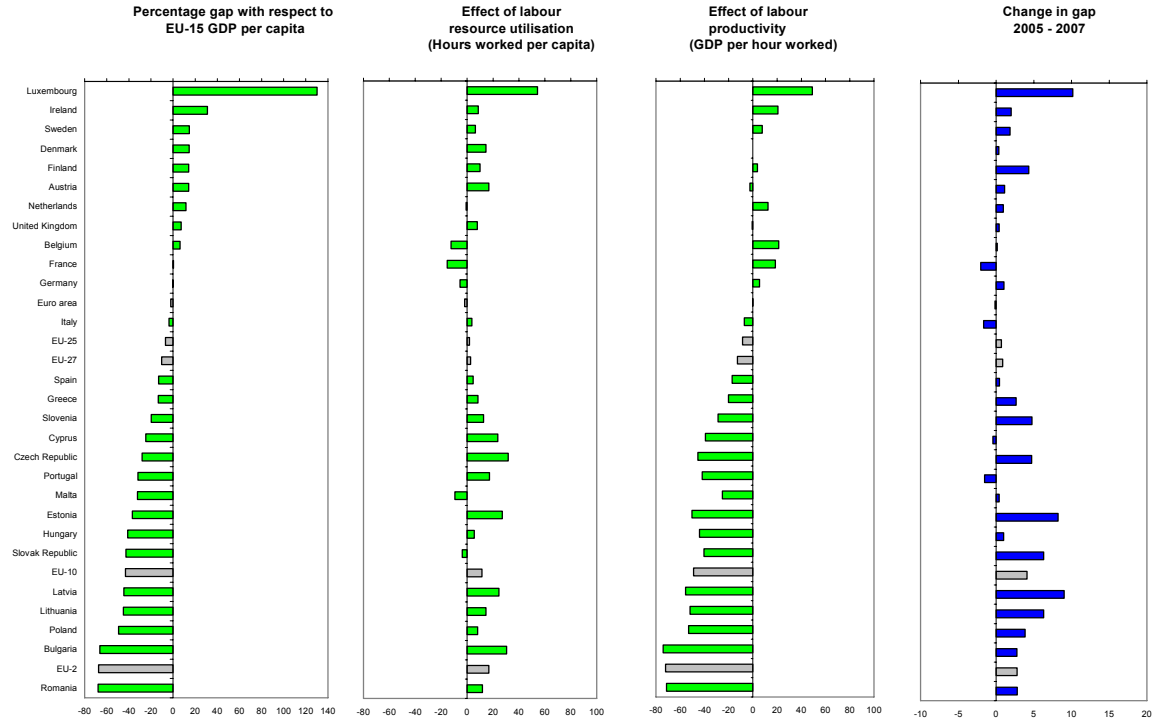
- projections indicate that in the coming decades potential GDP growth rates is set to gradually decline and to reach, by 2050, levels of about half of today's[7]. This

[7] See "Long-term labour productivity and GDP projections for the EU25 Member States: a production function framework", European Economy, Economic Papers, No 253, June 2006, http://ec.europa.eu/economy_finance/publications/economic_papers/2006/economicpapers253_en.htm

downward trend results from the future negative contributions to growth from the working age population due to demographic factors, leaving labour productivity as the key growth driver. The implication is that reform efforts contributing to an increase in labour productivity rates will become increasingly important over time;

- the trend towards increased competition through globalisation is set to continue. While deeper international trade links is expected to be beneficial for growth and employment in the aggregate, it will nevertheless risk in the short term to increase pressures on certain groups of the labour force and thus require a high degree of adaptability for a successful response[8].

Graph 3: Overview of the income gap in the EU25 Member States



***Note**: the gap is measures relative to the average of EU15 Member States*

2. ASSESSING PROGRESS WITH REFORMS THAT CONTRIBUTE TO MACROECONOMIC STABILITY

2.1. Securing economic stability for sustainable growth

Macroeconomic stability is a key framework condition for sustainable growth as expressed in Integrated Guideline N°1. Macroeconomic stability is secured by a

8 For an extensive analysis of globalisations by the Commission, see 'Rising international economic integration: opportunities and challenges', in the EU Economy: 2005 Review", http://ec.europa.eu/economy_finance/publications/european_economy/the_eu_economy_review2005_en.htm

sound mix of stability-oriented macro-economic measures and well designed structural reforms in product and factor markets. Monetary policy contributes by pursuing price stability. Sound budgetary positions allow the full and symmetric play of the budgetary stabilisers over the cycle. Fiscal restraint, effective financial supervision and the promotion of competitiveness help to contain external and internal imbalances. Moreover, budgetary and wage restraint limit the risk of domestic demand causing persistently higher inflation, potentially causing swings in real exchange rates and a protracted loss of competitiveness. Against this background, to assess how countries fare, and have made progress, in terms of macro-economic stability and budgetary policies, it is useful to look at budgetary positions, the fiscal stance and the extent to which medium-term budgetary positions provide enough safety margins to allow automatic stabilisers to play freely. Similarly, when looking at possible emerging macroeconomic imbalances it is relevant to examine external balances of countries together with domestic inflationary pressures, wage and labour market developments as well as asset price developments.

Over the 2005-2007 period, the consolidation of public finances has moved forward, even if further consolidation remains a challenge in several countries. The EU27 nominal budget deficit has been reduced from 2.5 % of GDP in 2005 to 1.1 % in 2007. According to the Commission forecast, on a "no policy change assumption", it is expected to remain at this level over the coming two years. The same trend is also reflected in structural budget positions which for 2007 are estimated to be -1.1% of GDP in EU27 and -0.7% of GDP in the euro area. This improvement is mainly driven by a reduction in government expenditures to GDP, although revenues as a share of GDP have also increased. At the start of 2006 twelve countries found themselves in a position of excessive deficit while at the end of 2007 only six countries are still there (CZ, HU, IT, PL, PT, SK). However, the pace of fiscal adjustment seems to have been reduced somewhat in the last year, and the opportunity to use the relatively strong growth conditions to reduce structural deficits by the 0.5% of GDP benchmark in the Stability and Growth Pact have not been fully taken in all Member States (applicable to euro area and ERM II countries). Moreover, a majority of countries still have some way to go to achieve medium-term budgetary positions that allows the budget to play fully its stabilising role[9].

Headline inflation in EU-27 has hovered just above 2% over the 2005-2007 period. In 2007, favourable energy-price base effects have contributed to reduce inflation. However, core inflation has continued to drift upwards and reached in 2007 levels close to 2%. This confirms on the one hand that a more mature cyclical position of the economy has been reached but on the other hand it also reflects some administrative measures (such as the VAT increase in DE) and strong increases in commodity prices. Service inflation continues to run at a relatively high rate. In the euro area, inflation in 2007 stood at 2%, somewhat lower than in 2006. The inflation differential between the three countries with highest inflation (IE, EL, SI) in the euro area and the three with lowest inflation (F, MT, FI) was 1.7%-points, similar to 2006.

[9] See the report "Public Finances in EMU-2007", European Economy No 3, 2007.

In 2007, five countries are projected to record an external deficit of at least 10% of GDP (LV, LT, EE, BG, RO). These countries display signs of overheating, characterised by excess aggregate demand evidenced by labour shortages, rapid increases in household borrowing, inflationary pressures and very high external imbalances. Among other Member States, EL, ES and PT have in 2007 external deficits between 8 and 10% of GDP; their external deficits owe mainly to structurally poor competitiveness, although robust growth in Greece and Spain is also a factor. In two other countries, HU and SK, the current account deficit was of a similar magnitude in recent years but has been on a declining trend, with the deficit expected to reach between 3 and 4% of GDP in 2007. It should be noted that in a catching-up country, even a widening external deficit need not be a cause for concern if there is a concomitant rise in productive potential in tradable goods and services and thus in the future export earnings generating capacity sufficient to service the external debt. However, to the extent that the widening external deficit reflects unrealistically optimistic expectations regarding future growth reflected in an excessively rapid increase in expenditure relative to income, an attitude of caution is warranted.

2.2. Safe-guarding economic and fiscal sustainability

Europe's ageing population poses a serious challenge to the long-term financial sustainability in EU countries, which is recognised in Integrated Guideline N°2. In the absence of appropriate reforms, this could lead to increasing debt burdens, lower potential output per capita due to the reduction in the working age population, and pressure for significant increases in public spending on pensions and health care. The economic, budgetary and social implications of ageing populations can be addressed by pursuing a three-pronged strategy, that encompasses an appropriate mix of policies to reduce debt at a fast pace, to raise employment rates especially amongst older workers (so that working lives are extended), and to reform pension and health care systems. Reforms to social protection need to be well designed so as to ensure that they are financially viable in the face of the population ageing and uncertain economic developments, while ensuring that social protection systems fulfil their goals in terms of access and adequacy.

In this context, when assessing how Member State's fare and have made progress in this regard it is relevant to look at debt and deficit developments and to what extent there has been consolidation efforts bringing medium-term budgetary positions in line with the medium-term budgetary objectives (MTO) within the Stability and Growth Pact. This should also take into account the projections of age related expenditures, carried out or planned reforms to pension and health care systems and how these are integrated in an overall assessment of budgetary sustainability.

In the EU over the 2005-2007 Lisbon cycle, some progress has been made to ensure sustainable public finances, although progress has been mixed across countries. The debt/GDP ratio has declined in EU27 over the 2005-2007 period, from 63 % of GDP in 2005 to just below 60 % in 2007. In the euro area, the debt ratio has been reduced from 70.4 % of GDP to 66.7% over the same period. The debt ratio both in Greece and Italy remains above 100% of GDP and in Belgium debt is close to 85% of GDP. Taking into account also projections of age related expenditures, a number of countries remains at what can be called high risk (CZ, EL, CY, HU, PT, SI). A number of countries progressed with the implementation of pension reforms. Rather comprehensive measures to reform the pension system have been conducted in recent years in some countries, in particular MT and PT.

Recently, additional measures, albeit at a lower scale, was introduced in some countries including progressing with on-going reforms (BE, DE, PL, UK). In other countries, where reforms are most needed, progress have been limited (EL, IT, CY, HU, SI). Health care measures were on the policy agenda in a number of countries (DE, CY, MT, LV, RO). In particular, in 2005 and 2006 progress has been shown in terms of increasing the participation rates for older workers which had increased by more than 3% over 2005-2006 in several countries (DE, EE, IE, CY, LV, AT, SI, SK, FI).

Overall, budgetary positions have improved since 2005, and there have been reforms to pension and health care systems in some countries. Nonetheless, important risks to the sustainability of public finances remain in many countries, and there is a need to press ahead with reform efforts, not least the effects of ageing on the size of the

working-age population will become more pronounced in the next three-year Lisbon cycle.

2.3. Ensuring that wage developments contribute to stability and growth.

Appropriate wage developments contribute to macro-economic stability and growth, highlighted in Integrated Guideline N°4. Provided that real wage increases are in line with the underlying rate of productivity growth over the medium term, they contribute to stable macroeconomic conditions and an employment friendly policy mix[10]. Variation in productivity caused by cyclical factors, or one off changes in the headline rate, should not cause an unsustainable shift in wage growth. In addition, relative wage developments that reflect local or sectoral labour market conditions help adaptability and counteract regional disparities. In this area, when assessing how countries fare and have made progress, it is necessary to examine wages and productivity developments, i.e. what this implies in terms of nominal unit labour costs (NULC) and to assess whether the latter are in line with price stability and competitiveness. It is also useful to look at real unit labour costs (RULC) and how these relate to labour market developments. Moreover, to the extent that regional unemployment is a serious problem, wage developments and measures that improve the adaptability to local conditions is relevant. Overall, the absence of wage pressure in the euro area and EU27 during the economic rebound has been a positive feature over the last few years. Wage moderation in the euro area and EU27 as seen in nominal and real unit labour costs has generally continued to support price stability over the 2005-2007 period, including the last 12 months, despite a tightening labour market and the closing of output gaps. In 2007, the annual growth rate in compensation per employee is forecast at 3.0% in EU27 and 2.5% in the euro area while the increase in labour productivity is 1.4% and 1.1% respectively. This implies that nominal unit labour costs increase by 1.7% in EU27 and 1.4% in the euro area which is somewhat higher than in 2005-2006 but in the aggregate remains in line with price stability objectives. More evidence of wage restraint in the face of stronger international competition is that real unit labour cost decreased by roughly 1% in 2006 and 2007, both in the euro area and in the EU as a whole. However, this may also reflect other structural factors, such as a gradual reallocation of value added towards sectors with a lower share of labour.

However, this overall assessment of favourable aggregate behaviour conceals sizeable differences between countries, with fairly divergent growth rates in nominal unit labour costs contributing to differing patterns in competitiveness and widening current account imbalances among EU members. At Member State level, two aspects warrant further attention:

- The catch-up process has triggered very high nominal wage growth, in excess of relatively high labour productivity, which has lead to deteriorating price competitiveness. This is particularly notable in EE, LT, LV, RO and BG (see also see section 3 on macro-economic stability where this is put in the context of external imbalances). Also, real unit labour costs have increased markedly over the last few years in EE, LV, RO and in 2007 in BG. Nevertheless, this has been coupled with above average employment growth and falling unemployment.

[10] Provided that they are also consistent with a rate of profitability allowing for productivity, capacity and employment-enhancing investments.

However, in HU increasing unit labour costs have been coupled with weak labour market developments.

- Wages adjust slowly over time to changing cyclical conditions, especially in some countries of the euro area, which means a long-lasting impact of shocks on economic activity. Indeed, the experience with adjustment to shocks in the early years of the euro area calls for flexibility despite a general background of marked wage moderation[11]. While wage moderation has been supportive of price stability in the aggregate, the continuously high-rates of long-term unemployment and the persistence of regional differences in employment performance suggest that there may be some lack of wage differentiation in some Member States (BE, DE, IT). Progress in terms of wage dispersion that reflects productivity differentials across sectors and regions has only been partial even though in some countries wage bargaining outcomes that better reflect local conditions can be observed. Additional flexibility seems however to have been achieved as regards working time organisation and greater opt-outs from collective agreements (AT, FR, DE, IE, NL, ES).

[11] See the "EU Economic review: 2006" which investigates how adjustment has been proceeding in the euro area and how the efficiency of adjustment could be improved. European Economy No 6, 2006.

2.4. Policies to make work pay

Policies to improve the financial incentives to work are largely recognised as being a key element of that comprehensive set of measures (macro, micro and employment), which is most needed to raise labour utilisation, and therefore contribute to the general objectives of the Growth and Jobs strategy (see in particular Integrated Guideline N°5). Improving the adaptability and adjustment capacity of economies helps respond to changes in both cyclical economic conditions and longer term trends such as globalisation and technology. In this regard, policies to "make-work pay" are particularly pertinent as they aim to attract more people into the labour market and to make the underlying incentive structure in the tax and benefit systems supportive to employment. This implies modernising tax (direct taxation on labour income and social security contributions paid by employers and employees) and benefit systems (unemployment insurance, in-work benefits, disability and sickness schemes, means-tested benefits and other forms of social assistance), so that they reduce benefit dependency and provide effective incentives to take up jobs, and remain in work, by making work economically attractive and rewarding relative to staying on benefits. Moreover, providing the right incentives to increase employment and hours worked is particularly important to improve labour utilisation, also in the light of budgetary challenges stemming from ageing populations.

Against this background, when assessing how Member States fare and have made progress in this regard, it is useful to look at performance indicators such as labour participation, employment and unemployment rates. Moreover, it is also important to take policy outcomes into account, measured by different tax wedges and marginal effective tax rates that give an indication of the size of unemployment, inactivity and low-wage traps.

In those Member States where employment and participation rates are relatively low (BE, BG, EL, MT, IT, PL, RO), or in those where labour market participation is higher but where generous welfare systems require extensive financing (SE, DK, NL), it is particularly challenging to improve incentives to work and hours worked. In other countries, the incentives to work embedded in their tax and benefit systems appear to be significantly low, as also results from their labour market situation (BE, PL). However, it can be observed that in several Member States a fair wealth of measures has been taken to improve the incentives to work, both as regards reforms in the benefit system, and in particular labour taxation, while in general much less has been done in the field of employment protection legislation.

In the area of unemployment and welfare-related benefits, some countries passed major reforms over the years of this Lisbon cycle (CZ, SE in 2007; BG, FR, SI in 2006; HU, NL in 2005; DE in 2004). In other Member States, policy action has been taken to promote labour market transition from unemployment and inactivity to work through stricter work availability criteria, the use of sanctions for non-compliance with rules, the strengthening of control mechanisms and streamlining the financing for labour market subsidies and income support (GR, NL, PT, SI in 2007). Many reforms that do not appear to directly target the financial incentives to work, such as strengthening the enforcement of rules and tightening up eligibility and work-availability requirements, may in fact well improve the overall incentive structure of the benefit system. However, risks remain of low-wage, unemployment and

inactivity traps for the unskilled and low income earners in a consistent number of Member States.

As regards labour taxes, many Member States have lowered the level of taxation on labour in recent years, either through general tax reductions, mainly focused on cutting the tax-wedge on low income groups (AT, FR, HU, SI, CZ, IT, MT, LT, SE), or by a straight reduction of the tax burden on low incomes (DK, FI, GR,NL, SL), there including extensions of the tax-free range of income or tax credits for low-income earners (LV, SE, FR, GR, IRL, NL, SK). In 2007, measures to this end was taken in FI, SI, BG, IT, CY, GR, LT, LV, IR, MT, NL and the UK. Also, a general trend towards reducing social security contributions for both employers and employees was recorded over recent years, often aimed at boosting labour demand and creating incentives to hire specific target groups (see for instance BE, SE, MT in 2007). Some convergence therefore appears to have taken place, as countries with highest tax rates in 2001 are those that have reduced most over the last years. Nonetheless, tax wedges on low wages remain high in a number of Member States (see in particular BE, DE, FR, AT, SE, HU, PL).

To favour labour attractiveness especially for the lowest earners, i.e. to prevent people from being discouraged to accept work because it could adversely affect their income, a consistent number of Member States have also introduced over recent years various sorts of in-work benefits schemes (BE, FR, PL, AT, CZ, SK, DK, UK). Other countries have taken actions to reduce the use of benefit schemes – either unemployment or disability schemes – as an alternative route for early retirement (see HU in 2007 and UK in 2006). The sickness system was also largely reformed in CZ and SE in 2007 and in the NL in 2006.

Overall, many countries have taken measures that go in the right direction, but the overall impact remains limited in many cases and thus there is a need to further pursue "making work pay" strategies along the principles of flexicurity. A further challenge in this respect is how to lower labour taxes further without endangering fiscal consolidation.

Table 2. Overview of situation in EU Member States on securing economic stability

	Performance				Areas where CSR have been proposed				
	Budget balance 2007	Fiscal stance 2005-07	Infla-tion rate 2007	External balance, 2005-07	2005 NRP	March 2007 Council		Dec. 2007 Comm. Prop.	
					Key chall-enge	CSR	PTW	CSR	PTW
BE	-0.3	-0.2	1.7	3.1					
BG	3.0	1.1	6.7	-14.3	X			X	
CZ	-3.4	-1.9	3.0	-2.7	X				
DK	4.0	-1.3	1.7	2.4					
DE	0.1	2.4	2.2	5.3		X			X
EE	3.0	1.7	6.2	-11.2					X
IE	0.9	0.2	2.7	-4.0			X		X
EL	-2.9	2.4	2.8	-8.8	X	X		X	X
ES	1.8	0.6	2.6	-7.8			X		X
FR	-2.6	1.0	1.4	-2.0	X	X		X	
IT	-2.3	2.0	1.9	-1.5	X	X		X	
CY	-1.0	2.1	1.8	-5.9*					
LV	0.9	0.6	9.5	-17.8	X	X		X	
LT	-0.9	-0.4	5.7	-9.2	X		X		X
LU	1.2	0.6	2.4	10.9*	X				
HU	-6.4	2.9	7.6	-5.2	X	X		X	
MT	-1.8	0.8	0.7	-3.4					
NL	-0.4	-1.0	1.6	6.9					
AT	-0.8	-0.1	1.9	3.6			X		X
PL	-2.7	1.1	2.3	-2.0	X	X		X	
PT	-3.0	2.8	2.4	-8.3	X	X		X	
RO	-2.7	-1.7	4.5	-10.3	X			X	
SI	-0.7	-0.3	3.4	-2.6					
SK	-2.7	-1.9	1.6	-6.7					
FI	4.6	0.7	1.5	5.4					
SE	3.0	0.6	1.6	6.4					
UK	-2.8	0.5	2.4	2.8	X		X		X

Note: CAB: cyclically-adjusted budget balance; Fiscal stance: measured as the change in the structural budget balance over 2005-2007 (a positive figure implies tightness, a negative looseness); CSR: country-specific recommendation; PTW: point to watch

Table 3. Overview of situation in EU Member States on securing long-term sustainability.

	Policy Performance				Areas where CSRs have been proposed				
	Debt ratio	Sustainability gap	Sustainability risk classification	Empl. rate older worker	2005 NRP	March 2007 Council		Dec. 2007 Comm. Prop.	
	2007	2007	2007	2006	Key Challenge	CSR	PTW	CSR	PTW
BE	85	2.7	Medium	32	X		X		X
BG	19	n.a.	-	-	X				X
CZ	30	8.0	High	45	X	X		X	
DK	25	0.3	Low	61	X				
DE	65	3.3	Medium	48	X	X			X
EE	3	-3.2	Low	59					
IE	25	2.4	Medium	53			X		X
EL	94	1.3	High	42	X	X		X	
ES	36	2.8	Medium	44			X		X
FR	64	3.2	Medium	38	X	X		X	
IT	104	3.0	Medium	33	X	X		X	
CY	61	7.0	High	54	X	X		X	
LV	10.	1.2	Low	53					
LT	18	2.4	Low	50					
LU	7	9.3	Medium	33			X		X
HU	66	12.3	High	34	X	X		X	
MT	63	-0.1	Medium	30	X		X		X
NL	47	2.4	Low	48					
AT	60	-0.1	Low	36	X				
PL	47	-1.4	Low	28					
PT	64	8.3	High	50	X				
RO	13	n.a.	-	-					X
SI	26	7.0	High	33		X		X	
SK	31	4.1	Medium	33					
FI	36	-0.7	Low	55	X				
SE	41	-1.5	Low	70					
UK	45	4.2	Medium	57	X		X		

Note: the S2 indicator measures the budget adjustment necessary to ensure sustainability given government debt and projections of age related expenditures. The sustainability risk class takes the S2 indicator into account as well as additional information: ource: Public Finances in EMU 2007, European Economy N°. 3, 2007. CSR: country-specific recommendation; PTW: point to watch.

Table 4. Overview of situation in Member States on wage developments and bargaining systems

	Policy Performance			Areas where CSRs have been proposed				
	Nominal Unit Labour Cost 2007	Real Unit Labour Cost 2007	Diversity of regional unem-ployment	2005 NRP Key Chall-enge	March 2007 Council		Dec. 2007 Comm. Prop.	
					CSR	PTW	CSR	PTW
BE	1.1	-1.0	47	*	*		*	
BG	10.5	2.8	47				X	
CZ	2.2	0.1	47	*		*		*
DK	4.4	2.0	20					
DE	0.8	-1.0	45					
EE	12.7	3.7	34					
IE	3.6	1.5	17					
EL	2.6	-0.4	30					
ES	2.0	-1.0	33					
FR	2.1	0.2	36					
IT	1.3	-1.3	63	*	*		*	
CY	1.1	-1.4	n.a.					
LV	21.0	4.6	23				X	
LT	7.9	0.1	21					
LU	3.3	-0.3	n.a.					
HU	3.0	-2.8	30			*	*	
MT	1.1	-1.4	n.a.					
NL	1.8	0.4	26	X				
AT	0.8	-1.4	41					
PL	4.2	1.3	22	*				
PT	1.1	-1.7	30					
RO	10.2	2.3	42				X	
SI	2.3	-0.5	31					
SK	0.4	-2.1	42	*				
FI	0.8	-1.2	29	X		X		
SE	2.8	0.4	16					
UK	1.7	-1.4	34					

Note: Diversity of regional unemployment is measured by the coefficient of variation of 2005 regional unemployment (source Eurostat). as a benchmark, 44% equals the EU average plus one standard deviation. CSR: country-specific recommendation; PTW: point to watch.***** in "policy orientations" column refers to a policy orientation dealing with regional unemployment disparities rather than directly mentioning wages *per se*.

Table 5. Overview of situation in Member States regarding policies for "making work pay".

	Policy Performance					Areas where CSRs have been proposed				
	Partici-pation rate 2006	Unempl oyment trap 2005	Inact-ivity trap 2005	Tax wedge 2006		2005 NRP Key Chall-enge	March 2007 Council		Dec. 2007 Comm. Prop.	
							CSR	PTW	CSR	PTW
BE	66.5	85	65	49		X	X	X	X	X
BG	64.5	74	n.a.	31						
CZ	70.0	66	56	40		X	X			
DK	80.6	90	88	39		X		X		X
DE	75.0	75	67	47		X	X		X	
EE	72.4	65	48	40*						
IE	71.8	74	74	16		X		X		X
EL	67.0	62	16	35		X	X		X	
ES	70.9	80	43	36		X				
FR	69.4	82	62	44		X		X		X
IT	63.0	72	23	41		X				X
CY	73.0	63	63	19*						
LV	71.3	87	61	42		X				
LT	67.4	80	39	41						
LU	66.6	88	69	31		X				
HU	62.0	55	44	43			X			X
MT	59.2	59	59	18*		X	X		X	
NL	77.4	83	83	41		X	X		X	
AT	73.7	67	65	44		X	X		X	
PL	63.0	81	58	42		X	X		X	
PT	73.9	81	38	32						
RO	64.1	61	n.a.	42		X				
SI	70.9	93	60	36		X	X		X	
SK	75.0	75	67	36						
FI	75.6	77	74	39		X				
SE	78.8	87	78	46		X		X		X
UK	75.5	68	68	30						

Note: Unemployment and Inactivity traps are calculated on the basis of marginal effective tax rates The "tax wedge" is the difference between the costs of a worker earning 67% of the average wage and the amount of net earnings received (* =2005 figure): sources: Eurostat CSR: country-specific recommendation; PTW: point to watch

II. MICRO-ECONOMIC PART

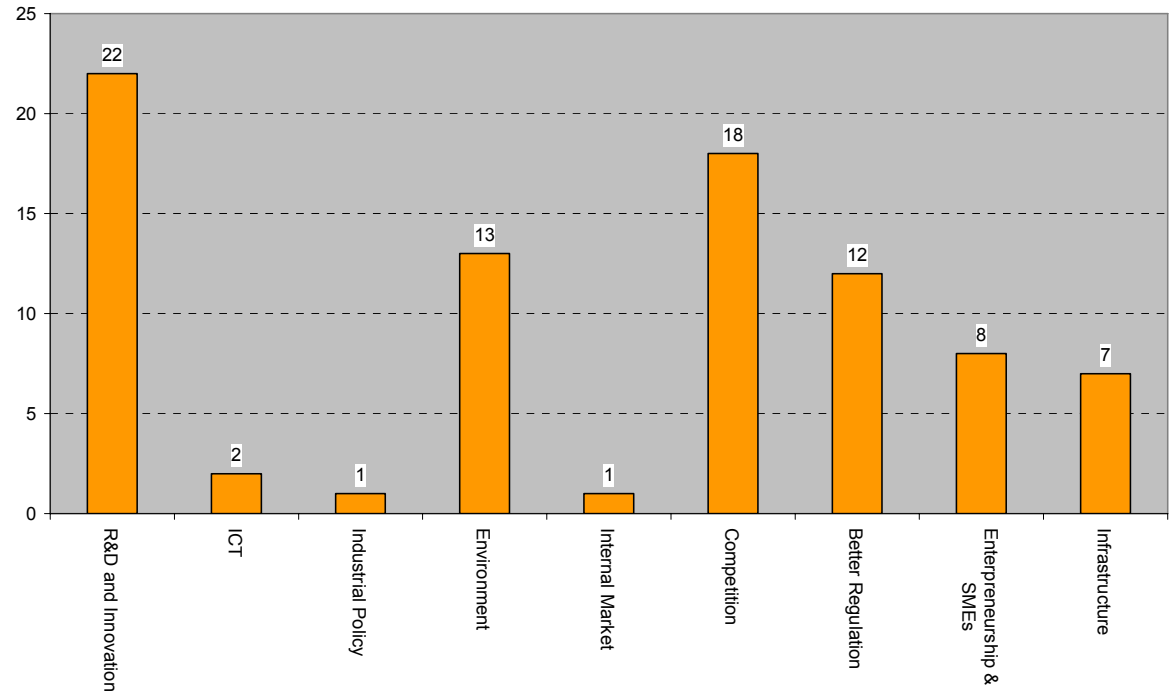
Summary and conclusions

Micro-economic reforms are the heart of the reform efforts of the Member States under the revised Growth and Jobs Strategy. Half of the main challenges, as identified by the Member States themselves in their National Reform Programmes for 2005-2008, are in the micro-economic area. Nearly half of the country specific recommendations and 'points to watch' which the Commission proposed and which the Council adopted in spring 2007, relate to micro-economic reforms (Graph 2).

The key challenges and country specific recommendations in the micro-economic area are strongly concentrated on research and innovation; competition; the regulatory environment and entrepreneurship/SMEs. Despite the focus on several micro-pillar issues, it is important to keep in mind that they form part of an integrated strategy: microeconomic reforms will be deprived of much of their effectiveness if complementary measures are not taken within the macroeconomic and employment pillars.

