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# COUNCIL

## COUNCIL OPINION

## of 7 March 2003

## on the updated Stability programme of Luxembourg, 2001 to 2005

(2003/C 64/01)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies [1], and in particular Article 5(3) thereof,

Having regard to the recommendation of the Commission

After consulting the Economic and Financial Committee,

HAS DELIVERED THIS OPINION:

On 7 March 2003 the Council examined the updated stability programme for Luxembourg, which covers the period 2001 to 2005. The programme does not fully comply with the requirements of the code of conduct on the content and format of the programmes endorsed by the Ecofin Council on 10 July 2001; in particular it has been transmitted with a six week delay. The programme partly conforms with the recommendations of the BEPGs.

In 2002, real GDP growth decelerated further to an estimated 0,5 %, from 1,0 % in 2001, which is well below the forecast included in the 2001 stability programme. The slowdown is to a large extent due to adverse developments in financial services, which accounts for around a quarter of total value added. On the basis of a cautious macroeconomic scenario, which assumes a somewhat more muted recovery of economic activity than in the Commission Autumn 2002 forecast, real GDP growth is expected to pick up only gradually, to around 3 % in 2005.

The Council notes that government finances deteriorated markedly in 2002 as revenues decelerated in response to the combined impact of the tax reform and the economic slowdown, while expenditure growth remained very strong. Consequently, the general government budget balance is expected to show a deficit of 0,3 % of GDP in 2002, a sharp deterioration compared to the large surplus of 6,1 % of GDP in 2001 [2]. The general government balance is projected to remain in deficit by 0,3 % of GDP in 2003, to deteriorate slightly further in 2004 to a deficit of 0,7 % of GDP, and to reach a position close to balance in 2005, with a slight nominal deficit of 0,1 % of GDP. The underlying general government balance is expected to remain positive over the horizon covered by the stability programme. Consequently, the Council considers that Luxembourg continues to be in conformity with the requirement of the stability and growth pact to reach a budgetary position of close to balance or in surplus in the medium term.

The Council notes that sound management of public finances continues to be the guiding principle of the 2002 update; the Council welcomes the main elements of the budgetary framework currently in place, which *inter alia* encompasses the use of cautious macroeconomic projections as the basis for budgetary policy, as well as the principle to let net public sector lending be positive, to achieve a balanced budget for central government, and not to let the rise in current expenditure exceed the growth of total expenditure. The Council welcomes the reduction of the tax burden through the implementation of tax reform while aiming for a sound budgetary position in the medium term; in this context it encourages a future government to adhere to real expenditure ceilings that are compatible with achieving a budgetary position close to balance or in surplus in the medium term.

However, the Council expresses some concern over the rapid deterioration of the budget balance of the central government, which only accounts for part of the general government sector. The balance of central government was still in surplus by 2,6 % of GDP in 2001 but is projected to register a deficit of 2,2 % of GDP in 2002 and of 2,1 % of GDP in 2003, while the central government deficit is expected to deteriorate further to 2,8 % of GDP in 2004 and 2005. The Council notes that this is partly due to revenue shortfalls in response to the economic slowdown, while central government expenditure is projected to increase rapidly; although the starting position of public finances in Luxembourg is extremely sound, a continued fast increase of current expenditure might become a factor of risk should economic growth in the medium term slow significantly.

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(1) OJ L 209, 2.8.1997.

(2) More recent data communicated on 1 March show that the central government deficit in 2002 was only 0,1 % of GDP, resulting in a general government surplus of 2,6 % of GDP in 2002. However, this information came too late to be reflected in the Commission's appraisal.

On the basis of current policies, the Council considers that public finances in Luxembourg are in a good position to meet the projected costs of an ageing population. However, the Council notes that the assessment of the sustainability of public finances in Luxembourg is very sensitive to developments as regards the number of cross-border workers. The Council considers that the commitment to sustain a balanced budget position in coming years is broadly appropriate in light of the projected budgetary impact of ageing populations, and welcomes measures to improve the attractiveness of third pillar private pensions.

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# COUNCIL OPINION

## of 7 March 2003

## on the updated Stability programme for Portugal, 2003 to 2006

(2003/C 64/02)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies [1], and in particular Article 5(3) thereof,

Having regard to the recommendation by the Commission,

After consulting the Economic and Financial Committee,

HAS DELIVERED THIS OPINION:

On 7 March 2003 the Council examined the updated stability programme for Portugal, which covers the period 2003 to 2006. The updated programme projects general government finances to improve steadily, from a deficit of 2,8 % of GDP in 2002 to a deficit of 0,5 % of GDP in 2006. Government gross debt is expected to decrease from 58,8 % of GDP in 2002 to 52,7 % in 2006.

The Council notes that the updated programme broadly complies with the requirements of the revised 'code of conduct on the content and format of stability and converge programmes'. The updated programme was adopted by the government on 20 December and presented to parliament, which discussed it and adopted early in January a declaration of approval by a large majority, including the support of the main opposition party. The updated programme was then formally submitted to the Commission. The Portuguese authorities have thus effectively kept the commitment made to the Council on 5 November, in the framework of the recommendation under Article 104(7), to present before the end of the year an updated stability programme. The Council considers that the economic policies as reflected in the planned measures in the programme update broadly comply with the 2002 Broad Economic Policy Guidelines.

The update's macroeconomic scenario shows a small acceleration of GDP growth to 1,3 % in 2003 (from an estimated growth rate of 0,7 % in 2002), which in the light of the most recent information available, pointing to a further deceleration in economic activity in the second half of 2002, looks somewhat optimistic. For the period 2004 to 2006, the macroeconomic scenario presented in the programme update appears plausible as far as the pace of economic growth is concerned (an average growth rate of close to 3 % per year). The planned measures of structural reform should generate beneficial supply side effects, allowing the economy to rely on greater export strength.

The Council considers that regaining an appropriate level of external competitiveness is of paramount importance for Portugal in the light of the level of inflation and real wage developments over the last years. To that end, securing wage moderation and sustained increases in productivity are key requirements, also as a way to secure a decline in inflation. In this context, the Council welcomes the government's guideline to use, from 2003 onwards, the average inflation forecast for the euro-area as the benchmark for wage negotiations, as well as the freezing of most wages in the government sector in 2003. This latter measure should have favourable spill-over effects in the private sector of the economy.

On 5 November 2002, in the light of a government deficit of 4,1 % of GDP in 2001, the Council decided that an excessive deficit existed in Portugal and issued a recommendation to Portugal according to Article 104(7) of the Treaty. In the terms of this recommendation, the Portuguese authorities were urged to:

(i) implement with resolve their budgetary plans for 2002 which aim at reducing the deficit to 2,8 % of GDP in that year. The Council established a deadline of 31 December 2002 for the Portuguese government to take all necessary measures to bring the excessive deficit to an end;

(ii) adopt and implement the necessary budgetary measures to ensure that the government deficit in 2003 is further reduced clearly below 3 % of GDP and that the government debt ratio is kept below the 60 % of GDP reference value.

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[1] OJ L 209, 2.8.1997, p. 1.