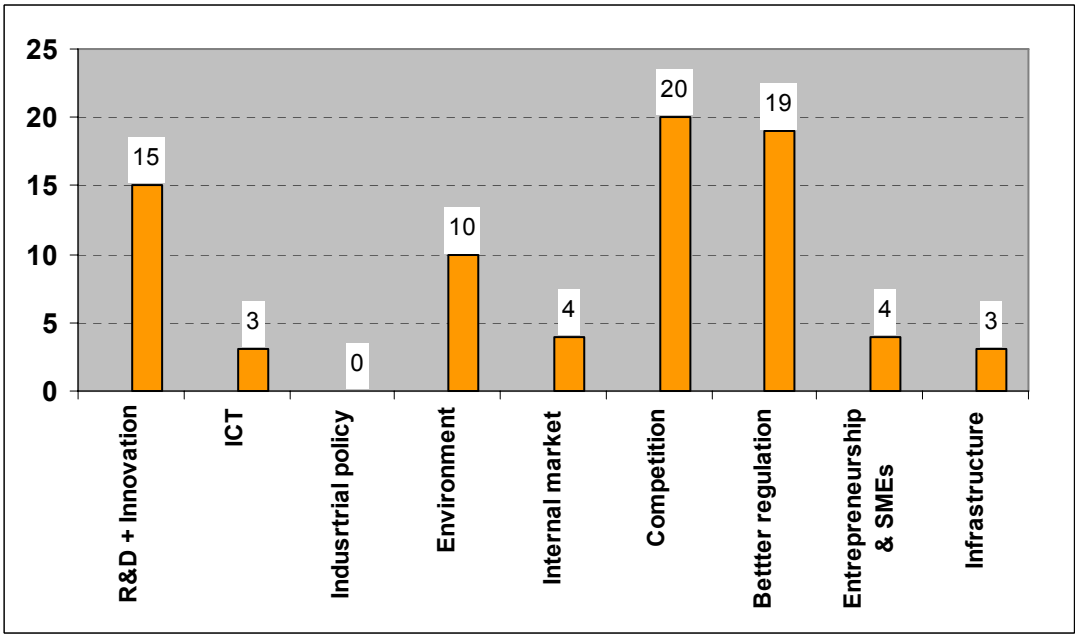
This chapter takes stock of the reform efforts under the microeconomic pillar of the Growth and Jobs strategy. Section 1 presents some of the theoretical and empirical evidence in support these efforts and Section 3 overviews progress achieved so far in the various policy areas. Section 4 draws some forward looking conclusions. This section shows that significant progress has been made in a number of areas with the implementation of the microeconomic reform agenda. Around half of all Member States have shown a strong policy response in the areas of R&D and ICT, and most others have at least made some progress in these areas. Regarding the aim to unlock the business potential, particularly of SMEs, where concrete objectives have been targeted for end-2007, a clear majority of Member States have shown at least a fairly good or strong policy response. About a third of Member States show a strong policy response with regard to energy and climate change. However, the uneven implementation record across Member States implies that progress overall could still be better. This stock-taking exercise concludes that measures in different policy areas call for a higher degree of policy coordination and integration, in order to maximise positive externalities. This does not apply only to the micro-pillar policies – where an integrated approach to the 'knowledge triangle' of research, innovation and education policies is called for – but also to the reform design across the three pillars of the renewed Lisbon strategy.

Graph 1. Number of key challenges in the microeconomic pillar in the National Reform Programmes of the Member States



Note: Number of EU27 Member States having identified the issue as a key challenge.

Graph 2. Number of country-specific recommendations and points to watch in the policy areas of the microeconomic micro-pillar



Note: Number of Member States for which the Council made a specific recommendation or raised a 'point to watch'.

1. ECONOMIC EFFECTS OF MICROECONOMIC REFORMS

Raising the long-term economic potential by increasing productivity growth is one of the fundamental objectives of the renewed Lisbon strategy. A large part of the reforms, in pursuit of this objective, are being undertaken in the microeconomic policy pillar of the strategy.

Given what is known about the relationship between microeconomic structural reforms and productivity growth, the present section undertakes a broad assessment of whether the types of reforms engaged by Member States since 2005 are likely to have the desired effects on growth in total factor productivity[12]. Some estimates of the size of these effects are presented in a separate staff working paper on spillovers and complementarities in the context of the Lisbon Strategy[13]. However, as the results of productivity-enhancing structural reforms can rarely be captured in the short term and since the measurement of their effects is complex and fraught with both methodological and empirical problems, a note of caution is in order.

Europe's success in achieving sustained economic growth during the post WWII era is associated mainly with capital accumulation and the imitation or adaptation of innovations made elsewhere. Once the catching up process was complete by the 1980s, this strategy was no longer sufficient to boost growth; increasing home-grown innovation had become a necessity. The required transition can be described as moving from the investment-driven phase of economic development to the innovation-driven phase. Which policies are likely to support this transition?

The adoption and use of ICTs are regarded as salient among the factors determining productivity growth. Against this background, detailed analyses have attributed the widening of the gap in productivity growth between the United States and Europe since the mid-1990s mainly to innovations in the ICT sector and their rapid spread across all sectors of the economy. Contrary to the United States, Europe has failed to keep up with regard to both the production and the use of ICT. ICT investment, in order to bring the desired productivity gains, needs to be accompanied by organisational change and the retraining of the workforce.

Many economic studies indicate that there is a significant relationship between market structure, and hence competition, and innovation. In general, competition is found to have a positive effect on innovation[14].

The design of growth-enhancing policies may need to change once countries move closer to the technological frontier. For instance, stringent protection of intellectual property can be more important for productivity growth in countries close to the frontier which are more heavily engaged in innovation rather than imitation.

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12 This section draws on the analysis developed in Chapter 2 of the European Competitiveness Report 2007 - SEC(2007) 1444, 31.10.2007.

13 Spillovers and complementarities in the context of the Lisbon Growth and Jobs Strategy including economic effects of the Community Lisbon Programme - SEC(2007) 1689.

14 See OECD - Economic Policy Reforms: "Going for Growth"; of 9th February 2006; by Jean Philippe Cotis; at http://www.oecdwash.org/PDFILES/gfg2006_cotis_washington.pdf#search=%22OECD%202006%20Going%20for%20Growth%22

Most empirical evidence suggests a negative relationship between the intensity of regulation and indicators of economic performance such as innovation or productivity. Reducing administrative burdens can boost GDP by freeing resources for more productive uses. This also underlines the importance of structural reforms in the labour market to facilitate the reallocation of production factors.

Studies on the links between regulation and productivity suggest that labour productivity has accelerated since the mid-1990s in lightly-regulated economies while it either grew more slowly or declined in highly-regulated countries. In addition, lower barriers to trade and less regulation appear to have increased the level and rate of productivity growth by stimulating business investment and promoting innovation. Studies on the impact of product market reforms on innovation in the EU find that intensifying competition tends to increase R&D investment, but mainly through increased innovative activity by incumbents rather than by new entrants.

Policy synergies

Claims that labour market reforms and product market reforms are complementary have been corroborated by simulations which indicate clear synergies between product and labour market policies. As an example, increasing skills and R&D raises real wages, which in turn is expected to lead to an increase in participation rates. The reduction of administrative burdens, through lower mark-ups, has synergies with the employment target due to a reduction in equilibrium unemployment. There are also clear synergies between the skills policy and R&D policies: without a sufficient supply of graduates in mathematics, science and technology, additional R&D expenditures will increase wages for these workers but will not impact output substantially.

2. THREE YEARS IN THE NEW REFORM AGENDA: AN ASSESSMENT OF PROGRESS BY POLICY AREA

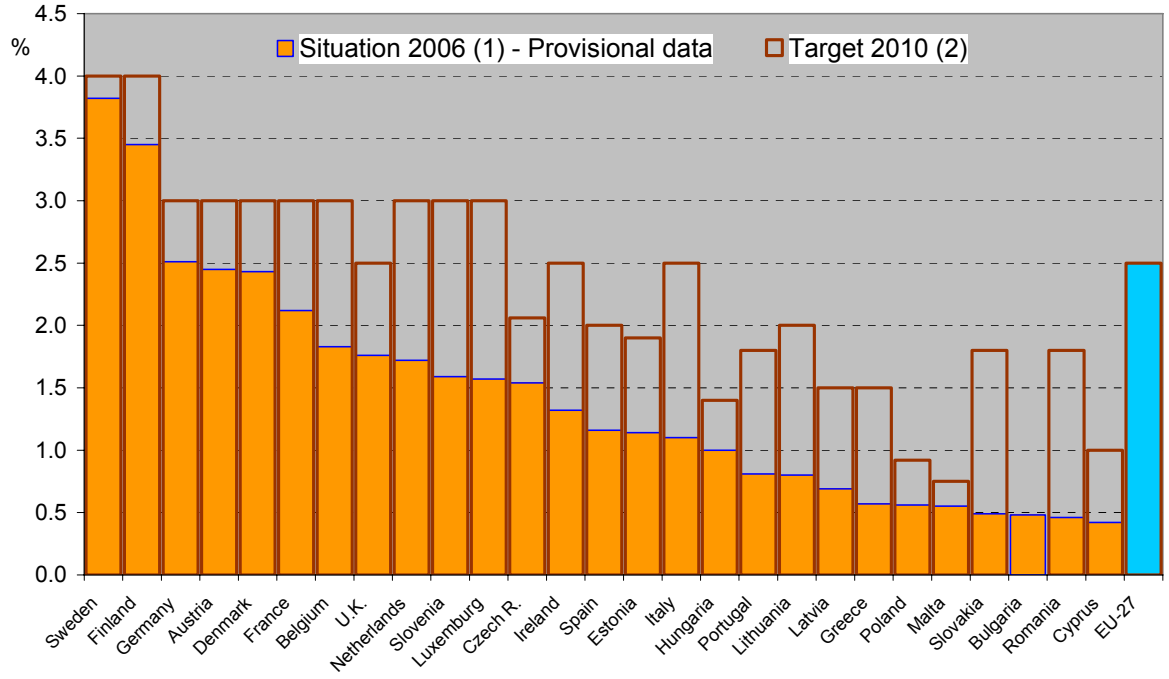
2.1. Knowledge and innovation

2.1.1. Research and innovation

Investment in knowledge (R&D and education) is the basis of innovation and technological progress. Raising the level and effectiveness of expenditure on knowledge is crucial for the EU to make the shift towards a knowledge based society. Following the re-launch of the Lisbon strategy in 2005, all Member States except BG have set national targets for R&D intensity and most of them have developed ambitious R&D and innovation strategies and accompanying measures to increase R&D intensity and the innovative capacity of their economy.

However, progress as concerns EU R&D intensity has so far been unsatisfactory, standing in 2006 at 1.84% GDP, a considerable way off the 3 % R&D target (see graph 3). Moreover, in 2007, France and Greece postponed their 2010 targets whereas Hungary, the Slovak Republic and Poland revised their targets towards lower levels of ambition. Should all Member States achieve their national targets, EU R&D expenditure is now forecasted to be 2.5% of GDP by 2010.

Graph 3: Gross domestic expenditure on R&D (GERD) as % of GDP – 2006 levels[1] (provisional data) & targets



Notes:

(1) IT, LU, PT, UK: 2005.

(2) EL: 2015; FI: 2011; FR: 2012; IE: 2013-GNP; SK: 2015; UK: 2014; EU27 = DG RTD est. for EU26

(3) Member States have been ranked according to the current level of R&D intensity from left to right.

Source: Eurostat, Member States

In general, Member States have followed up on their commitments by announcing increases in government budgets for R&D in nominal terms; however, concurring increases in GDP have led to budgets remaining either stable for many Member States or even slowly decreasing (FR, IT, NL, SK) in % GDP terms. On the other hand, public R&D spending has significantly increased in several Member States (CZ, EE, IE, ES, LT, SL, RO, LU, PT), showing that progress can be made when effectively prioritising R&D investment. Business R&D remains low in the EU and has seen no positive evolution since 2000, clearly indicating that improving the framework conditions for private R&D investments and the leverage of public R&D policy should remain policy priorities.

Tax incentives continue to be a major instrument for governments to stimulate private R&D investment. Over the past years, a clear EU wide shift has taken place in the direction of strengthened fiscal incentives. This trend continued throughout 2007 with a number of Member States (NL, UK, BE, FR, CZ, IE, PT, AT, RO, IT)

further developing their incentive systems while others undertook to evaluate their effectiveness.

In this context, the increasing role of Cohesion Policy in financing R&D can be clearly noticed, especially in some of the new Member States. The effective use of Structural Funds earmarked for research is an important opportunity for many countries that still have a low level of funding.

Assuring adequate levels of human resources will be a critical factor in raising R&D expenditure and is being addressed through measures such as increasing the number of scholarships or making researchers' career prospects more attractive. A recent trend has seen the setting up of programmes aimed at stimulating the recruitment and re-integration of excellent expatriate and foreign researchers. The planned Structural Funds interventions should provide an important contribution to develop the European human potential for research and innovation.

Reforms in R&D policies have up to now been designed almost exclusively from a national perspective. As R&D systems are, however, increasingly interconnected, it is important that national policy makers take explicit account of the European perspective in their national policies, in order to maximise the benefits from synergies and spillovers. This would increase the effectiveness of national systems and would, in the context of the European Research Area initiative, make a significant contribution towards developing the EU's research system as a whole to be a competitive player on the global scene.

However, increasing investments in research is not enough for bolstering the innovative capacity of the economy as around half of innovative firms in the EU do not conduct any formal R&D. At national level, improving science-industry linkages continues to receive significant policy attention. Setting up public-private partnerships to stimulate innovation is the most prominent approach. Measures range from improving the legal framework governing science-industry interaction, to networking, the establishment of technology transfer mechanisms, or the promotion of inter-sector mobility of researchers. Policy focus has recently shifted from traditional 'technology push' -type measures towards a more systemic approach to build innovation support mechanism. However, Member States still give a low priority to demand side issues, such as public procurement, faster commercialisation of innovative ideas and faster growth of innovative start-ups. In particular, better access to domestic and international finance by innovative SMEs remains an important challenge in most EU Member States.

There has been some progress in the EU's innovation strategy. In 2006, the Commission outlined an innovation strategy[15] for the years 2006 to 2008. This strategy is broad-based in that it brings together policies and measures from several different areas, and is complementary to regional and national measures foreseen in the context of the National Reform Programmes of the Lisbon process. On this basis, the December 2006 Competitiveness Council adopted nine strategic priorities for innovation action at EU level. Initiatives so far have covered areas of Intellectual

[15] Commission communication "Putting knowledge into practice: A broad-based innovation strategy for Europe" - COM(2006) 502.

Property Rights, standardisation in support of innovation,, public procurement in support of innovation. Joint Technology Initiatives, lead markets, the European Institute of Technology (EIT), clusters, innovation in services and risk capital markets**.**

2.1.2. Information Society

Throughout the first three years of the revised Lisbon agenda, there has been an increasing focus on mainstreaming ICT policies. The most frequent initiatives in the Implementation Reports relate to the spread of eGovernment, broadband and digital skills in education.

Member States have seen e-Government and the use of ICT in administrations as instrumental in improving government efficiency and service delivery. Online public services in the EU are moving rapidly towards the stage where a whole process can be conducted on-line.

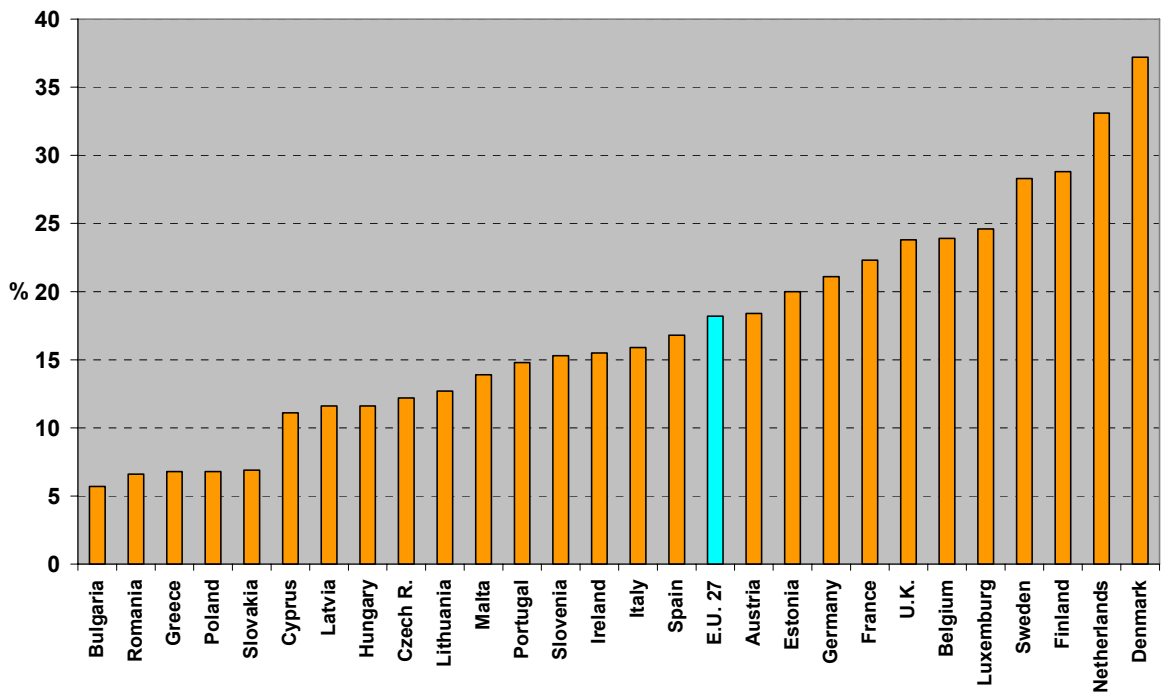
Austria has been leading the online public service league. Other top performers are Malta and Slovenia, while Portugal has made major progress since 2006. Businesses are still being better served than citizens, although the gap between the two is closing. In general, Implementation Reports show continued commitment to the development of e-government policy, with increasing attention devoted to one-stop shop government portals in all countries, digital signature, electronic identity cards, and the use of e-government for back-office re-organisation with a view to the modernisation of the public sector. The trend is very strong in the new Member States but also in large countries like Italy which need to catch up with the most advanced Member States.

In the area of **broadband**, take-up is progressing fast. The average penetration rate (number of subscribers per population) has increased from 10.5% in July 2005 (EU25) to 18.2% in July 2007 (EU27) (see graph 4 below). Although some European countries are world leaders in terms of broadband access, there is a growing gap between the best and worst performers. The main reasons for this are the lack of infrastructures in some Member States and the need for a more consistent and effective implementation of the existing e-communications regulatory framework.

Most Member States are stimulating take-up through the implementation of the regulatory framework and are extending broadband coverage in rural areas. The most significant gaps can be found in the rural areas of PL, EL, LV, SK but also in IT and DE. Actions in these areas are mostly funded through Cohesion policy programmes (mostly in the new Member States) and the European Agricultural Fund for Rural Development[16] (EAFRD).

[16] About one-third of the Rural Development Programs 2007–2013 take on board broadband initiatives.

Graph 4: EU Broadband penetration rate (July 2007)



Source: Communications Committee

In general, there is a need to bring forward more concrete and innovative policies, speeding up action on the interoperability of cross-border eGovernment services, stimulating business take-up and including e-skills strategies in life-long learning and skills policies.

2.1.3. Industrial competitiveness

The industrial competitiveness of Europe depends to a great extent on setting the appropriate framework conditions for the entire economy. Therefore, actions undertaken in other policy areas, such as R&D and innovation, reinforce industrial competitiveness in Europe. Yet, industrial competitiveness can require industry specific horizontal and sectoral initiatives.

The majority of Member States addressed industrial competitiveness over the period, notably through measures to increase the technological content of industry, to address the sustainability of industry, to promote sectoral competitiveness and to favour the internationalisation of companies by supporting exports or attracting foreign investments. In 2007 more emphasis was put on investment in environmental technologies.

2.2. Energy and climate change

The Lisbon strategy aims at strengthening the link between sustainable use of resources, environmental protection, climate and energy policies and growth. Many Member States have included environmental sustainability among their key priorities or challenges and report important new policy measures. However, recent analysis shows that tackling climate change, improving resource and energy efficiency, and halting biodiversity loss will remain key challenges for the period until 2011 and more efforts will be needed. Recognising this, new cohesion policy programmes plan a total investment of €50.6 billion under the heading of environmental protection and risk prevention. Further investment of €9.6 billion is planned in the area of energy.

Energy efficiency and conservation is a key issue in reducing greenhouse gas emissions and curbing energy demand. A majority of Member States is reporting progress in this area and outline a number of policy measures already implemented or in the planning stage. In addition, the EU average energy intensity had decreased at 0.4% annually from 2002 to 2005. While the data suggest general room for improvement in this area, notably through gains in energy generation or in buildings, a direct comparison of performance between Members States is hindered by the unique structure of the economy in each Member State. Improvements of performance against sectoral benchmarks are a key requirement for the future.

Renewable energy has an important role in reducing CO_2 missions, improving sustainability and the security of energy supply as well as creating new job opportunities, in particular in rural areas. According to the most recent data, nine Member States (DE, DK, ES, FI, HU, IE, LU, NL, SE) are on track to meet existing indicative targets for renewable electricity in 2010[17]. As a result of support schemes, including feed-in tariffs, the share of wind power and biomass in electricity production has increased significantly in some Member States. The corresponding industries have become world-class, allowing not only an improvement of the energy situation inside the EU but also exporting equipment and know-how.

Also promotion of **eco-innovations and environmental technologies** could have received more attention in the implementation reports. Most of the Member States reporting new, specific measures have already a strong competitive edge in the development and application of environmental technologies such as Sweden, Denmark, Austria, or Finland. Some Member States also report measures under consideration, for example, the expansion of the Environmental Fund in Slovenia for financing high risk investments in environmental technologies. Further promotion of environmental technologies would increase competitiveness in one of the fastest growing markets and has the potential to promote efficiency across all industries and generate new employment.

Some Member States report on measures to halt **biodiversity loss**, taking into account environmental and economic role of ecosystems. These measures include adoption and implementation of national biodiversity strategies, completion of

[17] Directive 2001/77/EC.

Natura 2000 network, providing economic incentives to biodiversity protection and rural development policies.

Efforts to break existing trends in **resource use and unsustainable consumption patterns** have generally not been highlighted in the Member States reports. However, some Member States report progress in implementation on green public procurement and resource management (e.g. waste, water and forestry) as well as on internalising the environmental costs through market-based instruments. Nevertheless, the average policy response on internalisation appears weak and slow, with a number of countries lagging behind expectations. Even when internalisation and the "polluter pays" principle are mentioned by Member States as policy priorities, concrete measures are missing in terms of environmental reform initiatives. Positive examples in this area include the environmental tax and fee systems of Denmark, Luxembourg, Netherlands and UK as well as a new environmental tax in Belgium partially offsetting the tax reduction on labour. An environmental tax reform shifting the tax burden from welfare-negative taxes (e.g. on labour) to welfare-positive taxes (e.g. on environmentally damaging activities) can be a win-win option to address both environmental and employment issues, and could be explored further by all Member States. Tax exemptions to promote biofuels, incentives for low emission vehicles, road charging reforms, use of market-based instruments, traffic management and shifts to more environmentally friendly modes of transport by several countries will help reduce external costs from the transport system.

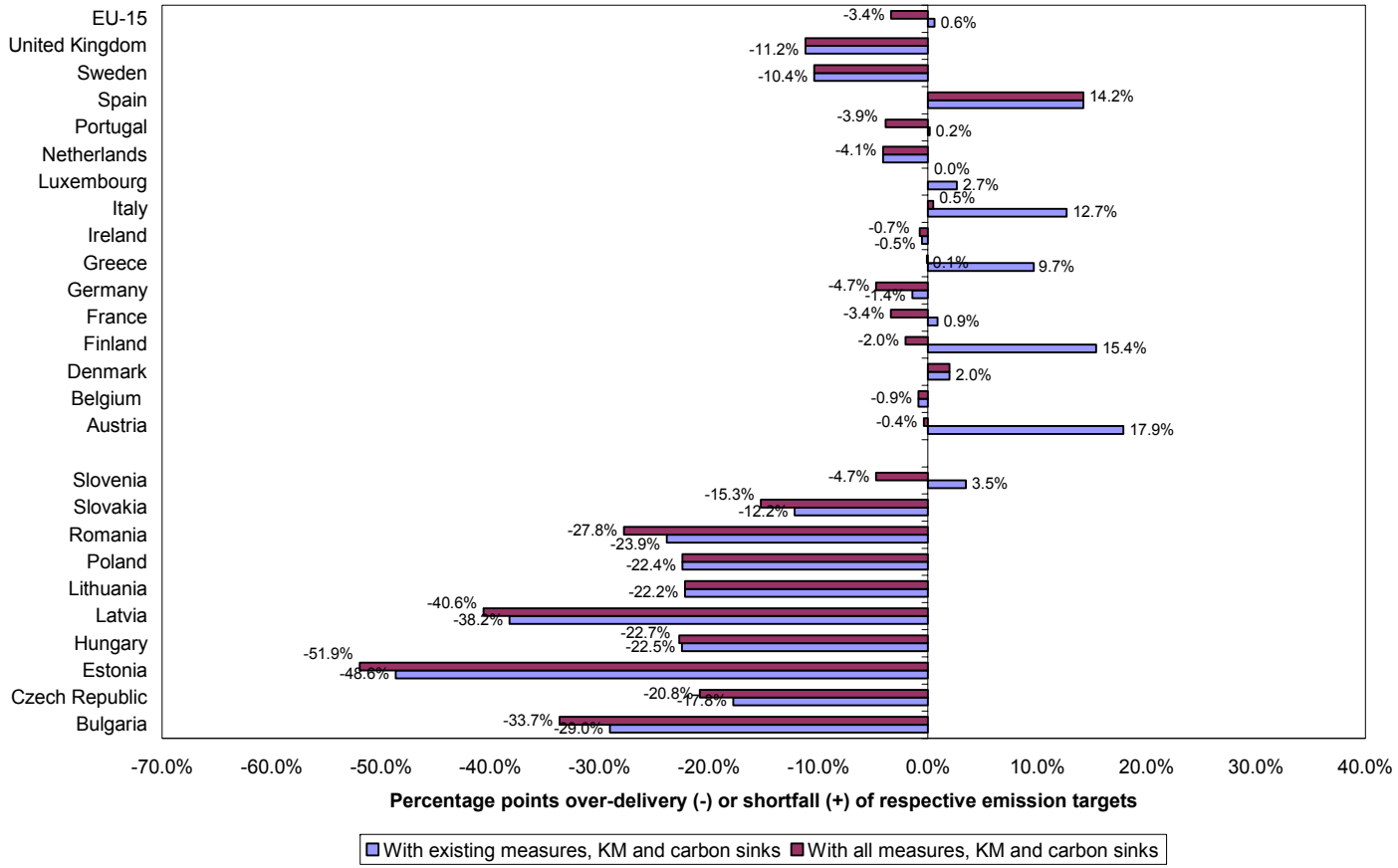
The issue of **climate change** represents a long-term challenge which, if left unaddressed, would bring about major economic costs for the European Union. According to the Stern Report[18] the overall costs and risks of climate change could be as much as 5-20% of global GDP, with the costs of strong and early action to reduce greenhouse gas emissions to avoid the worst impacts of climate change estimated at 1% of global GDP.

The EU has committed itself early to lead the global combat against climate change. Under the Kyoto Protocol, the European Community (EC) has agreed to reduce its greenhouse gas emissions by 8% by 2008–12, from base year levels. Through the burden sharing agreement this joint target has been distributed to individual Kyoto targets for the EU 15 Member States. All new EU Member States, except for Cyprus and Malta, also have agreed on targets for reducing greenhouse gases. While the EU overall has made progress in reaching the targets set the fight for climate change continues to be a real challenge, involving significant investments and potentially structural changes.

Progress in the implementation of measures against climate change so far is mixed. Several Member States will have to implement additional policies to comply with Kyoto targets (Austria, Finland, France, Greece, Luxembourg, Portugal and Slovenia), while most recent projections indicate that Italy, Spain and Denmark may not meet their targets even with additional policies (Graph 5).

[18] Stern (2006).

Graph 5: Relative distance between GHG projections for 2010 and the respective 2010 targets based on 'existing' and 'additional' domestic policies and measures, the use of Kyoto mechanisms and carbon sinks



Note: A negative sign (-) indicates an overachievement of the Kyoto target while a positive sign (+) a shortfall
Source: Draft Kyoto progress report 2007 pg. 9 Fig. 5

Several EU-wide common and coordinated policies and measures have been implemented, most notably the EU Emissions Trading Scheme (ETS), the RES-E directive, the directives on the energy performance of buildings and on biofuels, the promotion of co-generation (combined heat and power), and energy taxation. On average 10,800 installations participated in the first two years of the trading scheme (2005 and 2006) emitting approximately 2,020 Mt CO_2/yr. Two thirds of all installations are classified as combustion installations and are responsible for 72% of overall emissions. The assessment process for the second National Allocation Plans (NAP) started in 2006. On average, the proposed caps were reduced by 7% compared to the 2005/2006 verified emissions, which should bring an estimated emission reduction of 2.4% for the EU-27 compared to base year.

For the future, tackling climate change needs a long-term view. The European Council has set ambitious targets for 2020 to reduce greenhouse gas emissions by at least 20% and to increase the share of renewables in energy consumption to 20%. In addition, energy efficiency is to increase by 20% compared to the base trend and the share of biofuels in overall transport petrol and diesel consumption is to reach to 10%. This confirms the EU leadership in internalising the adverse effects of CO_2 emission at the global level. It is essential to reach these targets in a cost-effective way to maintain the competitiveness of the EU economy. Furthermore early action on adaptation to climate change will minimize risks to economic development, health, property, and infrastructure. If managed well, the challenge can create additional opportunities for innovative EU businesses that lead in developing new technologies and strategies.

2.3. Making Europe a more attractive place to invest and work

2.3.1. Internal Market and Competition

Internal Market and competition are complementary policies: the former focuses on the regulatory framework of the Internal Market and its effective implementation while the latter aims to ensure open and competitive markets, thereby enhancing consumer welfare. Since 2005, the policy attention given to these two areas has varied widely across the Member States.

As regards the Internal Market, the Member States in general have not identified concrete policy actions in their National Reform Programmes. Nonetheless, the transposition deficit of Internal Market legislation has improved considerably over the last period in a number of Member States.

As regards competition, the measures were often general in scope and rarely linked to quantitative indicators; often (in particular as regards network industries) references were simply made to the implementation of the existing *acquis*. The second most frequent measures – after network industries – were reforms relating to the enforcement of competition policy.

2.3.1.1. Progress on particular internal market and competition issues

- **Transposition of internal market directives** is mentioned as a specific issue in a number of NRPs but in the majority of cases it is not being dealt with in an operational way. There is however a considerable improvement in a number of

Member States of the transposition deficit over the last two years; but at the same time the number of infringements is increasing, indicating a deteriorating quality of transposition. As a follow up to the 2007 Spring Council conclusions the Member States concerned will need to address the question of how they intend to reduce their deficit to 1% by 2009 at the latest. There is also a need for a more qualitative approach, including by reinforcing the problem solving capacity of Member States in addressing incorrect application of internal market law.

- In spite of their economic importance, only very few NRPs address at present the issue of better functioning of **public procurement** markets. The key challenge is to make sure that Member States comprehensively transpose and implement the new public procurement framework adopted in 2004 in a correct, timely and coherent way.

- Experience so far is largely positive in the field of **competition policy enforcement**. Several Member States have taken measures contained in their NRPs strengthening national enforcement regimes (e.g. extending the powers and resources of national competition authorities) in line with the Modernisation of EC competition law in 2004[19]. Also, most if not all Member States and their national competition authorities are engaged in the screening of markets with the aim of removing obstacles to competition (a fact which is reflected in several NRPs). DK has a particularly advanced system in this respect. Rather large divergences in terms of ambition seem to exist. Less emphasis seems to have been put on the actual removal of obstacles identified.

Looking forward, ensuring convergence and uniformity in the application of EC competition rules through the European Competition Network (ECN)[20] remains a challenge. In programmes foreseeing immunity from or reduction in fines for undertakings revealing cartels (leniency) convergence is of key importance[21]. The role of national courts in ensuring convergent enforcement of EC competition law should be stressed. Further efforts should be undertaken to accelerate judicial proceedings in competition cases. Member States could in line with the existing case law of the Court[22] be encouraged to undertake procedural reforms facilitating antitrust damages actions.

- In its APRs the Commission has attached particular importance to the need for national action to remove unnecessary and disproportionate restrictions on competition in **professional services**. While some Member States are taking positive steps to remove restrictions, in some cases yielding rapid positive effects (IT), significant reforms are still needed on the part of other Member States (reflected in a number of country specific recommendations and points to watch).

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19 Regulation No 1/2003.

20 Comprising the Commission and the national competition authorities of the EU Member States.

21 See e.g. the ECN Model Leniency Programme. The OECD (see "Hard Core Cartels – Third Report on the Implementation of the 1998 Recommendation") refers to recent research estimating that the average overcharge is somewhere in the 20-30% range (with higher overcharges for international cartels).

22 The case law of the Court of Justice already today obliges Member States to guarantee effective procedures for obtaining damages in case of an antitrust infringement (see e.g. C-295/04 to C-298/04, Manfredi, paragraph 62).

The reforms should focus on the most severe restrictions (e.g. price regulation and unjustified barriers to entry).

- The persistence of barriers to competition combined with the economic significance of this sector justify that professional services remains a priority for the upcoming Lisbon cycle. Indeed, roughly one fifth of cases concerning infringements of competition results reported within the framework of the European Competition Network has related to professional services. Moreover, the Services Directive will oblige Member States to review and to assess the proportionality of their national legislation on requirements affecting inter alia professional service activities (e.g. fixed tariffs, multidisciplinary partnerships, numerus clausus) in addition to ongoing screening by national competition authorities of existing regulation and practices.

- Some NRP contain measures aimed mainly at removing public barriers to market entry and expansion in the **retail sector** (e.g. opening hours). Some measures have already produced positive effects in terms of prices in this area (IE). Given the economic importance of the retail sector (not least as a productivity driver) there would seem to be more scope for action (e.g. zoning laws, planning restrictions). Improving entry to and competition at the retail and distribution levels would also be helpful in ensuring that trade liberalisation agreed to by the EU feeds through to end consumers[23].

- Generally speaking Member States are making progress in shifting **state aid** to horizontal purposes (e.g. environment, R & D) ("better aid") while efforts to reduce the overall aid level has stagnated in recent years ("less aid"). As far as the NRPs are concerned, only a few Member States have included specific measures to reduce State aid or have reported on progress in reducing overall levels and shifting aid towards horizontal objectives[24]. Important complementary Community level measures under the State Aid Action Plan has been undertaken to promote better aid while reducing burdens on companies and Member States.

- The main challenge ahead is the timely and consistent implementation of the Services Directive, which will contribute to achieving a genuine **Internal Market in services.** By removing legal and administrative barriers to the development of services activities, it will facilitate the freedom of establishment and the freedom to provide cross-border services. The implementation process is a complex and challenging task both for the Member States and the Commission. Close cooperation is required, and the Commission has taken the commitment to provide guidance and to coordinate Member States' efforts until the December 2009 implementation deadline. To ensure that the necessary legislative measures can be adopted in 2009, Member States should aim at completing the screening and assessment of national legislation before end 2008. In parallel, the setting up of

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23 See '4. Conclusion – lessons to be drawn from the Irish experience of globalisation. European Economy No 6.

24 The overall level of State aid less agriculture, fisheries and transport stood at € 45 billion for the EU in 2005. There is a slight downwards trend from an annual average of € 52 billion in the period 2001-2003 to an annual average of € 47 billion in the period 2003-2005. There is a clear move towards "better targeted aid" with more than half of Member States now awarding more than 90% of their aid to horizontal objectives.

points of single contact, procedures by electronic means and of an effective system of administrative cooperation will require Member States to make a number of decisions and preparations in 2008.

- The importance of integration of **financial markets** is underlined in a number of NRPs; however in most of the cases without setting out concrete actions. Nevertheless, the transposition of the Financial Services Action Plan measures is well under way, even if the process should be accelerated in some Member States. As explained in the post-FSAP White Paper, the focus has now to be put from adopting new regulation to ensuring correct implementation and effective enforcement of existing measures and to removing remaining barriers to the further integration of financial markets.

2.3.1.2. Network industries

While many Member States address competition in network industries, notably in gas and electricity and electronic communications, from a growth and jobs perspective greater efforts (going beyond existing legal commitments) are needed in many countries in respect of issues such as unbundling (notably in the gas, electricity and rail sectors) as well as the need for clearly mandated and independent regulatory authorities with adequate levels of resources.

The focus on improving the functioning of network industry markets should be sharpened. The importance of network industries from a competitiveness perspective as well as from the point of view of citizens/consumers extends well beyond their 6-8% share of EU value added).

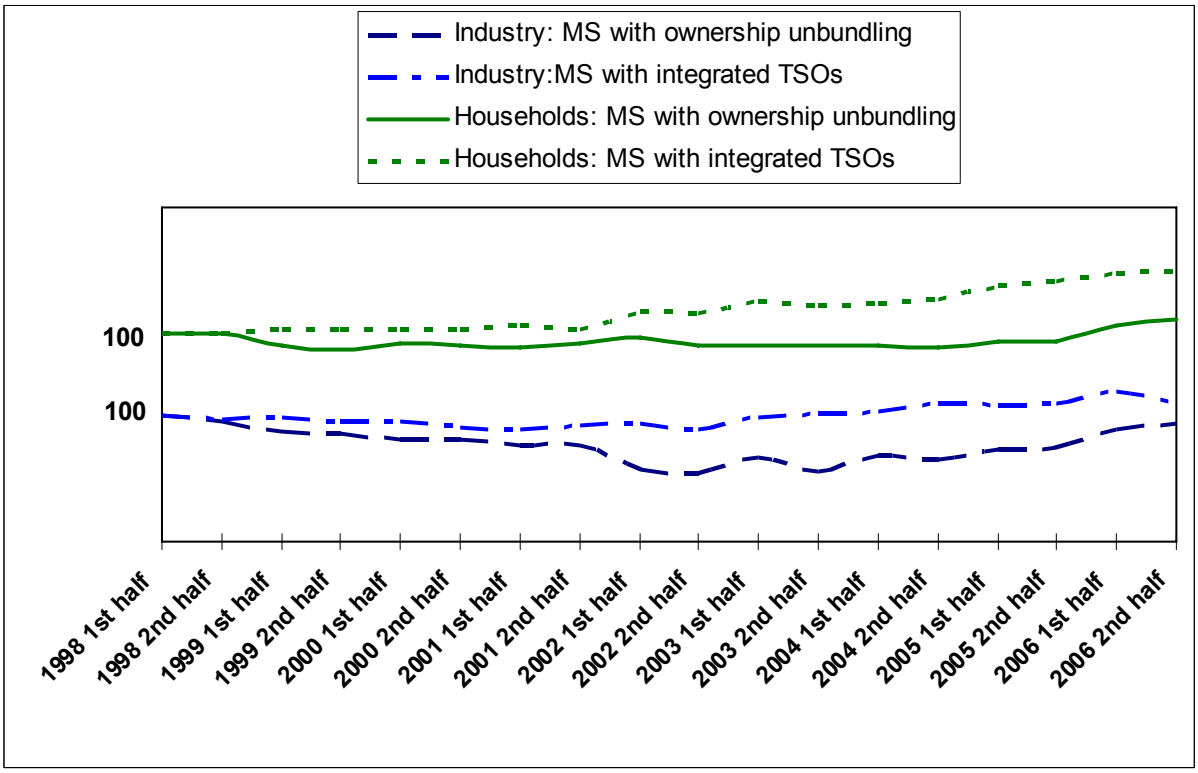
A common key challenge (in particular for gas, electricity, rail and electronic communications) is the need to ensure independent, clearly mandated and well resourced regulators (as well as intensified cooperation between the regulators themselves and with the Commission.

Continuous efforts should be made at finding the optimal balance between sector-specific regulation on the one hand, and general competition and internal market policy principles on the other hand. To the extent that competition intensifies, regulation may be progressively lifted.

Developments in the various network industries are as follows:

- Promoting competition in gas and electricity markets remains a key challenge and concern for most Member States. While it is undeniable some progress in opening up gas and electricity markets has been made in recent years, it is also true that in many Member States a real competitive European market for electricity and gas still needs to develop. Yet, the benefits to consumers and users of an effective liberalisation are clear (see a comparison of price developments between unbundled and integrated transmission system operators (TSOs) in graph 6). High levels of market concentration, vertical foreclosure and lack of transparency continue to characterise gas and electricity markets.

Graph 6: Electricity price evolution in EU-27 for the period 1998-2006 according to ownership structure of TSO



Source: Eurostat, European Commission calculations

The key problems to be addressed are well known (vertical integration and the need for more effective unbundling (preferably ownership unbundling). A particular problem is a tendency for Member States to maintain or impose price regulation.

- Competition in **electronic communications markets** is governed by the regulatory framework adopted in 2002. This is an innovative construction involving harmonisation legislation based on competition policy principles. The experience with the regulatory framework during its first three years of operation is positive. More competition has led to innovation and investment by both new entrants and incumbent operators as well as to significant retail price declines, for example, of around 40% for local fixed telephony costs on average. The independence of the national regulatory authorities both from ownership interests in the sector and from undue political interference, and transposition issues (in particular secondary legislation and amendments of existing laws) remain an issue.

- While competition in the **rail sector** is addressed in some National Reform Programmes, few Member States envisage concrete measures to tackle the key problems limiting competition (such as the insufficient separation between the infrastructure manager and the incumbent rail operator) and to ensure that the rail

regulators are independent and adequately endowed with resources. The major event in terms of Internal Market and competition regulation in the railway sector was the complete market opening for all kinds of rail freight services on the EU railway network on 1 January 2007 according to Directive 2004/51/EC of 30 April 2004 (part of the second railway package). The legal possibility of open access traffic has led to new market entry and the development of competition in rail freight services in a number of Member States. The number of new entrants and their market share has risen, for instance, in Poland, Romania, the Czech Republic and France. Strengthening the power of institutions on which the organisation of the sector depends, i.e. the rail infrastructure manager, the rail regulatory body and the safety authority, will be of crucial importance. On 23 October 2007, the European Parliament and the European Council adopted the 3rd railway package, which includes Community law on market opening for international rail passenger services by 2010, passenger rights in rail transportation and on the certification of train drivers.

- While all Member States have transposed the current directives, only a number of Member States have addressed **postal services** in their National Reform Programmes. Liberalisation has progressed well. Member States have embraced liberalisation as agreed thus far and most of them have taken steps to prepare their postal services sectors for further liberalisation. The actual level of competition in the sector however remains low. Looking ahead, the Commission proposal for liberalisation is expected to be adopted by EP and Council first semester of 2008. Objectives of the proposed action are to achieve an internal market for postal services through the removal of exclusive and special rights in the postal sector, safeguard a common level of universal services for all users in all EU countries and set harmonised principles for the regulation of postal services in an open market environment, with the aim of reducing other obstacles to the functioning of the internal market. The transposition and effective implementation of the directive will be an important challenge.

2.3.2. Better Regulation

In general, Member States have expressed their commitment to the key Better Regulations objectives in their National Reform Programmes, while implementation in the daily policy making processes has stalled. Moreover, Better Regulation has been treated as a reform measure rather than as an underlying principle of efficient public administration delivering effective, coherent and less burdensome legislation[25]. So far, action at national level has been limited to the eventual setting up of better regulation tools, without a real change in regulatory conditions and with limited impact on the business environment. The lack of specific targets, compliance incentives and monitoring and enforcement mechanisms has taken its toll in slowing down the implementation of announced measures as well as the process of cultural change in policy making.

The European Council has invited Member States to set their own national **administrative burdens** reduction targets by 2008 of comparable ambition to the

[25] BG and RO have not been included in the analysis, as they are at the very beginning of developing their approach to Better Regulation.

target set by the Commission, i.e. a 25% reduction. To this date, ten Member States (AT, DE, DK, EL, ES, IT, NL, SE, SK, UK) have set a 25% national reduction target, while another two Member States (CZ, FR) set a target of 20%. In comparison with last year this is considerable progress as the number of Member States with a quantitative target has doubled. However, there is still a considerable effort to be done in this regard by the end of next year.

The Commission and Member States will be entering a crucial phase next year when first results from the measurement will provide indications of how administrative burdens can actually be reduced. The key step was taken when most Member States opted for the same measurement methodology (standard cost model). Four Member States have so far carried out baseline measurement of administrative burdens (CZ, DK, NL, and UK); while another four are currently conducting them (AT, DE, FR, SE).

However, reduction of administrative burdens is only one of the **regulatory simplification** elements. Despite initial progress in developing systematic simplification programmes, the pace has slowed down with only two Member States advancing in this area in the course of last year (PL and LU). It is worth mentioning that in fourteen Member States (BE, CZ, CY, DK, IE, LU, MT, NL, PL, PT, SE, SI, SK and UK), stakeholders are involved in setting regulatory simplification priorities under existing programmes or ad-hoc measures.

Limited progress has been made in implementing **impact assessment** systems. Rigorous impact assessments analysing economic, social and environmental impacts of new legislative proposals are being carried out by a handful of Member States, (AT, DK, DE, IE, NL and UK). Moreover, only two out of these six Member States make their impact assessments publicly available (DK and UK). Overall, impact assessment quality among Member States varies widely and there is room for substantial improvement. Rather worrying remains the fact that very few institutional structures which would allow for a rigorous implementation of the impact assessment system and its quality control have been created (DE, IE and UK), while promising steps in this direction are being taken (EL, LT and LV).

Regular **consultation of stakeholders** remains the least developed Better Regulation tool in Member States. Even for those Member States which report on a formal obligation incorporated in their law making procedures (AT, BE, CZ, DE, DK, FI, IE, LT, LU, PL, SE, SI and UK), there is still scope for further improvement towards a systematic implementation of clear, consistent and transparent consultation rules across the board. Moreover, the understanding of the contribution that stakeholders could bring into the policy making process substantially differs across the Member States, as evidenced by the differences with regard to the stage in the law making process at which the stakeholders become involved and with regard to the methods used to reach them.

Lastly, progress in developing **Better Regulation strategies** has decelerated, with only one Member State (CZ) developing a strategy in 2007. Some of the originally promising plans have not yet resulted in explicit Better Regulation programmes which would ensure a coherent approach to policy making. This stalemate, in conjunction with the above mentioned lack of progress in the area of impact assessments and legislative simplification, holds back progress in increasing the

efficiency of public administration and in creating favourable regulatory conditions for businesses.

2.3.3. Entrepreneurship and SMEs

Overall, the measures and initiatives in the area of SME policies undertaken by Member States since the re-launch of the Lisbon partnership for growth and jobs in 2005 are going in the right direction. Progress has been particularly visible in improving the start-up procedures but also in the integration of the "think small first" principle into the policy-making process. In the area of entrepreneurship education, SME access to public procurement and recruitment of the first employee, policy actions have been initiated in almost all Member States while their results have not yet materialised. Most of the priorities set at the Spring European Council 2006 – start-ups, recruiting the first employee, entrepreneurship education, think small first – need to be seen in a long term perspective, and related policy actions need to be intensified.

Average time and cost to **start up** a private limited company is 12 days and cost is € 485 (see Table 1). This is substantially lower than the 24 days and € 830 for an equivalent company in 2002. Many Member States have established a one-stop-shop or equivalent arrangement even though in some cases they do not cover all types of companies: only 2 out of 3 one stop shop systems offer the possibility to register a private limited company. Member States that fully comply with all three objectives (one-stop-shop, time and cost) are BE, DK, EE, FR, HU, PT, RO, SI and UK. In general registration times have improved and in 13 Member States, it is now possible to register a company within one week. It should be noted, however, that this analysis only looks at the steps to get a company registered. In many countries there are further administrative steps and more time is required before a new SME can start its business operations[26].

Table 1: Results of the objectives set by the Spring 2006 Spring Council conclusions - One stop shop to start-up a company (1)

	Name	Fully operational	Time required to start-up a company	Cost to start-up a company**
Belgium	Guichet agreé d'entreprises	YES	1,5	€ 517
Bulgaria		NO*	12-30	€ 155
Czech Republic	Central Registration Offices (CRO)	NO*	42-56	€ 345 €
Denmark	Danish Commerce and Companies Agency (DCCA)	YES	3	€ 0
Germany	Starter-Center	NO*	6,5	€ 783
Estonia	Notaries	YES	2	€ 190
Ireland	Companies Registration Office (CRO)	NO*	2-5	€ 50
Greece	Directorate of Development at the prefectures (KYE)	NO*	30	€ **1.366**
Spain	Ventanilla Única Empresarial (VUE) + PAIT for Ltd.	YES	30-40	€ 617

[26] In this context, the timely implementation of the points of single contact foreseen in the Services Directive, to be implemented by end 2009, will also be an important task for Member States.

France	Centres de formalités des entreprises (CFE)	YES	4	€ 84
Italy	"Sportello unico"	YES	4	€ **2.673**
Cyprus	OSS at Ministry of Commerce, Industry and Tourism	YES	7	€ 265
Latvia	Register of Enterprises	NO*	4	€ 205
Lithuania	Centre of Registers	YES	6	€ 130-€ 289
Luxembourg	Guichet unique d'entreprises	YES	14	€ **1000**
Hungary	County Courts	YES	2-3	€ 392
Malta	Registrar of Companies – Malta Financial Services Authority (MFSA)	NO*	7-10	€ 450
Netherlands	Chambers of Commerce	NO*	3	€ **1.040**
Austria	WKO Gründerservice	YES	7-30	€ 400
Poland	Tax Offices	NO*	30	€ 735
Portugal	Enterprise Formality Centres (CFE)	YES	1	€ 300-€ 360
Romania	Counties Trade Registers	YES	3	€ 100-€ 125
Slovenia	VEM	YES	3	€ 250
Slovakia	Trade licence offices, companies register	NO*	14	€ 330
Finland	Trade Register	YES	14	€ 330
Sweden	Företagsregistrering	YES	21	€ 222
United Kingdom	Companies House & Business Link	YES	1	€ 54
AVERAGE			12 days	€ 485

Notes
(1) All figures on cost and time based on information provided by Member States which have not been fully validated. Calculation methods as described in Commission Staff Working Document SEC(2007)129.
*NO means that the services offered by the one-stop-shop are not sufficient to consider it a fully functional one-stop-shop.
**Cost: numbers in bold for countries with cost above the threshold.

Member States are increasingly integrating the **"think small first"** principle into the policy-making process. While only few have set up a specific body to represent SMEs interests, almost all of them consult SMEs representatives. A number of Member States (for example BE, DK, ET, MT, NL, SE, FI, UK) evaluates or is planning to evaluate the impact of new legislation on SMEs. Examples of specific provisions to alleviate the administrative burden on SMEs go from the simplified conditions for accessing subsidised finance (FR) to longer payment time for VAT (DK) or development of dedicated electronic services (FI). However, further national efforts are needed in the application of this principle in order to meet the specific needs of micro and small enterprises but also to maximise its positive contribution to the target of reducing by 25%, at EU level, the administrative burden by 2012.

Awareness of the need to enhance **entrepreneurship education** at school is constantly increasing in the Member States and in the last couple of years new plans and individual initiatives have been flourishing in this area. However reforms planned in a number of countries are sometimes described in rather generic terms and their implementation in practice will have to be monitored. In a few Member States, entrepreneurship is already a recognised objective of the education systems and is embedded explicitly in national framework curricula (ES, FI, IE, CY, PL, UK) but implementing means (teacher training, teaching materials) still need to be stepped up.

In some cases, elements of entrepreneurship are found horizontally throughout the curriculum, or entrepreneurship forms part of economic subjects (LV). Other Member States are starting to implement or are planning reforms in the same direction. However, Member States where entrepreneurship is well established in the curricula are still a small minority.

Almost all Member States have already taken or are currently introducing measures to raise SMEs' awareness on public tenders and to provide them with easy access to tender information (single electronic access points or electronic procurement, training and counselling, etc.). However, only a handful of Member States report on more specific measures to help SMEs' to participate in **public procurement** (use of prior information notices, dividing contracts into small lots) and only very few have put in place a strategy or specific measures to help SMEs to participate in public procurement (e.g. UK, IT, FR). A study published by the Commission in November 2007[27] showed that 42% of the value of public procurement contracts above the EU Directives' thresholds goes to SMEs. This share is smaller than the economic importance of SMEs in the EU, but above the SME quota for federal public procurement in the US (23%).

Since 2005, some limited progress has taken place in the simplification of procedures for recruiting a first employee. Overall, the average number of mandatory external contacts (social security organisations, tax offices, labour offices, etc.) has been reduced from 3 to 2.5 and the average number of procedures (filing forms, etc.) from 3.5 to 3. However, the target of having no more than one public administration point in that process is still far and the situation varies significantly from a Member State to another. Only three Member States (e.g. ES, MT, and PT) have a special one-stop-shop system for recruitment of first employee or one-stop-shops for start-ups that can also take care of recruitment. Several other Member States have procedures that are so simple that only one contact with a public administration is required (e.g. BG, FR, IE, LV, LT, SE). In others, at least the social security registration is organised as a one-stop-shop or one-window-system, i.e. one branch of the social security collects the registration and distributes the information to the other branches (e.g. DE, SK or the UK). BE is a special case where "social secretariats" take care of all employment related procedures for businesses, including the registration of new employees etc. but have to be paid by businesses.

2.3.4. European infrastructures in the transport sector

In 2007 the rate of progress towards the key objective of completing the Trans-European transport network has been high. The measures taken jointly by the Member States and the Community in support of the TEN-T and the 30 priority projects in particular, have resulted in an annual investment (EU 27) of € 40 billion, with approximately € 20 billion of this going to priority projects. PP 4, the High-speed railway axis east (section Paris-Bodrecourt) and PP6, the dedicated rail freight Betewe line, were completed during 2007, and PP 2 the High-speed railway axis - Paris-Brussels-Cologne-Amsterdam-London is now almost complete, while

[27] *Evaluation of SME Access to Public Procurement Markets in the EU,* Final Report by GHK and Technopolis, available at: http://ec.europa.eu/enterprise/entrepreneurship/public_procurement.htm

substantial progress has been made on other projects including PP 3 the High-speed railway axis of south-west Europe - Madrid-Barcelona, Madrid-Valladolid.

Looking to the future, the Community institutions support the introduction of a higher Community co-financing rate, in particular for cross-border projects, for those having a transit function, or those involving the crossing of natural barriers. The Multi-annual Programme will allocate between 80 and 85 % of the TEN-T financial reference amount of € 8,013 million for the period 2007-2013 to projects presenting the highest value to the Community (in particular cross-border projects), to the deployment of the European rail signalling system ERMTS/ETCS and to the development of Intelligent Transportation Systems. In the same period, new cohesion policy programmes plan to invest for the development of railways more than EUR 22 billion and more than EUR 17 billion for the development of TEN-T motorways.

3. IMPLEMENTING PRIORITIES FOR ACTION

The potential contribution of microeconomic structural reforms to the European Union's long-term economic performance through achieving stronger productivity growth is well established in the theoretical and empirical literature. An important part of the task to enhance total factor productivity growth consists of bringing about more propitious framework conditions. Well functioning markets and competition are a key condition for higher R&D spending to translate into innovation and better results in terms of productivity.

The previous section summarises the evidence on the implementation of micro-economic reforms since 2005, drawing on Member States' implementation reports throughout the first cycle of the strategy for Growth and Jobs. It shows that the types of reforms engaged by Member States in the last years have the potential to strengthen Europe's productivity performance and thereby make a key contribution to the objectives of the growth and jobs strategy. Full implementation of the reforms in the microeconomic area remains the most important condition for realising their potential in terms of productivity growth.

The analysis shows that significant progress has been made in a number of areas with the implementation of the microeconomic reform agenda. Around half of all Member States have shown a strong policy response in the areas of R&D and ICT, and most others have at least made some progress in these areas. Regarding the aim to unlock the business potential, particularly of SMEs, where concrete objectives have been targeted for end-2007, a clear majority of Member States have shown at least a fairly good or strong policy response. About a third of Member States show a strong policy response with regard to energy and climate change. However, the uneven implementation record across Member States implies that progress overall could still be better.

There are also important policy areas where overall progress across Member States has been not satisfactory and where significant implementation deficits remain despite the strong performance of some Member States. In the area of R&D, current efforts will probably not be sufficient to reach the established target. In the area of competition policy only few Member States have registered a good policy response, while overall progress has been limited. At the start of a new cycle these

implementation deficits give rise to concern. Member States commitment to the full implementation of their National Reform Programmes is important for the credibility of the strategy overall. It will be important to take any implementation deficits from the first cycle into account when defining the ambition of the National Reform Programmes for the new three-year cycle.

- In the area of R&D, innovation and industrial policy, Member States have given a high priority to the measures to enhance research and innovation. While all Member States have set a target for research spending and despite progress made in many Member States, important implementation gaps remain overall. The slight decline in R&D expenditure in 2006 after broadly stagnating levels in the years before is a sore reminder that one of the flagship objectives of the renewed Lisbon strategy—the 3% R&D expenditure target—may not be reached by 2010. More than insufficient public spending on R&D, this outcome reflects weaknesses in the existing framework conditions and in policy design. Going forward it will therefore be crucial to set up coherent R&D and innovation strategies where they are not yet in place and to address issues such as innovation in services organisational innovation, intellectual property rights, ensuring the availability of qualified researchers, and overcoming skills shortages.

- Regarding ICT, implementation gaps remain regarding the availability of digital content and related policies (IPRs), digital skills requirements, standardisation, next generation networks, and security of electronic payments, privacy, and interoperability.

- The implementation record in the areas of functioning markets and competition policy has been mixed across the Member States. While there is clear progress with transposition of internal market legislation, more attention to the quality of transposition, implementation and enforcement of internal market legislation is needed. More also needs to be done to ensure the good functioning of public procurement markets and, at the Community level, the development of a well balanced framework for intellectual property rights. The integration of financial markets, in particular in the area of retail financial services, has so far remained inadequate.

- State aid and competition in professional services have not been prominent on the Member States' reform agenda. Particular implementation deficits remain in the area of external openness, professional services and some network industries, in particular gas, electricity, and rail. It is telling that the more country-specific recommendations and points to watch have been proposed in the field of competition policy than in any other micro-economic area. This shows that this policy area constitutes a key challenge for most Member States also for the new three-year cycle.

- In the area of Better Regulation, the main progress has been reaching consensus on prioritising this policy area and in creating the necessary tools to serve it. However, implementation has been slow and the objective of embedding Better Regulation in every-day policy making is far from secured. Despite the recent progress, there is a need for more action to achieve the SME start-up targets set by

the 2006 Spring European Council. Improving SMEs' access to finance and mainstreaming of SME issues into other policy areas deserve more attention.

- Implementation of policies to address climate change and sustainable use of resources has been insufficient. Also, more action is needed to improve the interconnections of national energy networks and to integrate the energy markets. In the area of transport policy, interoperability and interconnection of the national networks remain priorities, while not enough has been done to promote the efficient use of infrastructure.

A general conclusion of this stock-taking exercise is the recognition that policy measures in the different policy areas need to be better integrated, so as to maximise their positive externalities. This does not apply only to the micro-pillar policies – where an integrated approach to the 'knowledge triangle' of research, innovation and education policies is called for – but also to the reform design across the three pillars of the renewed Lisbon strategy, i.e. the macro-economic, micro-economic and employment policy areas.

In order to ensure continued progress toward bringing about a better productivity performance in the European Union, it will be important that Member States in their National Reform Programmes for the new three-year cycle of the strategy take account of the microeconomic implementation deficits of the first cycle that have been outlined here. R&D and innovation policies as well as enhancing competition, market functioning and sustainable use of resources will remain key challenges in the period ahead both for both most Member States and the European Union as a whole. A sustained effort will be needed to narrow the EU's productivity gap vis-à-vis the global top performers.

III. THE COMMISSION DRAFT OF THE JOINT EMPLOYMENT REPORT 2007/8

Summary and conclusions

The favourable economic environment has left positive traces on the European labour markets. 2006 saw employment–intensive growth for the first time in almost a decade. The laast two year have seen the creation of almost 6.5 million new jobs and unemployment has reached the lowest levels in years. Part of this is cyclical but there are good reasons to believe that the European Employment Strategy and the integrated Lisbon strategy are showing results and that structural reform are starting to pay off. One of the most obvious sign of this is the recent decline in structural unemployment.

Despite the relatively favourable labour market outlook a number of serious concerns persist The most pressing is youth unemployment that continues to be a severe problem in many Member States. Young people have not benefited proportionately from the economic upswing; in 2006 they still remained exposed to unemployment more than twice as much as the overall work force. Today nearly one in six young people in the EU, or almost 7 million, still leave the education system prematurely and there has been virtually no increase in levels of educational attainment.

Further efforts are needed to reach the European employment targets. Moreover, the responsiveness of European labour markets to the challenges of globalisation and ageing remains insufficient. Structural unemployment still remains too high and more needs to be done within comprehensive flexicurity approaches to improve the functioning of European labour markets and to facilitate transitions with the aim of eliminating barriers to employment.

It is very encouraging that about half of the Member States have now developed or are developing comprehensive flexicurity approaches but the performance within the various underlying components is less positive. Labour market segmentation remains a significant problem in many Member States and the focus of the policy response still tends to be more on easing labour market regulation for new entrants and facilitating more contractual diversity than on reforming existing mainstream labour legislation. Reforms of social security systems have tended to be limited to pension reforms. Active labour market policies, although becoming more personalised, have been subject to a decline in expenditures since 2000 both as a share of GDP and per worker. Finally, participation in lifelong learning in the EU barely increased between 2005 and 2006, while it has actually decreased in half of the Member States, and adult training remains unevenly distributed. These figures are disappointing and worrying for the future. A substantial rise in the investments in human capital better targeted towards labour market needs is essential to close the productivity gap with our key global competitors.

Europe must continue labour market reforms for more and better jobs. People not working and in precarious work need special attention. An ageing Europe in an intensely competitive world needs more people working more productively.

1. PROGRESS IN ACHIEVING THE OBJECTIVES OF THE EUROPEAN EMPLOYMENT STRATEGY

1.1. Full Employment

Employment targets

Helped by the strong economic expansion employment growth picked up in 2006 and recorded the strongest increase since the nineties with nearly 4 million jobs being created during the year and the overall employment rate climbing to 64.3%. This employment expansion notably took place in an environment of accelerating productivity growth, not seen in a decade. Progress has been widespread but was in particular driven by a handful of Member States. Labour market performance is projected to continue at least next year and should lead to further progress towards reaching the employment targets.

Despite the positive performance in 2006 Europe remains short of the 2010 employment targets. The current employment rate implies that another 20 million jobs will have to be created by 2010 if the target is to be reached. Forecasts already suggest that another 5.5 million new jobs could be created by 2008[28]. With sustained efforts, the 2010 overall target of a 70% employment rate becomes closer.

Older workers still represent one of the largest target groups for raising employment. With a current employment rate of 43.5%, (6.5 pp from the 2010 target), there is still significant untapped potential among older workers and their numbers will continue to grow during the coming decades. Regarding gender, the employment rate for women has increased in almost all Member States reaching 57.2 % in 2006, and stands relatively close to the 2010 target of 60 %. With an employment rate of only 50%, people with disabilities also remain a potentially large untapped resource of additional labour supply.

Unemployment dropped significantly from 8.9% in 2005 to 8.2% in 2006 and almost all Member States contributed to this trend. Both women and men benefited as the unemployment rate fell to respectively 9% and 7.6%. A notable indicator of the robustness of the current labour market performance is that the long-term unemployment rate fell for the second year in a row, from 4% to 3.6%.

Youth unemployment remains a severe problem in many Member States. The overall youth unemployment rate did decrease over the last year but this was mainly attributable to significant reductions in a small number of Member States. The unemployment rate amongst young people has actually increased since 2004 in a number of other Member States. So far young people have not benefited enough from the favourable economic environment; they remain more than twice as exposed to unemployment as the overall work force. Finally, many Member States still fall short of the new activation targets. Despite also being a Lisbon priority since 2006, and given the importance of the young generations in addressing the future demographic challenges, these trends remain disappointing.

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[28] European Commission, Economic forecast, Spring 2007.

Structural reforms

There are a number of signs that structural labour market reforms in recent years are having an impact[29]. The strongest evidence however, is the significant reduction in structural unemployment throughout Europe[30]. While the period 1997-2003 was characterised by rather stable and high structural unemployment, it has been reduced by about one third since 2004 and is forecast to drop further in 2007. The level, however, is still significantly higher than that of our principal competitors.

Together this points to the existence of significant barriers to employment. European labour markets are not sufficiently responsive to the challenges of globalisation and ageing. More needs to be done to improve their functioning and to facilitate labour market transitions.

1.2. Quality and productivity at work

Productivity

One of the most striking challenges of globalisation is the enhanced requirements for productivity gains in order to ensure sustainable employment growth. Since the eighties, average labour productivity growth in the EU has been decreasing from around 2% a year in the second half of the 1990s, to around 1% between 2001 and 2003. Over the same time frame the US has sustained productivity growth rates of some 2% on average. Since 2003 however, there has been evidence that the decline in productivity growth in Europe is being reversed.

Table 1. GDP, employment and labour productivity growth (annual averages)

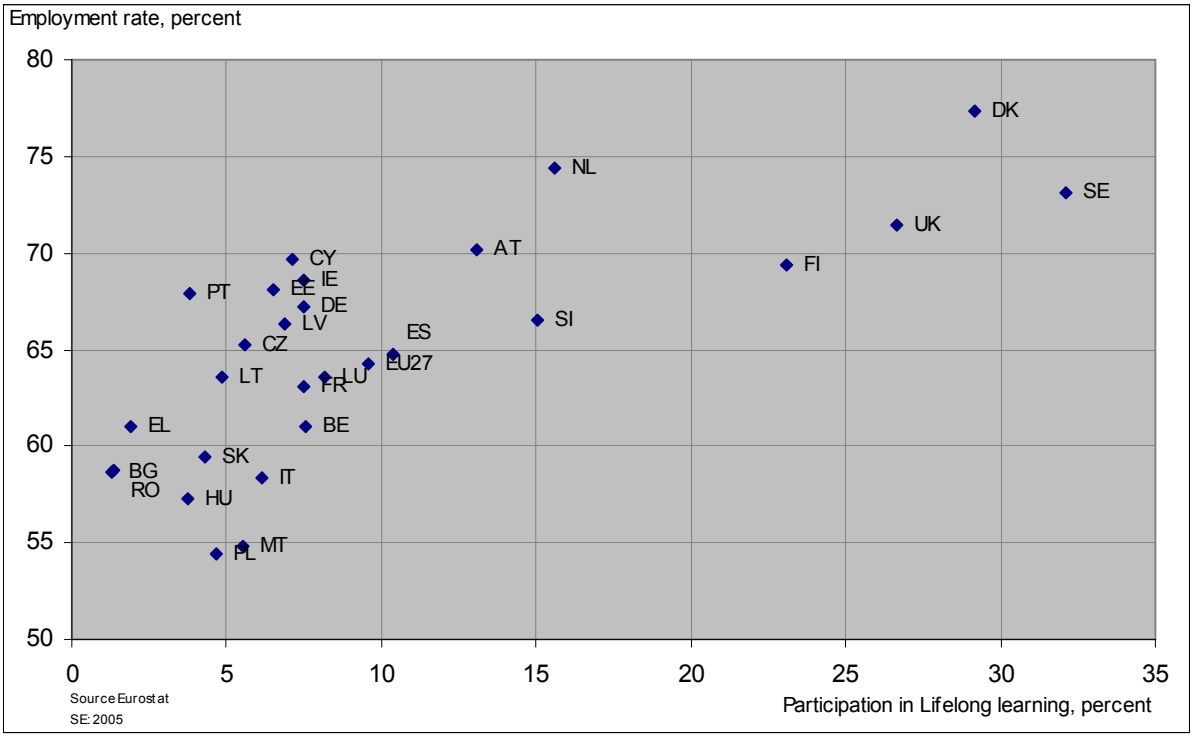
	1997-2000		2001-2003		2004-2006	
	EU27	US	EU27	US	EU27	US
1. GDP	3.1	4.2	1.5	1.6	2.4	3.2
2. Employment	1.1	2.1	0.3	0.0	1.1	1.6
3. Labour Productivity (per worker)	2.2	2.1	1.1	2.0	1.5	2.1
4. Hourly Labour Productivity		2.1	1.6	2.7	1.4	2.3

One important means of improving labour productivity is through investment in human capital, in particular by establishing comprehensive strategies for lifelong learning throughout the life cycle. In this regard, Europe is behind schedule.

[29] One of them is the development in wages. In the current economic upturn, there has been no significant pressure on wages which has been typical for cyclical driven expansions.

[30] European Commission, AMECO database, DG ECFIN.

Graph 2: Employment rates and participation in lifelong learning 2006



The graph indicates that there may be some correlation between employment rates and participation in lifelong learning. The graph might also indicate that to achieve very high employment rates it is necessary to exceed a certain level of participation in lifelong learning.

Clear progress has been made in recent years on reducing early school leaving, but in 2006, almost 7 million young people still left education prematurely. Progress is too slow in increasing youth educational attainment levels; figures have only improved moderately since 2000. The level of adult participation has remained stable or has even decreased in 20 out of 27 Member States since 2004. Participation levels are particularly low in Southern European countries and in most of the new Member States. The lowest participation rates throughout the EU continue to be those of older workers.

It is imperative that Europe steps up its investments in human capital[31]. Adequate incentives and cost sharing mechanisms for enterprises, public authorities and individuals must be developed.

Quality at work

Progress in the quest to increase quality at work again remains mixed[32] and implementation of policies to this aim is limited. In-work poverty still affects 8% of workers in the EU. While 2006 saw some further improvements in youth education

31 Currently US and Japan are for example spending twice as much as the EU on tertiary education.

32 For details of the 10 dimensions of quality at work see: Improving quality in work: a review of recent progress - COM(2003) 728, 26.11.2003.

levels there has been limited progress in other elements of quality at work, including in particular the transitions from insecure to secure jobs, and the issue of reducing labour market segmentation, the level of which is currently on the rise in many Member States. Adult participation in lifelong learning, one of the key indicators for quality at work shows stagnating or even declining trends.

1.3. Social and territorial cohesion

Social cohesion is crucial for sustainable employment growth. In 2007 in the framework of the open method of coordination in social protection and social inclusion, Member States have continued focusing their policies on fighting and preventing child poverty and promoting the active inclusion of people furthest from the labour market through an approach combining income support with activation policies.

In spite of the positive economic environment, in most countries there was no reduction of relative poverty and employment rates increases for vulnerable groups have been more limited than those for the labour force in general. In the EU, the percentage of adults and children living in jobless households has remained unchanged since 2000 at nearly 10%. Social protection reforms should in particular improve, where required, the adequacy of social benefits linked to employment activity. This is a pre-condition for a well functioning flexicurity approach.

The favourable economic environment has had significant impact on the magnitude of regional disparities which continued to narrow in 2006, especially as concerns unemployment. It is still characteristic that regional disparities on unemployment are markedly larger than on employment, but the former has been reduced by one third since 2001. Although this trend is observed in most Member States there is a handful recording a strong negative trend in regional disparities.

2. IMPLEMENTING PRIORITIES FOR ACTION

2.1. Attract and retain more people in employment, increase labour supply and modernise social protection systems

Promote a lifecycle approach to work

Still only very few Member States have a comprehensive lifecycle approach to work.

There has been some recent progress in encouraging active ageing strategies especially through restricting eligibility conditions, while compensating for particularly demanding or hazardous jobs, by increasing incentives to work longer for employees and employees (AT, FR, ES, DK), by enhancing work opportunities for older and particularly disabled workers and by improving working conditions while and providing opportunities for skills upgrading and retraining. The current average exit age from the labour market (60.9) still remains well below the 2010 target.

The progress in the field of gender equality has been mixed. The female employment rate has increased strongly but is still under 50% in 4 Member States (EL, IT, MT and PL). Only some countries (AT, CY, FR, EL, IE, LV, MT, PL, SE, SI)

systematically use statistics broken down by sex for reporting on employment. The gender pay gap shows no sign of reduction over the last few years and is still at 15 % overall in the EU. Few countries have taken concrete actions in this field (AT, BE, FI, FR, LU, NL, SE, SK, UK) and no new targets have been set following the Commission Communication on gender pay gap.

Box: Promoting the labour market integration of young people remains a key challenge

Only about half of the Member States have seen an improvement in youth unemployment between 2000 and 2006. There are still 17.5% of young men and 13.2 % of young women leaving school with at most a lower secondary education. Only six Member States have reached the target of no more than 10%.

Despite relatively poor results, increased efforts to fight youth unemployment are reported by many countries. Policy measures are pursued along 4 axes: Firstly, through improved vocational education and training pathways (AT, BE, LU), specific guidance and pathways for at-risk school leavers (BE, FR, DE, LU) and specific contract schemes with a training component (LU). Secondly, through intensified and personalised guidance and job-search support (PT) and creation of employment pathways (MT). Thirdly, through reduction of employers' social security contributions (BE, HU, SE), tax promotion for apprenticeship places (AT, FR), wage support for recruitment of long-term unemployed (DE). Fourthly, through strengthening the conditionality of social or unemployment benefits (CZ) and reduced taxation of students' jobs (FR)

At the 2006 Spring European Council Member States agreed that they should provide a "new start" for the young unemployed within 6 months by 2007 and 4 months by 2010. . According to the most recent EU data, only 15 countries manage to have a timely new start offered to at least two thirds of young unemployed. In a small lead group of countries nearly all young unemployed are offered a new start during their first months of unemployment (AT, FI, SE). Seven countries have reached an 80-90 % coverage (BE, FR, DE, IE, LT, NL, ES) while 4 countries only provide a 70-80% coverage (HU, LV, LU, PT). For the remaining countries no EU data are available.

The issue of reconciliation between work and private life is gaining some impetus in Member States, mostly through the commitment to improve the provision of childcare facilities (AT, DE, EL, LU, NL, PT, UK). However, many Member States are far from reaching the childcare targets and most do not even refer to them in their national strategies.

Ensure inclusive labour markets, enhance work attractiveness, and make work pay for job-seekers, including disadvantaged people, and the inactive

Efforts have increased in integrating people at the margins of the labour market and in an "active inclusion" approach. Low-skilled job seekers are subject to specific activation measures or support for placement from the employment services (UK), while financial incentives are created for employers to hire them (BG, DE) and train them (NL). Some measures aim at providing specific training opportunities, organised either through public employment services or on-the-job (AT, LT, BG, EE,

BE). A number of Member States have taken steps to develop and improve the programmes for basic literacy and numeracy of adults (FR, DK).

Specific training measures and language courses are being offered to migrants (SE, CY, DK, ES, AT, BE) and activation measures coupled with support from the employment services (DK, ES, DE, AT, EE, UK) are specifically aimed at this group. Wage subsidy schemes for employment of migrants and their descendents have been introduced in SE and DK. Some Member States are taking steps to better integrate children of immigrants into the educational system (LU, NL), while others with large shares of immigrants are launching specific programmes for geographic areas where migrants are highly concentrated (FR, UK). In a number of countries, immigration is seen as an important element in answering labour market needs (ES, DK, IE), and some Member States are planning to develop plans to attract highly skilled migrants (NL, CY, DK, LT), and to simplify the procedures for work and residence permits in sectors where there are labour shortages (SE, IE, AT, FI, EE, MT, BE, CY, DK, ES, LU, SI).

Some Member States have increased spending and raised the effectiveness of their active labour market policies (AT), notably by tightening eligibility conditions for unemployment benefits (EL), increasing the effectiveness of job-search assistance (BE, SK), providing targeted training for the unemployed (AT) and introducing "in-work" benefits (SE). Some Member States also subsidize self-employment (DE, LT, EL, SK, LV). An increasing focus is on the individual responsibility of job seekers (BE, MT, NL, SI, LU, UK, SE, DK, HU), with increased conditionality of unemployment benefits, increased monitoring of their job searching activities and in some cases their contracts concluded between job seeker and employment service defining rights and mutual obligations. The local or regional dimension of activation is often emphasized, and many Member States aim at improving the internal cooperation between the different agencies serving job seekers (NL, MT, HU, IE, SK). However, Member States rarely report on the "new start" target for unemployed, nor the activation target for long-term unemployed.

Some countries have lowered tax wedges in order to foster participation rates and job creation either through general tax reductions, mainly focused on cutting the tax-wedge on low income groups (AT, FR, HU, SI, CZ, IT, MT, LT, SE), or by a straight reduction of the tax burden on low incomes (DK, FI, GR,NL, SL). Also, a general trend towards reducing social security contributions for both employers and employees was recorded over recent years (BE, SE, MT). .

Financial incentives are being created to increase the readiness of people with a disability to take up work (IE, EE, SK), while subsidies are given to employers to hire disabled people and to adapt their workplace to their needs (NL, SE, PL, IE, SI, AT, BG, LV). Measures are also being taken to establish and develop guaranteed jobs and supported employment opportunities (CZ, DK, ES, SE, SI, DE, LT, SK).

Improve the matching of labour market needs

Adaptation to economic change is stated as a relevant priority for all Member States, although addressed through different tools at the level of the Public Employment Services. Different areas have seen particular investments: training and vocational qualifications (EE, IE, SI); skills upgrades (DK, PT, CY, IE) and involvement of

employers (EL, IT, UK); taxation measures to address disadvantaged social groups (FR, FI); targeted services according to age group, education/qualification levels and greater exposure to the risk of exclusion (PT); extension to a personal assistance scheme and reinforcement of services for people with disabilities (SK); work-life balancing (CY); actions for female and senior workers (LT) or young people (PL, SE); public-private partnerships (BE, IT[33]).

However, with very few exceptions (BE, IT in particular), not much progress on trans-national mobility has been achieved across Member States. Conversely, concerning the anticipation of skills needs, several Member States (AT, EL, LT, LV, MT, PT) are building infrastructures to forecast labour market needs and skills shortages.

2.2. Improve the adaptability of workers and enterprises

Promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of social partners

Whereas promoting the adaptability of workers and enterprises received little attention in the first year of the new cycle launched in 2005, a careful examination shows that the political prioritisation by the European Council and the wide debate since then on flexicurity has brought about an important turn-around, and increased the awareness of the benefits that flexicurity policies can bring. Flexicurity is now acknowledged throughout the EU as a key approach to make labour markets more responsive to the changes resulting from globalisation, as well as to reduce labour market segmentation.

Box 2: The increasing role of flexicurity

About half of the Member States have now developed or are developing comprehensive flexicurity approaches, and combining efforts on contractual arrangements, lifelong learning, active labour market policies and social security systems. This is a considerable improvement from only a handful in 2006. Various Member States are reporting on their intentions, including initiatives to develop national flexicurity pathways, seeking cooperation with or input from their social partners (for example AT, FI, IE, IT, SI, FR).

On July 23rd 2007, the **Italian** Government signed an agreement with the Social Partners on social protection, employment, competitiveness and sustainable growth. The agreement covers the areas of pensions, social benefits, contractual arrangements, work incentives, labour cost, and training. The agreement includes steps towards a more universal coverage of social protection, independent of the specifics of work contracts. It envisages limiting repetitive fixed term contracts, promoting 'long' part-time contracts and improving protection of workers on on-call contracts.

[33] The Italian NRP dedicates a specific section to PES and to the assessment of their reform process over the last 7 years.

Flexicurity measures are being implemented along two lines. On the one hand, measures are being pursued to strengthen flexibility in order to make labour markets more dynamic and responsive to change, both through internal and external flexibility instruments. SI, EL, BG, RO for instance report on how they wish to promote part-time employment. SK, PL, LU, LT, RO introduced tele-working as a new form of work providing more flexibility. In some countries, the regulation of permanent work contracts is allowing for more flexibility. Changes in employment protection legislation (EPL) for workers on open-ended contracts are relatively scarce. In LV, BG, NL, RO, attempts are being made to simplify EPL although political outcomes are sometimes uncertain.

Initiatives are also underway in several countries to extend security. Labour code reviews are quite frequent (AT, BG, CY, CZ, EE, FI, FR, HU, IT, LT, LU, NL, PL, PT, RO, SK, SI, SE) but their character seems to be gradually changing. They are tending to move away from focusing on increased flexibility through the introduction of new types of contracts, and towards a more balanced approach including more security for workers on temporary contracts. MT, SK, HU, NL, CY, IE, IT are improving social protection provisions for workers in part-time or fixed-term contracts. The regulation of temporary agency work is a policy focus in FI, AT, BG. Some countries aim to limit the consecutive use of fixed-term contracts (CZ, FI, IT, NL).

A move from passive to active labour market policies is slowly taking shape (e.g. by increasing job search support, benefit conditionality or by reforming tax and benefit systems to "make work pay"). Transition security for workers on open-ended contracts is not really recognised as an issue. The traditional attitude, concentrating on job security rather than on a broader concept of employment security, is still very much alive though policy efforts are restricted to the management of larger company restructurings. Standardised support for all workers faced with dismissal still remains to be implemented (SE, FI, LU).

Targeting segmentation is also an explicit goal in some countries, with for instance ES creating incentives for employers to transform time-limited contracts into permanent ones. On the whole, however, segmentation of labour markets remains to be addressed, especially for female workers, still affected by low quality jobs and weaker employment and social security. Between 2000 and 2006, the share of workers on temporary contracts in EU27 rose from 12.2% to 14.1%, whereas the share of workers on part time contracts rose from 16.4% to 18.1%. A high level of undeclared labour is another aspect of segmentation (IT, EL, SK, HU, LV, LT, SI, RO, BG). Most countries suffering from high levels of undeclared work are paying attention to this concentrating on reinforcing labour inspectorates or other control or surveillance measures and incentives to legalise labour relations (HU).

Policies aiming to modernise work organisations receive rather little attention in Member States (e.g. FI, IE, SE, LT, and LU). Innovations in working time management are most widespread (DE, LU). Only few countries are developing a comprehensive vision of high quality workplaces, combining greater demands and responsibilities on workers with increased autonomy at work (FI, SE).

Ensure employment-friendly labour cost developments and wage setting mechanisms

Employment-friendly policies should support wage developments in line with productivity in order to achieve high employment and contain inflation. Member States are largely successful in ensuring this balance. Wage flexibility is not widely addressed, although some countries, in cooperation with their social partners, promote wage settlements that reflect productivity differentials at company level. Efforts to reduce non-wage labour costs are widespread, and focus in particular on young people and workers with disabilities.

2.3. Increase investment in human capital through better education and skills

Expand and improve investment in human capital

Investing in human capital to achieve efficient and equitable outcomes is still a challenge in most Member States. Total public expenditure on education as a percentage of GDP increased in the EU between 2000 and 2003 from 4.7% to 5.2%, but then decreased again to 5.1% in 2004. Similarly, progress on private expenditure on educational institutions as a percentage of GDP slowed down in 2004. The European Social Fund (ESF) will invest around 34.3 billion EUR in improving human capital and life-long learning systems in the current programming period.

Most countries have made progress in defining comprehensive lifelong learning strategies covering all systems and levels of education and training. It is essential that those countries that have not yet adopted a lifelong learning strategy do so urgently. All countries have measures addressing the areas for which EU benchmarks have been set: reducing the number of early school leavers, and improving secondary attainment and increasing adult participation in lifelong learning. However, most countries have not set quantitative national targets (BE, DK, EE, EL, ES, FI, FR, HU, IE, LT, LV, MT, NL, PL, PT, RO, SI, SK, RO have) and the modest progress visible since 2000 is not sufficient to reach the EU targets set for 2010.

Every sixth young person (15.3%) aged 18-24 in the EU-27 still leaves school with no more than lower secondary education (male: 17.5%, female: 13.2%) and does not participate in any kind of education and training after this. Progress has so far not been sufficient to reach the EU benchmark of 10% by 2010. Several countries (ES, IT, MT, PT) still had very high levels (above 20%) in 2006 and in some countries performance has actually worsened since 2000 (ES, LU, SE, SK). Similarly, there has been some progress in improving upper secondary attainment levels, but not enough to achieve the objective of at least 85% of 22-years-olds to complete at least upper-secondary education by 2010.

Also adult participation in lifelong learning is no longer on track to achieve the EU benchmark of 12.5% by 2010. In 2006, an average of 9.6% of Europeans aged 25-64 was participating in education and training activities (men: 8.8%, women 10.4%), which is slightly less than in 2005. The participation rate remains lower for inactive and unemployed persons, for older persons, and for persons with low educational attainment. The participation of older workers is still only half of the overall rate and adults with a high level of education are still more than six times as likely to participate in lifelong learning as the low skilled.

A large part of the policy-making is focused on finding ways to encourage employers to invest in training and motivate employees to take part in it. Several Member States also see it as a particular challenge to motivate the less-educated and middle-aged part of the workforce to acquire new skills. Many measures imply financial incentives through tax reduction or grants for employers investing in training (MT, EE, BG, DE, NL, IE, DK, BE, LV), but some countries have also taken initiatives to simplify the conditions for educational leave (AT, LU). The role of agreements among social partners about the implementation of lifelong learning strategies is emphasized and stressed by some Member States (DK, FR, PL, NL).

Adapt education and training systems in response to new competence requirements

There is evidence suggesting that early education is receiving increasing attention in many Member States particularly in establishing the basis for learning throughout life and in facilitating access to education of citizens with a less favourable socio-economic background, and migrants. Some are working on teaching content (DE, DK), quality assessments (ES, LT), building the capacity of pre-primary teachers (CZ) and increasing their numbers (DK, HU, MT, NL, SE, SK, UK). Others are extending compulsory schooling to parts of the pre-primary level (CY, DK, EL, PL). Strengthening pre-primary education is a key measure to improve the efficiency and equity of education and training systems.

National qualifications frameworks in line with the European Qualifications Framework are being developed by the majority of countries (AT, BE, BG, CZ, DE, DK, EE, ES, FI, HR, HU, IT, LT, LU, LV, NL, PT, SI, SK), with a view to facilitating international mobility as well as the transition between different education and training sectors . They are an important means for ensuring flexible learning pathways which are also facilitated by many countries setting up systems for the validation of non-formal and informal learning (AT, BE, CZ, ES, IT, LT, LU, PL, RO, SE, SK, UK). The challenge here is to move from experiment to full application of such systems in national qualifications systems, including in access to higher education

These improvements are running in parallel with a greater focus on learning outcomes in learning programmes and qualifications which increases the relevance of both vocational education and training and higher education for the labour market. Despite renewed emphasis on apprenticeship and work-based learning, further work must be done to improve the quality and attractiveness of vocational education and training.

Little progress is visible in forecasting future skills and qualifications needs, despite the efforts made by some countries to improve their infrastructures (AT, EL, LT, LV, MT, PT). More also needs to be done by Member States to facilitate international mobility. Mobility is still much more widespread in higher education than in vocational education and training.

Given that the quality of teacher education is a prime factor influencing student performance, more attention must also be given to teacher education and training, in particular to continuing teacher training and professional development.

Finally, a number of countries are developing centres of excellence in higher education (DE, EE, EL, FI, UK), but more needs to be done to address education alongside research and knowledge transfer in the context of such initiatives, and to improve university-business cooperation.

IV. THE GENERAL APPROACH USED BY THE EUROPEAN COMMISSION TO ASSESS PROGRESS WITH STRUCTURAL REFORMS

The renewed Lisbon strategy marked a major change in the approach to the co-ordination of structural reforms in the EU. A "partnership approach" between EU and national authorities has been pursued to tackle the implementation gap between reform commitments and concrete actions. Based on 24 Integrated Guidelines, Member States in a bottom up exercise adopted National Reform Programmes covering the period 2005-07 period in which they themselves identified their "key challenges" to raise the growth potential. There is also an annual reporting and peer review process, which led to the adoption of policy recommendations in February 2007 by the Council which pointed to areas where good progress has been made as to areas where reform efforts as lagging. The recommendations were graduated with "country-specific recommendations" (CSRs) addressed to countries on policy areas where little progress was made and "points to watch" on policy areas where only some progress was made.

The main focus of attention within the current Strategic Report is on implementation. While account is taken of overall progress achieved since the re-launch of the Lisbon Strategy in 2005, the assessment mainly considers 2007 with a particular emphasis on tracking Member States' responses to country-specific recommendations (CSRs) or points to watch (PTWs) adopted by the Council in April 2007. The Commission attaches considerable importance is attached to having a robust and transparent framework for assessing progress with structural reforms which is comparable across policy areas and Member States. The main elements of the approach used by the Commission to arrive at its policy recommendations are outlined in the box below.

It should be underlined that given the relatively short period since the re-launch of the Lisbon Strategy, and given the inevitable time lags in adopting reforms and for them to have an impact on the real economy, the assessment essentially remains a tracking exercise which catalogues planned and enacted reform actions. There is only limited scope to evaluate in-depth the significance of reform measures or to quantify their impact on growth and jobs (although this is part achieved via a thematic review exercise on specific policy areas carried out by the Economic Policy Committee and the Employment Committee) Over time, the Commission will strive to enhance the evaluation exercise upgrade so that there are more multi-annual in character, and include a greater reliance on quantitative as well as qualitative analysis that is supported by modelling results.

The Commission services are investing considerable resources in developing robust methodologies for systematically identifying the key policy challenges facing Member States and for evaluating the impact of structural on growth and jobs. Much of this work is being carried out jointly together with national authorities via a Lisbon methodology working group (LIME) attached to the Economic Policy Committee[34]. Progress has already been made which has supported the assessment in the Strategic Report. In particular, most Member States have attached "streamlined reporting tables" to their National Implementation Reports submitted to the Commission in October 2007: these tables systematically report the relevant reform measures that according to the Member State contribute to the Lisbon process, and offer the

[34] See European Economy Research letter No 1., April 2007, http://ec.europa.eu/economy_finance/publications/researchletter_en.htm

potential of greater transparency on structural reform developments in real time. In addition, the Commission has made considerable progress in developing institutional databases that catalogue enacted structural reforms in a comprehensive and comparable manner across Member States. The LABREF database, which records information on enacted labour market reforms, has been backdated to 2000 and is starting to be actively used for analytical and surveillance purposes[35]. The MICREF database collects similar information on reforms falling under the microeconomic pillar of the Integrated Guidelines.

The approach used by the Commission to assess progress with structural reforms in the Strategic Report

In assessing progress with structural reforms, the European Commission took account of all relevant information at its disposal, including the information contained in the National Implementation reports submitted to the European Commission in 2007 along with the streamlined reporting tables. In broad terms, three considerations were taken into account when arriving at policy conclusions, and in particular whether a CSR or PTW should be issued to a Member States to signal the need for more progress in a specific policy area. They are:

- the ***performance of a Member State in different policy areas***: more weight will be attached to countries where the starting level of performance is poor or lagging. In doing so, relevant policy and performance indicators are considered

- the ***adequacy of the policy response***. This is the core element making use of information on structural reforms gathered from Lisbon missions and the National Implementation Reports. In doing so, the *degree of responsiveness* (whether a policy response has been approved and passed all the necessary legislative/administrative procedures to start being implemented) is considered, the *significance of a policy measure* (e.g. do they address core underlying problems, does the reform imply a significant change relative to existing institutional settings, has an adequate allocation of financial and personnel resources been foreseen to implement the policy, are targets/goals realistic), and the *degree of follow-up* (e.g. whether the design of the policy response foresees monitoring mechanisms);

- the ***relative priority of a policy area in terms of its potential contribution to growth and jobs in the country concerned***. The aim is to have a rounded view on the overall economic policy challenges facing a country, and to concentrate on those policy areas where countries are especially lagging behind the best-performer and which can contribute most to raising growth and jobs. In most instances, the priorities are well defined in the key challenges identified by Member States.

Overall, by looking at performance, policy responses and priorities, a robust and transparent assessment is arrived at which is comparable across policy areas and Member States. Naturally, all other relevant qualitative considerations, including wider political issues, are also taken into account.

[35] For access to the LABREF database, follow:
http://ec.europa.eu/economy_finance/indicators/labref_en.htm
The information in LABREF has been used to feed into economic analysis on the impact of labour market reforms, see papers from a Commission conference in March 2007on tracking and evaluating the impact of labour market reforms in Europe
http://ec.europa.eu/economy_finance/events/2007/events_brussels_1403_en.htm .

V. THE EUROPEAN GROWTH INITIATIVE

The European Action for Growth (or European Growth Initiative[36]) is an action plan endorsed by the European Council in December 2003. It aims at stimulating the long-term growth potential and the innovative capacity of the European Union by mobilising investment in transport, energy and electronic communication networks, and in research, development and innovation, with a particular focus on growth-enhancing technological areas.

At the European level, the initiative is supported by non-financial measures to improve the regulatory, administrative and financial environment for investment, as well as Community financial support, lending from the European Investment Bank (EIB) and venture capital from the European Investment Fund (EIF)[37], and innovative financing tools to mobilise private investment. At the Member States' level, it relies on supporting national actions to promote private investment, and on significantly redirecting public funding towards the areas of the initiative with a special emphasis on infrastructure investments.

In order to focus efforts on key investment projects of European interest, the Commission identified a list of TEN infrastructure projects and R&D technological areas, considered as sufficiently mature to be turned into action in the short run. This process was carried out in close collaboration with the EIB and was based on the explicit intentions of the Member States. The selection criteria included, in addition to project maturity, their trans-frontier dimension, the impact on growth and on innovation in an enlarged EU, and benefits for the environment. The "Quick Start programme" was endorsed by the European Council in December 2003. It was foreseen that the list might be updated, in the framework of the annual cycle for reporting to the Spring European Council, if other projects fulfilled the same criteria[38].

The Commission and the EIB were asked to provide a mid-term evaluation of the initiative by the end of 2007, on the basis of the following criteria: (i) effects on growth; (ii) impact on the internal market and cohesion in the enlarged EU; (iii) mobilisation of private sector capital, (iv) acceleration of the implementation of TENs and innovation and R&D projects including environment projects; (v) progress in reducing regulatory barriers; (vi) the impact on the environment and employment."

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36 This is an extract of the Commission Staff Working Paper "Mid-term review of European Action for Growth - Stocktaking on progress of the implementation of the European Action for Growth" - SEC(2007) 1695, 11.12.2007

37 The European Investment Fund (EIF) is part of the EIB group

38 The 31 Quick Start projects in the area of transport and the 17 projects in the area of energy are key sections of the TEN-T and TEN-E priority projects whilst the 8 projects related to electronic communications and knowledge reflect R&D, innovation and eEurope priorities within the Lisbon strategy for Growth and Jobs.

1. THE IMPROVED FRAMEWORK FOR INVESTMENT – PRELIMINARY RESULTS

1.1. Developments at European level

Almost all legislative measures identified by the Growth Initiative as necessary to improve the conditions for investment have been adopted and have entered into force (e.g. the TEN guidelines and financing rules, the Euro-vignette and cross-border mergers directives). They aim at facilitating investment in large-scale or complex cross-border infrastructure projects, and in research and innovation partnerships.

The Growth Initiative has given some initial impetus to set up new instruments and initiatives coordinating better funding from public sources and encouraging private investment in networks and R&D and innovation (e.g. nominating European coordinators for transport and energy priority projects, establishing Joint Technology Initiatives on nano-electronics and hydrogen and fuel cells).

The areas highlighted by the Initiative have benefited from significant funding over 2000-2006 and from increased budgets for the 2007-2013 period via the TEN-T and TEN-E programmes, the Structural and Cohesion funds, the 6th and 7th research framework programmes and the eTEN and Competitiveness and Innovation Programme.

The EIB has been actively engaged in supporting the Growth Initiative as well as the Lisbon reforms through increased lending facilities, the strengthening and development of financial instruments (e.g. the TEN investment facility), and the provision of technical expertise.

The EIB and the Commission have jointly developed new financial instruments, at least in part as a result of the commitments made in the Growth Initiative (e.g. the Loan Guarantee Instrument for TEN-transport LGTT, the Risk Sharing Finance Facility RSFF and the JEREMIE and JASPERS funds). The Member States look forward to using these new instruments to leverage private investments and improve access to risk capital.

1.2. Developments at national level

20 Member States replied to the Commission information request on the Growth Initiative and related infrastructure investments (Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Lithuania, Luxembourg, Poland, Portugal, Slovak Republic, Spain, Sweden, and the UK). The information provided is mostly qualitative but gives an insight on the national investment context onto which the Growth Initiative has developed its effects. As public infrastructure spending is commonly included in long-term strategies, it was difficult to analyse the influence of the Growth Initiative with a limited hindsight.

Public investment in transport infrastructure has accelerated in recent years in most Member States.

Investment in energy infrastructure is mainly market-driven. The need to modernise energy infrastructures and to better integrate national networks into the EU market is

prompting investments in most Member States. The promotion of energy efficiency and renewable energies, a new priority in many countries, also steadily necessitates high investment level. Increased demand for mobile communication services enables the private sector to invest in upgrading the networks to provide innovative high speed mobile services.

Investment into ICT networks serving scientific needs presenting important public good characteristics continue to be partly financed by national budget. The Member States have renewed their commitment to develop spatial technologies from which a wealth of applications with commercial or public services purposes will grow. Hydrogen technologies and nanoelectronics have also gained a priority position in the list of projects up for public R&D investment at the national level and national research capacities in these key areas for long term growth and sustainability have been reinforced.

1.3. Progress on the implementation of the Quick Start Projects

The improved enabling framework both at the European and the Member States level including the availability of financing has had significant knock-on effects on the implementation of the Quick Start projects. However, these effects fell significantly short of expectations voiced back in 2003, namely with respect to transport infrastructure projects.

The Quick Start transport projects are sections of the TEN-T large priority projects identified by the TEN Guidelines. They are spread over the entire territory of the EU, including a majority of railway links, some road and waterway links, as well as motorways of the sea, and the Galileo system. Some progress has been made in the implementation of these projects, but the overall picture remains mixed. The new instruments put in place by the TEN-T guidelines and financial regulations have played a role in unlocking some problematic areas. The new financial instruments have just become operational in 2007, so their effects on the implementation of TENs and mobilisation of private investment will be felt in the coming years only.

Progress in completion of electricity connections has remained generally slow, hampering the development of an efficient internal market, as shown in the Commission Communication on the Priority Interconnection Plan adopted in January 2007. This overall assessment applies to the Quick Start projects as well as to other projects of European interest. The main cause for delay is often not the lack of financing but the complexity of coordinating planning and authorisation procedures between several Member States. Conversely, the completion of the Quick Start gas pipelines has proceeded satisfactorily, and none suffers from significant delays.

The substantial financial support mobilised on Quick Start ICT projects from a combination of different sources of funding is one of the actions making tangible the commitment of the EC and the Member States to speed up the delivery and the use of high capacity communication networks. This continued commitment is already living up to its expectations: creating improved access to ICT networks offering new ways of creating and sharing knowledge for work, research and leisure.

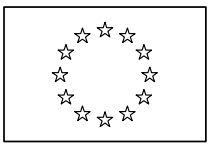
For all Quick Start R&D projects, investments decisions proceed according to the initial plans, while a tight integration of funding from different sources is clearly

taking place. The support to Nanoelectronics projects is in line with the original targets of the Initiative. Adequate funding has been made available to set up the next generation laser infrastructures key for Europe's research. Funding hydrogen and fuel cell research at European level is playing, as expected, an important role reinforce coordination between various sources of funding. Finally it is at least partly due to the Growth Initiative if the critical mass of public and private resources (both financial and technological) has been quickly and timely assembled to finalise the design of the GMES satellites and to install a new spatial launch site.

2. THE GROWTH INITIATIVE WITHIN THE LISBON STRATEGY FOR GROWTH AND JOBS

The European Growth Initiative operates on an instrumental level but within the Lisbon Strategy's comprehensive approach.

The measures proposed in the European Growth Initiative are now being brought at full speed by the Lisbon Strategy for Growth and Jobs. To name but a few examples, improving the patent system in Europe, as longed for by the European Growth Initiative, was taken over in 2005 as a key policy issue of the Strategy for Growth and Jobs. The i2010 initiative, a European Information Society for Growth and Employment addresses the challenges also mentioned in the European Growth Initiative, but it is fully developed under the Lisbon Strategy. The European Growth Initiative emphasised the need for updating the rules applied to State aid for R&D and innovation to make them more conducive to investments. The new framework on state aid for R&D and innovation has been adopted under the impetus of the Lisbon Strategy where state aid control is a prominent issue. The Growth Initiative hinted at the need for measures on risk capital investment to improve SMEs' access to finance especially for innovation. These measures have actually been launched under the main thrust of the Lisbon Strategy. In future, the instruments and projects of the Growth Initiative will be merged even further in the Lisbon Strategy, with corresponding repercussions for reporting on progress of implementation.



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 11.12.2007
COM(2007) 803 final
PART IV

Recommendation for a

COUNCIL RECOMMENDATION

on the 2008 up-date of the broad guidelines for the economic policies of the Member States and the Community and on the implementation of Member States' employment policies

(presented by the Commission)

EXPLANATORY MEMORANDUM

In 2005, the Lisbon Strategy was streamlined and renewed and the focus placed firmly on growth and employment. New governance structures were established, with a clear division of responsibilities between the Community and the national levels. As part of this, all Member States drew up three-year National Reform Programmes setting out their response to the particular challenges facing them.

In its 2006 Annual Progress Report[1], the Commission assessed the National Reform Programmes, pointed out their strengths and weaknesses and asked Member States to make improvements where necessary. The 2006 Spring European Council welcomed this assessment and urged Member States to implement their National Reform Programmes with vigour. It also identified four priority areas: investing more in knowledge and education; unlocking business potential, especially of SMEs; increasing employment opportunities for priority categories; and an integrated energy policy for Europe. In each one of these areas, it agreed a number of specific actions which it urged Member States to implement by the end of 2007.

In October 2006, Member States presented their first reports on the implementation of their National Reform Programmes. Based on these implementation reports, the Commission prepared the 2007 Annual Progress Report[2]. This contained a detailed assessment of the progress made and took account of the work carried out by the Council on selected themes. In the light of this assessment, and following the requests made by the Council to rely more on Treaty-based instruments in the implementation of the renewed strategy, the Commission decided in 2007 to propose guidance to Member States in the form of country specific recommendations under Articles 99(2) and 128(4) of the Treaty. These were subsequently endorsed by the European Council and adopted by the Council on 8 and 9 March 2007.

Implementing structural reforms requires focus and continuity. Since the country-specific recommendations and 'points to watch' have only been adopted recently, and given that it takes time to implement structural reforms and see results, the Commission's proposes to maintain the current set of recommendations largely unchanged and to fine-tune them in the light of progress made since their adoption.

Romania and Bulgaria have been fully integrated into the Lisbon Strategy following their accession to the European Union on 1 January 2007. Both have submitted national reform programmes. The Commission's proposal for Council recommendations, therefore, covers both countries.

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1 COM(2006) 30.

2 COM(2006) 816.

Recommendation for a

COUNCIL RECOMMENDATION

on the 2008 up-date of the broad guidelines for the economic policies of the Member States and the Community and on the implementation of Member States' employment policies

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 99(2) and Article 128(4) thereof,

Having regard to the recommendation from the Commission,

Having regard to the conclusions of the European Council on 8 and 9 March 2007,

Having regard to the opinion of the Employment Committee,

Whereas:

(1) The Council adopted in July 2005 a recommendation on the broad guidelines for the economic policies of the Member States and the Community (2005 to 2008)[3] and a decision on Guidelines for the employment policies of the Member States[4], which together form the "Integrated guidelines for growth and jobs". Member States were invited to take the integrated guidelines for growth and jobs into account in their national reform programmes (NRPs).

(2) Member States submitted their NRPs by October 2005, which the Commission assessed and reported on in its contribution to the 2006 Spring European Council.

(3) The 2006 Spring European Council took note of these documents and identified four priority areas (R&D and innovation, business environment, employment opportunities and an integrated energy policy) within which it agreed a limited number of specific actions which it urged Member States to complete before the end of 2007.

(4) In accordance with the conclusions the 2006 Spring European Council, the Member States presented annual reports on the implementation of the national reform programmes (implementation reports). These were analysed by the Commission, which presented its findings in the 2007 Annual Progress Report[5].

(5) On the basis of this analysis, a number of country-specific recommendations were issued to the Member States in 2007. In order to pursue the Lisbon strategy for growth

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3 OJ L 205, 6.8.2005, p. 28.
4 OJ L 205, 6.8.2005, p. 21.
5 COM(2006) 816, Part II.

and jobs in a coherent, integrated manner, these recommendations were adopted in a single instrument[6]. This approach reflected the integrated structure of the NRPs and Implementation Reports, as well as the necessary consistency between the employment guidelines and the Article 99(2) broad economic policy guidelines, as underlined in Article 128(2).

(6) The Commission analysed the response to the recommendations as presented in the 2007 Implementation Reports of the Member States, and has presented its analysis of this response in the Strategic Report[7]. On the basis of this analysis, and recognising that it takes some time to implement structural reforms, this document provides a proposal to largely maintain these recommendations, fine-tuning them in light of progress made since their adoption in spring 2007.

(7) To fully implement the Lisbon strategy for growth and jobs, this recommendation should also contain specific recommendations to the Member States belonging to the euro area.

(8) In order to reinforce co-ordination of reforms and enhance the multilateral surveillance process in Council, Member States should include action plans in their annual implementation reports, setting out their specific policy responses to the country-specific recommendations and 'points to watch'.

(9) The European Parliament has adopted a resolution regarding this Recommendation,

HEREBY RECOMMENDS that Member States should take action along the lines set out in the Annex and report on their follow up in their next implementation reports in the framework of the renewed Lisbon strategy for growth and jobs.

Done at Brussels,

For the Council
The President

[6] COM(2006) 816.
[7] COM(2007) 803.

ANNEX

TABLE OF CONTENTS

EXPLANATORY MEMORANDUM 2

COUNCIL RECOMMENDATION 3

BELGIUM 8

BULGARIA 9

CZECH REPUBLIC 11

DENMARK 12

GERMANY 13

ESTONIA. 15

IRELAND 15

GREECE 16

SPAIN 18

FRANCE 19

ITALY 20

CYPRUS 22

LATVIA 23

LITHUANIA 24

LUXEMBOURG 25

HUNGARY 26

MALTA 28

THE NETHERLANDS 29

AUSTRIA 30

POLAND 31

PORTUGAL 33

ROMANIA 35

SLOVENIA 37

SLOVAKIA 38

FINLAND 40

SWEDEN 41

UNITED KINGDOM 42
EURO AREA MEMBER STATES 43

BELGIUM

1. In the light of Belgium's 2007 Implementation Report and the Commission's assessment of progress made to implement key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Belgium has made good progress in implementing its National Reform Programme over the 2005-2007 period. Belgium has shown some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows some policy response to the Council recommendations, but further reform is still necessary. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Among the strengths shown by the Belgium's 2007 Implementation Report are the emission reduction policies and the promising results of the guidance and monitoring system of unemployed people.

5. The policy areas in the Belgian National Reform Programme where challenges need to be tackled with the highest priority are reducing the tax burden on labour whilst strengthening fiscal consolidation and improving labour market performance. Against this background it is recommended that Belgium:

   - continues efforts to further reduce the tax burden on labour towards the average of its neighbouring countries, especially by reducing the tax wedge on low skilled workers, while strengthening fiscal consolidation;

   - reinforces the policy measures to improve the performance of its labour market through a comprehensive strategy, in accordance with an integrated flexicurity approach, to enhance labour market participation, lower regional disparities, and increase participation in lifelong learning.

6. In addition, it will be important for Belgium to focus on the following challenges: to fully implement the strategy aiming to ensure the long term sustainability of public finances, including expenditure restraints, fiscal surpluses, and a persistent reduction of government debt; urgently take further measures to improve competition in gas and electricity markets, including through independent and effective regulators and additional measures concerning transmission and distribution operators; to increase substantially its commitment to stimulating R&D and innovation notably by increasing both the level and impact of public funding and developing a coordinated policy mix at all levels; continuing the implementation of the measures to increase the employment rate for older workers and vulnerable groups, monitor their impact and, if need be, take further activation measures.

BULGARIA

1. In the light of Bulgaria's 2007 Implementation Report and the Commission's assessment of its National Reform Programme and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Overall, the National Reform Programme focuses on the right challenges, but in some areas lacks concrete and substantial measures in particular as regards strengthening administrative capacity. Furthermore the National Reform Programme lacks measures aimed at urgently and significantly reducing red tape to make the business environment more dynamic and competitive. Given the growing economic imbalances it is particularly important for Bulgaria to accelerate the implementation of its National Reform Programme in order to create the necessary conditions for sustainable growth and jobs in the medium to longer term.

3. The National Reform Programme's strengths include a clear problem analysis and right prioritisation and sequencing of reforms as well as strong political ownership. Important provisions for a tight monitoring of progress at the highest political level have been put in place, which should prove an effective tool for ensuring a rapid and effective implementation of the National Reform Programme. The National Reform Programme is furthermore underpinned by a tight fiscal policy which offers a solid basis for accelerating the needed structural reforms to ensure long-term growth.

4. The policy areas in the Bulgarian National Reform Programme where challenges need to be tackled with the highest priority and budgetary impacts of measures and details on the monitoring and evaluation procedures should be clearly spelled out are: administrative capacity; macro-economic imbalances; red tape; and the functioning of the labour market. Against this background, Bulgaria is recommended to:

   - urgently strengthen administrative capacity in particular focus on key government functions, including regulatory authorities, and the judiciary;

   - contain the growing current account deficit and inflationary pressures, in particular by a tight fiscal policy, improving the quality of public expenditure and promoting wage moderation in order to keep wage developments in line with productivity gains;

   - take rapid measures substantially to cut red tape and shorten procedural delays in order to improve the business environment (in particular for SMEs and facilitating start-ups), which will also help in the fight against corruption;

   - increase the quality of labour supply and the employment rate by improving the efficiency and effectiveness of active labour market policies and further reform the education system to raise skills to levels that better match labour market needs and reduce early school leaving.

5. In addition, it will be important for Bulgaria over the period of the National Reform Programme to focus on: taking further measures to ensure the long-term sustainability of public finances, in particular with regard to potential risks in terms of adequacy and sustainability of pensions; creating all necessary pre-conditions for strong competition in network industries; elaborating an integrated policy for R&D

and innovation notably aimed at reforming the public R&D system, shifting public support to R&D- based on an overall R&D intensity target for 2010- towards more competitive funding focused on key priorities; tackling undeclared work by strengthening institutional capacity to perform inspections and ensure legal enforcement; completing the lifelong learning strategy and increasing participation.

CZECH REPUBLIC

1. In the light of the 2007 Czech Republic Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. The Czech Republic has made some progress in implementing its National Reform Programme over the 2005-2007 period. The Czech Republic had made some progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas.

3. The Implementation Report shows some policy response to the recommendations adopted by the Council. There has been some policy response on the additional areas requiring attention, as identified in the Council conclusions.

4. Among the strengths shown by the 2007 Czech Republic Implementation Report are the coherent strategy to improve the regulatory framework for enterprises, reforms to make work pay, of the curricula for primary and secondary education, to increase participation in tertiary education, and the adoption of the lifelong learning strategy.

5. The policy areas in the Czech Republic National Reform Programme where challenges need to be tackled with the highest priority are the long-term sustainability of public finances in the context of an ageing population, fulfilling the commitments for public R&D expenditure and further increasing its effectiveness, improving security and flexibility in the labour market, improving the efficiency and equity in education and training and increasing participation in lifelong learning. Against this background it is recommended that the Czech Republic:

   - with a view to improving the long-term sustainability of public finances, implements the announced reform programme of the pension system without delay, and implements reforms announced in the healthcare system;

   - meets the targets for public R&D expenditure and increases its effectiveness, notably by promoting a better collaboration between business, universities and public R&D institutions, and by providing the necessary human resources for research and development;

   - within an integrated flexicurity approach, further modernises employment protection, including legislation, improves the efficiency and equity of education and training, especially its responsiveness to labour market needs, provide incentives to invest in training particularly for older workers and the low-skilled, and increases the diversification of tertiary education supply.

6. In addition, it will be important for the Czech Republic to focus over the period of the National Reform Programme on the following challenges: improving the protection of intellectual property rights; speeding up progress in the ICT area, including by implementing and monitoring a fully enabled legal environment for e-government; improving access to finance for innovative companies, in particular through further developing the venture capital market; increasing the coverage of entrepreneurship education; better integrating disadvantaged groups into the labour market; reducing regional disparities; reconciling work and family life; tackling the gender pay gap; and implementing the active ageing strategy.

DENMARK

1. In the light of the 2007 Danish Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Denmark has been making very good progress in implementing its National Reform Programme over the 2005-2007 period. Denmark has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a good policy response to the areas identified by the Council as requiring attention.

4. Among the strengths shown by the 2007 Danish Implementation Report is the comprehensive and integrated approach to reform planning and implementation, within a framework for ensuring long-term fiscal sustainability, combined with the active participation of stakeholders.

5. It will be important for Denmark over the period of the National Reform Programme to focus on the following challenges: continuing to implement measures on energy interconnection in order to improve the functioning of the electricity and gas markets; increasing labour supply and hours worked over the medium term, including further initiatives to work and additional steps to integrate older workers, immigrants and their descendants into the labour market; reinforcing, in a cost-effective manner, measures to improve primary and secondary education and the number of students finalising upper-secondary or tertiary education to reach the ambitious targets set.

GERMANY

1. In the light of Germany's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Germany has made good progress in implementing its National Reform Programme over 2005-2007 and good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows that there has been some policy response to the recommendations adopted by the Council. There has been a good response in consolidating public finances, and a more limited response regarding competition in services and on tackling structural unemployment. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Among the strengths shown by the 2007 German Implementation Report are: the consolidation of public finances; the strengthening of high-class research and innovation; the progress in tackling youth unemployment; and the determined approach to increasing childcare facilities.

5. The policy areas in the German National Reform Programme where challenges need to be tackled with the highest priority: are competition in services and structural unemployment. Against this background it is recommended that Germany:

   - improve the framework for competition in services, notably by continuing to relax restrictive rules in regulated trades and professions, improving public procurement procedures, without exempting new telecom markets from regulation and effectively regulating wholesale bitstream access;

   - tackle structural unemployment by maintaining the path of the reforms outlined in the National Reform Programme. Focus should be placed on integrating the low skilled into the labour market through a flexicurity approach combining better access to qualifications with the implementation of the announced comprehensive tax and –benefit reform and more effective employment services for unemployed recipients of basic income support.

6. In addition, it will be important for Germany over the period of the National Reform Programme to focus on the following challenges: securing the long-term sustainability of public finances by firmly locking in the achieved fiscal consolidation, including in the ongoing revision of budgetary institutions in the federal system, and by carefully monitoring the impact of the health care reform to keep expenditure growth in check and strength efficiency in the health sector; improving the framework for competition in the rail sector, and in the gas and electricity networks, where competition remains insufficient due to high concentration; continue further with the establishment of one-stop-shops and the improvement of start-up times; and in the context of the planned measures to promote lifelong learning, enhance continuing vocational training.

ESTONIA

1. In the light of the 2007 Estonian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Estonia has been making very good progress in implementing its National Reform Programme over the 2005-2007 period. Estonia has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation report shows some policy response to the areas identified by the Council as requiring attention. There has been some policy response on competition policy, active labour market policies and educational policy. The most substantial response has been on R&D and Innovation policy. Estonia has not moved significantly forward on the modernisation of labour law.

4. Among the strengths shown by the Estonian Implementation Report are: the establishment of an ambitious long-term and systematic new R&D and Innovation strategy; the measures to facilitate start-ups and financing of innovative SMEs; a strong increase in the employment rate and the measures for raising the quality of higher and vocational education.

5. The policy areas in the Estonian National Reform Programme where challenges need to be tackled with the highest priority are: the employment area where progress on the modernisation of labour law has been limited.

6. It will be important for Estonia over the period of the National Reform Programme to focus on the following challenges: improving macro-economic stability and containing inflation through adequate structural reforms and determined fiscal policy; reinforcing efforts to ensure that R&D results are translated into innovative services or products; encouraging closer cooperation between universities and enterprises; launching the new immunity and leniency programme and strengthening competition enforcement; reinforcing active labour market policies and increasing the supply of skilled labour by implementing a comprehensive lifelong learning strategy that responds to labour market needs; reducing labour market rigidities by urgent progress towards labour law modernisation and by promoting flexible forms of work.

IRELAND

1. In the light of the 2007 Irish Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Ireland has been making very good progress in implementing its National Reform Programme over the 2005-2007 period. Ireland has been showing good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a good policy response to the areas identified by the Council as requiring attention. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

4. Among the strengths of the Irish National Reform Programme and its implementation is the comprehensive and coherent national strategy. The document also highlights the usefulness of the Lisbon process through its role in focussing on the prioritisation and implementation of specific actions, and emphasising its key role in addressing the challenges and opportunities associated with globalisation.

5. It will be important for Ireland over the period of the National Reform Programme to focus on the following challenges for the future: speeding up progress in formulating concrete measures to reform pension arrangements; an intermediate target for R&D investment should be set for 2010; accelerating progress in increasing labour market participation, including by establishing a comprehensive childcare infrastructure; further developing the policy framework for the labour market and social integration of migrants and placing a particular emphasis on support to older and low-skilled workers; and developments in the housing market, affecting short and medium-term growth, should be carefully monitored.

GREECE

1. In the light of the 2007 Greek Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Greece has made steady progress in implementing its National Reform Programme over the period 2005-2007. Greece has shown some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows there has been some policy response to the recommendations adopted by the Council. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

4. Amongst the strengths shown by the 2007 Greek Implementation Report are: good progress made to consolidate public finances, promoting female employment, implementing internal market legislation, and improving the business environment. There are promising signs of progress to fix a timetable to implement pension reforms designed to improve long-term fiscal sustainability.

5. Policy areas in the Greek National Reform Programme where challenges need to be tackled with the highest priority are: long-term fiscal sustainability, implementation of the public administration reform agenda, the consolidation of active labour market policies, tackling high youth unemployment, tackling undeclared work and acceleration of education and life-long learning reforms. Against this background it is recommended that Greece:

   - pursue fiscal consolidation and debt reduction, and proceeds rapidly with the implementation of the pension reform, with a view to improving long-term fiscal sustainability;

   - implement the reform of its public administration, by building up effective regulatory, control and enforcement capacities, by modernising its human resources policy, and through effective use of the Structural Funds;

   - within an integrated flexicurity approach, modernise employment protection including legislation, reduce the tax burden on labour, strengthen active labour market policies and transform undeclared work into formal employment;

   - accelerate the implementation of reforms on education and lifelong learning, in order to improve quality and responsiveness to labour market needs, increase participation, and allow for a smooth transition into employment, particularly for the young.

6. In addition, it will be important for Greece over the period of the National Reform Programme to focus on the following challenges: contain inflationary pressures and the current account deficit; accelerate efforts to set up a research and innovation

strategy and increase investment in R&D; improve further the transposition of internal market legislation; speed up progress towards meeting the SME policy targets set by the 2006 Spring European Council; strengthen competition in the area of professional services; protect the environment by prioritising effective solid and water waste management and curb greenhouse gas emissions; encourage further female participation in employment; reduce early school leaving and put in place a coherent active ageing strategy.

SPAIN

1. In the light of Spain's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Spain has made good progress with implementing its National Reform Programme over the 2005-2007 period. Spain has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in three of the four priority action areas.

3. The Implementation Report shows a good policy response to the recommendations adopted by the Council. With regard to the other areas on which Spain was asked to focus, there has been a limited response in the macro-economic domain. The points to watch in the micro-economic and employment domains have been partially addressed. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Among the strengths shown by Spain's 2007 Implementation Report are: a faster than targeted reduction of government debt; good progress on implementation of the R&D and innovation plan; and satisfactory progress towards the employment rate objective, in particular for female employment.

5. The policy areas in the Spanish National Reform Programme where challenges now need to be tackled with the highest priority are improving competition in electricity markets and further improvements to education and training. Against this background it is recommended that Spain:

   - take further measures to increase competition in the energy sector, notably by eliminating the distorting price setting mechanisms and improving cross-border interconnection capacity to ensure security of supply;

   - ensure the effective implementation of education reforms, also at regional level, to reduce early school leaving.

6. In addition, it will be important for Spain over the period of the National Reform Programme to focus on the following challenges: contain the current account deficit and inflationary pressures and monitor developments in the housing market; raising competition in professional services and retail markets; improving the regulatory framework; implementing environmental measures, in particular to reduce CO_2 emissions; further modernise employment protection, including legislation, in order to foster flexicurity in the labour market to counter segmentation and promote the attractiveness of part-time work; raising productivity by raising skill levels and innovation; integrating immigrants into the labour market; further increase of access to childcare; and implement pension and healthcare reforms so as to improve long term fiscal sustainability.

FRANCE

1. In the light of France's 2007 Implementation Report and the Commission's assessment of progress made in implementation of key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. France has made steady progress in implementing its National Reform Programme over the 2005-2007 period. France has shown some progress in fulfilling the commitment agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a limited policy response to the recommendations issued to France by the Council. There has been some policy response on the other areas identified in the Council conclusions as requiring attention in particular an important reform has been undertaken with regard to stimulating and supporting entrepreneurship and young businesses. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

4. Among the strengths shown by French 2007 Implementation Report are: the reform of R&D and innovation strategies, the concrete results of measures in the area of ICT, and the announced, comprehensive set of measures to improve the functioning of the labour market, including through changes in legislation.

5. The Implementation Report presents a noticeably modified strategy in which employment is to become a factor of economic policy aiming at enhanced growth. The extent to which increased competition is integrated in this new policy framework is, as yet, less clear. It is important that France strengthens its budgetary efforts in order to simultaneously implement a concerted reform strategy and further consolidates public finances. Significant or sustained further measures are needed to achieve budgetary consolidation, to increase competition in network industries and to improve labour market performance. Against this background, it is recommended that France:

   - ensures the sustainability of public finances, taking into account the ageing of the population, by considerably strengthening budgetary consolidation and debt reduction, and with a view to achieving a balanced budget in 2010. The negotiation on pension systems scheduled for 2008 will have to build on the gains made following the introduction of the 2003 reform;

   - improves the framework for competition in the gas, electricity and rail freight sectors;

   - within an integrated flexicurity approach, improves the efficiency of lifelong learning and modernises employment protection, in order notably to combat labour market segmentation among contract types, and make it easier to switch between fixed term contracts and permanent contracts.

6. In addition, it will be important for France over the period of the National Reform Programme to focus on the following challenges: further strengthening competition in regulated trades and professions, further enhancing better regulation policies by including impact assessments; continuing to increase labour supply and making work pay.

ITALY

1. In the light of the 2007 Italian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Italy has made good progress in implementing its National Reform Programme over the 2005-2007 period. There has been some response in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority areas.

3. The Implementation Report shows some policy response to the recommendations adopted by the Council. Given the scale of the challenge, significant further reforms are needed. There has been some policy response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Amongst the strengths shown by the 2007 Italian Implementation Report are the initial steps to improve the business environment, measures to enhance competition in professional and financial services and retail distribution, recent improvements in its transposition deficit of EU legislation; and e-government actions to modernise the public sector.

5. The policy areas in the Italian National Reform Programme where challenges need to be tackled with the highest priority are: fiscal sustainability, where efforts need to be pursued and the pension reform process needs to be completed; enhanced competition in product and service markets and pursuing the full implementation of announced reforms; further fighting regional disparities in the employment; and improving education and lifelong learning. Against this background it is recommended that Italy:

   - rigorously pursues fiscal consolidation, in particular by curbing growth in current primary expenditure, and completes the pension reform process with a view to improving the long-term sustainability of public finances;

   - continues the progress made to enhance competition in product and services markets and vigorously pursues the implementation of announced reforms;

   - improves the quality and labour market relevance of education, promotes lifelong learning, tackles undeclared work and ensures the efficient operation of employment services, within a flexicurity approach and with a view to reducing regional disparities.

6. In addition, it will be important for Italy to focus over the period of the National Reform Programme on the following challenges: increasing R&D investment and efficiency, where despite welcome policy developments, further efforts are needed to reach the 2010 target and to enhance the efficiency of public spending; increasing efforts to meet the CO_2 emission reduction targets; improving the quality of regulation by strengthening and fully implementing the system of impact assessment, notably for SMEs; implementing plans to improve infrastructure; increasing childcare provision with a view to reconciling work and family life and fostering

labour market participation of women; and putting in place a consistent active ageing strategy to increase employment of older workers, and with a view to improving pension adequacy.

CYPRUS

1. In the light of the 2007 Implementation Report for Cyprus and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Cyprus has made good progress in the implementation of its National Reform Programme over the 2005-2007 period. Cyprus had made good progress in fulfilling the specific commitments agreed at the 2006 Spring European Council in the priority areas.

3. The Implementation Report shows a good policy response to the recommendations adopted by the Council. With a view to the long term sustainability of public finances there has been a satisfactory initial response in reforming the health care system but a limited response on pension reform, enhancing lifelong learning and reforming the vocational education and training system. There has been some policy response on the additional areas identified in the Council conclusions as requiring attention.

4. Amongst the strengths of the Implementation Report is progress in the field of fiscal consolidation, in both deficit and debt reduction; a new policy to develop a comprehensive research and innovation system; and the maintenance of a good overall employment performance supported by a broad range of active labour market measures.

5. The policy areas in the Cypriot National Reform Programme where weaknesses need to be tackled with the highest priority are: addressing ageing-related expenditure; implementing a lifelong learning strategy and increasing training and labour market opportunities for young people. Against this background, it is recommended that Cyprus:

   - take steps to implement reforms of the pension and health care systems and sets a timetable for their implementation with a view to improving fiscal sustainability;

   - enhance life long learning, and increase employment and training opportunities for young people by implementing the reforms of the vocational, education, training and apprenticeship system.

6. In addition, it will be important for Cyprus over the period of the National Reform Programme to focus on measures to: improve competition in the area of professional services; further stimulate private sector R&D; and address the very high gender pay gap.

LATVIA

1. In the light of Latvia's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Latvia has made some progress in implementing its National Reform Programme over the 2005-2007 period and some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows that there has been some progress in responding to the recommendations adopted by the Council. There has been a mixed response to the additional areas identified by the 2007 Spring European Council as requiring attention.

4. Among the strengths shown by the Implementation Report are: the first positive steps in the field of knowledge and innovation; the progress achieved on certain SME and entrepreneurship issues; the strengthened role of the Competition Authority in market surveillance; and further measures to promote energy efficiency and the use of renewable energy resources. Latvia has also implemented a set of measures that have successfully supported labour market performance.

5. The policy areas in the Latvian National Reform Programme where weaknesses need to be tackled with the highest priority are: more concrete measures to secure macroeconomic stability in the face of overheating pressures; further development of the R&D strategy to improve prioritisation and increase private sector involvement; and stronger measures to increase labour supply and strengthen the skills of the labour force. Against this background, it is recommended that Latvia:

   - pursue a more restrictive fiscal policy, with a careful prioritisation of expenditures and wage developments that are in line with productivity, in order to contribute to correcting overheating pressures and reducing the risk of macroeconomic instability;

   - make faster progress in the implementation of the research and innovation policy reforms, in order to meet the ambitious targets set. This concerns especially policies to stimulate partnerships between research and education institutions and businesses;

   - within an integrated flexicurity approach, intensifies efforts to increase labour supply and productivity by improving regional mobility and, enhancing the responsiveness of education and training systems to labour market needs, by putting in place a lifelong learning system and pursuing active labour market policies.

6. In addition, it will be important for Latvia over the period of the National Reform Programme to focus on: improving further the regulatory environment, notably by means of an explicit better regulation policy; and improving access to childcare.

LITHUANIA

1. In the light of the 2007 Lithuania's Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Lithuania has made good progress in implementing its National Reform Programme over 2005-2007. Lithuania has also been showing some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a limited policy response to the recommendations adopted by the Council. There has been some policy response on the additional areas identified by the Council as requiring attention.

4. Among the strengths shown by the 2007 Lithuania's Implementation Report are: approval of priority areas for R&D development and adoption of the Vocational Training Law.

5. The policy areas in the Lithuanian National Reform Programme where challenges need to be tackled with the highest priority are implementing measures: increasing and improving the efficiency of investment in R&D and support for innovation; to increase internal mobility of labour, promote adult participation in lifelong learning, especially among older workers, and reform the education and training systems to ensure quality and labour market relevance. Against this background it is recommended that Lithuania:

   - accelerates the implementation of the structural reform of its R&D and innovation system so as to raise the efficiency of public spending and create conditions favourable to increased private investments in this area, including for innovation in traditional and low-tech sectors;

   - intensifies efforts to increase the supply of skilled labour, with a special focus on the participation of older workers by: improving the regional mobility, reforming the education and training systems to ensure their quality and relevance to the labour market needs and implementing the revised lifelong learning strategy.

6. In addition, it will be important for Lithuania to focus over the period of the National Reform Programme on the following challenges: improving macro-economic stability and containing inflation; increasing foreign direct investment; improving the efficiency of regulatory environment with particular focus on legislative simplification; improving youth employability; expanding entrepreneurship education; increasing the availability of childcare; and strengthening occupational health and safety.

LUXEMBOURG

1. In the light of the Luxembourg 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Luxemburg has made very good progress in implementing its National Reform Programme over the 2005-2007 period. Luxembourg has shown some progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a mixed policy response to the areas identified by the Council as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Among the strengths shown by the Luxembourg's 2007 Implementation Report are: investments to integrate the economy into the international context, efforts to develop an extensive simplification policy focussed on business needs, the development of childcare infrastructures, reform of professional training, and the introduction of new forms of employment.

5. It will be important for Luxembourg over the period of the National Reform Programme to focus on the following challenges: accelerate the implementation of measures aimed at increasing the employment rate of older workers, in particular through reform to discourage early retirement; take further measures to reduce the number of early school leavers, and to remove the artificial barriers between different types of education; closely monitoring the impact of recently adopted measures to reduce unemployment amongst the young; and in order to deliver a more attractive economic environment, greater support is needed to deliver competitive markets, improve the transposition of EU legislation, and support SMEs.

HUNGARY

1. In the light of the 2007 Hungarian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Hungary has made limited progress in implementing its National Reform Programme over 2005-2007. Hungary has shown limited progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a mixed policy response to the recommendations adopted at the Council. There has been some policy response on the additional areas identified in the Council conclusions as requiring more attention.

4. Among the strengths shown by the 2007 Implementation Report are: strong improvements on fiscal consolidation, the adoption of various structural reform steps, the shortening of the setting-up time for businesses and the efforts to reduce administrative costs, the introduction of further incentives to work and to remain on the labour market and the transformation of undeclared work into formal employment.

5. The policy areas in the Hungarian National Reform Programme where challenges need to be tackled with the highest priority are: correcting the excessive deficit as planned, further improving the sustainability of public finances, improving the labour market situation of disadvantaged groups, reducing persistent regional disparities in employment and reforming the education and training systems. Against this background, it is recommended that Hungary:

   - continues to implement the necessary measures to ensure a durable reduction of the government deficit and of the public debt ratio, with increased reliance on the expenditure side, including through the establishment of more thorough and comprehensive expenditure rules;

   - continues to reform the public administration, health care, pension and education systems with a view to ensuring long-term fiscal sustainability and improving economic efficiency. This should include steps to further limit early retirement, reduce the number of new recipients of disability pensions and further restructure health care;

   - reinforces active labour market policies to improve the labour market situation of disadvantaged groups; and reduces persistent regional disparities in employment;

   - ensures access to high quality education and training for all, upgrade skill levels, and increases responsiveness of education and training systems to labour market needs.

6. In addition, it will be important for Hungary over the period of the National Reform Programme to focus on the following challenges for the future: further reforming the public research system, increasing the effectiveness of public R&D expenditure and improving linkages between public and private R&D; reducing and redirecting state

aids; improving the regulatory environment through further reducing administrative burden and legislative simplification; introducing further incentives to work and to remain in the labour market; ensuring better reconciliation of work and private life; completing the establishment of the integrated employment and social services system; transforming undeclared work into formal employment; and implementing the lifelong learning strategy.

MALTA

1. In the light of the 2007 Maltese Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Malta has made good progress in the implementation of its National Reform Programme over the 2005-2007 period. Malta has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a limited policy response to recommendations adopted by the Council. There has also been a limited policy response to the additional areas identified by the Council as requiring attention.

4. Among the strengths of the Maltese National Reform Programme and its implementation are its governance and the progress achieved in fiscal consolidation as well as progress in strengthening the business environment, liberalising certain markets (e.g. ports), reforming education and increasing ICT use.

5. The policy areas in the National Reform Programme where weaknesses need to be tackled with the highest priority are competition policy and persistent labour market problems. Against this background, it is recommended that Malta:

   - strengthens competition, notably by reducing state aids and redirecting them towards horizontal objectives as well as by reinforcing the competition authority and by further steps in opening up professional services;

   - steps up efforts to attract more people into the labour market, particularly women and older workers; maintain efforts to tackle undeclared work and take further action on the benefit system to make declared work more attractive.

6. In addition, it will be important for Malta over the period of the National Reform Programme to focus on: continue implementing and reinforcing measures on health care reform; further improving the regulatory environment by continuing simplifying legislation, by introducing systematic impact assessments and effective one stop shops for business start-ups; diversifying its energy sources, including enhancing energy efficiency and renewable energy and connecting Malta to Europe's energy networks; continuing efforts to raise educational attainment and reduce early school leaving.

THE NETHERLANDS

1. In the light of the 2007 Dutch Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. The Netherlands has made significant progress in implementing its National Reform Programme over the 2005-2007 period. The Netherlands has shown a good response to fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows some policy response to the recommendation adopted by the Council. There has been a limited policy response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Among the strengths of the National Reform Programme and its implementation are: the efforts to reduce administrative burden and to improve the business climate; the ambitious plans in the area of energy and climate change; and incentives to improve childcare provision.

5. The policy area in the Dutch National Reform Programme where challenges need to be tackled with the highest priority is in improving labour supply. Against this background it is recommended that the Netherlands:

   - take further measures to improve labour supply of women, older workers and disadvantaged groups with a view to raising overall hours worked in the economy.

6. In addition, it will be important for the Netherlands over the period of the National Reform Programme to focus on the following challenges: stepping up efforts aimed at increasing private sector R&D expenditure by avoiding fragmented policy governance structures and putting in place a coherent strategy for R&D and innovation which addresses the interaction between private R&D and public research as well as foreign R&D investment.

AUSTRIA

1. In the light of the 2007 Austrian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Austria has made significant progress in implementing its National Reform Programme over the 2005-2007 period. Austria has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a limited policy response to the employment recommendation adopted by the Council. There has been some response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Among the strengths shown by the 2007 Austrian Implementation Report are: good practices to boost innovation, such as the innovation voucher; increased budgets for R&D in line with the 3% target; the creation of a climate and energy fund; the successful implementation and further development of its flexicurity model.

5. The policy areas in the Austrian National Reform Programme where challenges need to be tackled with the highest priority are: increasing labour supply of older workers and improving the skills and employability of disadvantaged young people. Against this background it is recommended that Austria:

   - further improve incentives for older workers to continue working by implementing a comprehensive strategy including enhanced job-related training, adaptation of working conditions and tightening the conditions for early retirement; and improve education outcomes for vulnerable youth.

6. In addition, it will be important for Austria to focus over the period of the National Reform Programme on the following challenges: strengthening the fiscal adjustment in order to achieve a balanced budget before 2010; increasing competition in services, in particular in professional services; strengthening entrepreneurship education; identifying further emission reduction policies and measures; tackling the gender segregation of the labour market, including by further improving the availability of childcare.

POLAND

1. In the light of the 2007 Poland's Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Poland has made limited progress in implementing its National Reform Programme over the 2005-2007 period and has shown limited progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a mixed policy response to the recommendations adopted by the Council. There has been some policy response on the additional areas identified in the Council conclusions as requiring attention.

4. Among the strengths shown by the 2007 Poland's Implementation report are: the attention paid to developing entrepreneurship; initial steps to bring down the tax burden on labour; the priority and funding allocated to active labour market measures; and the strong linkage of the National Reform Programme priorities with EU funding.

5. The policy areas in the Polish National Reform Programme where challenges need to be tackled with the highest priority are: a stronger commitment to address the sustainability of the public finances; vigorous actions to improve regulation and to promote opening of markets in network industries; rapid implementation of the R&D reforms; further measures to address the low employment rate of older workers; better focusing of active labour market policy on the most vulnerable groups; and putting in place the lifelong learning strategy. Against this background Poland is recommended to:

   - strengthen the fiscal consolidation and supplement the nominal state budget deficit "anchor" (deficit ceiling) with further mechanisms to enhance control over expenditure;

   - improve the framework for competition in network industries, including through a review of the role of regulators, and vigorously continue the process of the liberalisation of energy markets;

   - pursue the reform of the public research sector with a view to R&D and innovation being boosted, and implementing the framework for private sector R&D, thereby maximising the benefits from foreign direct investment;

   - with a view to developing an integrated flexicurity approach, increase the level and efficiency of active labour market policy, notably for older persons and groups vulnerable to poverty, review benefit systems to improve the incentive to work, put in place the lifelong learning strategy, and modernise education and training systems in view of labour market needs.

6. In addition, it will be important for Poland over the period of the National Reform Programme to focus on the following challenges: upgrading transport infrastructure;

speeding-up the business registration process; ensuring timely implementation of the e-government programmes; improve the transposition of internal market legislation; and increasing the provision of childcare facilities.

PORTUGAL

1. In the light of the 2007 Portuguese Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Portugal has made good progress in implementing its National Reform Programme over the 2005-2007 period. Portugal has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a good policy response to the recommendations issued by the Council. There has also been some policy response on the additional areas identified by the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Some of the strengths shown by the 2007 Portuguese Implementation Report are: the progress achieved in correcting fiscal imbalances and promoting sustainable reforms of the public administration, on pension and health-care reform, progress on unlocking business potential and the implementation of the Technological Plan.

5. The policy areas in Portugal's National Reform Programme where challenges need to be tackled with the highest priority are: consolidating public finances, whilst improving its quality and sustainability, and gearing public spending towards raising Portugal's growth potential; improving the efficiency of the educational system notably by improving attainment levels and reducing early school leaving; modernising employment protection to curb the segmentation of the labour market. Against this background it is recommended that Portugal:

   - in the context of the on-going correction of fiscal imbalances and public administration reform, redirect public spending towards uses more supportive to potential economic growth, while maintaining firm expenditure control overall;

   - further implement measures to strongly improve the efficiency of the educational system notably by improving attainment levels of the young, fighting early school leaving and developing a vocational training system that is relevant to the labour market needs and based on the National Qualifications Framework;

   - continue efforts to modernise employment protection, including legislation to reduce the high levels of labour market segmentation, within the flexicurity approach.

6. In addition, it will be important for Portugal over the period of the National Reform Programme to focus on the following challenges for the future: narrowing its current account deficit in a sustained way; pursuing the implementation of the Technological Plan, consolidating the linkages between research, higher education and industry, and involving the private sector further; ensuring effective competition, notably in energy and financial services markets; further implement a better regulation programme and in particular strengthen the impact assessment system; reducing the deficit in

transposing EU legislation into national law; devising and implementing the measures needed to reduce green house gas emissions; and continuing to address factors undermining social cohesion.

ROMANIA

1. In the light of Romania's 2007 Implementation Report and the Commission's assessment of the National Reform Programme and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate

2. Overall, the National Reform Programme focuses on the right challenges. However, in some critical areas, such as strengthening administrative capacity and improving the business environment, the programme lacks ambition. In other areas, information about the content of measures, their timelines and budgetary support is sometimes lacking which makes it difficult to assess whether measures will bring solutions to the problems and challenges identified.

3. The programme's strengths include initiatives aimed at implementing a medium-term expenditure framework, reducing non-wage labour costs and reforming research structures.

4. The policy areas in the Romanian National Reform Programme where weaknesses need to be tackled with the highest priority are: strengthening administrative capacity, addressing overheating and improving budget planning and the quality of expenditure; cutting red tape and activating labour supply and raising skill levels. Against this background, it is recommended that Romania:

   - urgently strengthen administrative capacity at both central and local levels of government by building up effective regulatory, control and enforcement capacity;

   - avoid pro-cyclical fiscal policy to contain the growing current account deficit and inflationary pressures, keep wage developments in line with productivity growth and improve budget planning and execution as well as the quality of public finances by reviewing the composition of public spending and by reducing and redirecting state aid to horizontal objectives;

   - take rapid measures to reduce substantially administrative procedures and delays to obtain authorisations as part of a coherent better regulation policy in order to improve the business environment, which will also help in the fight against corruption;

   - implement an integrated approach to increasing employment, activity rates and productivity levels, especially by accelerating reforms of the education system to respond better to labour market needs, by reducing early school leaving, by significantly increasing adult participation in education and training; and by transforming subsistence/semi-subsistence farming into sustainable employment.

5. In addition it will be important for Romania over the period of the National Reform Programme to focus on: taking further measures to ensure the long-term sustainability of public finances, in particular with regard to potential risks in terms of adequacy and sustainability of pensions; reinforcing measures to tackle fragmentation of the research base whilst ensuring that planned increases in public research funding yield effective returns by vigorously implementing the national R&D and innovation strategy and by regularly monitoring its results; pursuing a

more integrated approach to infrastructure development and roll-out of ICT; intensifying efforts to tackle undeclared work; improving the effectiveness and geographical scope of public employment services, particularly to assist vulnerable groups.

SLOVENIA

1. In the light of the 2007 Slovenian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Slovenia has made good progress in implementing its National Reform Programme over the 2005-2007 period. Slovenia has also been showing some progress in fulfilling the commitments agreed by the 2006 Spring European Council.

3. The Implementation Report shows some policy response to the recommendations issues by the Council. There has also been some policy response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report does not however specifically address the recommendations issued to the euro area countries.

4. Among the strengths shown by the 2007 Implementation Report are: the involvement of social partners in drafting all major labour market reforms; efforts to strengthen the link between education and scholarship systems and the economy; the shortening of business start-up times and the reduction of administrative burden. Slovenia's entry into the euro area is the central achievement in the macro field.

5. The policy areas in the National Reform Programme where challenges need to be tackled with the highest priority are: further pension reform and effective implementation of the active ageing strategy; and a more flexible labour market combined with a more effective personalised approach in the implementation of active labour market policies. Against this background it is recommended that Slovenia:

   - take further steps to strengthen the reform of the pension system and promote active ageing, with a view to increasing the employment rate of older workers and improving long-term sustainability;

   - within an integrated flexicurity approach, promotes more flexible contractual arrangements and improves the effectiveness of employment services, particularly in relation to persons with low employment prospects, in order to counter labour market segmentation mainly affecting young people.

6. In addition, it will be important for Slovenia to focus over the period of the National Reform Programme on the following challenges: develop an effective research and innovation strategy and ensure its effective implementation; also with a view to containing inflation, improve competition in the services sector, with particular emphasis on retail, financial services, utilities and professional services; improve implementation of energy efficiency measures, particularly with regard to CO_2 emissions and unfulfilled Kyoto targets; implement the ambitious plans to strengthen the link between the education system and the labour market.

SLOVAKIA

1. In the light of the 2007 Slovak Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Slovakia has made some progress in implementing its National Reform Programme over the period 2005-2007. There has been a limited response in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority areas.

3. The Implementation Report shows a mixed policy response to the recommendations adopted by the Council. Further reforms are necessary to increase R&D and education expenditure, implement strategies in the micro-economic area, to tackle long-term unemployment and to complete education and training reform. There has been a mixed response on the additional areas identified in the Council conclusions as requiring attention.

4. Among the strengths shown by the 2007 Slovak Implementation Report are: the foreseen reduction of the public finance deficit to below 3% of GDP in 2007; the adoption of a number of strategy documents in the area of R&D and innovation, energy efficiency and renewably energy; the partial implementation of a one-stop-shop for start-up companies; the revision of employment legislation; the adoption of the lifelong learning strategy; and efforts to revise active labour market policies to better comply with labour market developments.

5. The policy areas in the Slovak National Reform Programme where challenges need to be tackled with highest priority are: increasing expenditure to education, R&D and innovation, improving the regulatory environment, tackling long-term unemployment, completing the reform of the education and training system and raising its quality in line with labour market needs. Against this background, it is recommended that Slovakia:

   - reallocate resources to education, R&D and innovation, and duly implement a coherent R&D and innovation strategy with a particular focus on the institutional reform of the public research sector and substantial improvement of business-research cooperation;

   - improve the regulatory environment, notably by implementing a comprehensive better regulation strategy covering both impact assessment and simplification of existing legislation;

   - within an integrated flexicurity approach, ensures implementation of the lifelong learning strategy addressing the needs of the labour market, completes the reforms of primary, secondary and tertiary education to improve qualification and skill levels, and enhance access to employment, notably for the long-term unemployed and vulnerable groups.

6. In addition, it will be important for Slovakia over the period of the National Reform Programme to focus on: further developing ICT policies, especially for broadband infrastructure; full implementation of one-stop shops for start-up companies;

introducing entrepreneurship education; increasing competition in power supply; addressing the gender gap in pay and employment; developing an active ageing strategy; and creating job opportunities for young people.

FINLAND

1. In light of the 2007 Implementation Report for Finland and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Finland has made very good progress in implementing its National Reform Programme over the 2005-2007 period. Good progress has been shown in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows some policy response on the additional areas identified by the Council as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.

4. Among the strengths of the 2007 Implementation Report are the ongoing reforms to further improve the functioning of the national innovation system and the observed increase in the employment rate of older workers.

5. It will be important for Finland over the period of the National Reform Programme to focus on the following challenges: continue reforms to improve competition and productivity in services, and create the necessary leverage to reduce high price levels; implement announced measures to reach its Kyoto target; continue reforms to address bottlenecks in the labour market, with a particular view to tackling high structural unemployment, especially unemployment of low skilled workers, including young people, and taking into account the contribution economic migration can make.

SWEDEN

1. In the light of Sweden's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Sweden has made very good progress in implementing its National Reform Programme over the 2005-2007 period. Sweden has also shown very good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a good policy response to the areas identified by the Council as requiring attention.

4. Among the strengths shown by the 2007 Sweden's Implementation Report are: the action plan for regulatory simplification and the commitment to improve the impact assessment system; the progress with increasing labour supply and reducing unemployment; the sustainable use of energy; and the progress made on increasing public investment in R&D.

5. It will be important for Sweden to take further regulatory measures to increase competition, notably in services; and to focus on the implementation and impact evaluation of recent reforms to increase work incentives, to tackle youth unemployment, to raise the employment rate of immigrants and to reintegrate people on sickness-related schemes.

UNITED KINGDOM

1. In the light of the UK's 2007 Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. The UK has made significant progress in implementing its National Reform Programme over 2005-2007. The UK has shown good progress in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority action areas.

3. The Implementation Report shows a good policy response to the recommendation issued by the Council. There has also been a good policy response on the additional areas identified in the Council conclusions as requiring attention.

4. Among the strengths shown by the 2007 UK Implementation Report are: the plans to provide an integrated approach to employment and skills, moves towards the creation of a business-friendly regulatory environment, and the forward-looking plans on energy policy.

5. The policy areas in the UK National Reform Programme where challenges need to be tackled with the highest priority are improving skills levels to increase productivity and reduce disadvantage in the labour market. Against this background it is recommended that the UK:

   - implement recent plans to substantially improve skill-levels and establish an integrated approach to employment and skills in order to improve productivity and increase opportunities for the disadvantaged.

6. In addition, it will be important for the UK to focus on the following challenges for the future: progressively increase housing supply in order to meet medium term demand pressures; ensure progress towards the UK's R&D intensity target through full implementation of the recent review of R&D and innovation policy, particularly taking fuller account of the specific needs of the services sector.

EURO AREA MEMBER STATES

1. In the light of the 2007 Implementation Reports of the euro area Member States, and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate.

2. Based on their Implementation Reports, the euro area Member States have been making some progress in implementing policy measures that improve the functioning of the euro area.

3. Significant further reforms are necessary to fulfil the micro-economic and employment recommendations. The progress recorded in 2007 concerning the macro-economic area needs to be sustained.

4. Among the strengths shown by the 2007 Implementation Reports of the euro area Member States are: budgetary adjustment in 2007, the implementation of legislation to foster financial market integration, and wage bargaining systems more conducive to wage flexibility in some Member States.

5. The policy areas in the euro area where challenges now need to be tackled with the highest priority are: the sustainability of public finances and their contribution to growth; competition in product and service markets, especially in services, financial integration and competition in financial retail services, in order to facilitate adjustment and more flexible prices; adequate wage developments at the aggregate, sector, regional and occupational level; flexicurity in labour markets; and more labour mobility in order to foster labour market adjustment.

6. Against this background it is recommended that the euro area Member States together with their country specific recommendations:

   - pursue budgetary consolidation towards their medium-term objectives in line with the Stability and Growth Pact, hence striving to achieve an annual structural adjustment of at least 0.5% of GDP as a benchmark;

   - improve the quality of public finances by reviewing public expenditures and taxation, with the intention to enhance productivity and innovation, thereby contributing to economic growth and fiscal sustainability;

   - effectively implement measures that improve competition, especially in services, and step up measures that promote the full integration of financial markets and the competition in retail financial services, whilst strengthening stability and supervisory arrangements;

   - improve flexibility and security on labour markets inter alia by implementing "flexicurity" strategies, better aligning wage and productivity developments, and enacting measures to promote labour mobility across borders and between occupations.

7. For the future it will also be important for euro area to further strengthen governance to maximise policy synergies, which are stronger in a monetary union, and enhance political ownership of reforms. The Eurogroup's April 2007 Berlin orientations on public finances are a welcome step in this regard and a similar approach should be extended to other fields. A strengthening of the euro's representation in international financial institutions and fora would be in line with its potential as a pole of stability and growth in the global economy.

COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 11.12.2007
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PART V

COMMUNICATION FROM THE COMMISSION TO THE SPRING EUROPEAN COUNCIL

INTEGRATED GUIDELINES FOR GROWTH AND JOBS (2008-2010)

including a

COMMISSION RECOMMENDATION

on the broad guidelines for the economic policies of the Member States and the Community (under Article 99 of the EC Treaty)

and a

Proposal for a

COUNCIL DECISION

on guidelines for the employment policies of the Member States (under Article 128 of the EC Treaty)

(presented by the Commission)

TABLE OF CONTENTS

Explanatory Memorandum 3

The state of the EU Economy 4

Part 1 - Commission Recommendation on the Broad Economic Policy Guidelines (2005-2008) 7

Section A – Macroeconomic Policies for Growth and Jobs 8

A.1 Macroeconomic policies creating the conditions for more growth and jobs 8

A.2 Ensuring a dynamic and well-functioning euro area 11

Section B – Microeconomic reforms to raise Europe's growth potential 13

B.1 Knowledge and innovation — engines of sustainable growth 13

B.2 Making Europe a more attractive place to invest and work 18

Part 2 The Employment Guidelines (2008-2010) 23

ANNEX 26

1. Attract and retain more people in employment, increase labour supply and modernise social protection systems 28

2. Improve adaptability of workers and enterprises 30

3. Increase investment in human capital through better education and skills 32

EXPLANATORY MEMORANDUM

In the Spring Council in 2005, Heads of State and Government renewed the Lisbon Strategy and placed its focus on growth and jobs. They organised the Lisbon Strategy around three-year cycles, whilst strengthening ownership and accountability by clearly distinguishing between reforms which should be undertaken by Member States and those for which the Community should take the lead. As one of the instruments to implement the Strategy, the Council approved a set of integrated guidelines and adopted the necessary legal instruments based on Articles 99 and 128 of the Treaty. These guidelines are meant to guide Member States, as they implement national reforms, through their National Reform Programmes (NRP). The integrated guidelines will expire at the end of the first three-year cycle, and will therefore need to be renewed for the next cycle. The re-launch of the Lisbon Strategy in Spring 2005 put Europe back on track to create sustainable growth and jobs.

During the first cycle of the renewed Lisbon Strategy (2005-2008) Member States have stepped up the implementation of structural reforms, although the pace and intensity differs between them. Whilst most of the upturn of the EU economy is due to cyclical factors, Lisbon-type reforms have helped increase the growth potential of Member States' economies. They have also helped to make the European economy more resilient in dealing with external shocks, such as higher energy and commodity prices and currency fluctuations. Further integration of Member States economies and alignment of business cycles, especially in the euro area, will allow for a monetary policy geared better to Member States needs.

Viewed as a whole, therefore, the strategy has helped to speed up the pace of reform, helping Member States to implement sometimes difficult but necessary change to address the challenges of globalisation. The new governance of the Lisbon Strategy, with its emphasis on partnership between the European and the Member States level, has proved its worth. An independent evaluation of the Integrated Guidelines concluded that they constitute a comprehensive and open framework which accommodates the essential policy developments related to growth and employment in Europe. The evaluation also concluded that stakeholders wish to focus on implementation, as the guidelines remain relevant. The integrated guidelines, hence, are fulfilling their role and thus do not require revision.

However, more remains to be done to prepare the EU and its Member States for globalisation and to strengthen the foundations for economic success in the medium- to longer term. At the same time they need to keep pace with fast changing social realities (longer working lives, increasingly diverse family structures, new patterns of mobility and diversity) The EU must better adapt its existing policies and instruments, but also build upon new policies such as the Globalisation Adjustment Fund, in order to better respond to the legitimate concerns of people adversely affected by changes in trade patterns and by economic and social change. The goal of making the EU a dynamic, competitive, knowledge based society remains essential. Within this framework, an even higher priority needs to be given to the social dimension, flexicurity policies, energy and climate change and to education and skills as elements to modernise European markets, promote innovation and ensure new opportunities for citizens in a knowledge society. The Lisbon toolbox is already bringing the different strands of policy together to offer a more comprehensive vision of how the EU and Member States can work in harness to tackle the complex issues facing Europe today. The common objective during the next cycle should be to use the Lisbon instruments, including the country-specific recommendations as adopted by Council in 2007 linked to the integrated guidelines, to full effect in order to speed up the effective delivery of outstanding reforms.

The integrated guidelines for the period 2008-2010 are presented in one comprehensive document with two parts:

Part 1 – The Broad Economic Policy Guidelines

Section A deals with the contribution that macroeconomic policies can make in this respect. Section B focuses on the measures and policies that the Union and the Member States must carry out in order to make Europe a more attractive place to invest and work and to boost knowledge and innovation for growth.

Part 2 – The Employment Guidelines

This part of the integrated guidelines includes the proposal for a Council decision on the Employment Guidelines, on which the European Parliament, the European Social and Economic Committee and the Committee of the Regions will be consulted, in accordance with Article 128 of the Treaty.

For Member States both economic, and employment policy, are a matter of common concern (Articles 99 and 126). For the purpose of multilateral surveillance and to ensure closer cooperation of economic and employment policies, Member States report on measures taken under these guidelines through National Reform Programmes (and Annual Implementation Reports). Based on these reports, where it is established that the economic or employment policies of a Member State are not consistent with the Integrated Guidelines, the Council may, using the possibilities under Articles 99 and 128, make recommendations to the Member State concerned.

THE STATE OF THE EU ECONOMY

Economic conditions have been favourable since 2005 when the Lisbon Growth and Jobs Strategy was re-launched, although recent months have witnessed growing downside risks. Growth picked up to almost 3 % in 2007, increasingly driven by domestic demand and leaving Europe better placed to cope with adverse external shocks. However, recent financial turmoil and the slowdown of the US economy have substantially increased the risks to the downside, and the outlook for 2008-2009 indicates a deceleration in growth. Tighter financial conditions will take their toll on investment growth, in particular of construction investment, while the good performance of the labour market will support private consumption growth. While most of the recent upturn is cyclical in nature, there is some evidence of a structural component linked to past reforms enacted by EU Member States. Structural improvements have been most evident in labour markets, with the unemployment rate declining to below 7% and the employment rate approaching 65%, with particular strong increases recorded amongst women and older workers. Since mid-2005, productivity growth in the EU has picked up and while most of the acceleration in productivity growth can be attributed to cyclical factors, it does seem that the decade long decline in trend productivity growth has been interrupted. It is encouraging that job creation and productivity improvements have occurred simultaneously for the first time in a decade.

Notwithstanding the favourable developments over recent years, the recent international turbulences call for action to increase the resilience of the economy and to use the existing scope to improve both labour utilisation and labour productivity. In some countries, unfortunately, reform seems to be slowing down. The EU's employment rate has remained low relative to our competitors. Moreover, the rate of unemployment, especially of long-term

nature and amongst young people, remains far too high. While many manufacturing enterprises have been sufficiently productive to withstand international competition, productivity growth in several service sectors has stalled. Looking forward the economic and budgetary impact of ageing populations is fast approaching, with the large baby boom cohorts coming towards retirement in many countries. This makes it imperative to reduce public debt at an accelerated pace and to modernise pension and health care systems. An emerging challenge is also to improve capacity of the financial system to respond to shocks in 2007. Financial market transparency, effective competition rules and appropriate regulation and supervision will continue to be crucial for both confidence and performance. As will be social partner enabled wage developments compatible with employment growth and macroeconomic stability.

The EU now has an opportunity to pursue, even accelerate, structural reform efforts. The policy challenge is to avoid complacency and to continue addressing the structural weaknesses that are still holding back job creation, innovative activity, the adoption of technological progress, and limit the EU capacity to respond to international shocks. At the same time, there is a need to pursue macroeconomic policies that succeed in ensuring stability, containing inflationary pressures and reducing public budget deficits.

INTEGRATED GUIDELIINES FOR GROWTH AND JOBS (2008-2010)

Macroeconomic guidelines

(1) To secure economic stability for sustainable growth.

(2) To safeguard economic and financial sustainability as a basis for increased employment.

(3) To promote a growth and employment orientated efficient allocation of resources.

(4) To ensure that wage developments contribute to macroeconomic stability and growth.

(5) To promote greater coherence between macroeconomic, structural and employment policies.

(6) To contribute to a dynamic and well-functioning EMU.

Microeconomic guidelines

(7) To increase and improve investment in R&D, in particular by private business.

(8) To facilitate all forms of innovation.

(9) To facilitate the spread and effective use of ICT and build a fully inclusive information society.

(10) To strengthen the competitive advantages of its industrial base.

(11) To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth.

(12) To extend and deepen the internal market.

(13) To ensure open and competitive markets inside and outside Europe and to reap the benefits of globalisation.

(14) To create a more competitive business environment and encourage private initiative through better regulation.

(15) To promote a more entrepreneurial culture and create a supportive environment for SMEs.

(16)	To expand, improve and link up European infrastructure and complete priority cross-border projects.
Employment guidelines	
(17)	Implement employment policies aimed at achieving full employment, improving quality and productivity at work, and strengthening social and territorial cohesion.
(18)	Promote a lifecycle approach to work.
(19)	Ensure inclusive labour markets, enhance work attractiveness, and make work pay for job seekers, including disadvantaged people and the inactive.
(20)	Improve matching of labour market needs.
(21)	Promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of the social partners.
(22)	Ensure employment-friendly labour cost developments and wage setting mechanisms.
(23)	Expand and improve investment in human capital.
(24)	Adapt education and training systems in response to new competence requirements.

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Consequently, the Commission:

– recommends the following broad guidelines for the economic policies of the Member States and the Community, in accordance with Article 99(2) of the EC Treaty, and

– proposes the following Council Decision on guidelines for the employment policies of the Member States, in accordance with Article 128(2) of the EC Treaty.

Part 1

Commission Recommendation on the Broad Economic Policy Guidelines (2005-2008)

COMMISSION RECOMMENDATION

on the broad guidelines for the economic policies of the Member States and the Community

Section A – Macroeconomic Policies for Growth and Jobs

A.1 Macroeconomic policies creating the conditions for more growth and jobs

Securing economic stability to raise employment and growth potential

As macroeconomic stability is secured by a sound mix of many economic policies, challenges to stabilisation should be addressed by macroeconomic measures as well as by implementing structural reforms in product, labour and capital markets. Monetary policies can contribute by pursuing price stability and, without prejudice to this objective, by supporting other general economic policies with regard to growth and employment. For new Member States, it will be important that monetary and exchange rate policies contribute towards achieving convergence. Exchange rate regimes constitute an important part of the overall economic and monetary policy framework and should be orientated towards achieving real and sustainable nominal convergence. Participation in ERM II, at an appropriate stage after accession, should help those endeavours.

Securing a sound budgetary position will allow the full and symmetric play of the automatic budgetary stabilisers over the cycle with a view to stabilising output around potential. For those Member States that have already achieved sound budgetary positions, the challenge is to retain that position. For the remaining Member States, it is vital to take all the necessary corrective measures to achieve their medium term budgetary objectives in particular if economic conditions improve, thus avoiding pro-cyclical policies and putting themselves in a position in which sufficient room for the full play of automatic stabilisers over the cycle is ensured prior to the next economic downturn. In particular, an annual fiscal adjustment of 0.5% of GDP as a benchmark (more under cyclically favourable conditions) should be achieved in euro area and ERM II Member States. In line with the 2005 reform of the Stability and Growth Pact, for individual Member States the medium-term budgetary objectives (MTO's) are differentiated according to the diversity of economic and budgetary positions and developments as well as of fiscal risk to the sustainability of public finances, also in the face of prospective demographic changes. Moreover, in accordance with the report on the SGP reform endorsed by the European Council on 22 March 2005, introducing or strengthening national fiscal rules and institutions, including monitoring mechanisms can usefully complement the Pact and support its objectives.

An additional macroeconomic policy challenge for some Member States is to operate in an environment of robust catching up, which is to varying degrees accompanied by external deficits, rapid credit expansion and financial deepening. Fiscal restraint, effective financial supervision and promoting competitiveness are essential in order to contain external and internal imbalances. A cautious fiscal stance is one important way to keep external deficits within the range where sound external financing can be secured. Fiscal restraint can also limit the risk of surging domestic demand causing persistently higher inflation and the occurrence of macro-financial risks which could cause swings in real exchange rates and a protracted loss of competitiveness.

Guideline 1. To secure economic stability for sustainable growth

1. In line with the Stability and Growth Pact, Member States should respect their medium-term budgetary objectives. As long as this objective has not yet been achieved, they should take all the necessary corrective measures to achieve it. Member States should avoid pro-

cyclical fiscal policies. Furthermore, it is necessary that those Member States having an excessive deficit take effective action in order to ensure a prompt correction of excessive deficits.

2. Member States posting current account deficits that risk being unsustainable should work towards correcting them by implementing structural reforms, boosting external competitiveness and, where appropriate, contributing to their correction via fiscal policies. See also integrated guideline 'To contribute to a dynamic and well-functioning EMU' (No 6).

To safeguard economic and fiscal sustainability as a basis for increased employment

Europe's ageing population poses serious risks to the long-term sustainability of the European Union economy in the form of an increased debt burden, lower potential output per capita, due to the reduction in the working age population, and difficulties in financing the pension, social insurance and health care systems. As documented in the Commission's Sustainability Report, a substantial sustainability gap for the EU in aggregate is likely to emerge. Several Member States are exposed to high sustainability risk, and a number of others to medium risk.

Member States should address the economic implications of ageing by, as part of the well established three pronged strategy for tackling the budgetary implications of ageing, pursuing a satisfactory pace of debt reduction and providing incentives to raise employment rates and increase labour supply so as to offset the impact of future declines in the number of persons of working age. In order to accomplish this further budgetary consolidation is necessary, going beyond recent progress, and resulting in the attainment of the MTO's by all Member States. It is also essential to modernise social protection systems so as to ensure that they are financially viable, providing incentives to the working age population to actively participate in the labour market, while at the same time ensuring that they fulfil their goals in terms of access and adequacy. Action on health prevention and promotion would help to increase healthy life years and ensure the sustainability of health care systems. In particular, improved interaction between social protection systems and labour markets can remove distortions and encourage the extension of working lives against a background of increased life expectancy.

Guideline 2. To safeguard economic and fiscal sustainability as a basis for increased employment

Member States should, in view of the projected costs of ageing populations,

1. undertake a satisfactory pace of government debt reduction to strengthen public finances;

2. reform and re-enforce pension, social insurance and health care systems to ensure that they are financially viable, socially adequate and accessible;

3. take measures to increase labour market participation and labour supply especially amongst women, young and older workers, and promote a lifecycle approach to work in order to increase hours worked in the economy.

See also integrated guideline 'Promote a lifecycle approach to work' (Nos 18, and 4, 19, 21).

Promote a growth, employment orientated and efficient allocation of resources

Well-designed tax and expenditure systems that promote an efficient allocation of resources are a necessity for the public sector to make a full contribution towards growth and

employment, without jeopardising the goals of economic stability and sustainability. This can be achieved by redirecting expenditure towards growth-enhancing categories such as Research and Development (R&D), physical infrastructure, environmentally friendly technologies, human capital and knowledge. Member States can also help to control other expenditure categories through the use of expenditure rules and performance budgeting and by putting assessment mechanisms in place to ensure that individual reform measures and overall reform packages are well-designed. A key priority for the EU economy is to ensure that tax structures and their interaction with benefit systems promote higher growth through more employment and investment.

Guideline 3. To promote a growth- and employment-orientated and efficient allocation of resources

Member States should, without prejudice to guidelines on economic stability and sustainability, re-direct the composition of public expenditure towards growth-enhancing categories in line with the Lisbon strategy, adapt tax structures to strengthen growth potential, ensure that mechanisms are in place to assess the relationship between public spending and the achievement of policy objectives, and ensure the overall coherence of reform packages.

See also integrated guideline 'To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth' (No 11).

Ensure that wage developments contribute to growth and stability and complement structural reforms

Wage developments can contribute to stable macroeconomic conditions and an employment friendly policy mix. This requires that real wage increases are in line with the underlying rate of productivity growth over the medium term and are consistent with a rate of profitability that allows for productivity, capacity and employment-enhancing investment. This requires that temporary factors such as variation in productivity caused by cyclical factors or one off rises in the headline rate of inflation do not cause an unsustainable trend in wage growth and that wage developments reflect local labour market conditions. In countries with declining market shares, real wages would need to grow below productivity in order to restore competitiveness. These issues need to be taken into account in the continued dialogue and information exchange between monetary and fiscal authorities and the social partners via the Macroeconomic Dialogue.

Guideline 4. To ensure that wage developments contribute to macroeconomic stability and growth

And to increase adaptability, Member States should encourage the right framework conditions for wage-bargaining systems, while fully respecting the role of the social partners, with a view to promote nominal wage and labour cost developments consistent with price stability and the trend in productivity over the medium term, taking into account differences across skills and local labour market conditions.

See also integrated guideline 'Ensure employment-friendly labour cost developments and wage-setting mechanisms' (No 22).

Promote coherent macroeconomic, structural and employment policies

The role of sound macroeconomic policies is to provide conditions conducive to employment creation and growth. Structural reforms, consistent with sound fiscal positions in the short and medium term, are essential to increase productivity and employment in the medium-term, thus leading to the full realisation and strengthening of growth potential. They also contribute to fiscal sustainability, macroeconomic stability and resilience to shocks. At the same time, appropriate macro-economic policies are key for reaping the full growth and employment benefits of structural reforms. A key feature of Member States' overall economic strategy is to ensure that they have a consistent set of structural policies that support the macroeconomic framework and vice versa. In particular, market reforms need to improve the overall adaptability and adjustment capacity of economies in response to changes in both cyclical economic conditions and longer-term trends such as globalisation and technology. In this regard, reform of tax and benefit systems are important in order to make work pay and avoid any disincentive for labour market participation.

Guideline 5. To promote greater coherence between macroeconomic, structural and employment policies

Member States should pursue labour and product markets reforms that at the same time increases the growth potential and support the macroeconomic framework by increasing flexibility, factor mobility and adjustment capacity in labour and product markets in response to globalisation, technological advances, demand shift, and cyclical changes. In particular, Member States should: renew impetus in tax and benefit reforms to improve incentives and to make work pay; increase adaptability of labour markets combining employment flexibility and security; and improve employability by investing in human capital.

See also integrated guideline 'Promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of the social partners' (No 21; No 19).

A.2 Ensuring a dynamic and well-functioning euro area

Since the creation of the euro area almost ten years ago, the euro has embedded economic stability in euro area countries, shielding them from exchange rate turbulence. Subdued growth performance and persistent divergences in growth and inflation raise questions as to whether internal adjustment in the euro area is working smoothly, suggesting that economic policies and governance structures may not yet have fully adjusted to draw the full benefit from the monetary union. Since euro-area countries can no longer make independent use of monetary or exchange rate policies, [further] reforms are key to develop alternative mechanisms to help their economies adjust to economic shocks and competitiveness challenges.

The policy mix in the euro area needs to support economic growth while safeguarding long-term sustainability and stability. At the current juncture, it is important that the policy mix underpins confidence among consumers and investors, which also implies commitment to medium-term stability. Budgetary policy has to ensure a fiscal position which can support price stability, and is consistent with the need to prepare for the impact of ageing populations on the one hand and to accomplish a composition of public expenditure and revenues that fosters economic growth on the other. Euro-area Member States committed accelerate adjustment towards the MTO so that most of them would achieve their MTOs in 2008 or 2009

and all of them should aim for 2010 at the latest. Due to the high share of the public sector in economic activity in the euro area, the quality of public finances has a considerable influence on economic performance. Therefore, it is crucial that resources are spent in a growth-supportive manner and distortions arising from the financing of public activity are minimised. Comprehensive structural reforms will allow the euro area to raise its growth potential over time and ensure that stronger growth does not build up potential for higher inflation. Reforms catering for more adaptable labour markets, more competition on product markets and deeper financial market integration accompanied by growth and stability-oriented macroeconomic policies are particularly salient for euro area Member States as they have an important impact on their capacity to adequately adjust to shocks.

To contribute to international economic stability and better represent its economic interests, it is critical for the euro area to play its full role in international monetary and economic policy cooperation. While the appointment of a Eurogroup President for a two-year term of office as of 2005 has brought greater stability to the external representation of the euro area, further steps are needed to improve the external representation of the euro area, so that the euro area can take a leading strategic role in the development of the global economic system that is commensurate with its economic weight.

Spill-over effects are most powerful and the need for a common agenda is strongest in the euro area. Sharing a common currency and a common monetary policy offers an extra dimension to coordination that could strengthen the role of the euro area in delivering growth and jobs for the whole EU. The Commission will present a comprehensive review of the functioning of EMU to mark its tenth anniversary, with ideas on how policies, coordination and governance can help the euro area to work to best effect.

Guideline 6. To contribute to a dynamic and well-functioning EMU, euro area Member States need to ensure better co-ordination of their economic and budgetary policies, in particular:

1. pay particular attention to fiscal sustainability of their public finances in full compliance with the Stability and Growth Pact;

2. contribute to a policy mix that supports economic recovery and is compatible with price stability, and thereby enhances confidence among business and consumers in the short run, while being compatible with long term sustainable growth;

3. press forward with structural reforms that will increase euro area long-term potential growth and will improve its productivity, competitiveness and economic adjustment to asymmetric shocks, paying particular attention to employment policies; and

4. ensure that the euro area's influence in the global economic system is commensurate with its economic weight.

Section B – Microeconomic reforms to raise Europe's growth potential

Structural reforms are essential to increase the EU's growth potential and support macroeconomic stability, because they increase the efficiency and adaptability of the European economy. Productivity gains are fuelled by competition, investment and innovation. Raising Europe's growth potential requires making progress in both job creation and productivity growth. After lagging US productivity growth for more than a decade, productivity growth in the EU has accelerated since mid-2005. Sustaining this improvement is a major challenge facing the Union, especially in the light of its ageing population. Population ageing alone is estimated to reduce by nearly half the current rate of potential growth. A continuation of the productivity upswing, and increasing the hours worked are thus indispensable to maintain and increase future living standards, and to ensure a high level of social protection.

B.1 Knowledge and innovation — engines of sustainable growth

Knowledge accumulated through investment in R & D, innovation, education and life long learning, is a key driver of long-run growth. Policies aimed at increasing investment in knowledge and strengthening the innovation capacity of the EU economy are at the heart of the Lisbon strategy for growth and employment. This is why national and regional programmes for the period 2007-2013 have been increasingly targeted on investments in these fields in accordance with the Lisbon objectives.

Increase and improve investment in R & D, with a view to establishing the European Knowledge Area

A high level of R&D is crucial for our future competitiveness. R&D affects economic growth through various channels: first, it can contribute to the creation of new markets or production processes; second, it can lead to incremental improvements in already existing products and production processes; and third, it increases the capacity of a country to absorb new technologies.

The EU is currently spending about 1.85% of GDP on R&D (although ranging from below 0.5 % to nearly 4 % of GDP across Member States). The level of R&D spending has remained slightly decreased since 2000. Moreover, only around 55 % of research spending in the EU is financed by the business sector. Low levels of private R&D investments are identified as one of the main explanations for the EU/US innovation gap. More rapid progress towards establishing the European Research Area, including meeting the collective EU target of raising research investment to 3 % of GDP is needed. Member States are invited to report on their R&D expenditure targets for 2010 and the measures to achieve these in their National Reform programmes and the annual Progress Reports paying attention in particular to integrating the European dimension within their national R&D policies. The main challenge is to put in place framework conditions, instruments and incentives for companies to invest more in research.

Public research expenditure must be made more effective and the links between public research and the private sector have to be improved. Poles and networks of excellence should be strengthened, better overall use should be made of public support mechanisms to boost private sector innovation, and a better leverage effect of public investments and a modernised management of research institutions and universities should be ensured. It is also essential to

ensure that companies operate in a competitive environment since competition provides an important incentive to private spending on innovation. In addition, a determined effort must be made to increase the number and quality of researchers active in Europe, in particular by attracting more students into scientific, technical and engineering disciplines, and enhancing the career development and the transnational and intersectoral mobility of researchers, and reducing barriers to mobility of researchers and students. The international dimension of R & D should be strengthened in terms of joint financing, development of a more critical mass at the EU level in critical areas requiring large funds and through reducing barriers to mobility of researchers and students.

Guideline 7. To increase and improve investment in R & D, in particular by private business, the overall objective for 2010 of 3 % of GDP is confirmed with an adequate split between private and public investment, Member States will define specific intermediate levels. Member States should further develop a mix of measures appropriate to foster R & D, in particular business R & D, through:

1. improved framework conditions and ensuring that companies operate in a sufficiently competitive and attractive environment;

2. more effective and efficient public expenditure on R & D and developing PPPs;

3. developing and strengthening centres of excellence of educational and research institutions in Member States, as well as creating new ones where appropriate, and improving the cooperation and transfer of technologies between public research institute and private enterprises;

4. developing and making better use of incentives to leverage private R & D;

5. modernising the management of research institutions and universities;

6. ensuring a sufficient supply of qualified researchers by attracting more students into scientific, technical and engineering disciplines and enhancing the career development and the European, international as well as inter-sectoral mobility of researchers and development personnel.

Facilitate innovation

The dynamism of the European economy is dependent on its innovative capacity. The economic framework conditions for innovation need to be in place. This implies well-functioning financial and product markets as well as efficient and affordable means to enforce intellectual property rights. Innovations are often introduced to the market by new enterprises, which may meet particular difficulties in obtaining finance. Measures to encourage the creation and growth of innovative enterprises, including improving access to finance, should therefore enhance innovative activity[1]. Technology diffusion, and policies to better integrate national innovation and education systems, can be fostered by the development of innovation

[1] The EU's broad based innovation strategy therefore addresses intellectual property rights, standardisation, the use of public procurement to stimulate innovation, joint technology initiatives, boosting innovation in lead markets, such as cooperation between higher education, research and business, encouraging innovation in regions, innovation in services and non-technological innovation, and improving businesses' access to risk capital.

poles and networks as well as by innovation support services targeted at SMEs. Knowledge transfer via researcher mobility, foreign direct investment (FDI) or imported technology is particularly beneficial for lagging countries and regions. It is also crucial to strengthen further the integration of the knowledge triangle of R&D, education and innovation.

The EU's broad based innovation strategy therefore addresses intellectual property rights, standardisation, the use of public procurement to stimulate innovation, joint technology initiatives, boosting innovation in lead markets, cooperation between higher education, research and business, encouraging innovation in regions, innovation in services and non-technological innovation, and improving businesses' access to risk capital.

It is now imperative to deliver a unitary, affordable Community patent, set up an EU-wide jurisdictional system for patent litigation and facilitate the enforcement of intellectual property rights in the Internal Market.

Guideline 8. To facilitate all forms of innovation, Member States should focus on:

1. improvements in innovation support services, in particular for dissemination and technology transfer;

2. the creation and development of innovation poles, networks and incubators bringing together universities, research institutions and enterprises, including at regional and local level, helping to bridge the technology gap between regions;

3. the encouragement of cross-border knowledge transfer, including from foreign direct investment;

4. encouraging public procurement of innovative products and services;

5. better access to domestic and international finance;

6.efficient and affordable means to enforce intellectual property rights.

The diffusion of information and communication technologies (ICT), in line with the objectives and actions of the i2010 initiative, is also an important way to improve productivity and, consequently, economic growth. The EU has been unable to reap the full benefits of the Information and communication technologies (ICT), due especially to the continuing under-investment in ICT, organisational innovation and in digital skills. Wider and more effective use of ICT and the establishment of seamless Single Market in electronic communication services are essential for the future competitiveness of European businesses. . It is also important to reduce and prevent fragmentation of the 'e-Internal Market' by putting in place interoperable e-services between the Member States.

Guideline 9. To facilitate the spread and effective use of ICT and build a fully inclusive information society, Member States should:

1. encourage the widespread use of ICT in public services, SMEs and households;

2. fix the necessary framework for the related changes in the organisation of work in the economy;

3. promote a strong European industrial presence in the key segments of ICT;

4. encourage the development of strong ICT and content industries, and well-functioning markets;

5. ensure the security of networks and information, as well as convergence and interoperability in order to establish an information area without frontiers;

6. encourage the deployment of broad band networks, including for the poorly served regions, in order to develop the knowledge economy.

See also integrated guideline 'Promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of the social partners' (No 21).

To strengthen the competitive advantages of the European industrial base

A strong industrial base is of key importance for Europe's economy. The competitiveness of the EU depends on the ability of the economy to reorient activities towards sectors with higher productivity. An approach where innovation, employment, regional and other policies are integrated, supports upgrading the EU industrial base.

In order to enhance and sustain economic and technological leadership, Europe must increase its capacity to develop and market new technologies, including ICT and environmental technologies. The synergies from jointly addressing research, regulatory and financing challenges at the European level, where for reasons of scale or scope individual Member States cannot successfully tackle market failures in isolation, should be analysed and exploited. The EU has still not managed to fully realise its technological potential. The pooling of European excellence and the development of public-private partnerships and cooperation between Member States where the benefits for society are larger than those for the private sector will help tap this potential.

Guideline 10. To strengthen the competitive advantages of its industrial base, Europe needs a solid industrial fabric throughout its territory. The necessary pursuit of a modern and active industrial policy means strengthening the competitive advantages of the industrial base, including by contributing to attractive framework conditions for both manufacturing and services, while ensuring the complementarity of the action at national, transnational and European level. Member States should:

1. start by identifying the added value and competitiveness factors in key industrial sectors, and addressing the challenges of globalisation;

2. also focus on the development of new technologies and markets:

(a) this implies in particular commitment to promote new technological initiatives based on public private partnerships and cooperation between Member States, that help tackle genuine market failures;

(b) this also implies the creation and development of networks of regional or local clusters across the EU with greater involvement of SMEs.

See also integrated guideline 'Improve matching of labour market needs' (No 20).

Encourage the sustainable use of resources

Lasting success for the Union also depends on addressing a range of resource and environmental challenges which, if left unchecked, will act as a brake on future growth. Recent developments have emphasised the importance of energy efficiency and reducing the vulnerability of the European economy to oil prices variations. An integrated approach to climate and energy policy is needed to increase the security of supply, ensure the competitiveness of the EU economy and the availability of affordable energy, and combat climate change. Member States and the Community must both contribute to achieving the EU targets of at least a 20 % reduction in greenhouse gas emissions, a 20 % share of renewable energies as well as a 20 % improvement in energy efficiency by 2020. Member States should continue the fight against climate change in order that the global temperature increase does not exceed 2°C above pre-industrial levels, and implementing the Kyoto targets in a cost-effective way. Member States should halt the loss of biological diversity between now and 2010, in particular by incorporating this requirement into other policies, given the importance of biodiversity for certain economic sectors. The use of market-based instruments, so that prices better reflect environmental damage and social costs, plays a key role in this context. Encouraging the development and use of environment-friendly technologies, the greening of public procurement with particular attention to SMEs, and the removal of environmentally harmful subsidies alongside other policy instruments can improve innovative performance and enhance the contribution to sustainable development. For example, EU companies are amongst the world leaders in developing new renewable energy technologies. In a context of continued upward pressure on energy prices, and accumulating threats to the climate, it is important to push energy efficiency improvements as a contribution to both growth and sustainable development.

Guideline 11. To encourage the sustainable use of resources and strengthen the synergies between environmental protection and growth, Member States should:

1. give priority to energy efficiency and co-generation, the development of sustainable, including renewable, energies and the rapid spread of environmentally friendly and eco-efficient technologies, (a) inside the internal market on the one hand particularly in transport and energy, *inter alia*, in order to reduce the vulnerability of the European economy to oil price variations, and (b) towards the rest of the world on the other hand as a sector with a considerable export potential;

2. promote the development of means of internalisation of external environmental costs and decoupling of economic growth from environmental degradations. The implementation of these priorities should be in line with existing Community legislation and with the actions and instruments proposed in the Environmental Technologies Action Plan (ETAP), *inter alia*, through, (a) the use of market based instruments, (b) risk funds and R & D funding, (c) the promotion of sustainable production and consumption patterns including the greening of public procurement, (d) paying particular attention to SMEs, and (e) a reform of subsidies that have considerable negative effects on the environment and are incompatible with sustainable development, with a view to eliminating them gradually;

3. pursue the objective of halting the loss of biological diversity between now and 2010, in particular by incorporating this requirement into other policies, given the importance of biodiversity for certain economic sectors;

4. continue to fight against climate change, while implementing the Kyoto targets in a cost-effective way, particularly in regard to SMEs.

See also integrated guideline 'To promote a growth- and employment-orientated and efficient allocation of resources' (No 3).

B.2 Making Europe a more attractive place to invest and work

The attractiveness of the European Union as an investment location depends, *inter alia*, on the size and openness of its markets, its regulatory environment, the quality of its labour force and its infrastructure.

Extend and deepen the internal market

Whilst the internal market for goods is relatively well integrated, services markets remain, legally or *de facto,* rather fragmented. The complete and timely implementation of the Services Directive will be a significant step towards a fully operational Internal Market for services The elimination of obstacles through administrative burden reduction to cross-border activities it will help unleash the untapped potential of the services sector in Europe. Finally, the full integration of financial markets would raise output and employment by allowing more efficient allocation of capital and creating better conditions for business finance.

The further improvement of the transposition of internal market directives should remain a priority in order to reap the benefits of a Single European market. Furthermore, directives are often not implemented or applied correctly, as illustrated by the high number of infringement proceedings launched by the Commission. Member States need to cooperate more positively with each other and with the Commission to ensure that they deliver the full benefits of internal market legislation to their citizens and businesses. For example, there is considerable scope for further improvements in public procurement practices. Such improvements would be reflected in an increase in the share of public procurement publicly advertised. Moreover, more open procurement would lead to significant budgetary savings for the Member States.

Guideline 12. To extend and deepen the internal market, Member States should:

1. speed up the transposition of internal market directives;

2. give priority to stricter and better enforcement of internal market legislation;

3. eliminate remaining obstacles to cross-border activity;

4. apply EU public procurement rules effectively;

5. promote a fully operational internal market of services, while preserving the European social model;

6. accelerate financial market integration by a consistent and coherent implementation and enforcement of the Financial Services Action Plan.

See also integrated guideline 'To improve matching of labour market needs' (No 20).

Ensure open and competitive markets inside and outside Europe

An open global trading system is of essential interest for the EU. As the world's leading trader and investor, our openness allows lower cost inputs for industry, lower prices for consumers, a competitive stimulus for business, and new investment. At the same time, it is important for the EU to use its influence in international negotiations to seek openness from others. Therefore the EU remains committed to further breaking down barriers to trade and investment, while it will stand firm against unfair practices in trade, investment and distorted competition.

Competition policy has played a key role in ensuring a level playing field for firms in the EU. It can also be beneficial to look at the wider regulatory framework around markets, in order to promote the conditions which allow firms to compete effectively. A further opening of European markets to competition can be achieved by a reduction in the general level of remaining State aid. This movement must be accompanied by a redeployment of remaining State aid in favour of support for certain horizontal objectives. The review of State aid rules has facilitated this.

Structural reforms that ease market entry are particularly effective for enhancing competition. These will be particularly important in markets that were previously sheltered from competition because of anticompetitive behaviour, the existence of monopolies, over-regulation (for example permits, licences, minimum capital requirements, legal barriers, shop opening hours, regulated prices, etc. may hinder the development of an effective competitive environment), or because of trade protection.

In addition, the implementation of agreed measures to open up the network industries to competition (in the areas of electricity and gas, transport, telecommunications and postal services) should help ensure lower overall prices and greater choice whilst guaranteeing the delivery of services of general economic interest to all citizens. Competition and regulatory authorities should ensure competition in liberalised markets. The satisfactory delivery of high quality Services of general economic interest at an affordable price must be guaranteed.

Empowered consumers who make informed choices will more quickly reward efficient operators. Further efforts are needed to improve the enforcement of consumer legislation which both empowers consumers and opens up the internal market to more intense competition at retail level.

External openness to trade and investment, by increasing both exports and imports, is an important spur to growth and employment and can reinforce structural reform. An open and strong system of global trade rules is of vital importance for the European economy. The successful completion of an ambitious and balanced agreement in the framework of the Doha-Round as well as the development of bilateral and regional free trade agreements, should further open up markets to trade and investment, thus contributing to raising potential growth.

Guideline 13. To ensure open and competitive markets inside and outside Europe and to reap the benefits of globalisation, Member States should give priority to:

1. the removal of regulatory, trade and other barriers that unduly hinder competition;

2. a more effective enforcement of competition policy;

3. selective screening of markets and regulations by competition and regulatory authorities in order to identify and remove obstacles to competition and market entry;

4. a reduction in State aid that distorts competition;

5. in line with the Community Framework, a redeployment of aid in favour of support for certain horizontal objectives such as research, innovation and the optimisation of human capital and for well-identified market failures;

6. the promotion of external openness, also in a multilateral context;

7. full implementation of the agreed measures to open up the network industries to competition in order to ensure effective competition in European wide integrated markets. At the same time, the delivery, at affordable prices, of effective services of general economic interest has an important role to play in a competitive and dynamic economy.

Improve European and national regulation

Market regulation is essential to create an environment in which commercial transactions can take place at a competitive price. It also serves to correct market failures or to protect market participants. Nevertheless, the cumulative impact of legislation and regulation may impose substantial economic costs. It is therefore important that legislation is e well-designed, proportionate and regularly reviewed. The quality of the European and national regulatory environments is a matter of joint commitment and shared responsibility at both the EU and Member State level.

The better regulation culture has begun to take root in the EU. In the Commission's approach to better regulation, the economic, social and environmental impacts of new or revised legislation are carefully assessed to identify the potential trade-offs and synergies between different policy objectives. Moreover, existing regulation is screened for simplification potential, including of administrative burdens, and its impact on competitiveness is assessed. Finally, a common approach to measuring the administrative costs of new and existing legislation has been agreed, and an ambitious target has been set to achieve a 25 % reduction in the burden arising from EU legislation and its national transposition by 2012.

Member States should set equally ambitious reduction targets for administrative burdens stemming from all levels of national legislation. More generally, Member States should adopt a comprehensive and explicit better regulation strategy, including appropriate institutional structures, monitoring tools and resources. Member States should systematically assess costs and benefits of legislative initiatives and revisions. They should improve the quality of regulation, while preserving their objectives, and simplify existing legislation. They should consult widely on the costs and benefits of regulatory initiatives; particularly where trade-offs between different policy objectives are implied. Member States should also ensure that appropriate alternatives to regulation are given full consideration. This is especially important for small and medium-sized enterprises (SMEs), which usually have only limited resources to deal with the regulatory requirements imposed by both Community and national legislation. Hence, special consideration should be given to whether SMEs could be exempted in total or in part from administrative requirements.

Guideline 14. To create a more competitive business environment and encourage private initiative through better regulation, Member States should:

1. reduce the administrative burden that bears upon enterprises, particularly on SMEs and startups;

2. improve the quality of existing and new regulations, while preserving their objectives, through a systematic and rigorous assessment of their economic, social (including health) and environmental impacts, while considering and making progress in measurement of the administrative burden associated with regulation, as well as the impact on competitiveness, including in relation to enforcement;

3. encourage enterprises in developing their corporate social responsibility.

Europe needs to foster its entrepreneurial drive more effectively and it needs more new firms willing to embark on creative or innovative ventures. Learning about entrepreneurship through all forms of education and training should be supported and relevant skills provided. The entrepreneurship dimension should be integrated in the life long learning process from school. Partnerships with companies should be encouraged. The creation and growth of businesses can be encouraged by improving access to finance and strengthening economic incentives. This can include adapting tax systems to reward success, reducing non-wage labour costs and reducing the administrative burdens for start-ups, notably through the provision of relevant business support services (especially for young entrepreneurs) and setting up of single contact points. Particular emphasis should be put on facilitating the transfer of ownership and improving rescue and restructuring proceedings in particular with more efficient bankruptcy laws. The implementation of the proposals which will be part of the upcoming 'Small Business Act' for the EU will contribute to unlocking the growth and jobs potential of SMEs.

Guideline 15. To promote a more entrepreneurial culture and create a supportive environment for SMEs, Member States should:

1. improve access to finance, in order to favour their creation and growth, in particular micro-loans and other forms of risk capital;

2. strengthen economic incentives, including by simplifying tax systems and reducing non-wage labour costs;

3. strengthen the innovative potential of SMEs;

4. provide relevant support services, like the creation of one-stop contact points and the stimulation of national support networks for enterprises, in order to favour their creation and growth in line with Small firms' Charter. In addition, Member States should reinforce entrepreneurship education and training for SMEs. They should also facilitate the transfer of ownership, modernise where necessary their bankruptcy laws, and improve their rescue and restructuring proceedings.

See also integrated guidelines 'To promote a growth- and employment-orientated and efficient allocation of resources' (No 3) and 'To facilitate all forms of innovation' (No 8, Nos 23 and 24).

Expand and improve European infrastructure

Modern infrastructure is an important factor affecting the attractiveness of locations. It facilitates mobility of persons, goods and services throughout the Union. Modern transport, energy and electronic communication infrastructure are an important factor element of the Lisbon strategy. By reducing transport costs and by widening markets, interconnected and interoperable trans-European networks help foster international trade and fuel internal market dynamics. Moreover, the ongoing liberalisation of European network industries fosters competition and drives efficiency gains in these sectors.

In terms of future investment in European infrastructure, the implementation of 30 priority transport projects identified by Parliament and Council in the trans-European network (TEN) transport guidelines, as well as the completion of the quick-start cross-border projects for transport, renewable energy and broadband communications and research (identified under the European Initiative for Growth and the implementation of the other transport projects, supported by the Cohesion Fund) should be a priority. Infrastructure bottlenecks within countries also need to be tackled. Appropriate infrastructure pricing systems can contribute to the efficient use of infrastructure and the development of a sustainable modal balance.

Guideline 16. To expand, improve and link up European infrastructure and complete priority cross-border projects with the particular aim of achieving a greater integration of national markets within the enlarged EU, Member States should:

1. develop adequate conditions for resource-efficient transport, energy and ICT infrastructures, in priority, those included in the TEN networks, by complementing Community mechanisms, notably including in cross-border sections and peripherical regions, as an essential condition to achieve a successful opening up of the network industries to competition;

2. consider the development of public-private partnerships;

3. consider the case for appropriate infrastructure pricing systems to ensure the efficient use of infrastructures and the development of a sustainable modal balance, emphasizing technology shift and innovation and taking due account of environmental costs and the impact on growth.

See also integrated guideline ‘To facilitate the spread and effective use of ICT and build a fully inclusive information society’ (No 9).

Part 2

The Employment Guidelines (2008-2010)

Proposal for a

COUNCIL DECISION

on guidelines for the employment policies of the Member States (under Article 128 of the EC Treaty)

Proposal for a

COUNCIL DECISION

on guidelines for the employment policies of the Member States

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 128(2) thereof,

Having regard to the proposal from the Commission[2],

Having regard to the Opinion of the European Parliament[3],

Having regard to the Opinion of the European Economic and Social Committee[4],

Having regard to the Opinion of the Committee of the Regions[5],

Having regard to the Opinion of the Employment Committee,

Whereas:

1. The reform of the Lisbon Strategy in 2005 has placed the emphasis on growth and jobs. The Employment Guidelines of the European Employment Strategy and the Broad Economic Policy Guidelines have been adopted as an integrated package[6], whereby the European Employment Strategy has the leading role in the implementation of the employment and labour market objectives of the Lisbon Strategy.

2. The examination of the Member States' National Reform Programmes contained in the Commission's Annual Progress Report and in the draft Joint Employment Report shows that Member States should continue to make every effort to address the priority areas of

   – attracting and retaining more people in employment, increasing labour supply and modernising social protection systems,

   – improving adaptability of workers and enterprises, and

   – increasing investment in human capital through better education and skills.

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2 OJ C …, …, p. .
3 OJ C …, …, p. .
4 OJ C …, …, p. .
5 OJ C …, …, p. .
6 OJ L 205, 6.8.2005, p. 21 (Employment Guidelines) and p. 28 (Broad Economic Policy Guidelines).

3. In the light of both the Commission's examination of the National Reform Programmes and the European Council conclusions, the focus should be on effective and timely implementation, paying special attention to the agreed quantitative targets and benchmarks, and in line with the conclusions of the European Council.

4. The Employment Guidelines are valid for three years, while in the intermediate years until 2010 their updating should remain strictly limited.

5. Member States should take the Employment Guidelines into account when implementing programmed Community funding, in particular of the European Social Fund.

6. In view of the integrated nature of the guideline package, Member States should fully implement the Broad Economic Policy Guidelines.

HAS ADOPTED THIS DECISION:

Article 1

The guidelines for Member States' employment policies as set out in the Annex are hereby adopted.

Article 2

The guidelines shall be taken into account in the employment policies of the Member States, which shall be reported upon in the National Reform Programmes.

Article 3

This decision is addressed to the Member States.

Done at Brussels,

For the Council
The President

ANNEX

Guidelines for the employment policies of the Member States: promoting the European Social Model

Member States, in cooperation with the social partners, shall conduct their policies with a view to implementing the objectives and priorities for action specified below so that more and better jobs support an inclusive labour market. Reflecting the Lisbon strategy and taking into account the common social objectives, the Member States' policies shall foster in a balanced manner:

– *Full employment:* Achieving full employment, and reducing unemployment and inactivity, by increasing the demand for and supply of labour through an integrated flexicurity approach is vital to sustain economic growth and reinforce social cohesion. This requires policies that address simultaneously the flexibility of labour markets, work organisation and labour relations, and employment security and social security.

– *Improving quality and productivity at work:* Efforts to raise employment rates go hand in hand with improving the attractiveness of jobs, quality at work, labour productivity growth, reducing segmentation and the proportion of working poor. Synergies between quality at work, productivity and employment should be fully exploited.

– *Strengthening social and territorial cohesion*: Determined action is needed to strengthen and reinforce social inclusion, fight poverty - especially child poverty-, prevent exclusion from the labour market, support integration in employment of people at a disadvantage, and to reduce regional disparities in terms of employment, unemployment and labour productivity, especially in regions lagging behind. Strengthened interaction is needed with the Open Method of Coordination in Social Protection and Social Inclusion.

Equal opportunities and combating discrimination are essential for progress. Gender mainstreaming and the promotion of gender equality should be ensured in all action taken. Particular attention must also be paid to significantly reducing all gender related gaps in the labour market in line with the European Pact for Gender Equality. This will assist Member States in addressing the demographic challenge. As part of a new intergenerational approach, particular attention should be paid to the situation of young people, implementing the European Youth Pact, and to promoting access to employment throughout working life. Particular attention must also be paid to significantly reducing employment gaps for people at a disadvantage, including disabled people, as well as between third-country nationals and EU citizens, in line with any national targets.

Member States should aim towards active social integration of all through promotion of labour force participation and fight poverty and exclusion of those and groups who are most marginalized in society.

In taking action, Member States should ensure good governance of employment and social policies and ensure that the positive developments in the fields of economics, labour and social affairs are mutually reinforcing. They should establish a broad partnership for change by fully involving parliamentary bodies and stakeholders, including those at regional and

local levels and civil society organizations. European and national social partners should play a central role. A number of targets and benchmarks which have been set at EU level in the framework of the European Employment Strategy in the context of the 2003 guidelines should continue to be followed up with indicators and scoreboards. Member States are also encouraged to monitor the social impact of reforms and define their own commitments and targets, for which they should take these into account, as well as the country specific recommendations agreed at EU level.

Good governance also requires greater efficiency in the allocation of administrative and financial resources. In agreement with the Commission, Member States should target the resources of the Structural Funds, in particular the European Social Fund, on the implementation of the European Employment Strategy and the Union's social objectives and report on the action taken. Particular attention should be paid to strengthening institutional and administrative capacity in the Member States.

Guideline 17. Implement employment policies aiming at achieving full employment, improving quality and productivity at work, and strengthening social and territorial cohesion.

Policies should contribute to achieving an average employment rate for the European Union (EU) of 70 % overall, of at least 60 % for women and of 50 % for older workers (55 to 64) by 2010, and to reduce unemployment and inactivity. Member States should consider setting national employment rate targets.

In addressing these objectives, action should concentrate on the following priorities:

– attract and retain more people in employment, increase labour supply and modernise social protection systems,

– improve adaptability of workers and enterprises,

– increase investment in human capital through better education and skills.

1. Attract and retain more people in employment, increase labour supply and modernise social protection systems

Raising employment levels is the most effective means of generating economic growth and promoting socially inclusive economies whilst ensuring a safety net for those unable to work. Promoting a lifecycle approach to work and modernising social protection systems to ensure their adequacy, financial sustainability and responsiveness to changing needs in society are all the more necessary because of the expected decline in the working-age population. Special attention should be paid to tackling the persistent employment gaps between women and men, further increasing the employment rates of older workers and young people, as part of new intergenerational approach, and the promoting active inclusion of those most excluded from the labour market. Intensified action is also required to improve the situation of young people in the labour market and to significantly reduce youth unemployment, which is on average double the overall unemployment rate.

The right conditions must be put in place to facilitate progress in employment, whether it is first time entry, a move back to employment after a break or the wish to prolong working lives. The quality of jobs, including pay and benefits, working conditions access to lifelong learning and career prospects, are crucial for a flexicurity approach, as are support and

incentives stemming from social protection systems. To enhance a life cycle approach to work and to promote reconciliation between work and family life policies towards childcare provisions are necessary. Securing coverage of at least 90 % of children between 3 years old and the mandatory school age and at least 33 % of children under 3 years of age by 2010 is a useful benchmarks. The increase in the average employment rate of parents, especially single parents, requires measures to support families. In particular, Member States should take account of the special needs of single parents and families with many children. Furthermore to prolong working lives, the effective average exit age from the labour market by 2010 would require a five year increase at EU level (compared to 59.9 in 2001). Member States should also enact measures for health protection, for prevention and for the promotion of healthy lifestyles with the goal of reducing sickness burdens, increasing labour productivity and prolonging working life.

The implementation of the European Youth Pact should also be a contribution to a lifecycle approach to work in particular by facilitating transition from education to the labour market.

Guideline 18. Promote a lifecycle approach to work through:

- a renewed endeavour to build employment pathways for young people and reduce youth unemployment, as called for in the European Youth Pact,

- resolute action to increase female participation and reduce gender gaps in employment, unemployment and pay,

- better reconciliation of work and private life and the provision of accessible and affordable childcare facilities and care for other dependants,

- support for active ageing, including appropriate working conditions, improved (occupational) health status and adequate incentives to work and discouragement of early retirement,

- modern social protection systems, including pensions and healthcare, ensuring their social adequacy, financial sustainability and responsiveness to changing needs, so as to support participation and better retention in employment and longer working lives.

See also integrated guideline 'To safeguard economic and fiscal sustainability as a basis for increased employment' (No 2).

Active inclusion policies can increase labour supply and strengthen society's cohesiveness and are a powerful means of promoting the social and labour market integration of the most disadvantaged. Every person becoming unemployed must be offered a new start in a reasonable period of time. In the case of young people this period should be short, e.g. at most 4 months by 2010; for adult people at most 12 months. Policies aiming at offering active labour market measures to the long-term unemployed should be pursued, taking into consideration the participation rate benchmark of 25 % in 2010. Activation should be in the form of training, retraining, work practice, a job or other employability measure, combined where appropriate with on-going job search assistance. Facilitating access to employment for job seekers, preventing unemployment and ensuring that those who become unemployed remain closely connected to the labour market and employable are essential to increase participation, and combat social exclusion. This is also in line with a flexicurity approach. Attaining these objectives requires removing barriers to the labour market by assisting with

effective job searching, facilitating access to training and other active labour market measures, ensuring affordable access to basic services and providing adequate levels of minimum resources to all. This approach should, at the same time, ensure that work pays for all workers, as well as remove unemployment, poverty and inactivity traps. Special attention should be paid to promoting the inclusion of disadvantaged people, including low-skilled workers, in the labour market, including through the expansion of social services and the social economy, as well as the development of new sources of jobs in response to collective needs. Combating discrimination, promoting access to employment for disabled people and integrating immigrants and minorities are particularly essential.

Guideline 19. Ensure inclusive labour markets, enhance work attractiveness, and make work pay for job-seekers, including disadvantaged people, and the inactive through:

- active and preventive labour market measures including early identification of needs, job search assistance, guidance and training as part of personalised action plans, provision of necessary social services to support the inclusion of those furthest away from the labour market and contribute to the eradication of poverty,

- continual review of the incentives and disincentives resulting from the tax and benefit systems, including the management and conditionality of benefits and a significant reduction of high marginal effective tax rates, notably for those with low incomes, whilst ensuring adequate levels of social protection,

- development of new sources of jobs in services for individuals and businesses, notably at local level.

To allow more people to find better employment, it is also necessary to strengthen the labour market infrastructure at national and EU level, including through the EURES network, so as to better anticipate and resolve possible mismatches. Better transitions between jobs and into employment are an essential part of a flexicurity concept and policies to enhance mobility and matching on the labour market should be promoted. Job-seekers throughout the EU should be able to consult all job vacancies advertised through Member States' employment services. Mobility of workers within the EU should be fully ensured within the context of the Treaties. Full consideration must also be given on the national labour markets to the additional labour supply resulting from immigration of third-country nationals.

Guideline 20. Improve matching of labour market needs through:

- the modernisation and strengthening of labour market institutions, notably employment services, also with a view to ensuring greater transparency of employment and training opportunities at national and European level,

- removing obstacles to mobility for workers across Europe within the framework of the Treaties,

- better anticipation of skill needs, labour market shortages and bottlenecks,

- appropriate management of economic migration.

2. Improve adaptability of workers and enterprises

Europe needs to improve its capacity to anticipate, trigger and absorb economic and social change. This requires employment-friendly labour costs, modern forms of work organisation and well-functioning labour markets allowing more flexibility combined with employment security to meet the needs of companies and workers. This should also contribute to preventing the emergence of segmented labour markets and reducing undeclared work. To successfully meet these challenges an integrated flexicurity approach is needed, covering contractual arrangements; life long learning; active labour market policy; and social security systems (see also Guidelines 18, 19, 23).

In today's increasingly global economy with market opening and the continual introduction of new technologies, both enterprises and workers are confronted with the need, and indeed the opportunity, to adapt. While this process of structural changes is overall beneficial to growth and employment, it also brings about transformations which are disruptive to some workers and enterprises. Enterprises must become more flexible to respond to sudden changes in demand, adapt to new technologies and innovate constantly, in order to remain competitive. They must also respond to the increasing demand for job quality related to workers' personal preferences and family changes, and they will have to cope with an ageing workforce and fewer young recruits. For workers, working life is becoming more complex as working patterns become more diverse, irregular and an increasing number of transitions need to be managed successfully throughout the lifecycle. With rapidly changing economies, workers must be prepared for and furnished with lifelong learning opportunities, in order to cope with new ways of working, including enhanced exploitation of Information and Communication Technologies (ICT), and changes in their working status with associated risks of having to face temporary losses of income better accommodated through the provision of appropriate modernised social protection.

Member States should implement their own pathways, based on the common principles adopted by the Council. Flexicurity involves four key components that should be taken into account: flexible and reliable contractual arrangements through modern labour laws; collective agreements and work organisation; comprehensive lifelong learning (LLL) strategies to ensure the continual adaptability and employability of workers, particularly the most vulnerable; effective active labour market policies (ALMP) that help people cope with rapid change, reduce unemployment spells and ease transitions to new jobs; and modern social security systems that provide adequate income support, encourage employment and facilitate labour market mobility (this includes broad coverage of social protection provisions, unemployment benefits, pensions and healthcare, that help people combine work with private and family responsibilities such as childcare). Geographical mobility is also needed to access job opportunities more widely and in the EU at large.

Guideline 21. Promote flexibility combined with employment security and reduce labour market segmentation, having due regard to the role of the social partners, through:

- the adaptation of employment legislation, reviewing where necessary the different contractual and working time arrangements,

- addressing the issue of undeclared work,

- better anticipation and positive management of change, including economic restructuring, notably changes linked to trade opening, so as to minimise their social costs and facilitate adaptation,

- the promotion and dissemination of innovative and adaptable forms of work organisation, with a view to improving quality and productivity at work, including health and safety,

- support for transitions in occupational status, including training, self-employment, business creation and geographic mobility.

See also integrated guideline 'To promote greater coherence between macroeconomic, structural and employment policies' (No 5).

To maximise job creation, preserve competitiveness and contribute to the general economic framework, overall wage developments should be in line with productivity growth over the economic cycle and should reflect the labour market situation. The gender pay gap should be reduced. Particular attention should be given to the low level of wages in professions and sectors which tend to be dominated by women and to the reasons which lead to reduced earnings in professions and sectors in which women become more prominent. Efforts to reduce non-wage labour costs and to review the tax wedge may also be needed to facilitate job creation, especially for low-wage employment.

Guideline 22. Ensure employment-friendly labour cost developments and wage-setting mechanisms by:

- encouraging social partners within their own areas of responsibility to set the right framework for wage bargaining in order to reflect productivity and labour market challenges at all relevant levels and to avoid gender pay gaps,

- reviewing the impact on employment of non-wage labour costs and where appropriate adjust their structure and level, especially to reduce the tax burden on the low-paid.

See also integrated guideline 'To ensure that wage developments contribute to macroeconomic stability and growth' (No 4).

3. Increase investment in human capital through better education and skills

Europe needs to invest more and more effectively in human capital. Too many people fail to enter, progress or remain in the labour market because of a lack of skills, or due to skills mismatches. To enhance access to employment for men and women of all ages, raise productivity levels, innovation and quality at work, the EU needs higher and more effective investment in human capital and lifelong learning in line with the flexicurity concept for the benefit of individuals, enterprises, the economy and society.

Knowledge-based and service-based economies require different skills from traditional industries; skills which also constantly need updating in the face of technological change and innovation. Workers, if they are to remain and progress in work and be prepared for transition and changing labour markets, need to accumulate and renew skills regularly. The productivity of enterprises is dependent on building and maintaining a workforce that can adapt to change. Governments need to ensure that educational attainment levels are improved and that young people are equipped with the necessary key competences, in line with the European Youth Pact. In order to improve labour market prospects for youth, the EU should aim at an average

rate of no more than 10 % early school leavers; and that at least 85 % of 22-year olds should have completed upper secondary education by 2010. Policies should also aim at increasing the EU average level of participation in lifelong learning to at least 12.5 % of the adult working-age population (25 to 64 age group). All stakeholders should be mobilised to develop and foster a true culture of lifelong learning from the earliest age. To achieve a substantial increase in public and private investment in human resources per capita and guarantee the quality and efficiency of these investments, it is important to ensure fair and transparent sharing of costs and responsibilities between all actors and to improve the evidence base of education and training policies. Member States should make better use of the Structural Funds and the European Investment Bank for investment in education and training. To achieve these aims, Member States must implement the coherent and comprehensive lifelong learning strategies to which they have committed themselves.

Guideline 23. Expand and improve investment in human capital through:

- inclusive education and training policies and action to facilitate significantly access to initial vocational, secondary and higher education, including apprenticeships and entrepreneurship training,

- significantly reducing the number of early school leavers,

- efficient lifelong learning strategies open to all in schools, businesses, public authorities and households according to European agreements, including appropriate incentives and cost-sharing mechanisms, with a view to enhancing participation in continuous and workplace training throughout the life-cycle, especially for the low-skilled and older workers.

See also integrated guideline 'To increase and improve investment in R & D, in particular by private business' (No 7).

Setting ambitious objectives and increasing the level of investment by all actors is not enough. To ensure that supply meets demand in practice, lifelong learning systems must be affordable, accessible and responsive to changing needs. Adaptation and capacity-building of education and training systems is necessary to improve their labour market relevance, their responsiveness to the needs of the knowledge-based economy and society and their efficiency and equity. ICT can be used to improve access to learning and better tailor it to the needs of employers and employees. Greater mobility for both work and learning purposes is also needed to access job opportunities more widely in the EU at large. The remaining obstacles to mobility within the European labour market should be lifted, in particular those relating to the recognition and transparency and use of qualifications and learning outcomes, notably through the implementation of the European Qualifications Framework. It will be important to make use of the agreed European instruments and references to support reforms of national education and training systems, as is laid down in the Education and Training 2010 Work Programme.

Guideline 24. Adapt education and training systems in response to new competence requirements by:

- raising and ensuring the attractiveness, openness and quality standards of education and training, broadening the supply of education and training opportunities and ensuring flexible learning pathways and enlarging possibilities for mobility for students and trainees,

- easing and diversifying access for all to education and training and to knowledge by means of working time organisation, family support services, vocational guidance and, if appropriate, new forms of cost sharing,

- responding to new occupational needs, key competences and future skill requirements by improving the definition and transparency of qualifications, their effective recognition and the validation of non-formal and informal learning.